

# Delaware Trust Act 2018 Legislative Update

## **Client Alert**

09.18.2018

Recently enacted legislation (“Trust Act 2018”) provides settlors, beneficiaries, fiduciaries and nonfiduciary powerholders with an even greater ability to accomplish their objectives using Delaware trusts. The most significant changes to Delaware trust law resulting from Trust Act 2018 include:

- Expanding Delaware’s virtual representation statute in a manner that will greatly enhance the utility of the statute, reduce costs and provide greater certainty regarding the validity and enforceability of a wide variety of matters related to Delaware trusts.
- Modifying various provisions of Title 12 of the Delaware Code to expand their application to both fiduciaries and nonfiduciaries alike.
- Expanding the definition of “trustee” for important issues such as remedies and damages, liability, entitlement to attorneys’ fees and costs, limitations on actions, protections for reliance upon an instrument or lack of knowledge related to the happening of an event, and beneficiary consents, releases, ratifications and indemnification.
- Modifying Section 3585 of Title 12 of the Delaware Code to limit the time that *any person* may make a claim against a trustee following a trustee’s report and shortening the time that such persons are permitted to make a claim under certain circumstances.

Delaware Governor John Carney signed Senate Bill 195 into law on July 11, 2018.

### **Section 3547 - Representation by a person with a substantially identical interest.**

One of the most important changes to Delaware trust law found in Trust Act 2018 is the expansion of Delaware’s virtual representation statute, Section 3547 of Title 12 of the Delaware Code. To appreciate the scope of the revisions to Section 3547, it is helpful to consider the statute as it existed prior to Trust Act 2018.

Subsection (a) of Section 3547, which remains unchanged, establishes the foundational rule that, unless otherwise represented, a minor, incapacitated, or unborn person, or a person whose identity is unknown or not reasonably ascertainable, may be represented and bound by another who has a substantially identical interest with respect to the particular question or dispute but only to the extent that there is no material conflict of interest between the representative and the person

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represented with respect to the particular question or dispute. The logic behind the statute is that someone with a substantially identical economic interest and no material conflict of interest should be permitted to serve as a proxy for someone who cannot otherwise represent themselves. This provision, which has existed in essentially the same form since it was enacted in 2000, is frequently used to represent and bind others with respect to a wide variety of judicial and non-judicial matters related to Delaware trusts including releases, accountings, non-judicial settlement agreements, consent modifications and consent petitions to the Court of Chancery.

In 2007, subsection (b) of Section 3547 was adopted to expand the utility of the statute by enabling a presumptive remainder beneficiary to represent and bind contingent successor remainder beneficiaries in the same circumstances, and to the same extent as an ascertainable competent beneficiary may represent a minor or person who is incapacitated, unborn or unascertainable under subsection (a). The term “presumptive remainder beneficiary” was defined, but “contingent successor remainder beneficiary” was not. Moreover, the subsection did not account for situations in which all contingent successor remainder beneficiaries could not be represented and bound by a presumptive remainder beneficiary, such as when the presumptive remainder beneficiaries’ interests are not substantially identical to the interests of the contingent successor remainder beneficiaries with respect to that particular issue or when the presumptive remainder beneficiary is being appointed to a fiduciary or nonfiduciary office with respect to the trust. Such circumstances increased both the risk and the expense of an otherwise routine action, and at times prevented a transaction from occurring altogether.

Trust Act 2018 modifies Section 3547(b) to address these issues. First, Section 3547(b) includes a new provision that allows contingent successor remainder beneficiaries, or those who represent them under any other subsection of Section 3547, to represent and bind more remote contingent successor remainder beneficiaries for the same purposes, in the same circumstances, and to the same extent as an ascertainable competent beneficiary may represent and bind a minor or person who is incapacitated, unborn or unascertainable. Consequently, if a presumptive remainder beneficiary is not able to bind some or all of the contingent successor remainder beneficiaries, the adult contingent successor remainder beneficiaries may now bind those who are more remote. Further, new Section 3547(b) includes definitions for both “contingent successor remainder beneficiary” and “more remote”, which will provide greater certainty with respect to any transaction that relies upon virtual representation.

Trust Act 2018 also inserts a new subsection (c) into Section 3547, which causes the provisions that previously appeared as subsections (c) through (e) to be moved to subsections (d) through (f), respectively. In a significant expansion of the statute, new subsection (c) provides that the holder of a general testamentary or inter vivos power of appointment, or a nongeneral testamentary or inter vivos power of appointment that is expressly exercisable in favor of any person or persons, except for the holder of the power, his or her estate, his or her creditors, or the creditors of his or her estate

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(commonly referred to as a “broad limited power of appointment”), may represent and bind persons whose interests, as takers in default, are subject to the power, but only to the extent that there is no material conflict of interest between the holder and the persons represented with respect to the particular question or dispute. In light of the prevalence of general and broad limited powers of appointment, this provision should be useful in many circumstances by reducing the number of participants who may have previously needed to participate in a transaction, thereby reducing the expense, burden and risk associated with many matters involving Delaware trusts. For example, if a current beneficiary possesses a general power of appointment or broad limited power of appointment, the presumptive remainder beneficiaries, contingent successor remainder beneficiaries and more remote beneficiaries may not even be necessary if there is no conflict of interest present, and the current beneficiary could be the only necessary party.

Since 2007, former Section 3547(c), which now appears in subsection (d), has generally permitted the parents (or in some circumstances, the parent) of an otherwise unrepresented minor or incapacitated beneficiary to represent both their child and unborn or unascertainable persons with an interest that is substantially identical to their child’s interest, so long as neither parent has a material conflict of interest with the child with respect to the question or dispute. Trust Act 2018 expands new Section 3547(d) to provide that such parents may also represent and bind another minor or incapacitated person who has an interest that is substantially identical to the interest of the parents’ minor or incapacitated child; provided that there is no material conflict of interest between their minor or incapacitated child and the other minor or incapacitated person. This provision will allow minor beneficiaries whose parents could not represent them, for example, if their parent(s) had a conflict of interest, to be represented by another minor beneficiary’s parents. New Section 3547(d) also permits the parent of an unborn beneficiary to represent and bind such unborn beneficiary and other minor, incapacitated, unborn or unascertainable persons with a substantially identical interest to the interest of the unborn child to the same extent, and subject to the same restrictions, as parents may represent their own minor or incapacitated child. In sum, new Section 3547(d) expands both the scope of beneficiaries who may be represented by the parents of another beneficiary and the scope of parents (or prospective parents) who may represent such beneficiaries. These revisions greatly expand the utility of the statute and will reduce transaction costs and will provide greater certainty that a transaction is both valid and enforceable.

Prior to Trust Act 2018, there was some uncertainty surrounding the representation of a trust that is a beneficiary of another trust, particularly when the trust to be represented did not yet exist. To address this issue, Trust Act 2018 adds a new Section 3547(g), which provides that a “beneficiary trust”, which is defined to mean a trust that is a beneficiary of another trust, may be represented by its trustee or, if it is not yet in existence, by those persons who would be beneficiaries of the beneficiary trust if the beneficiary trust were then in existence. Although this new provision reflects how many trustees and practitioners expected virtual representation to work under such

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circumstances, the addition of this new provision provides parties with certainty on the issue moving forward.

### **Section 3302 - Degree of care; authorized investments.**

Section 3302 of Title 12 of the Delaware Code was modified to expressly allow fiduciaries who have investment responsibility over trust property, when considering the needs of beneficiaries, to not only consider the financial needs of the beneficiaries but to also consider the beneficiaries' personal values, including the beneficiaries' desire to engage in sustainable investing strategies that align with the beneficiaries' social, environmental, governance or other values or beliefs. This revision recognizes the reality of so-called Environmental, Social and Governance ("ESG") investing and the fact that many settlors and beneficiaries desire to effect positive impact through strategic investments. This new feature of Delaware law provides fiduciaries who have investment responsibility over Delaware trusts with greater confidence to invest trust property in a manner desired by the beneficiaries. It continues the trend towards permitting non-traditional investments in Delaware trusts, and is also consistent with recent developments in the Delaware corporations law, which now allows for the formation of public benefit corporations that balance stockholders' pecuniary interests with the interests of those materially affected by the corporations' conduct and the public benefits identified in the corporation's certificate of incorporation.

### **Section 3303 - Effect of provisions of instrument.**

Similar to the revisions to Section 3302 of Title 12 of the Delaware Code designed to acknowledge ESG investing, Section 3303 of Title 12 of the Delaware Code was revised to expressly provide that a trust instrument may expand, restrict, eliminate or otherwise vary laws pertaining to the manner that a fiduciary should invest assets, including whether to engage in one or more sustainable or socially responsible investment strategies, in addition to, or in place of any other investment strategies, with or without regard to investment performance.

### **Section 3313 - Advisers.**

Section 3313 of Title 12 of the Delaware Code recognizes that a trust instrument may provide for the appointment of various "advisers" who may direct, consent to or disapprove of a fiduciary's investment decisions, distribution decisions or other decisions related to a trust. Trustees of Delaware trusts are frequently directed by an investment adviser with respect to all "investment decisions" related to a trust. Trust Act 2018 modifies subsection (d) of Section 3313 to clarify that a power to lend for investment purposes constitutes an investment decision of the trust only with respect to loans other than those described in Section 3325(19)(b) and (c) of Title 12 of the Delaware Code, meaning that the term "investment decisions" does not include certain loans that are made in lieu of a distribution amount that could have been made currently to or for a beneficiary. This

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clarification will aid fiduciaries of Delaware trusts in determining whether an adviser is acting within the scope of its authority when directing, consenting to or disapproving of a loan from the property of a trust.

Trust Act 2018 also adds a new subsection (g) to Section 3313, which provides that a person who accepts an appointment as an adviser or acts as an adviser of a trust submits to the personal jurisdiction of Delaware with respect to any matter related to the trust. This provision provides fiduciaries and beneficiaries of Delaware trusts with greater clarity that advisers with the power and authority to direct, consent to or disapprove of such fiduciaries' decisions cannot avoid a claim related to the adviser's direction, consent or disapproval based upon a personal jurisdiction defense.

### **Section 3313A - Excluded cotrustee.**

In 2017, Delaware adopted Section 3313A of Title 12 of the Delaware Code, which addresses the duties and liability of a trustee when a trust instrument grants a cotrustee exclusive authority to take specified actions on behalf of the trust, including the power to direct or prevent certain actions of the excluded trustee. At the time of its enactment, subsection (a)(2) of Section 3313A provided that, if the terms of the governing instrument confer upon the cotrustee exclusive authority to exercise any power, the excluded trustee is not liable, individually or as a fiduciary, for any loss resulting directly or indirectly from the action taken by the cotrustee in the exercise of the power. Trust Act 2018 goes a step further by revising Section 3313A to provide that the excluded cotrustee is not a fiduciary with respect to any power as to which the governing instrument has conferred upon the cotrustee exclusive authority but remains a fiduciary with respect to any powers or other matters as to which the governing instrument has not conferred exclusive authority on the cotrustee.

### **Section 3317 - Co-fiduciaries and co-nonfiduciaries; duty to keep informed.**

Section 3317 of Title 12 of the Delaware Code generally provides that each trust fiduciary has a fiduciary duty upon request to keep the other fiduciaries reasonably informed about the administration of the trust to the extent that such information is reasonably necessary for the other fiduciaries to perform their duties. Section 3317 protects the fiduciary requesting and receiving any such information by providing that such fiduciary shall have no duty to monitor the conduct of the fiduciary providing the information, no duty to provide advice to or consult with the fiduciary providing the information and no duty to communicate with or warn any beneficiary or third party when the fiduciary receiving the information might have exercised its discretion in a different manner.

Trust Act 2018 modifies Section 3317 to make two significant changes. First, Section 3317 was modified to render the provisions equally applicable to nonfiduciary officeholders of the trust as well. Next, Trust Act 2018 adds a new Subsection (2) to Section 3317, which extends the protections

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afforded to the fiduciary requesting the information to the fiduciary or nonfiduciary providing the information as well. Consequently, in light of the modifications to Section 3317, both fiduciaries and nonfiduciaries of Delaware trusts have a duty to provide information to other fiduciaries and nonfiduciaries upon request as provided by the statute, but the provision of such information will not give rise to a duty to monitor, advise, consult, communicate, or warn.

### **Section 3323 - Co-fiduciaries and co-nonfiduciaries.**

Section 3323 of Title 12 of the Delaware Code generally provides that, unless provided otherwise by the governing instrument, any power vested in three or more fiduciaries may be exercised by a majority of such fiduciaries and that ministerial functions may be delegated by the fiduciaries to any one of the fiduciaries. Section 3323 protects a fiduciary who dissents in writing from the action of the majority of fiduciaries, subject to certain limitations. Trust Act 2018 modifies Section 3323 to provide that the section is now also applicable to nonfiduciaries. This revision reflects the reality that governing instruments may allocate powers and responsibility to a committee of nonfiduciaries officeholders.

### **Section 3330 - Construction or interpretation affecting validity under rule against perpetuities, applicability of later-enacted laws, and class determination; effect of survivorship requirement.**

To improve the organization of Title 12, Trust Act 2018 moves certain existing provisions related to the rule against perpetuities and the application of later-enacted laws from Chapter 2 of Title 12 of the Delaware Code to a new Section 3330(a). Moving these provisions to Chapter 33 of Title 12, which contains many of the provisions that are particularly germane to Delaware's national trust practice, is expected to make them more readily apparent to out-of-state fiduciaries and professionals.

### **Section 3338 - Nonjudicial settlement agreements.**

Nonjudicial settlement agreements pursuant to 12 Del. C. § 3338 are frequently used to address a wide variety of issues related to Delaware trusts. Although the list of matters that may be resolved by a nonjudicial settlement agreement provided in Section 3338 is non-exhaustive, Trust Act 2018 modifies Section 3338(d) to expressly provide that the removal of a trustee is a matter that may be the subject of a nonjudicial settlement agreement.

### **Section 3341 - Consequences of trust merger and similar transactions.**

In 2017, Subsection (5) was added to 12 Del. C. § 3341 to address the effect of mergers, decantings and other similar transactions upon powers of appointment over trusts that received their initial funding before such merger, decanting or other similar transaction. To prevent the inadvertent

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expansion of a pre-existing power of appointment over property that such power was never intended to cover, Section 3341(5) provides that any power of appointment exercisable over property of either trust participating in the merger or other transaction shall, following the transaction, be exercisable over property of the transferee trust only to the extent expressly provided by the terms of the written documents effecting the merger or other transaction. Trust Act 2018 adds to Section 3341(5) that if any person holds substantially identical powers of appointment over all of the property of each trust participating in the merger, such person's power of appointment over the property of the transferee trust shall be exercisable over all of the property of the transferee trust following the merger unless the instrument of merger or other written document effecting the merger expressly provides otherwise. Moreover, Trust Act 2018 modifies Section 3341(5) to provide, subject to a single exception, that Section 3341 shall not be construed to address the validity or effect of a written exercise of a power of appointment over property of any trust participating in a trust merger that was executed prior to a trust merger. These revisions effectively create a safeguard to ensure that the donee of a power will not inadvertently lose a power of appointment as a result of a merger, decanting or other similar transaction unless that is the intended result.

### **Section 3342 - Modification of trust by consent while trustor is living.**

The Delaware trust consent modification statute, 12 Del. C. § 3342, now provides that a modification pursuant to the statute is not limited to adding new provisions to a trust instrument, but may also be used to modify existing provisions, provided that such provisions could have been included in the governing instrument if such trust was created upon the date of the modification.

### **Section 3528 - Trustee's authority to invade principal in trust.**

Trust Act 2018 modifies Delaware's decanting statute, Section 3528 of Title 12 of the Delaware Code, to provide that the exercise of a power to invade principal or income or both of a trust shall be affected by an instrument in writing, thereby removing the requirement that such writing be acknowledged and filed with the records of the trust. This revision further simplifies the decanting process under Delaware law and removes technical requirements that might have been overlooked.

### **Section 3536 - Rights of creditors and assignees of beneficiary of trust.**

Trust Act 2018 expands Section 3536 of Title 12 of the Delaware Code to provide that a trustor may release a beneficial interest that is contingent on surviving the trustor's spouse so as to accelerate the next succeeding beneficial interests. Delaware common law previously prevented such a release. This enactment creates greater flexibility and new planning opportunities for trustors of Delaware trusts.

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### **Section 3545 - Limitations on oral trusts; execution requirements for written trusts.**

Although Delaware law does not require trust instruments to be executed with the same formalities as wills in order to be valid in all circumstances, Section 3545 of Title 12 of the Delaware Code sets forth execution requirements for the creation, modification or revocation of a trust whereby a person other than the trustor acquires or is divested of an interest that is contingent upon surviving the trustor. Trust Act 2018 clarifies these execution requirements by providing that a writing executed by the trustor in accordance with the statute must be witnessed in writing in the trustor's presence by a person or persons qualified to serve as a witness pursuant to the statute. Prior to Trust Act 2018, there was ambiguity with respect to the witness requirements.

### **Section 3580 - Definition of "trustee".**

Subchapter VII of Chapter 35 of Title 12 of the Delaware Code addresses matters related to liability and the rights of people dealing with a trustee. Subchapter VII encompasses Sections 3580 - 3595, which cover such issues as remedies and damages related to a breach of trust, the liability of a trustee in the absence of a breach of trust, entitlement to attorneys' fees and costs, limitations on actions following a trustee's report, protections afforded to a trustee for reliance on an instrument or lack of knowledge related to the happening of an event and beneficiary consents, releases, ratifications and indemnification. Prior to Trust Act 2018, the term "trustee" was defined for purposes of Subchapter VII to include only fiduciaries and other persons exercising, or directing the exercise of, trust powers. Trust Act 2018 expands this definition to encompass powers and duties that arise under a trust instrument or otherwise under Title 12 of the Delaware Code, and also to include persons consenting to the exercise of such powers and duties, and those who are required to be consulted before the exercise of trust powers, including designated representatives under Section 3339 of Title 12. This enactment expands the reach of very important statutes to persons with powers, duties and offices related to Delaware trusts who may not have fallen within the definition of "trustee" in the past.

### **Section 3585 - Limitation of action against trustee following trustee report.**

Prior to Trust Act 2018, Section 3585(a) limited the time that a beneficiary may initiate a proceeding against a trustee for breach of trust until the first to occur of: (1) two years after the date the beneficiary was sent a report that adequately disclosed the facts constituting a claim; (2) 120 days after a beneficiary is sent a report from a trustee who no longer serves, subject to certain disclosure requirements; and (3) the date the proceeding was otherwise precluded. Trust Act 2018 modifies Section 3585 to limit the time that *any person* may make a claim against a trustee, and shortens the time limitation provided under Section 3585(a)(1) from two (2) years after the beneficiary was sent a report to one (1) year after the beneficiary or other person was sent such report, thereby providing even stronger protections to trustees of Delaware trusts.

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### **Section 3588 - Beneficiaries consent, release, ratification or indemnification.**

Section 3588 protects trustees from claims by beneficiaries who have consented to, ratified, or released a trustee from liability related to the conduct constituting such claims, subject to certain limitations described in the statute. Trust Act 2018 expands these protections to claims by any person, not only beneficiaries, subject to the same limitations. Further, Section 3588 was revised to provide that indemnifications, much like consents, releases and ratifications, need not be supported by consideration.

### **25 Del. C. § 505 - Exercise of powers of appointment.**

Trust Act 2018 adds a new subsection (e) to Section 505 of Title 25 of the Delaware Code, which allows a donee of a nongeneral power of appointment to appoint all or a portion of the assets subject to such power to the donee's revocable trust for the benefit of one or more objects of such power without subjecting the assets to claims of creditors of the donee, the donee's estate, or the donee's revocable trust, by creating a separate trust within such revocable trust. This provision further exhibits Delaware's strong stance on asset protection and provides individuals with the ability to take advantage of the flexibility provided by revocable trusts.

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Trusts & Estates/Private Client

