

# Delaware Trust Act 2021 Legislative Update

## Client Alert

07.12.2021

On June 30, 2021, Delaware Governor John C. Carney signed House Bill 164 (“Trust Act 2021”) into law. The legislation includes the following highlights:

- Amendments to Delaware’s designated representative statute, 12 Del. C. § 3339, to (i) expand the manner of acceptance of appointment of a designated representative, (ii) permit the appointment of a designated representative to represent minor, unborn, incapacitated and unascertainable beneficiaries, and allow beneficiaries to appoint a designated representative for themselves, even in cases where the governing instrument does not restrict or eliminate those beneficiaries’ rights to information about their interest, (iii) cause designated representatives to be subject personal jurisdiction in Delaware, and (iv) provide that a trustor may only appoint a designated representative to the extent one is not appointed by the first three methods identified in the statute.
- Enactment of new 12 Del. C. § 3550 to allow trust agreements and most other trust-related documents to be executed electronically in accordance with the Uniform Electronic Transactions Act.
- Amendments to Delaware’s spendthrift statute, 12 Del. C. § 3536, to abrogate the relation-back doctrine when a beneficiary of a trust created by a trustor exercises a power of appointment in further trust that includes among its beneficiaries the trustor of the first trust.
- Expansion of Delaware’s income tax reimbursement statute, 12 Del. C. § 3344, to expressly include county, metropolitan, city, local, foreign, and other income taxes among the categories of taxes for which the trustor may be reimbursed, and limit the application of the statute if it would affect an otherwise available marital deduction.
- Expansion of Delaware’s statutory trustee resignation and removal provisions, 12 Del. C. § 3326 and 3327, to also cover advisers, such as investment advisers, distributions advisers and trust protectors, as well as designated representatives.
- Clarification that the execution safe harbor under 12 Del. C. § 3545 applies to all trusts, not just trusts in which a person other than the trustor acquires or is divested of an interest in the trust the possession or enjoyment of which is contingent upon surviving the trustor.

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### SECTION 3339 – DESIGNATED REPRESENTATIVES OF TRUSTS

A “designated representative” under Section 3339 of Title 12 of the Delaware Code is a person appointed to represent and bind trust beneficiaries in judicial and nonjudicial matters. Prior to Trust Act 2021, the statutory powers of a designated representative were only triggered by Section 3303 (d) of Title 12 of the Delaware Code, which provides that a designated representative may represent and bind a beneficiary for any judicial proceeding or nonjudicial matter when the governing instrument restricts or eliminates such beneficiary’s rights to be informed of the beneficiary’s interest. Trust Act 2021 made a number of substantial revisions to Section 3339. It permits the appointment of a designated representative to represent minor, unborn, incapacitated and unascertainable persons, and allows beneficiaries to appoint a designated representative for themselves, even if their rights to information are not limited by the terms of a governing instrument. It also includes other changes, including expansion of the ways in which a designated representative shall be deemed to have accepted service, providing that the trustor may only appoint a designated representative pursuant to the statute in the absence of appointment pursuant to one of the first three mechanisms identified in the statute, and causing designated representatives to be subject to personal jurisdiction in Delaware, similar to other advisers. Trust Act 2021’s modifications to Section 3339, in the order in which they appear in the statute, are:

- Section 3339 previously defined a designated representative as a person who delivers to the trustee a written acceptance of the office of designated representative. Trust Act 2021 modifies this definition to also include a person who has otherwise agreed, through service or similar action to serve as designated representative. This change should broaden the facts and circumstances where a person shall be deemed to have assumed the position of designated representative even in the absence of a written acceptance. It may also be beneficial for trusts with governing instruments that pre-date the designated representative statute, where a person has been authorized in the governing instrument to be the recipient of account statements on behalf of other beneficiaries in a representative capacity and has served in that role.
- Since its enactment, Section 3339 has permitted a designated representative to be appointed by any of the following means: (i) an express appointment under the terms of the governing instrument, (ii) an authorization or direction under to the terms of the governing instrument to represent or bind one or more beneficiaries, (iii) an appointment by someone authorized by the governing instrument to appoint a person as designated representative or otherwise to represent or bind one or more beneficiaries, (iv) an appointment by a beneficiary to act as designated representative for such beneficiary, or (v) an appointment by the trustor to act as designated representative for one or more beneficiaries. Trust Act 2021 revises the statute to provide that the appointment of a designated representative by the trustor is only available if a designated representative is not otherwise appointed under one of the first three methods

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and the appointment of a designated representative by a beneficiary is only available if a designated representative is not otherwise appointed under any of the other available methods.

- New Subsection 3339(b) adds two additional circumstances in which a designated representative may be appointed to bind and represent beneficiaries beyond situations described in Section 3303(d) where the governing instrument limits or restricts the beneficiary's rights to information. It provides that a designated representative may be appointed (i) for purposes of representing a beneficiary whose rights to information are limited or restricted in accordance with Section 3303(d), (ii) for purposes of representing a minor, incapacitated, unborn or unascertainable beneficiary in any nonjudicial matter as such term is defined in Section 3303(e), and (iii) by the beneficiary appointing a designated representative for him or herself for purposes of representing the appointing beneficiary in any nonjudicial matter as such term is defined in Section 3303(e). Appointment of a designated representative by a beneficiary to represent and bind such beneficiary is only available if a designated representative is not appointed pursuant to any other permissible method. Additionally, when a trustor appoints a designated representative to represent a minor, incapacitated, unborn, or unascertainable beneficiary and whose rights to information regarding their interest in the trust are not restricted or eliminated under the terms of the governing instrument, pursuant to Subsection 3339(a)(4), the appointed designated representative must serve in a fiduciary capacity, the appointed designated representative must not be related or subordinate to the trustor within the meaning of Section 672(c) of the Internal Revenue Code, and the trustor must provide written notice to the surviving and competent parent or parents or custodial parent or guardian of the property of the beneficiary who will be represented by the appointed designated representative within 30 days of appointment. The reason for these safeguards is that the trustor's ability to unilaterally appoint a designated representative to represent and bind a minor, unborn, incapacitated or unascertainable beneficiary for nonjudicial matters can supplant, or be used in lieu of, virtual representation by both parents under Section 3547.
- Subsection 3339(c) confirms that a designated representative appointed for a minor, unborn, incapacitated or unascertainable person, and a designated representative appointed by a beneficiary for him or herself, for any nonjudicial matter, may represent and bind the beneficiary notwithstanding that the governing instrument does not restrict or eliminate the right of such beneficiary to be informed of the beneficiary's interest in the trust. Previously, the only way a designated representative could be used to bind a beneficiary for purposes of a nonjudicial matter, such as a release, nonjudicial settlement agreement, or consent modification, is if the trust's governing instrument contained a provision that restricts or limits the beneficiary's rights to information. Situations can arise where minor, unborn, incapacitated or unascertainable beneficiaries cannot be virtually represented under Section 3547 in

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nonjudicial matters because of a conflict of interest. For example, a minor, unborn or incapacitated beneficiary could not be represented and bound in connection with a transaction because (i) virtual representation was unavailable due to conflicts of interest or because no competent adult had a substantially identical interest to the minor, unborn or incapacitated beneficiary for purposes of that particular transaction and (ii) a designated representative could not be appointed because the terms of the governing instrument did not expressly restrict or eliminate the rights of such beneficiary to receive information regarding their interest in the trust (thereby rendering representation under Section 3303(d) unavailable). Section 3339 now permits a designated representative to be appointed to represent and bind those beneficiaries in nonjudicial matters who previously could not be represented or bound.

- New Subsection 3339 contains a new provision that provides that a designated representative who accepts appointment or acts as designated representative submits to personal jurisdiction in the State of Delaware.

### SECTION 3550 – ELECTRONIC EXECUTION OF DOCUMENTS

In another significant development, Delaware has enacted new Section 3550 of Title 12 of the Delaware Code providing for the electronic execution of trust agreements and many other trust documents used regularly in the Delaware trust industry. Specifically, new Section 3550 provides that, if otherwise validly executed, these trust documents may be executed in accordance with the Uniform Electronic Transactions Act (“UETA”).

UETA, which has been enacted in 49 states (all but New York), the District of Columbia, and the US Virgin Islands, validates the use of electronic signatures. The term “electronic signature” is defined by UETA to mean “an electronic sound, symbol, or process attached to or logically associated with a record and executed or adopted by a person with the intent to sign the record.” Consequently, UETA does not create one single form of electronic execution, but rather permits execution in a variety of ways.

Subsection (a) of new Section 3550 provides that, if otherwise validly executed, the following documents may be executed in accordance with UETA:

- governing instruments, other than wills or codicils;
- trust merger instruments;
- nonjudicial settlement agreements;
- consent modification instruments;
- instruments allocating duties among multiple trustees;

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- decanting instruments;
- any trust agreement described in Section 3545 of Title 12 of the Delaware Code;
- an instrument effecting the resignation, removal, appointment or acceptance of appointment of a trustee, adviser, protector, or designated representative;
- consent, release, ratification, or indemnification instruments; and
- any other document addressed by Chapters 33 and 35 of Title 12 not excluded from UETA.

Although UETA was codified in Delaware law in 2000, it was not entirely clear which trust-related documents were subject to the statute, in part because UETA applies to transactions “between two or more persons relating to the conduct of business, commercial, or governmental affairs,” and expressly excludes transactions governed by a law governing the creation and execution of wills, codicils, or testamentary trusts. To clarify this ambiguity, all of the documents described in Subsection (a) are now deemed to be a “transaction” within the meaning of UETA.

Developments in technology have altered the way that business is conducted and the COVID-19 pandemic has only highlighted the importance of being able to transact business electronically. Because of Delaware’s global standing as a leading trust-law jurisdiction, transactions involving Delaware trusts often involve trustors, beneficiaries, trustees, advisers, protectors and counsel located in a variety of locations. The process of printing, signing and collecting original trust documents has traditionally been cumbersome. The enactment of Section 3550 will create far greater flexibility and efficiency by permitting the electronic execution of documents without the need to print, execute and exchange paper documents. Morris, Nichols, Arsht & Tunnell is already prepared to assist our clients with the efficient and convenient execution of documents consistent with this recent development in Delaware law using Docusign® as an electronic document signature platform.

### **SECTION 3344 – INCOME TAX REIMBURSEMENT OR PAYMENT**

In 2019, Delaware enacted Section 3344 of Title 12 of the Delaware Code, which permits a trustee to reimburse a trustor who is treated as an owner of all or part of the property of a trust for income tax purposes under the Internal Revenue Code for such trustor’s state and federal income tax liabilities. Trust Act 2021 expands the categories of taxes for which a trustor may be reimbursed beyond state and federal income tax to include county, metropolitan-region, city, local, foreign, and other income taxes.

Furthermore, from the time of its enactment, Section 3344 has included a provision that prevents the application of the statute if it would reduce the charitable deduction available to any person for state or federal income, gift, or estate tax purposes. Trust Act 2021 revises that provision to prevent its application if it would disqualify a trust for, or reduce the amount of, a marital or charitable

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deduction for federal income, gift, and estate tax purposes.

### **SECTION 3545 – LIMITATION ON ORAL TRUSTS; EXECUTION REQUIREMENTS FOR WRITTEN TRUSTS**

Section 3545 of Title 12 of the Delaware Code provides that the creation, modification or revocation of a trust whereby a person other than the trustor acquires or is divested of an interest in the trust the possession or enjoyment of which is contingent upon surviving the trustor must be in writing and describes the execution requirements applicable to such transactions. Such trust instruments must be (i) in a writing executed by the trustor (or by some other person subscribing the trustor's name in the trustor's presence and by the trustor's express direction) and witnessed in writing in the trustor's presence by at least 1 disinterested or 2 credible persons; or (ii) in a writing executed by a trustee who is a disinterested person without regard to whether any other person, including the trustor, has executed the writing. Thus, a trust instrument that falls under Section 3545 is validly executed if it is signed by a trustee that is a disinterested person. This condition can be generally satisfied by a Delaware corporate fiduciary, which effectively eliminates any notary or witness requirement for the trustor's signature and allow for declarations of trust and deeds of trust that are only signed by the disinterested trustee. While Section 3545 only technically applied to trusts whereby a person other than the trustor acquires or is divested of an interest in the trust the possession or enjoyment of which is contingent upon surviving the trustor, it was generally viewed as a safe harbor execution requirement for all trust instruments.

Trust Act 2021 adds new subsection Section 3545(c) to make clear that that the creation, modification or revocation of a trust that is not described in the statute is also validly executed if executed in accordance with the statute, and further provides that the provisions of the new subsection do not limit the creation, modification, or revocation of a trust by any other means provided by law. Consequently, Section 3545 makes clear that it is an execution safe harbor for any trust agreement by providing that the creation, modification or revocation of a trust, whether or not described in Section 3545(a), will be effectively executed if executed in accordance with the execution requirements described in the statute. Notably, all such documents are now also included among those listed in Section 3550 as being eligible for electronic execution in accordance with UETA.

### **SECTIONS 3326 AND 3327 – RESIGNATION AND REMOVAL OF OFFICE HOLDERS**

Trust Act 2021 amends Sections 3326 and 3327 of Title 12 of the Delaware Code, which previously only applied to the resignation and removal of a trustee, to make them applicable to all "officeholders". The term "officeholder" is defined to include a trustee, an adviser as defined in Section 3313 of Title 12 of the Delaware Code, and a designated representative as defined in Section 3339 of Title 12 of the Delaware Code.

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Section 3326 was also modified to require that, when a governing instrument is silent regarding an officeholder's power to resign, and an officeholder resigns under the statutory authority granted by Section 3326, then notice of an officeholder's resignation must be provided to those with the power to appoint a successor officeholder in addition to the beneficiaries and other officeholders.

In regard to officeholder removal under Section 3327, the section was amended to clarify that an officeholder may be removed in accordance with the terms of a governing instrument. Furthermore, in addition to expanding the scope of the statute from covering trustees to covering all officeholders, three of the bases for judicial removal of an officeholder were modified slightly. First, judicial removal based on "A lack of cooperation among co-trustees substantially impairs the administration of the trust" was changed to "The continued service of the officeholder substantially impairs the administration of the trust". Second, judicial removal for "Unfitness, unwillingness or inability of the trustee to administer the trust properly" was changed to "Unfitness, unwillingness or inability of the officeholder to administer the trust or perform its duties properly". Lastly, judicial removal for "Hostility between the trustee and beneficiaries that threatens the efficient administration of the trust" was changed to "Hostility between the officeholder and beneficiaries or other officeholders that threatens the efficient administration of the trust."

### **SECTION 3536 – RIGHTS OF CREDITORS AND ASSIGNEES OF BENEFICIARY OF TRUST**

Subsection (c) of Section 3536 of Title 12 of the Delaware Code was revised to provide that a person who becomes a beneficiary of a trust due to the exercise of a power of appointment by someone other than such person is not considered to be a trustor of that trust, even if the person who became the beneficiary was the person who created and funded the original trust with respect to which the power of appointment was exercised. The purpose of this amendment was to override the common law relation-back doctrine that might apply if a trustor creates a trust over which a beneficiary has a power of appointment, and that power of appointment is exercised in further trust which includes the trustor of the first trust as a beneficiary. If the trustor of the first trust was deemed to be the trustor of the trust created by the exercise of the power of appointment, then there could be creditor protection issues and potential estate inclusion issues for the trustor. Take the example of a trustor who creates a Spousal Lifetime Access Trust (SLAT) for the benefit of his spouse and descendants over which the spouse has a testamentary limited power of appointment exercisable in favor of anyone other than the spouse, the spouse's estate, the spouse's creditors or the creditors of the spouse's estate. Further assume that the spouse exercises the testamentary power of appointment in favor of a trust for the benefit of the trustor of the first trust and his descendants. Planners have wrestled with the question of whether that new trust (created by the exercise of the spouse's power of appointment) would be subject to the claims of the original trustor's creditors by application of the relation-back doctrine, and whether the assets would thus be

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includible in his estate. The conventional solution to that issue under Delaware law is to ensure that the trust created by the spouse's exercise of the power of appointment qualifies as a so-called "asset protection trust" that is not includible in the trustor's taxable estate. Now Section 3536 clarifies that there is additional support for the conclusion that the new trust is not subject to the claims of the trustor's creditors because Section 3536 provides that if the trustor becomes the beneficiary of a trust created by exercise of a testamentary power of appointment by another person, he or she will be treated as a beneficiary, and shall not be treated as the trustor, of the trust so created and his or her creditors may not satisfy their respective claims from his or her interest in the trust even if he or she granted the power of appointment to the other person. Thus, it should be possible for the trust created pursuant to the exercise of the testamentary limited power of appointment to be excluded from the taxable estate of the beneficiary who was the trustor that created the power of appointment.

### SECTION 3315 – TRUSTEE'S EXERCISE OF DISCRETION; REVIEW BY COURT; DISCRETIONARY INTERESTS

Trust Act 2021 also amends Section 3315 of Title 12 of the Delaware Code to clarify that a discretionary interest is a mere expectancy and not a property right, and that a beneficiary eligible to receive distributions from a trust in the discretion of a trustee or other fiduciary has a discretionary interest in the trust, even if such interest is subject to an ascertainable standard. This clarification should significantly bolster the strong creditor protections afforded under Delaware law.

### SECTION 3342 – MODIFICATION BY CONSENT WHILE TRUSTOR IS LIVING

Prior to Trust Act 2021, Delaware's consent modification statute, Section 3342 of Title 12 of the Delaware Code, provided that notwithstanding any provision of law or the trust's governing instrument limiting or prohibiting amendment of the trust, an irrevocable trust may be modified by the addition of a new provision or the modification of any existing provision—so long as such provision could have been included in the governing instrument of a trust were such trust created upon the date of the modification—by written consent or written nonobjection of all of the trust's trustors, all then serving fiduciaries and all beneficiaries having an interest in the trust, regardless of whether the modification may violate a material purpose of the trust. The Section previously stated that it applies "Notwithstanding any provision of law or the trust's governing instrument limiting or prohibiting amendment of the trust". Trust Act 2021 modifies Section 3342 to clarify that drafters can opt out of the application of the statute by express reference. The introductory language of Section 3342 now provides that it applies "Unless the trust's governing instrument expressly provides that the governing instrument may not be modified pursuant to Section 3342, under a nonjudicial settlement agreement under Section 3338 [of Title 12 of the Delaware Code] or similar provision of law, or under modification agreement".

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### **PRACTICE AREAS**

Trusts & Estates/Private Client

