DELAWARE SUPREME COURT PEIERLS OPINIONS

On October 4, 2013, the Delaware Supreme Court issued three related *en banc* opinions in the Peierls consent petition matters which were the subject of three notable Court of Chancery decisions near the end of 2012. See IMO: Peierls Family Inter Vivos Trusts, No. 16812 (Del. Oct. 4, 2013); IMO: Ethel F. Peierls Charitable Lead Trust, No. 16811 (Del. Oct. 4, 2013); and IMO: Peierls Family Testamentary Trusts, No. 16810 (Del. Oct. 4, 2013). These landmark opinions have a significant impact on the field of Delaware trust law, clarifying when Delaware law governs the adminstration of trusts migrating to Delaware, the Delaware court's jurisdiction and its role with respect to trust modifications, instructions and other matters. Most notably, the Court held that absent evidence that a settlor intended that the laws governing the administration of a trust at its inception shall always govern administration, a settlor's choice of governing law is not absolute and unchangeable. Under the Peierls decisions, Delaware law will govern the adminstration of any trust that allows for the appointment of a successor trustee without geographic limitation once the Delaware trustee is appointed and the trust is administered in Delaware, unless a choice of law provision expressly provides that another jurisdiction's laws shall always govern.

BACKGROUND

These opinions resulted from the appeal of three opinions of the Delaware Court of Chancery issued in connection with consent petitions filed for seven testamentary trusts (the "Testamentary Trusts"), a charitable lead unitrust (the "Charitable Trust"), and six inter vivos trusts (the "Inter Vivos Trusts"). Each of the uncontested consent petitions requested that the Court (i) approve the resignation of individual trustees, and in the case of the Inter Vivos Trusts and Charitable Trust only, replace a corporate trustee; (ii) confirm the appointment of a Delaware trust company as successor corporate trustee; (iii) determine that Delaware law governs administration of the trust; (iv) confirm Delaware as the trust situs; (v) reform the trusts to modify the administrative provisions and create the positions of Investment Direction Adviser and Trust Protector; and (vi) accept jurisdiction over the trust. The Court of Chancery denied all of the requested relief and set forth analysis concerning when Delaware law will govern the administration of existing trusts that migrate to Delaware.

The Delaware Court of Chancery analyzed Delaware's long-standing case law concerning the application of Delaware law to trusts and found that where the settlor chooses a governing law, that choice is dispositive and the settlor need not deploy "talismanic language" or specify a litany of trust issues to be governed by the chosen law in order to prevent the law governing administration from changing when the place of administration changes to Delaware. The Court explained that the settlor's intent to choose a particular law may be implied from the trust document as a whole and when a settlor has selected a governing law, the power to appoint a successor trustee in and of itself is insufficient to override this intent, unless the trust document expressly provides for such a change. The Court held that the appointment of a successor trustee combined with a change in situs will change the law governing administration only if the trust document so provides or can be construed to contemplate such a change. Those decisions were overturned by the Delaware Supreme Court.

GOVERNING LAW ISSUES

Delaware Law Governing Administration

One of the most significant holdings of the Delaware Supreme Court in these opinions was its decision with respect to the application of Delaware law governing administration of the trusts. The Court's analysis of those issues primarily appears in the opinion addressing the Inter Vivos Trusts, and the opinions addressing the Testamentary Trusts and the Charitable Trust referenced and incorporated that analysis.

There were several sets of governing law provisions among the Inter Vivos Trusts. The Inter Vivos Trusts created in 1953 contained a provision that stated: "all questions pertaining to its validity, construction, and administration shall be determined in accordance with the laws of the State of New York". The Inter Vivos Trust created in 1957 contained a provision that stated its "validity and effect [are] determined by the laws of the State of New Jersey". The Inter Vivos Trusts created in 1975 contained a provision that stated that the trusts: "shall be governed by and [their] validity, effect and interpretation determined by the laws of the State of New York". Relevant to the Court's analysis, all of the trust instruments permitted the appointment of a successor trustee without any geographic limitation.

The Court recognized that Delaware has a choice of law statute, namely 12 Del. C. § 3332. That Section provides that "[e]xcept as otherwise expressly provided by the terms of a governing instrument or by court order, the laws of this State shall govern the administration of a trust while the trust is administered in this State." However, the Court noted that for all of the trusts in this matter, the Delaware trustee was appointed on a conditional basis, subject to judicial approval. The Court found that because the Delaware trustee has not yet assumed its role, Delaware is not yet the place of administration and Section 3332 does not apply to this analysis. Consequently, the Court did not engage in an analysis of Delaware's Section 3332, but instead turned to an analysis of Delaware's conflicts of laws jurisprudence.

The Court quoted Lewis v. Hanson, 128 A.2d 819, 826 (Del. 1957) for the proposition that "a creator of an inter vivos trust has some right of choice of selection of the jurisdiction, the law of which will govern the administration of the trust". The Court elaborated on this principal by stating that a settlor may "designate, either expressly or implicitly within the trust instrument, the law governing the trust's administration". The Court expressed that when confronted with a choice of law issue, Delaware courts adhere to the Restatement (Second) of Conflicts of Laws (the "Restatement"). The Court entered into an extensive analysis of Section 272 of the Restatement. Most importantly, the Court addressed whether the law governing a trust's administration changes following a change of situs. The answer to this question depends "upon the terms of the trust, express or implied." The Supreme Court agreed with the Vice Chancellor's conclusion that in the absence of a choice of law provision, the settlor implicitly intended to allow a change in the law governing administration by allowing the appointment of a successor trustee in another jurisdiction. However, the Supreme Court disagreed with the Vice Chancellor's conclusion that the law governing administration can only be changed in those limited circumstances. The Court stated: "Without evidence that the settlor intended for the law governing administration of the trust at its inception to always govern the trust, a settlor's initial choice of law is not absolute and unchangeable."

The crux of the Court's holding was that a trust instrument may implicitly authorize a change in the law governing the administration of the trust "such as when the trust instrument contains a power to appoint a trustee in another named state." Even a simple power to appoint a successor trustee may be construed to include a power to appoint a trust company or individual in another state. Regardless of whether the trust instrument expressly or implicitly authorizes a change in the trust's administrative law, "the law governing the administration of the trust thereafter is the local law of the other state and not the local law of the state of original administration." That rule applies even when the trust instrument contains a choice of law provision. The Court disagreed with the Vice Chancellor's conclusion that a choice of law provision governing a trust's administration reflects a settlor's intent that a particular state's law will always govern a trust's administration, irrespective of whether the beneficiaries validly exercise a power to appoint an out-of-state trustee. The Court concluded: "when a settlor does not intend his choice of governing law to be permanent and the trust instrument includes a power to appoint a successor trustee, the law governing the administration of the trust may be changed".

As applied to the Peierls trusts, the Court agreed with the Vice Chancellor that at the time of the creation of the trust, the settlor's intent was that the law of the original jurisdiction would govern administration. However, the Court disagreed with the Vice Chancellor's conclusion that a valid appointment of a trustee in another state would effect a change in the law governing administration only "if the settlor has not selected a particular law to govern the trust." The Court reached this conclusion even in the case of the 1953 Inter Vivos Trusts which included a choice of law provision stating that the "validity, construction and administration shall be determined in accordance with the laws of the State of New York". The Court stated: "we adopt the Restatement's enlightening commentary concerning testamentary trusts, namely, that a change in the place of administration resulting from the valid appointment of a successor trustee will result in a change of the law of administration, unless the change would be contrary to the testator's intent. Such a circumstance could arise 'when [the testator] has expressly or by implication provided in the will that the administration of the trust should be governed by the local law of the state of his domicil[e] at death, even though the place of administration should be subsequently changed.'" None of the Inter Vivos Trusts include any language suggesting that the law governing the trust's administration must always remain the law of the original jurisdiction. Accordingly, the Court held that the settlors "implicitly permitted the law of administration to change with a change in the place of administration" and the settlors manifested that intent by permitting the appointment of a successor trustee without geographic limitation. The Court concluded for all of the Inter Vivos Trusts, that the "law of administration would change with a change in the place of administration."

Explanation of Delaware's Conflicts of Laws Cases

Delaware has a fairly well-developed common law history concerning conflicts of laws of trusts. The Vice Chancellor interpreted some of the important cases in this body of law to reach its conclusions. The Supreme Court considered each of those cases and articulated a more constrained interpretation of their application. First tackling the admittedly confusing series of Wilmington Trust v. Wilmington Trust cases, the Court stated: "We read the Wilmington Trust trilogy to stand

for the narrow proposition that a trust instrument, through a power to appoint a trustee combined with 'to the same effect as though now named herein' language can reflect a settlor's intent to allow a beneficiary to reestablish a trust in a different state." Then the Court read Wilmington Trust Co. v. Sloane to hold "that a settlor can permit a beneficiary to exercise a power of appointment over the trust's assets to create a new trust in another state." Finally, the Court read Annan v. Wilmington Trust Co., as "supporting the proposition that a choice-of-law provision concerning the law governing a trust instrument's construction will remain effective even if the trust's place of administration is changed." The Court explained that none of those cases supports the Vice Chancellor's conclusion that "[w]hen a settlor has selected a governing law, the power to appoint a successor trustee in and of itself is insufficient to override this intent, unless the trust document as construed by the Court expressly provides for such a change."

Validation of Change of Governing Law and Situs Provisions

The governing instrument of the Charitable Trust included flexible change of situs and change of governing law provisions, and the Court upheld the application of those provisions. With regard to situs, the governing instrument provides: "The situs of the trust shall, as to personal property, be (i) the location of the main business office of the Trustee who then has custody of the trust records, wherever the Trustee may locate that office, or (ii) any other situs (designated by the Trustee in a writing filed with the trust) that has sufficient contact with the trust to support jurisdiction of its courts over the trust." The Court confirmed the validity and effect of this provision, stating that it would appear that upon the appointment of a corporate trustee in Delaware with custody of the trust records, the situs of the trust would automatically move to Delaware under the express terms of the trust instrument. The Court continued, stating that if the petitioners are not convinced of this, the trustee may file a written election with the trust records. The governing law provision designated Washington law to govern administration but provided that the law would change to the jurisdiction where situs is located. The Court concluded that the settlor's intent was clear that the law governing administration will change with the situs of the trust.

COURT JURISDICTION

The Court found that all of the matters before it pertained to matters of administration and, consequently, the question of whether the Delaware courts have jurisdiction over the trusts required the Court to address which courts have jurisdiction over administration of the trusts. In the opinion addressing the Testamentary Trusts, the Court cited Section 267 of the Restatement for the proposition that "[w]here the trustee has qualified as trustee in a particular court, that court usually has a continuing jurisdiction over the administration of the trust." Furthermore, "[e]ven though the trustee has qualified as trustee in a court, its jurisdiction is not exclusive and the courts of other states may exercise jurisdiction in proper cases if they have jurisdiction over the trustee, or if they have jurisdiction over trust assets insofar as interests in those assets are concerned." The Court noted that all interested parties consented to the Court of Chancery's jurisdiction and, having obtained jurisdiction over the trustees, the Court of Chancery had jurisdiction to adjudicate issues of administration of the trusts under the Restatement test adopted by the Court.

The issue of whether the Court of Chancery had jurisdiction to evaluate the petitions is distinct from the issue of whether the Vice Chancellor should have exercised jurisdiction to do so. This question, according to the Supreme Court, is largely one of which court has "primary supervision" over the trusts. The Court held that "[i]f the court in which the trustee has qualified 'does not exercise active control over the administration of the trust,' then the court of the place of administration 'may exercise primary supervision.'" The Court found that the record reflects that the Superior Court of New Jersey continues to supervise the 1960 Testamentary Trusts and, consequently, it is for the New Jersey courts, and not Delaware, to exercise jurisdiction as to all questions which may arise in the administration of the trust. With respect to the 1969 Testamentary Trusts migrating from Texas, the Court noted that there is no record of interaction with the Texas courts after 2001 and the Texas courts did not appear to exercise active control over the trusts. The Court concluded that because the Texas Probate Court's jurisdiction over the 1969 Testamentary Trusts is not exclusive, and because of the absence of evidence that any court retains primary supervision over the Trusts, no interstate comity concerns prevents the Court of Chancery, which has personal jurisdiction over the trustees, from having jurisdiction over the 1969 Testamentary Trusts and addressing the petitions. The 1957 Inter Vivos Trust was subject to ongoing supervision of the New Jersey courts. The Court concluded that the Petitioners should first seek the permission of the New Jersey Superior Court to terminate its supervision over the trust before it would become subject to Delaware court supervision.

TRUST MODIFICATION

The Court's orders analyzed the necessary conditions for judicial modification of a trust. In the Charitable Trust opinion, the Court highlighted the semantic confusion between the use of the word "reformation" as opposed to "modification" to describe the relief sought in the petitions. A traditional reformation action, of course, has its own set of common law doctrines and criteria, whereas modification merely seeks an exercise of equitable power to modify the terms of a trust

instrument based upon the consent of all interested parties. In the Charitable Trust opinion, the Court held that substituting the word "modify" for "reform" would not lead to a different result. In either instance, the Petitioners seek to have the court invoke its equitable powers to change the terms of a trust instrument. In all three opinions, the Court held that "the Court of Chancery's power to reform a trust depends on which state's law governs the administration of the trust." In other words, if the laws of a state other than Delaware govern the administration of a trust, then parties to a petition for modification or reformation must address reformation or modification under the laws of that state to satisfy the burden. Of course, the holdings in Peierls regarding the change of law governing administration will pave the way for reformation or modification matters to be addressed by Delaware law after a Delaware trustee is appointed. But prior to Peierls, parties routinely petitioned the Court of Chancery for modification, and obtained Court orders granting the relief they were requesting regardless of the governing law, based on the premise that the Court had jurisdiction over the trust and could exercise its equitable powers to modify the terms of the trust instrument. The Court's holdings in Peierls will likely have an impact on the trust modification petition practice in Delaware. With respect to the Peierls trusts, the Court declined to address the issue because Delaware law did not yet govern the administration of the trusts because of the conditional appointment of the Delaware trustee and the issue was not briefed under the laws of the other jurisdictions.

NO "ADVISORY OPINIONS"

The Court concluded that the Vice Chancellor properly declined to approve the resignation and appointment of trustees of the Inter Vivos Trusts, Charitable Trust and Testamentary Trusts because the trust instruments expressly authorize the resignation and appointment of trustees without court approval. The Court concluded that any judicial ruling on this issue would be an impermissible advisory opinion and that no actual controversy exists (even though the trustees made the resignation and appointment of successor trustee conditioned upon the court order and "essentially attempted to create their own controversy"). This holding will also have a material impact on the trust consent petition practice in Delaware. In the past, there has been a practice in Delaware of seeking judicial approval or instructions concerning certain actions that do not necessarily require judicial approval, and in light of Peierls, that practice now appears to be halted.

CONDITIONAL APPOINTMENT AND ACCEPTANCE OF DELAWARE TRUSTEE

In the past, parties sometimes conditionally appointed a Delaware trustee, effective upon the entry of a Delaware court order modifying the trust and granting relief similar to that requested in the Peierls matters. For example, parties who desire to convert a trust to a so-called "directed trust" would sometimes seek a judicial modification of the trust, and the Delaware trustee would be appointed conditionally effective upon the Delaware court's order modifying the trust, so that the Delaware trustee would become a directed trustee from the outset. The Peierls decisions seem to make it clear that it is no longer a viable practice to appoint a successor Delaware trustee, conditioned upon obtaining an order of the Delaware Court of Chancery granting the types of relief requested in the Peierls matters. First, the Court will not grant relief if it is possible for the parties to achieve the same result without judicial intervention because it is an advisory opinion, and this includes approval of the appointment of the Delaware trustee. Under Peierls, it now seems clear when Delaware law will govern administration and when the Delaware court will take jurisdiction over a matter, and confirmation of those items may now be viewed as advisory opinions. If a Petitioner seeks a judicial modification of a trust on the basis of a conditional appointment of the Delaware trustee, and consequently Delaware law does not yet govern administration, the parties will now be required to brief the modification issue under non-Delaware law. Consequently, the conditional appointment of a Delaware trustee, subject to obtaining a Delaware court order, has effectively been halted by Peierls.

CONCLUSION

The Delaware Supreme Court's Peierls opinions have important implications on the Delaware trust industry. The opinions clarify when Delaware law will govern matters pertaining to trust administration, court jurisdiction, judicial modification, and the parameters of the issues traditionally addressed by Delaware trust consent petitions. These decisions may even have implications beyond Delaware, as the conflicts of laws issues addressed by Peierls have not been so clearly articulated in a court's decisions elsewhere in the nation, and certainly not by a court with the stature and reputation of the Delaware Supreme Court. These decisions should help bring clarity to the confusing field of conflicts of laws associated with the inter-state migration of trusts.

Most significantly, the Peierls decisions make it clear that Delaware law will govern the administration of any trust that allows for the appointment of a successor trustee without geographic limitation once a Delaware trustee is appointed and the trust is administered in Delaware, unless the choice of law provision expressly provides that another jurisdiction's laws shall always govern the administration even if the place of administration or situs changes. According to the Court, the ability to appoint a trustee in Delaware reflects the settlor's implied intent that Delaware law will govern the administration of the trust following such appointment. This is the result where

the trust instrument is silent as to governing law, or even where the trust instrument provides that some other jurisdiction's laws shall govern the validity, construction and administration of the trust. Based on this holding, the two situations where Delaware law would not govern the administration of a trust of which a Delaware trustee has been appointed are either (1) where the governing law provision expressly states that the law the original jurisdiction will continue to always govern administration even if a successor trustee is appointed in another jurisdiction, or (2) where the governing instrument does not provide any ability to appoint a successor trustee or the ability to appoint a successor trustee is limited to one located in the original jurisdiction.

Once a Delaware trustee is appointed and Delaware law governs administration, a trust can avail itself of all of the advantages of Delaware law that pertain to administration including, without limitation: decanting (although the decanting statute expressly provides that it would already be available to any trust administered in Delaware), trust merger, general trustee powers, trustee releases, virtual representation, nonjudicial consent settlement agreements, the prudent investor rule, permissible affiliated investments, trustee compensation, total return unitrust conversions, and the trustee's power to adjust.

In a nutshell, the Peierls decisions held the following:

- **Choice of Law.** Absent evidence that the settlor intended that the laws governing administration at a trust's inception shall always govern administration, a settlor's choice of governing law is not absolute and unchangeable. A settlor manifests an implied intent to change the law governing administration by permitting the appointment of a successor trustee without geographic limitation. Delaware law will govern the administration of any trust that allows the appointment of a successor trustee without geographic limitation once the Delaware trustee is appointed and the trust is administered in Delaware unless a choice of law provision expressly provides that another jurisdiction's laws shall always govern administration.

- **Explanation of Delaware's Line of Conflicts of Laws Cases.** The Court elucidated the seminal cases found in Delaware's long-standing conflicts of laws case law.

- **Court Jurisdiction.** The Court noted that all interested parties consented to the Court of Chancery's jurisdiction and, having obtained jurisdiction over the trustees, the Court of Chancery had jurisdiction to adjudicate issues of administration of the trusts under the Restatement test that was adopted by the Court. However, if another court has retained primary jurisdiction over a Trust (as with the 1960 Testamentary Trusts) then the Delaware court will not take jurisdiction to address questions pertaining to administration. But where another court has not retained ongoing or primary jurisdiction, then the Delaware courts can exercise jurisdiction.

- **Conditional Appointment and Acceptance of Delaware Trustee.** The practice of conditioning a Delaware trustee's appointment upon the entry of a Delaware court order has effectively been halted.

- **Trust Modification.** The issue of whether the Court can modify or reform a trust is a question to be determined by the law that governs administration. The Court denied the modifications in Peierls because Delaware law did not yet govern administration and the parties did not brief the issue of modification or reformation under applicable law. Apparently modification is not an exercise of equitable powers that the Court of Chancery can simply exercise based on the consents of all parties, without regard to the law that governs administration.

- **No "Advisory Opinions".** The Court will not enter an order with respect to any matter that can be accomplished without court approval because that is an advisory opinion.

- **Validation of Change of Situs and Governing Law Provisions.** The Court validated the effectiveness of change of situs and change of governing law provisions often found in trust instruments.

Please feel free to contact any member of the Morris Nichols Trusts, Estates & Tax Group to discuss how the Peierls decisions might impact you or your clients.

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