

UPDATE ON THE UTAH UNIFORM TRUST CODE AND USE IN TRUST PRACTICE

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I. OVERVIEW

The Utah Uniform Trust Code (UUTC) was enacted in 2004 with an effective date of July 1, 2004, so we have now had 4½ years experience with the UUTC. The UUTC adopted most of the provisions of the Uniform Trust Code (UTC), but with several changes as well. Utah was one of the early states to adopt the UTC (I believe the 5th state), but many states have followed suit (approximately 21 in total as of December, 2008, including the neighboring states of Arizona, New Mexico and Wyoming). This outline will focus on key provisions of the UUTC and their impact on trust administration and trust practice.

II. SELECTED PROVISIONS AND ISSUES FOR DISCUSSION.

A. BENEFICIARY RIGHTS.

UTC gives “qualified beneficiaries” certain non-waivable rights in the administration of an irrevocable trust including notification of the existence of the trust and accountings. (As defined in the UTC, “qualified beneficiary” would include remainder and probably contingent beneficiaries.) Under the UUTC the Settlor can dictate to whom reporting is made and in absence of such direction any “qualified beneficiary” would be entitled to the information. “Qualified Beneficiary” is defined in the UUTC as current income and principal beneficiaries and vested remainder beneficiaries, but not contingent beneficiaries. Beneficiary rights were the most discussed item by the Estate Planning Section Committee reviewing the UTC (this was also true for most of the other states adopting the UTC).

B. SPENDTHRIFT PROVISIONS AND CREDITOR RIGHTS.

UTC exempts child support, alimony and perhaps governmental unit claims from spendthrift protection in third party spendthrift trust (e.g. trust created by parent for the benefit of a child). UTC also provides that creditors of settlor can reach assets of revocable trust at the death of Settlor and assets of an irrevocable trust where settlor retains beneficial rights. Utah, of course, adopted self-settled asset protection trusts in 2003, effective January 1, 2004, which allows Settlor to avoid certain future creditors if assets are transferred to a qualified asset protection trust (i.e. irrevocable, total discretion, corporate trustee or co-trustee, etc.) Under Utah’s self-settled asset protection trust provisions, child support, alimony, marital property divisions, governmental claims and certain contract creditors are excluded from the asset protection shield. The rules can be, and historically have been, different regarding asset protection to the Settlor as compared to asset protection to a beneficiary of a third party spendthrift trust. The approach taken in the UUTC continues asset

protection on third party spendthrift trusts even if beneficiary is a trustee or co-trustee. Child support would be excluded from asset protection, but alimony and marital settlements would not. The theory is that assets in a third party spendthrift trust come from someone other than the beneficiary and the beneficiary's spouse should not have claim to the assets. In short, the asset protection features of a self-settled asset protection trust in Utah will be a little different than those of a third party spendthrift trust.

C. MODIFICATION AND TERMINATION.

UTC contains detailed provisions allowing for trust modification and termination both with and without court approval. The intent is to simplify the process in seeking interpretation of provision(s) of a trust and making changes to accomplish the intent of the Settlor. UUTC follows the key provisions of the UTC in this area. A recent issue raised is whether the statutory power of the Settlor and the beneficiaries to modify a trust without court approval could cause part or all of the irrevocable trust to be included in the Settlor's estate under IRC § 2036 (a)(2) or § 2038. (Common law has historically allowed Settlor and beneficiaries to modify).

D. COORDINATION WITH SELF-SETTLED ASSET PROTECTION TRUSTS

UUTC attempts to coordinate provisions in the UUTC with those of the self-settled asset protection legislation passed in 2003. For example, provisions on jurisdiction and place of administration are the same as those enacted as a part of the self-settled asset protection legislation. Some of the apparent mistakes in section numbering in the UUTC are attributable to such coordination (e.g., U.C.A. §§ 75-7-201 and 204 were modified as a part of self-settled asset protection legislation and were not changed by the UUTC—also there are no §§ 75-7-601-603, which were enacted and then repealed as a part of the self-settled asset protection legislation.). I believe Utah is currently the only state that has enacted both the UTC and self-settled asset protection legislation (although at least Wyoming is considering self-settled asset protection legislation).

III. ORGANIZATION AND HIGHLIGHTS

The UUTC follows the organization of the UTC and has 11 parts, starting at section 75-7-101. Some highlights are as follows (statutory reference is to section only—i.e. 75-7-____--I have also made some comments and observations below some sections:

Part 1. General Provisions

- (103) Adds new definitions to those in § 75-1-201, including "Qualified Beneficiary."
- (102) UUTC applies to express trusts but not business trusts (business trusts are sometimes used in other states, but fairly rare in Utah).

- (105) Sets forth certain rules which cannot be overridden by the terms of the trust.
- (109) Sets forth methods of giving notice and also provides that notice of judicial proceeding must be given as provided in applicable rules of civil procedure—does this mean a petition on a trust issue must be served like a complaint in a civil action, instead of just filing the petition and having notice of the petition and hearing sent by regular mail? (at least one judge has so ruled).
- (110) Allows for non-judicial settlements among beneficiaries and interested persons over matters such as trust interpretation, accounting approval and specific actions of a trustee, as long as it does not violate material purpose of the trust.
- (111) Rules of construction on wills also apply to trust.
- (112) Limits the scope of a penalty clause (historically referred to an ‘in terrorem’ clause) in a trust to same as in a will.

Part 2. Judicial Proceedings

- (201-203) Continues jurisdiction of District Courts in trusts issues.
- (205) Provides venue similar to current law and similar to matters involving wills.

Part 3. Representation

- (305) Explains when notice is binding on interested persons, including those represented by another.
- (302-304) Provides detailed rules on ability of one person to represent and bind another, including unborn beneficiaries. (These provisions are essentially the same as in prior law § 75-1-403 and can be particularly helpful in proceedings that could affect minor and incapacitated beneficiaries).
- (305) Allows for appointment of guardian ad litem or other representative when needed. (Is there a difference in serving as counsel for minor or incapacitated beneficiaries as compared to being appointed as guardian ad litem?)

Part 4. Creation, Validity, Modification and Termination of Trust

- (402) Sets forth requirements for creating valid trusts, including capacity of settlor which is the same as for a will.
- (405-408- 409) Allows for charitable trusts, trusts for animals (same as prior law) and trusts without a definite beneficiary (same as prior law).

- (407) Oral trusts can be enforced by “clear and convincing evidence.” (Has anyone been successful in using this statute?)
- (410-412) Provides for both non-judicial and judicial procedures for modification or termination of trust. (These rules follow common law and can be very significant in trust administration—some states still require court approval of modification or termination of trust even if Settlor is still alive, in an attempt to avoid IRC Section 2036 or 2038 challenge by IRS. Some states, like New York, have “decanting” statutes which allow the trustee under certain circumstances to distribute all of the assets of an existing trust into a new trust, the provisions of which contain the desired changes. Although decanting does not seem necessary in a UTC state, some UTC states (Wyoming, for example) are considering adding decanting statutes as well).
- (414) Increases amount of “uneconomic trust” from \$25,000 to \$100,000.
- (415-417) Allows for reformation to correct mistakes, achieves settlor’s tax objectives and to divide or consolidate trusts (this can particularly helpful with generation skipping and long-term trusts).

Part 5. Creditor’s Claims – Spendthrift and Discretionary Trusts

- (502-503) Continues common law rules on spendthrift protection and third party spendthrift trust even if beneficiary is trustee or co-trustee, but excepts child support claims.
- (504) Alimony creditor of beneficiary of discretionary trust cannot compel distribution but may be able to secure court order requiring distribution if trustee abuses discretion.
- (505) Creditor of settlor can pursue assets of settlor’s living trust and assets of settlor’s irrevocable trust to the extent of settlor’s interest in trust, unless the trust meets the special requirements of self-settled asset protection trust.
- (508-519) Provides for notice to creditors and creditor claim provisions for revocable trust at death of settlor essentially the same as in a probate proceeding (same as current probate law - §§ 75- 3-803-814).

Part 6. Revocable Trust

- (601-603) These sections were deleted with no substitute sections.
- (604) Provides that standard of capacity to create or modify a revocable trust is the same as for a will. (Some argue that higher “contract” standard of capacity should apply to trusts as compare to lower standard of capacity for wills).

- (605) Provides that new trust created will be presumed to be revocable unless stated to be irrevocable. (Reverses common law presumption.)
- (607) Provides for shortened periods of time (90 days after notice is given or three years if no notice is given) to contest the validity of a revocable trust after death of settlor. Also limits trustee's liability in making distributions from trust after the death of settlor.

Part 7. Office of Trustee

- (701) Provides rules on accepting or declining trusteeship.
- (703) Provides rules and guidelines on actions or inactions by co-trustees including ability to delegate, taking action when one trustee does not respond and dealing with breach of trust by a co-trustee.
- (706) Provides procedures for removal of a trustee and grounds for removal, including when requested by all beneficiaries if not inconsistent with material purpose of trust.

(Trustee removal and surcharge are often listed as causes of action in fiduciary litigation involving trusts—any “war stories” on using these UUTC provisions?)

Part 8. Duties and Powers of Trustee

- (802-803) Sets forth the common law duties of loyalty and impartiality. Conflict of interest transactions may be voidable if not authorized by trust, court or beneficiaries. (There is a lot of meat in these provisions and parts were added in connection with the self-settled asset protection trust legislation.)
- (811) Sets forth trustee's duty to inform and report to qualified beneficiaries unless settlor provides otherwise in trust, including notice of acceptance by trustee, notice of death of settlor of revocable trust, change in trustee compensation and annual accountings if requested by qualified beneficiary. (If Settlor directs in trust to not provide accountings, etc. to vested remainder beneficiaries, such as to children so long as second spouse survives Settlor, would you want to serve as trustee of such trust? How does the trustee get “closure” on trust accountings and actions in such a case?)
- (812) Limits beneficiary-trustee's powers in tax sensitive areas, including limitation on power to distribute to himself or herself to an ascertainable standard under IRC § 2041. (This has been referred to as an attorney malpractice “relief” act).
- (813-814) Provides general and specific powers of trustee essentially the same as under current law.

- (815) Allows trustees to send out proposed plan of final distribution which would be deemed approved unless objected to by beneficiary within 30 days (a sort of “either complain now or forever hold your peace” provision).

Part 9. Utah Uniform Prudent Investor Act

This Act is essentially the same as prior law but with better organization.

Part 10. Liability of Trustees and Rights of Persons Dealing with Trustee

- (1001) Sets forth multiple remedies for breach of trust, including damages, removal, denying compensation and compelling trustee action.
- (1002) Establishes measure of damages for breach of trust and limits contribution among co-trustees if one trustee is substantially more at fault.
- (1003) Allows court to allocate attorney’s fees and costs in trust litigation and controversies to any party or to the trust based upon equity and justice. (Courts frequently allow all of a portion of legal fees and costs incurred by an interested person in trust litigation to be reimbursed from the trust).
- (1005) Limits period of time beneficiary can sue trustee for breach of trust (6 months after full disclosure notice to beneficiary or 1 year after terminating event—this 1 year statute can surprise some).
- (1008) Provision in trust limiting liability of trustee is not effective if breach committed in bad faith or with reckless indifference, or if clause was inserted by trustee without disclosure. (Some corporate fiduciaries will decline trusteeship unless some exoneration language is included).
- (1009) Provides that informed release or consent by beneficiary of breach of trust is valid.
- (1010) Provides detailed provisions on allocation of damages between trustee and trust, protects trustees from some liability on investments if trust gives investments powers to someone else, and generally protects successor trustee from acts of prior trustee.
- (1013) Provides for certification of trust and reliance upon certifications.

Part 11. Miscellaneous Provisions

- (1103) UUPC applies to all trusts created after July 1, 2004 and to judicial proceedings commenced after July 1, 2004, even for trusts created before July 1, 2004.