

DRAFT  
FOR DISCUSSION ONLY

## **TRUST ACT**

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NATIONAL CONFERENCE OF COMMISSIONERS  
ON UNIFORM STATE LAWS

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**October 21, 1996 Draft**

## **TRUST ACT**

With Comments

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NATIONAL CONFERENCE OF COMMISSIONERS  
ON UNIFORM STATE LAWS**

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## **TRUST ACT**

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**ARTICLE 1.**  
**DEFINITIONS AND GENERAL PROVISIONS**

**Section**

- 1-101.      Short Title.**  
**1-102.      Definitions.**  
**1-103.      Common Law of Trusts.**

**SECTION 1-101.    SHORT TITLE.**    This [Act] may be cited as the  
[Trust Act].

**SECTION 1-102.    DEFINITIONS.**    In this [Act]:

(1) "Account," as it relates to a contract of deposit between a depositor and a financial institution, includes a checking account, savings account, certificate of deposit, share account, and other like arrangement.

(2) "Beneficiary," as it relates to a trust beneficiary, includes a person who has any present or future interest, vested or contingent, and also includes the owner of an interest by assignment or other transfer; and as it relates to a charitable trust, includes any person entitled to enforce the trust.

(3) "Charitable trust" means a trust created for a charitable purpose as specified in Section 5-101, excluding the interests of any noncharitable beneficiary.

(4) "Conservator" means a person appointed by a court to manage the estate of a minor or adult individual.

(5) "Court" means the [\_\_\_\_ Court].

(6) "Fiduciary" includes a personal representative, guardian, conservator, trustee, and agent acting under the authority of a power of attorney.

(7) "Financial institution" means a state or national bank, state or federal savings and loan association or credit union, or like organization.

(8) "Guardian" means a person appointed by a court [, parent, or spouse] to make decisions with respect to the support, care, education, health, and welfare of a minor or adult individual, but excludes one who is merely a guardian ad litem.

(9) "Instrument" means a signed writing.

(10) "Interested person" includes a trustee, a successor trustee, a beneficiary, any other person having a property right in or claim against a trust, and a fiduciary representing an interested person.

(11) "Person" means an individual, corporation, business trust, estate, trust, partnership, limited liability company, association, joint venture, or any other legal or commercial entity.

(12) "Petition" includes a complaint or statement of claim.

(13) "Property" means anything that may be the subject of ownership, whether real or personal, legal or equitable, and any interest therein, including a chose in action, claim, or beneficiary designation under a policy of insurance, employees' trust, or other arrangement, whether revocable or irrevocable.

(14) "Settlor" means a person who creates or funds a trust, including the testator of a will which creates a testamentary trust.

(15) "State" means a State of the United States, the

District of Columbia, the Commonwealth of Puerto Rico, or any territory or insular possession subject to the jurisdiction of the United States.

(16) "Terms of the trust" means the manifestation of the settlor's intent regarding a trust's provisions at the time of the trust's creation, whether expressed in writing, by spoken words or conduct, by rule of construction or otherwise, but only to the extent made in a manner admitting of its proof in a judicial proceeding.

(17) "Trust" means an express trust, charitable or noncharitable, with additions thereto, wherever and however created, including a trust created or determined by a judgment or decree under which the trust is to be administered in the manner of an express trust. The term does not include:

- (i) a Totten trust account;
- (ii) a custodial arrangement pursuant to the Uniform Transfers to Minors Act of any State;
- (iii) a business trust that is taxed as a partnership or corporation;
- (iv) an investment trust subject to regulation under the laws of this State or any other jurisdiction;
- (v) a common trust fund;
- (vi) a voting trust;
- (vii) a security arrangement;
- (viii) a transfer in trust for purpose of suit or enforcement of a claim or right;

(ix) a liquidation trust;

(x) a trust for the primary purpose of paying debts, dividends, interest, salaries, wages, profits, pensions, or employee benefits of any kind;

(xi) an arrangement under which a person is a nominee or escrow agent for another.

(18) "Trust company" means a person that has qualified to engage in and conduct a trust business in this State.

(19) "Trustee" includes an original, additional, or successor trustee, whether or not appointed or confirmed by a court.

#### **Comment**

Several of the definitions are based on definitions from the Uniform Probate Code, but only such portions as are pertinent to the law of trusts. The following is a comparison table:

<u>Definition</u>	<u>Subsection of Act</u>	<u>Uniform Probate Code Section</u>
account	1-102(1)	6-103(1)
beneficiary	1-102(2)	1-201(3)
fiduciary	1-102(6)	1-201(16)
trust	1-102(17)	1-201(53)
trustee	1-102(19)	1-201(54)

"Account" (paragraph(1)) is not used in the defined sense when employed to refer to an accounting to the beneficiaries or court. See, e.g., Section 4-213 (trustee's duty to inform and account)

"Beneficiary" (paragraph (2)) refers only to a beneficiary of a trust as defined in the Act. Other terms, such as "devisee" or "heir", are used when the reference is to a nontrust beneficiary.

Under the Act, only the charitable portion of a trust with both charitable and noncharitable beneficiaries qualifies as a "charitable trust" (paragraph (3)). Consequently, a split-interest trust will in certain instances be governed by two sets of provisions, one applicable to the charitable interests, the other the noncharitable. Compare, e.g., Section 2-205 (termination of noncharitable trust with uneconomically low value) with Section 5-103 (termination of charitable trust with

uneconomically low value).

The definition of "fiduciary" (paragraph (6)) refers to the office as opposed to the fiduciary duties or obligations of the office. A fiduciary is an "interested person" (paragraph (10)) who may act on behalf of those whom the fiduciary represents. A trustee may engage in transactions with another trust, decedent's estate or conservatorship estate of which the trustee is the fiduciary (Section 4-202(d)). A trustee has a duty to redress a breach of trust committed by a predecessor fiduciary from whom the trustee received trust property (Section 4-212).

Under the Act, a "guardian" (paragraph (8)) makes decisions with respect to personal care; a "conservator" (paragraph (4)) manages property. Enacting jurisdictions not using these terms in the defined sense may wish to substitute their own terminology. The definition of "guardian" accommodates those jurisdictions, including jurisdictions which have enacted the Uniform Probate Code, which allow appointment of a guardian by a parent or spouse in addition to the court. Enacting jurisdictions which allow appointment of a guardian solely by a court should delete the bracketed language.

The definition of "property" (paragraph (13)) removes any lingering uncertainty that a revocable designation under an employee plan or life insurance contract is not a sufficient property interest to activate a trust. See also Section 2-101 and comment (methods of creating trusts).

Determining the identity of the "settlor" (paragraph (14)) is usually not at issue. The same person will both create and fund the trust. If more than one person contributes to a trust, the contributors are ordinarily settlors in accordance with their proportional contribution. See *McColgan v. Walter Magee, Inc.*, 155 P. 995 (Cal. 1916); *Parscal v. Parscal*, 196 Cal. Rptr. 462 (App. 1983). Sometimes, however, particularly in the case of a revocable trust, a later contribution will be intended as a donative transfer to the person who originally created the trust. In that event, only the person who created the trust, and not the later donor, will be the settlor of the trust. Ascertaining the identity of the settlor is important primarily for determining rights in revocable trusts. See Sections 3-102 (revocation or modification of revocable trust), 3-105 (claims of creditors following settlor's death), and 3-106 (limitation on contest of revocable trust). While the settlor of an irrevocable trust ordinarily has no continuing rights except for a right to terminate the trust with the beneficiaries' consent (see Section 2-202), under the Act the settlor of an irrevocable trust may also petition for removal of the trustee. See Section 4-107. Also, per Section 5-104, the settlor is an interested person in a proceeding involving a charitable trust.

"Terms of the trust" (paragraph (16)) is a phrase used with some frequency in the Act. While the wording of a written trust instrument is almost always the most important determinant of a trust's terms, the defined phrase is not so limited. Oral statements, the settlor's family circumstances, and, to the



extent the settlor was otherwise silent, rules of construction, all may have a bearing on determining a trust's meaning. If a trust established by order of court is to be administered as an express trust, the terms of the trust are determined from the court order as interpreted in light of the general rules governing interpretation of judgments. See Restatement (Third) of Trusts Sec. 4 and comment (Tent. Draft No.1, 1996).

Not all evidence may be considered in determining the terms of the trust. Under the Act, a trust of real property must be in writing and oral trusts of personal property receive only limited recognition. See Sections 2-103 (Statute of Frauds as applied to trusts), and 2-104 (oral trust of personal property). Evidence otherwise relevant to determining the terms of the trust may also be excluded under other principles of law, such as the parol evidence rule. For the evidence which may be considered in establishing the terms of a testamentary trust, see Restatement Third, Property (Donative Transfers) Sec. 10.2, 11.1-11.3 (Tent. Draft No.1, 1995).

The Act applies only to express trusts, whether private or charitable, and to trusts created by court judgment or decree which are to be administered in the manner of an express trust. The definition of "trust" (paragraph (17)) excludes a variety of business arrangements, which while governed by a trust instrument, are not created pursuant to a donative transfer. Also, because the Act applies only to express trusts, the Act has no effect on the law relating to constructive and resulting trusts, which are remedial devices implied by law.

Under the definition of "trust company" (paragraph (18)), whether an entity has qualified to engage in and conduct a trust business in this State depends on other law. To fall within the definition of "trust company", a corporation, association, or other entity must satisfy the requirements of state or federal law that apply to the particular type of entity.

**SECTION 1-103. COMMON LAW OF TRUSTS.** Except to the extent that the common law governing trusts is modified by this [Act] or another statute, the common law of trusts supplements this [Act].

**Comment.**

Source: Cal. Prob. Code (CPC) Section 15002.

The Act is not comprehensive but codifies only those portions of the law of express trusts which are most amenable to codification. The Act is at all points supplemented by the rich heritage of the common law, particularly as presented in the Restatement of Trusts. As used in this section, the common law is not static but includes the contemporary and evolving rules of decision developed by the courts in exercise of their power to adapt the law to new situations and changing conditions.

**ARTICLE 2.**  
**CREATION, VALIDITY, MODIFICATION, AND TERMINATION OF TRUSTS**

**Part**

- 1. Creation And Validity of Trusts.**
- 2. Modification and Termination of Trusts.**
- 3. Spendthrift Protection.**

**PART 1.**  
**CREATION AND VALIDITY OF TRUSTS**

**Section**

- 2-101. Methods of Creating Trusts.**
- 2-102. Requirements for Validity.**
- 2-103. Statute of Frauds.**
- 2-104. Oral Trust of Personal Property.**
- 2-105. Honorary Trusts; Trusts for Pets.**

**SECTION 2-101. METHODS OF CREATING TRUSTS.** A trust may be created by:

(1) Transfer of property to another person as trustee during the settlor's lifetime, or by will or other instrument taking effect upon the settlor's death;

(2) Declaration by the owner of property that the owner holds the property as trustee;

(3) Exercise of a power of appointment to another person as trustee; or

(4) An enforceable promise to transfer property to another person as trustee.

**Comment.**

Source: CPC Section 15200.

This section is based on Section 17 of the Restatement (Second) of Trusts (1959) and Section 10 of the Restatement (Third) of Trusts (Tent. Draft No.1, 1996).

A trust is not created unless there is trust property or an enforceable promise to transfer trust property. The property interest need not be substantial. A dollar bill stapled to the instrument, or a revocable designation of the trustee as beneficiary of a life insurance policy or employee benefit plan,

all may constitute trust property. See Section 1-102(13) ("property" defined). The property interest need not be transferred contemporaneously with the execution of the trust instrument. A trust created by means of a lifetime document is not invalid simply because the trust is not funded until a later date, including after the settlor's death.

Consideration is not required to create a trust, but a promise to create a trust in the future which is not supported by consideration does not create a trust. A promise to create a trust is enforceable only if the requirements for an enforceable contract are satisfied. See Restatement (Third) of Trusts Sec. 15 (Tent. Draft No.1, 1996).

#### **SECTION 2-102. REQUIREMENTS FOR VALIDITY.**

(a) A trust is created only if a settlor with capacity indicates an intention to create a trust and the trust has a purpose that is not unlawful or against public policy. If the settlor is sole trustee, a trust is created only if the trust has one or more beneficiaries other than the settlor. Unless the trust is a charitable trust or an honorary trust or trust for the care of an animal as described in Section 2-105, a trust is created only if there is a definite or ascertainable beneficiary.

(b) A trust created for an indefinite or general purpose is not invalid for that reason if it can be determined with reasonable certainty that a particular use of the trust property falls within that purpose.

(c) A definite or ascertainable beneficiary includes a beneficiary or class of beneficiaries that is:

(1) ascertainable with reasonable certainty or sufficiently described by the terms of the trust so it can be determined that some person meets the description or is within the class; or

(2) designated pursuant to a grant by the terms of the

trust of a power to the trustee or another person to select the beneficiaries based on a standard or in the discretion of the trustee or other person.

#### **Comment.**

Source: CPC Sections 15201-15205, 15209.

Subsection (a) codifies the basic requirements for the creation of a trust. Subsections (b)-(c) address specific applications of the trust purpose and definite or ascertainable beneficiary rules.

Subsection (a) is primarily derived from the Restatement of Trusts. To create a valid trust, the settlor must indicate an intention to create a trust. Restatement (Second) of Trusts Sec. 23 (1959); Restatement (Third) of Trusts Sec. 13 (Tent. Draft No. 1, 1996). But only such manifestations of intent as are admissible as proof in a judicial proceeding may be considered. See Sections 1-102(16) ("terms of the trust" defined), 2-103 (Statute of Frauds as applied to trusts), 2-104 (oral trusts of personal property). A trust may not be created for a purpose that is unlawful or against public policy. Restatement (Second) of Trusts Sec. 60-65 (1959). A trust, other than a charitable trust or honorary trust or trust for the care of an animal, must also have an ascertainable or definite beneficiary.

To create a trust, a settlor must have the requisite mental capacity. To create a revocable or testamentary trust, the settlor must have the capacity to make a will. To create an irrevocable trust, the settlor must have capacity during lifetime to transfer the property free of trust. See Section 3-101 (capacity to create revocable trust), and see generally Restatement (Third) of Trusts Sec. 11 (Tent. Draft No.1, 1996).

Subsection (a) also addresses what is known as the doctrine of merger. Under this doctrine, a trust is not created if the settlor is the sole trustee unless there are one or more beneficiaries other than the settlor. The doctrine of merger has been inappropriately applied by the courts in some jurisdictions to invalidate self-declarations of trust in which the settlor is the sole life beneficiary but other persons are designated as beneficiaries of the remainder. The doctrine of merger, however, is properly applicable only if all beneficial interests, both life interests and remainders, are vested in the settlor. Under the Act, a beneficiary of a trust includes any person who has a present or future interest, vested or contingent. See Section 1-102(2) ("beneficiary" defined).

Subsection (b) permits a trust for indefinite or general purposes to be created and enforced, even though it is not limited to charitable purposes. This changes the rule applicable under cases such as *In re Estate of Sutro*, 102 P. 920 (Cal. 1970). This section is not intended to affect the law relating to the purposes for which a charitable trust may be created. See

Section 5-101 (purposes for which charitable trust may be created). Contrast Restatement (Second) of Trusts Section 123, under which a trust, if its purposes are indefinite or unenforceable, may be honored by the trustee but not enforced by a beneficiary.

Subsection (c) requires that a beneficiary be indicated with "reasonable certainty," a requirement which is met as long as it can be determined that someone satisfies the criteria specified by the terms of the trust. Under subsection (c)(1), a class of beneficiaries can satisfy the requirement if the class is ascertainable presently or in the future. Subsection (c)(2) provides the settlor a greater degree of flexibility in creating a trust. A disposition that would be valid as a power of appointment will not fail just because it is made in trust.

### **SECTION 2-103. STATUTE OF FRAUDS.**

(a) Except as provided in Section 2-104, a trust is not enforceable unless evidenced by:

(1) a written instrument signed by the trustee, or by the trustee's agent if authorized in writing; or

(2) a written instrument conveying the trust property signed by the settlor, or by the settlor's agent if authorized in writing.

(b) If an owner of property declares that property is held upon a trust for which a written instrument is required, the written instrument evidencing the trust must be signed by the settlor (i) before or at the time of the declaration, or (ii) after the time of the declaration but before the settlor has transferred the property.

(c) If an owner of property while living transfers property to another person to hold upon a trust for which a written instrument is required, the written instrument evidencing the trust must be signed (i) by the settlor concurrently with or before the transfer, or (ii) by the trustee concurrently with or

before the transfer, or after the transfer but before the trustee has transferred the property to a third person.

**Comment.**

For the Statute of Frauds generally, see Restatement (Second) of Trusts Sections 40 et seq. For a description of what the writing must contain, see Restatement (Third) of Trusts Sec. 22 (Tent. Draft No. 1, 1996). Subsections (b)-(c), addressing when the written instrument must be signed, is based on Restatement (Third) of Trusts Sec. 23 (Tent. Draft No. 1, 1996).

**SECTION 2-104. ORAL TRUST OF PERSONAL PROPERTY.** An oral trust of personal property is enforceable only if (i) created by a transfer of property to a trustee other than the transferor, and (ii) the transferor expresses concurrently with or before the transfer an intention to create a trust.

**Comment.**

Source: CPC Section 15207; Tex. Prop. Code Ann. Sec. 112.004.

This section recognizes that purported oral trusts of personal property, because of difficult problems of proof, are inherently suspect. This problem is particularly acute when it is maintained that a settlor, who is now deceased, created such a trust by means of an oral self-declaration. To create an oral trust of personal property under the Act, there must at a minimum be a transfer of property accompanied or preceded by an oral statement by the transferor that the transferee holds the property in trust. Constructive delivery, such as by earmarking property or recording it in the name of the transferee, is also sufficient to comply with the requirements of this section.

In the case of an oral trust, a reference in this Act to the terms of the trust means the terms of the trust as established pursuant to this section. Although Section 3-102(a) provides that a trust is revocable unless the terms of the trust expressly make it irrevocable, an oral trust may be shown to be irrevocable if this is one of its terms.

Nothing in this section or this Act affects the law relating to resulting or constructive trusts. In appropriate circumstances, an attempted disposition of property that fails to satisfy the requirements for an oral trust under this section may be remedied through the mechanism of a resulting or constructive trust. For the circumstances under which a resulting or constructive trust may be imposed on a failed oral trust, see

**SECTION 2-105. HONORARY TRUSTS; TRUSTS FOR PETS.**

(a) A trust for a lawful noncharitable purpose for which there is no definite or ascertainable beneficiary is valid but may be performed by the trustee for only [21] years, whether or not the terms of the trust contemplate a longer duration.

(b) A trust for the care of a designated domestic or pet animal is valid. The trust terminates when no living animal is covered by its terms.

(c) No portion of the trust property of a trust authorized by this section may be converted to any use other than its intended use unless the terms of the trust provide otherwise or the Court determines that the value of the trust property substantially exceeds the amount required.

(d) The intended use of a trust authorized by this section may be enforced by a person designated for that purpose in the terms of the trust or, if none, by a person appointed by the Court.

**Comment.**

Source: UPC Section 2-907.

Subsection (a) of this section validates so-called honorary trusts but places a 21-year limit on their duration. The figure "21" is bracketed to indicate that an enacting jurisdiction may select a different duration.

Subsection (b) addresses a particular type of honorary trust, a trust for the care of a domestic or pet animal. Subsection (b) is independent of (a). A trust for the care of a designated animal may last longer than 21 years if the animal designated at the trust's creation is still living.

Subsections (c) and (d) address administrative issues commonly encountered in connection with honorary trusts. Unless the terms of the trust provide otherwise, no portion of the trust

property of such a trust may be applied other than for its intended use. Provision is made for partial termination, however, if the trust property substantially exceeds the amount needed.

This section is based on Section 2-907 of the Uniform Probate Code but is much less elaborate. The UPC provision also addresses a number of trust issues that are covered elsewhere in this Act.

## **PART 2. MODIFICATION AND TERMINATION OF TRUSTS**

### **Section**

- 2-201. Termination or Modification of Trust.**
- 2-202. Modification or Termination by Settlor and All Beneficiaries.**
- 2-203. Modification or Termination of Irrevocable Trust by All Beneficiaries.**
- 2-204. Modification or Termination Due to Unanticipated Circumstances**
- 2-205. Noncharitable Trust with Uneconomically Low Value.**
- 2-206. Combination of Trusts.**
- 2-207. Division of Trusts.**

### **SECTION 2-201. TERMINATION OR MODIFICATION OF TRUST.**

(a) In addition to the methods specified in Sections 2-202 to 2-205, a trust terminates when:

- (1) the term of the trust expires;
- (2) the trust purpose is fulfilled;
- (3) the trust purpose becomes unlawful or impossible to fulfill; or
- (4) the trust is revoked.

(b) On termination of a trust, the trustee may exercise the powers necessary to wind up the affairs of the trust and distribute the trust property to those entitled.

(c) Termination or modification of a trust may occur under this [Part] notwithstanding that the terms of the trust contain spendthrift provisions.

### **Comment.**



Source: CPC Section 15407; Tex. Prop. Code. Ann. Sec. 112.052.

Subsection (a) lists the ways in which trusts typically terminate. Subsection (b), which is similar to Section 344 of the Restatement (Second) of Trusts, clarifies that even though the trust has terminated, the trustee retains the powers needed to wind up the affairs of the trust and distribute the remaining trust property. For other provisions relating to trustees' powers, see Sections 4-401 and 4-402.

Subsection (c), which provides that a trust may be modified or terminated under this Part notwithstanding that the terms of the trust contain spendthrift provisions, is contrary to the Restatement (Second) of Trusts. Under the Restatement (Second), the presence of a spendthrift provision precludes a termination unless the trust is revoked, the settlor and all beneficiaries consent, or the purposes of the trust become unlawful, impossible to achieve, or have otherwise been accomplished. See, e.g., Restatement (Second) of Trusts Section 338, comment d. As to a trust purpose becoming unlawful or impossible, see Restatement (Second) of Trusts Section 335.

#### **SECTION 2-202. MODIFICATION OR TERMINATION BY SETTLOR AND ALL BENEFICIARIES.**

(a) If the settlor and all beneficiaries of a trust consent, they may modify or terminate the trust.

(b) If a beneficiary does not consent to the modification or termination of a trust, upon petition to the Court, the Court, with the consent of the settlor and other beneficiaries, may approve a requested modification or partial termination if the interests of the beneficiaries who do not consent are not substantially impaired.

(c) Upon termination of the trust, the trustee must distribute the trust property as agreed by the settlor and beneficiaries.

#### **Comment.**

Source: CPC Section 15404, 15410(b).  
Subsections (a) and (b) of this section are drawn from

Section 338 of the Restatement (Second) of Trusts (1959). A trust may be modified or terminated pursuant to this section without court approval and even over a trustee's objection, but a court order may be sought by petition under Section 6-202.

Subsection (c) recognizes that the power to terminate the trust includes the right to direct how the trust property is to be distributed.

**SECTION 2-203. MODIFICATION OR TERMINATION OF IRREVOCABLE TRUST BY ALL BENEFICIARIES.**

(a) If all beneficiaries of an irrevocable trust consent, they may modify or terminate the trust.

(b) Upon petition to the Court, the Court may prohibit a requested modification or termination if the interest in continuing the trust to accomplish its purposes outweighs the reason for termination or modification.

(c) Upon termination of the trust, the trustee must distribute the trust property as agreed by the beneficiaries.

**Comment.**

Source: CPC Section 15403, 15410.

This section is based in part on Section 337 of the Restatement (Second) of Trusts (1959). The consent of the settlor or trustee is not required, although the settlor or trustee may petition the court to prevent the termination or modification. This section does not follow the material purpose doctrine, which has often been rigidly construed, but permits the court to make an overall assessment of whether the reason for modification or termination outweighs the need to continue the trust to satisfy its purposes. For provisions governing modification or termination of trusts if the consent of all beneficiaries cannot be obtained, see Sections 2-204 (modification or termination due to unanticipated circumstances) and 2-205 (trust with uneconomically low value). This section is limited to irrevocable trusts. If the trust is revocable by the settlor, the method of revocation specified in Section 3-102 applies. Compare Section 2-202 (modification or termination by settlor and all beneficiaries).

**SECTION 2-204. MODIFICATION OR TERMINATION DUE TO UNANTICIPATED CIRCUMSTANCES.**

(a) On petition by a trustee or beneficiary, the Court may modify the administrative or dispositive provisions of a trust or terminate the trust if, because of circumstances not anticipated by the settlor, continuation of the trust under its terms would defeat or substantially impair the accomplishment of the trust purposes. If necessary to carry out the purposes of the trust, the Court may order the trustee to do acts that are not authorized or that are forbidden by the terms of the trust.

(b) Upon termination of a trust under this section, the trust property must be distributed in accordance with the probable intention of the settlor under the circumstances.

**Comment.**

Source: CPC Section 15409-15410.

The first sentence of subsection (a) is drawn from Sections 167 and 336 of the Restatement (Second) of Trusts (1959). See also Section 4-401(b) (power of court to relieve trustee from restrictions or confer additional powers). The second sentence of subsection (a) is based on a provision of the Texas Trust Code. See Tex. Prop. Code Ann. Sec. 112.054 (Vernon 1984).

This section permits modification or termination whenever there are circumstances not anticipated by the settlor. This may include circumstances in existence at the time of the trust's creation which were not considered by the settlor. Unlike the Restatement, this section extends equitable deviation to the dispositive provisions of a trust. Modification of the dispositive provisions for the support of a beneficiary may be appropriate, for example, in a case where the beneficiary has become unable to provide for support due to poor health or serious injury. See, e.g., *Whittingham v. California Trust Co.*, 4 P.2d 142 (Cal. 1931).

**SECTION 2-205. NONCHARITABLE TRUST WITH UNECONOMICALLY LOW VALUE.**

(a) If the trust property of a noncharitable trust does not exceed [\$50,000] in value, the trustee may terminate the trust.

(b) On petition by a trustee or beneficiary, the Court may

terminate or modify a noncharitable trust or appoint a new trustee if it determines that the value of the trust property is insufficient to justify the cost of administration involved and continuation of the trust under its existing terms or trustee would defeat or substantially impair the accomplishment of the trust purposes.

(c) Upon termination of a trust under this section, the trustee must distribute the trust property in accordance with the probable intention of the settlor under the circumstances.

**Comment.**

Source: CPC Section 15408, 15410.

Subsection (a) establishes a presumption that a trust with a value of \$50,000 or less is inherently uneconomical. Consequently, court approval of the termination is not required. For the comparable provision on termination of charitable trusts, see Section 5-103.

**SECTION 2-206. COMBINATION OF TRUSTS.**

(a) A trustee, without approval of court, may combine two or more trusts with substantially similar beneficial interests.

(b) On petition by a trustee or beneficiary, the Court may combine two or more trusts, whether or not their terms are similar, if the Court determines that administration as a single trust will not defeat or substantially impair the accomplishment of the trust purposes or the interests of the beneficiaries.

**Comment.**

Source: CPC Section 15411.

Subsection (a) allows a trustee to combine two or more trusts although their terms are not identical. Trusts often vary in almost imperceptible ways, such as the presence of differing perpetuities savings periods. The section merely requires

similarity of the beneficiaries' interests. The trustee's management powers need not be identical.

Subsection (b) recognizes that the interests of efficient trust administration may dictate that two or more trusts be combined even though their beneficial interests are not substantially similar.

This section applies to all trusts, whether created by will or otherwise. In addition, a trust created by will may be combined with a trust created during the settlor's lifetime.

#### **SECTION 2-207. DIVISION OF TRUSTS.**

(a) Without approval of court, a trustee may divide a trust into two or more separate trusts with substantially similar terms.

(b) On petition by a trustee or beneficiary, the Court may divide a trust into two or more separate trusts, whether or not their terms are similar, if the Court determines that dividing the trust is in the best interest of the beneficiaries and will not defeat or substantially impair the accomplishment of the trust purposes.

#### **Comment.**

Subsection (a) recognizes that division of trusts may be beneficial and, in certain circumstances, almost routine. For example, a division of trusts is often necessitated by a desire to obtain maximum advantage of exemptions available under the federal generation-skipping tax.

Subsection (b) authorizes a court to divide a trust, whether or not the trusts which result are identical. Conflicts among beneficiaries, including differing investment objectives, may often dictate such a division. A division under this section does not require the consent of the beneficiaries.

For a list of statutes authorizing division of trusts, either by the trustee or court order, see Restatement Third, Property (Donative Transfers), Sec. 12.2 Statutory Note (Tent. Draft No.1, 1995).

### **PART 3. SPENDTHRIFT PROTECTION**

#### **Section**

**2-301. Spendthrift Protection Recognized.**

- 2-302.        **Exceptions to Spendthrift Protection.**  
2-303.        **Discretionary Trusts and Trusts Subject to Standard.**  
2-304.        **Self-Settled Trusts.**

**SECTION 2-301. SPENDTHRIFT PROTECTION RECOGNIZED.**

(a) A settlor may provide in the terms of the trust that the interest of a beneficiary in the income or principal may not be voluntarily or involuntarily transferred.

(b) Except as otherwise provided in Section 2-302, if the terms of the trust provide that a beneficiary's interest in the income or principal is not subject to voluntary or involuntary transfer, the beneficiary's interest may not be transferred and is not subject to enforcement of a money judgment until paid to the beneficiary.

[(c) A disclaimer by a beneficiary of all or part of that beneficiary's interest is not a transfer under this section.]

**Comment.**

Source: CPC Section 15300-15302, 15309; Tex. Prop. Code Ann. Sec. 112.035.

Under this section, a settlor has the power to restrain transfer of the beneficiary's interest, regardless of the nature of the interest. A restraint may be placed on an interest in the income, the principal, or both. A creditor of the beneficiary is prohibited from attaching a protected interest until paid to the beneficiary unless one of the exceptions under Section 2-302 applies. This section is similar to Restatement (Second) of Trusts Sections 152-153.

A voluntary assignment by a beneficiary as to periodic payments otherwise due the beneficiary may be honored by a trustee but is revocable by the beneficiary at anytime.

Subsection (c) is drawn from Wisconsin law. See Wis. Stat. Ann. Sec. 701.06(3) (West 1981). It is placed in brackets because the enacting jurisdiction may already address this issue in its disclaimer statute.

**SECTION 2-302. EXCEPTIONS TO SPENDTHRIFT PROTECTION. A**

term of a trust prohibiting an involuntary transfer of a

beneficiary's interest shall be invalid as against claims by:

(1) a spouse or child of the beneficiary for support, or a spouse for alimony;

(2) a provider of necessary services rendered or necessary supplies furnished to the beneficiary;

(3) a tort creditor of the beneficiary;

(4) any creditor of the beneficiary if the beneficiary is the settlor;

(5) following an event terminating or partially terminating the trust, any creditor of the beneficiary as to a distribution to be made upon that event.

#### **Comment.**

Source: CPC Section 15301-15302, 15304-15305; O.C.G.A. Sec. 53-12-28; Restatement (Second) of Trusts Sec. 153, 157.

This section states some of the important exceptions to spendthrift protection. The section is not exclusive. For example, the extent to which a spendthrift provision may bar claims by state and local governments, particularly claims for services provided to individuals with disabilities, is a matter left to the enacting jurisdiction to decide. Additional exceptions are also created by federal law, such as claims for unpaid taxes.

The fact that a creditor is not subject to a spendthrift bar does not mean that the creditor may collect the debt from the trust. The nature of the beneficiary's interest must also be considered. See Section 2-303.

Paragraph (1) provides that a spendthrift provision is invalid as to claims of a beneficiary's spouse or child for support, or a spouse for alimony. The provision extends to support and alimony ordered by the court, as well as to claims for support by a child or spouse during the marriage. The Act does not attempt to prescribe the procedures whereby a spouse or child may collect from the trust, leaving that matter to local collection law. For an example of such a procedure, see Cal. Prob. Code Sec. 15305.

Paragraph (3), relating to claims of tort creditors, is drawn from the Georgia statute. See O.G.C.A. Sec. 53-12-28. This exception is not found in the Restatement or in most state statutes. However, commentators have long recommended the creation of such an exception. See, e.g., George Bogert, Trusts

and Trustees Sec. 224, at 478-79 (Rev. 2d ed. 1992); Erwin N. Griswold, Spendthrift Trusts Sec. 365, at 442-44 (2d ed. 1947); Austin W. Scott & William F. Fratcher, 2A The Law of Trusts Sec. 157.5, at 220 (4th ed. 1987).

Paragraph (4) provides that a spendthrift provision is ineffective against a creditor of the settlor. For the amount such a creditor may collect from the trust, see Section 2-304. This paragraph is the same in substance as Section 156(1) of the Restatement (Second) of Trusts (1959). This section does not supersede other laws which provide spendthrift protection to pension trusts and other employee plans. See Section 1-102(17) ("trust" defined to exclude a trust for the primary purpose of paying pensions).

Paragraph (5) is based on Restatement (Second) of Trusts Section 153 but with an important modification. Under Section 153, a spendthrift provision is invalid to the extent a beneficiary is entitled to an immediate transfer of the principal of the trust. Under Section 152, however, a creditor may not reach a distribution of income until paid to the beneficiary. The reason behind the Restatement's separate treatment of income and principal was to prevent a creditor from reaching periodic distributions while allowing a creditor to reach the assets following termination of the trust and before their payment to the beneficiary. Modern portfolio theory, as articulated by the Uniform Prudent Investor Act, recognizes that the distinction between income and principal is often artificial. Paragraph (5) strives to achieve the original purpose of the Restatement without relying on this often artificial distinction. Consequently, following an event terminating or partially terminating the trust, Paragraph (5) allows the creditor to secure an order compelling payment from the terminated assets, whether they consist of principal or accumulated income.

**SECTION 2-303. DISCRETIONARY TRUSTS AND TRUSTS SUBJECT TO STANDARD.** Except as otherwise provided in this section, if the terms of the trust provide that the trustee shall pay to or for the benefit of a beneficiary income or principal of the trust subject to a standard or in the discretion of the trustee, a transferee or creditor of the beneficiary may not compel a distribution from the trust, whether or not the trustee has abused the discretion or complied with the standard. To the extent the trustee has abused the discretion or has not complied with the standard, a distribution may be compelled only by a



spouse or child who has a claim for support or alimony from the beneficiary, a provider of necessary services rendered or necessary supplies furnished to the beneficiary, or a tort creditor of the beneficiary.

**Comment.**

Source: CPC 15303.

This section is based on but is broader than Section 155 of the Restatement (Second) of Trusts, which applies only to trusts over which the trustee has "uncontrolled discretion." Under this section, a beneficiary's creditor cannot compel the trustee of a discretionary trust or a trust subject to a standard to pay any part of the trust to the creditor, even though the beneficiary could compel the payment. The creditor may be able to reach any payment the trustee decides to make, however.

Under Section 4-214, a trustee must exercise a discretionary power reasonably regardless of the breadth of discretion provided by the terms of the trust.

**SECTION 2-304. SELF-SETTLED TRUSTS.** If a settlor is a beneficiary of a trust created by the settlor, a transferee or creditor of the settlor may reach the maximum amount that the trustee could pay to or for the settlor's benefit. In the case of a trust with multiple settlors, the amount the creditor or transferee of a particular settlor may reach may not exceed the portion of the trust attributable to that settlor's contribution.

**Comment.**

Source: CPC Section 15304(b).

This section is drawn from Section 156(2) of the Restatement (Second) of Trusts (1959). See also the comments to Restatement Section 156. For the rights of creditors if the settlor has retained a power of revocation, see Section 3-105. For the definition of "settlor", see Section 1-102(14).

**ARTICLE 3.**  
**PROVISIONS RELATING TO REVOCABLE TRUSTS**

**Section**

- 3-101.      **Capacity to Create Revocable Trust.**
- 3-102.      **Revocation or Modification.**
- 3-103.      **Other Rights of Settlor.**
- 3-104.      **Rights of Holder of Power of Appointment.**
- 3-105.      **Creditor's Rights Against Revocable Trust.**
- 3-106.      **Contest of Revocable Trusts.**

**SECTION 3-101. CAPACITY TO CREATE REVOCABLE TRUST.**    An individual has capacity to create a revocable trust to the same extent the individual has capacity to make a will.

**Comment.**

The purpose of this section, which is patterned after Restatement (Third) of Trusts Sec. 11 (Tent. Draft No. 1, 1996), is to provide some clarification to what has become a major issue in the law of trusts due to the recent and widespread use of the revocable trust as an alternative to a will.

This section recognizes that the revocable trust is used primarily as a will substitute, with its key provision being the determination of the persons to receive the trust property upon the settlor's death. To solidify the use of the revocable trust as a device for transferring property at death, the settlor usually also executes a pourover will under which property not transferred to the trust during life will be consolidated with the trust property following the settlor's death. Given this primary use of the revocable trust as a device for disposing of property at death, the capacity standard for wills, and not for lifetime gifts, should apply. Should lifetime management issues arise, they may be dealt with by reformation or other appropriate remedies that will not jeopardize the overall plan of disposition by making the standard for the trust different or higher than that for making a will. Restatement (Third) of Trusts Sec. 11 comm. b (Tent. Draft, 1996).

**SECTION 3-102. REVOCATION OR MODIFICATION.**

(a) Unless the terms of the trust expressly provide that a trust is irrevocable, the settlor may revoke or modify the trust.

(b) Except as otherwise provided by the terms of the trust, if a trust is created or funded by more than one settlor, each settlor may revoke or modify the trust as to the portion of the trust contributed by that settlor .

**[ALTERNATIVE PROVISION FOR COMMUNITY PROPERTY STATES]**

[(b) Except as otherwise provided by the terms of the trust, if a trust is created or funded by more than one settlor:

(1) to the extent the trust consists of community property, the trust may be revoked or modified by either spouse acting alone;

(2) to the extent the trust consists of other property, each settlor may revoke or modify the trust as to the portion of the trust contributed by that settlor.]

(c) A trust that is revocable by the settlor may be revoked or modified:

(1) by compliance with any method specified by the terms of the trust; or

(2) unless the terms of the trust expressly make the method specified exclusive, (i) by a writing, other than a will, signed by the settlor and delivered to the trustee during the settlor's lifetime, or (ii) by a will expressly referring to the trust or which revokes the trust by necessary implication.

(d) Upon termination of a revocable trust, the trustee must distribute the trust property as the settlor directs.

(e) The settlor's powers with respect to revocation or modification may be exercised by an agent under a power of attorney only and to the extent the power of attorney expressly so authorizes.

(f) A conservator may revoke or modify a trust to the extent authorized by other applicable law unless prohibited or otherwise

restricted by the terms of the trust.

#### **Comment.**

Source: CPC 15400-15402, 15410(a).

Subsection (a), which provides that a settlor may revoke or modify a trust unless the terms of the trust expressly state that the trust is irrevocable, is contrary to the common law. See Restatement (Second) of Trusts Sec. 330 (1959). This subsection will not govern certain trusts created in other states. Choice of law principles may dictate that the law of a state following the common law rule is to govern, in which event the trust would be irrevocable unless expressly made revocable. In addition, this subsection does not prevent a trust from being reformed to make it irrevocable if the settlor was proceeding under a mistake of law at the time of its creation. See Section 6-204 (reformation of trust).

A power of revocation includes the power to modify. See Restatement (Second) of Trusts Section 331, comment g (1959). An unrestricted power to modify may also include the power to revoke a trust. See Restatement (Second) of Trusts Section 331, comment h.

Subsection (b) provides a default rule for revocation or modification of a trust with multiple settlors. An individual settlor of such a trust may only revoke or modify the portion of the trust attributable to that settlor's contribution. The effect of this provision is to overrule cases such as Estate of Wernicke, 20 Cal. Rptr. 2d 481 (1st Dist. 1993), which hold that a trust with multiple settlors may be revoked or modified only by action of all of the settlors. However, good estate planning practice dictates that this topic should usually be specifically addressed in the instrument. For the definition of "settlor", see Section 1-102(14)

Under subsection (c), the settlor may revoke a revocable trust by a writing delivered to the trustee or by a will even if the terms of the trust specify a method of revocation. Only if the method specified by the terms of the trust is exclusive are use of the other methods prohibited.

Subsection (c) does not necessarily preclude revocation by other methods, such as by oral statement or by physical act coupled with a withdrawal of the property. Less formal methods, because they provide less reliable indicia of intent, are not to be encouraged, however. Nor does subsection (c) require the trustee to concur in a modification of the trust. Should a modification of the trust substantially change the trustee's duties, the trustee is free to resign. See Section 4-106(a)(4).

Subsection (d), dealing with distribution of trust property upon revocation, codifies a provision commonly included in revocable trust instruments.

Under subsection (e), an agent under a power of attorney may revoke a revocable trust but only to the extent the power of attorney expressly so permits.

This section defers to other law on whether a conservator may exercise a power of revocation. Many states allow for such revocation with prior court approval. See, e.g., Unif. Prob. Code Sec. 5-407. The effect of subsection (f) is to clarify that such a revocation may be prohibited by the terms of the trust.

The settlor's power to revoke under this section does not preclude termination of the trust under another section.

**SECTION 3-103. OTHER RIGHTS OF SETTLOR.** Except to the extent the terms of the trust otherwise provide, while a trust is revocable and the individual holding the power to revoke the trust has capacity:

(1) the holder of the power, and not the beneficiary, has the rights afforded beneficiaries under this [Act];

(2) the duties of the trustee are owed to the holder of the power;

(3) if the consent of a beneficiary is required before an action may be taken, the holder of the power, and not the beneficiary, has the power to consent or withhold consent;

(4) a notice otherwise required to be given to a beneficiary must be given to the holder of the power and not to the beneficiary; and

(5) the trustee shall follow a written direction given by the holder of the power to revoke or the part thereof with respect to which the direction is given, including a person to whom the power is delegated, without liability for so doing.

#### **Comment**

Source: CPC Section 15800-15802, 16001.

This section has the effect of postponing the enjoyment of rights of beneficiaries of revocable trusts until the death or incapacity of the settlor or other person holding the power to revoke the trust. See also Section 3-104 (holder of presently

exercisable general power of appointment treated as settlor). This section thus recognizes that the holder of a power of revocation is in control of the trust and should have the rights to enforce the trust. A corollary principle, also recognized in this section, is that the holder of the power to revoke may direct the actions of the trustee.

Under this section, the duty to inform and account to beneficiaries is owed to the person holding the power to revoke during the time that the trust is presently revocable and the holder of the power has capacity. See Section 4-213 (trustee's duty to inform and account to beneficiaries). The introductory clause recognizes that the terms of the trust may grant rights to the beneficiaries which, under this section, would otherwise be held by the holder of the power to revoke.

Paragraph (3) recognizes the principle that the consent of a beneficiary of a revocable trust should not have any effect during the time that the trust is presently revocable, because the power over the trust is held by the settlor or other person holding the power to revoke.

Paragraph (4) recognizes that notice to the beneficiary of a revocable trust would be an idle act in the case of a revocable trust because the beneficiary is powerless to act.

Paragraph (5) requires the trustee to comply with a written direction of the holder of a power to revoke. A trustee who wishes not to comply may choose to resign. See Section 4-106(a)(4) (resignation of trustee).

This section no longer applies should the holder of the power to revoke lose capacity. In that event, the beneficiaries are granted all rights normally afforded the beneficiaries of irrevocable trusts, subject to a possible right of a conservator or agent to revoke or modify the trust. See Section 3-102(e)-(f).

See also Sections 6-205 and 6-302, which authorize the holder of the power to revoke to represent and bind the beneficiaries to judicial orders and nonjudicial settlements.

#### **SECTION 3-104. RIGHTS OF HOLDER OF POWER OF APPOINTMENT.**

The holder of a presently exercisable general power of appointment over a trust has the rights of a holder of the power to revoke a trust under Section 3-103 to the extent of the holder's power over the trust property.

#### **Comment.**

Source: CPC Section 15803.

This section makes clear that a holder of a presently

exercisable general power of appointment is treated as a settlor for purposes of Section 3-103 due to the holder's equivalent position to control the trust as it relates to the property covered by the power. See also Sections 6-205 and 6-302, which authorize the holder of a presently exercisable general power of appointment to represent and bind the beneficiaries to judicial orders and nonjudicial settlements.

#### **SECTION 3-105. CREDITOR'S RIGHTS AGAINST REVOCABLE TRUST.**

(a) During the lifetime of the settlor, the trust property of a revocable trust is subject to the claims of the settlor's creditors to the extent of the settlor's power of revocation.

(b) Following the death of a settlor, the trust property of a revocable trust which was subject to the settlor's power of revocation at the time of death is subject to the claims of the settlor's creditors and costs of administration of the settlor's estate to the extent the settlor's estate is inadequate to satisfy those claims and costs.

#### **Comment.**

Source: CPC Sections 18200, 19001.

Subsection (a) is contrary to the common law rule as expressed in the Restatement. See Restatement (Second) of Trusts Section 330, comm. o (1959). But because a settlor usually also retains a beneficial interest which a creditor may reach, the common law rule is normally of little significance. See Section 2-304 (rights of creditor in self-settled trust); and Restatement (Second) of Trusts Section 156(2) (1959).

Subsection (b) recognizes that a revocable trust is normally used as a will substitute. As such, its assets, following the death of the settlor, should be subject to the settlor's debts. However, to promote efficiency in the settlement of the settlor's estate, subsection (b) requires that the assets of the settlor's probate estate be exhausted before the creditors may reach the assets of the revocable trust.

#### **SECTION 3-106. LIMITATION ON CONTEST OF REVOCABLE TRUST.**

(a) Unless previously barred by adjudication, consent, or other limitation, a proceeding to contest the validity of a

revocable trust must be brought no later than three years following the death of the settlor.

(b) Unless a proceeding contesting its validity is pending, six months following the death of the settlor, the trustee of a revocable trust may assume the trust's validity and proceed to distribute the trust property in accordance with the terms of the trust without liability for so doing, liability for an improper distribution in such case being solely on the beneficiaries.

#### **Comment.**

The purpose of this section is to provide some finality to when a contest of a revocable trust may be brought and to encourage the expeditious distribution of the trust property following the death of the settlor. Subsection (a), which requires that a contest be brought no later than three years following the death of the settlor, is consistent with the Uniform Probate Code, which places a three-year limit on the probate or contest of a will if not barred earlier. Subsection (b) is also consistent with the Uniform Probate Code, which discharges a personal representative six months following the filing of a statement of informal closing, even though the beneficiaries may still be liable for improper distribution. Subsection (b) only protects a trustee from personal liability. Should a successful contest later be brought, the contestants may reach any trust property still in the trustee's possession.

### **ARTICLE 4. TRUST ADMINISTRATION**

#### **Part**

- 1. Office of Trustee.**
- 2. Duties of Trustee.**
- 3. Uniform Prudent Investor Act.**
- 4. Powers of Trustee.**
- 5. Liability of Trustee to Beneficiaries.**
- 6. Rights of Third Persons.**

#### **PART 1. OFFICE OF TRUSTEE**

#### **Section**

- 4-101. Acceptance or Rejection of Trust by Trustee.**
- 4-102. Trustee's Bond.**



- 4-103.      **Actions by Cotrustees.**
- 4-104.      **Vacancy in Office of Trustee.**
- 4-105.      **Filling Vacancy.**
- 4-106.      **Resignation of Trustee.**
- 4-107.      **Removal of Trustee.**
- 4-108.      **Delivery of Property by Removed or Resigning Trustee.**
- 4-109.      **Compensation of Trustee.**
- 4-110.      **Notice of Increase in Trustee's Compensation.**
- 4-111.      **Repayment for Expenditures.**

**SECTION 4-101.   ACCEPTANCE OR REJECTION OF TRUST BY TRUSTEE.**

(a) A person named as trustee accepts the office of trustee by:

    (1) signing the trust instrument, or signing a separate written acceptance; or

    (2) except as provided in subsection (c), knowingly accepting delivery of the trust property or exercising powers or performing duties as trustee.

(b) A person named as trustee who has not yet accepted the office of trustee may in writing reject the trust.

(c) If there is an immediate risk of damage to the trust property, the person named as trustee may act to preserve the trust property without accepting the office of trustee, if within a reasonable time after acting the person delivers a written rejection of the trust to the settlor or, if the settlor is dead or lacks capacity, to a beneficiary.

**Comment.**

Source: CPC Sections 15600, 15601; Ind. Code Ann. Sec. 30-4-2-2 (West 1979).

This section, while listing the preferred methods of acceptance, is not exclusive. This section does not preclude oral acceptance, or an acceptance by estoppel or damages for an unreasonable delay in signifying a decision as to an acceptance or rejection.

The provision in subsection (a)(2) for acceptance of the trust by acts of the person named as trustee is consistent with case law. See, e.g., *Heitman v. Cutting*, 174 P. 675 (Cal. App. 1918).

The appropriate recipient of the written rejection depends upon the circumstances of the particular case. Ordinarily, it would be appropriate to give the rejection to the person who informs the person of the proposed trusteeship. If proceedings involving the trust are pending, the rejection could be filed with the court clerk. In the case of a person named as trustee of a revocable trust, it would be appropriate to give the rejection to the settlor. In any event it would be best to give notice of rejection to a beneficiary with a present interest in the trust because the beneficiary would be motivated to seek appointment of a new trustee.

A trustee's rejection of a trust normally precludes a later acceptance of the trust but does not cause the trust to fail. See Restatement (Second) of Trusts Section 102. As to filling vacancies, see Section 4-105.

Subsection (c) makes clear that the authority to act in an emergency does not impose a duty to act. Under this subsection, the person named as trustee may act in an emergency without being considered to have accepted the trust under the rule set out in subsection (a)(2).

#### **SECTION 4-102. TRUSTEE'S BOND.**

(a) A trustee is not required to give a bond to secure performance of the trustee's duties unless:

- (1) a bond is required by the terms of the trust; or
- (2) a bond is found by the Court to be necessary to protect the interests of beneficiaries, whether or not bond is waived by the terms of the trust.

(b) If a bond is required, it must be filed and in an amount and with sureties and liabilities as the Court may order. The Court may excuse a requirement of a bond, reduce or increase the amount of a bond, release a surety, or permit the substitution of another bond with the same or different sureties.

(c) The amount of a bond otherwise required may be reduced

by the value of trust property deposited with a financial institution in a manner that prevents its unauthorized disposition, and by the value of real property which the trustee, by express limitation of power, lacks power to convey without Court authorization.

(d) Except as otherwise provided by the terms of trust or ordered by the Court, the cost of a bond is charged to the trust.

(e) A trust company may not be required to give a bond, whether or not the terms of the trust require a bond.

#### **Comment.**

Source: CPC Section 15602.

Subsections (a)-(b) of this section are drawn from Section 7-304, and subsection (c) is drawn from Sections 3-604 and 5-410 of the Uniform Probate Code. See also Sections 4-104 (vacancy in office of trustee), 4-105 (appointment of trustee to fill vacancy). Because a bond is required only if the terms of the trust require bond or a bond is found by the court to be necessary to protect the interests of beneficiaries, bond will rarely be required under the Act.

Subsection (e) clarifies that a trust company is not required to give a bond. See Section 1-102(18) ("trust company" defined). A nonprofit or charitable corporation acting as trustee under a charitable trust is not, in the absence of special enabling legislation, a trust company as defined in the Act, and thus is subject to the provisions of subsection (a) relating to when a bond is required.

**SECTION 4-103. ACTIONS BY COTRUSTEES.** Except as otherwise provided by the terms of the trust:

(1) a power held by cotrustees may be exercised by majority action;

(2) if a vacancy occurs in the office of a cotrustee, the remaining cotrustees may act for the trust as if they are the only trustees;

(3) if a cotrustee is unavailable to perform duties because

of absence, illness, or other temporary incapacity, the remaining cotrustees may act for the trust, as if they were the only trustees, if necessary to accomplish the purposes of the trust or to avoid irreparable injury to the trust property.

**Comment.**

Source: CPC 15621, 15622.

Paragraph (1) is in accordance with Restatement (Second) of Trusts Section 383, which allows action by a majority in the case of charitable trusts.

Under paragraph (2), a vacancy in the office of a cotrustee is disregarded in the operation of the trust if there is at least one trustee remaining. In determining the requisite majority, only a majority of the remaining trustees need be counted, even though the number of trustees constituting a majority is now less than before the vacancy occurred. This rule is subject to contrary provision in the terms of the trust, as noted in the introductory clause. See also Sections 4-104 (vacancy in office of trustee), 4-105 (appointment of trustee to fill vacancy).

Paragraph (3) addresses a problem that may arise when a cotrustee is temporarily unable to perform duties but the office of trustee is not vacant.

Per Section 4-602, a dissenting trustee is not liable to a third party for failing to join in the majority's exercise of a power. However, should the action by the majority constitute a breach of trust, the dissenting trustee may be held liable for failing to take action to rectify the acts of the cotrustees. See Section 4-208 (trustee's duties with regard to cotrustees).

**SECTION 4-104. VACANCY IN OFFICE OF TRUSTEE.** There is a vacancy in the office of trustee if:

- (1) the person named as trustee rejects the trust;
- (2) the person named as trustee cannot be identified or does not exist;
- (3) the trustee resigns or is removed;
- (4) the trustee dies; or
- (5) a guardian or conservator of the trustee's person or estate is appointed.

**Comment.**

Source: CPC Section 15643.

This section lists the typical ways in which the office of trustee becomes vacant. It does not preclude other methods, such as the suspension of the powers of a trust company under federal or state banking regulations. For the rules on filling a vacancy, see Section 4-105. See also Section 1-102(18) ("trust company" defined), 4-101 (rejection of trust), 4-106 (resignation and liability of resigning trustee), 4-107 (removal of trustee), 4-603 (protection of third person dealing with former trustee).

#### **SECTION 4-105. FILLING VACANCY.**

(a) A trustee must be appointed to fill a vacancy in the office of trustee only if the trust has no trustee or the terms of the trust require a vacancy in the office of cotrustee to be filled.

(b) A vacancy in the office of trustee shall be filled:

(1) By the person named in or nominated pursuant to the method specified by the terms of the trust;

(2) If the terms of the trust do not name a person or specify a method for filling the vacancy, or the person named or nominated pursuant to the method specified fails to accept;

(i) By a trust company designated on agreement of the adult beneficiaries specified in subsection (c); or

(ii) By a person appointed by the Court on petition of an interested person or of a person named as trustee by the terms of the trust. The Court, in selecting a trustee, shall consider any nomination made by the adult beneficiaries.

(c) For purposes of this section, the term "adult beneficiaries" shall not include (i) beneficiaries lacking capacity who are not represented by a guardian, conservator, or agent; and (ii) beneficiaries who are not entitled or eligible to

receive trust income or a distribution of principal were the trust to terminate at the time the agreement is made.

**Comment.**

Source: CPC Section 15660.

For a listing of the circumstances when a vacancy in the office of trustee may occur, see Section 4-104. Subsection (a) clarifies that a vacancy in the office of a cotrustee need be filled only if the trust so requires. If the vacancy in the office of cotrustee is left open, the remaining cotrustees may continue to administer the trust under Section 4-103, unless the terms of the trust provide otherwise.

Subsection (b) (2) (i) permits a vacancy in the office of trustee to be filled, without the need for court approval, by a trust company selected by agreement of the adult beneficiaries as defined in subsection (c). The adult beneficiaries who must agree to the new trustee are the same as those who must consent to a resignation under Section 4-106(a) (3). A trust company may be appointed to fill a vacancy whether or not the former trustee was a trust company. If a trustee resigns pursuant to Section 4-106(a) (3), the trust may be transferred to a trust company pursuant to this section, all without court approval.

Subsection (b) (2) (ii) authorizes the court to fill a vacancy if the trust does not name a successor who is willing to accept the trust or the trust does not provide another method of appointment. Requiring the court to give consideration to the wishes of the beneficiaries is consistent with Restatement (Second) of Trusts Section 108, comments d, i (1959).

For a limitation on the rights of certain beneficiaries of revocable trusts, see Section 3-103. As to obligations of successor trustees, see Section 4-212.

**SECTION 4-106. RESIGNATION OF TRUSTEE.**

(a) A trustee who has accepted a trust may resign by any of the following methods:

(1) as provided by the terms of the trust;

(2) with the consent of the person holding the power to revoke the trust if the holder has capacity or is represented by a guardian, conservator, or agent;

(3) with the consent of the adult beneficiaries as defined in Section 4-105(c) if the trust is irrevocable or the

holder of the power to revoke lacks capacity or is not represented by a guardian, conservator, or agent;

(4) upon written notice to the holder of the power to revoke if the holder substantially changes the trustee's duties and the trustee does not concur; or

(5) 90 days following the filing by the trustee of a petition to resign under Section 6-202 or upon approval of the petition by the Court, whichever first occurs. The Court must accept the trustee's resignation but may impose such orders and conditions as are reasonably necessary for the protection of the trust property, including the appointment of a receiver or temporary trustee.

(b) The liability for acts or omissions of a resigning trustee or of any sureties on the trustee's bond is not released or affected by the trustee's resignation.

#### **Comment.**

Source: CPC Section 15640, 15641.

This section is based in part on Section 106 of the Restatement (Second) of Trusts (1959), except that under subsection (a)(3) the class of persons whose consent is needed is more limited and the Restatement section does not address revocable trusts. Under this section, court approval is not required to accomplish a resignation except under subsection (a)(5). Whether court approval is required under subsection (a)(1) depends on the terms of the trust. Subsection (a)(2) is a provision that recognizes that the person holding the power to revoke a revocable trust, and not the beneficiaries, has control over the trust. See Section 3-103. Under subsection (a)(5) the court has authority to accept a resignation regardless of whether the trust provides a manner of resignation.

Section 4-213 requires an accounting whenever there is a change of trustees. See also Restatement (Second) of Trusts Section 106, comment a, which is in accord with subsection (b).

#### **SECTION 4-107. REMOVAL OF TRUSTEE.**

(a) A trustee may be removed in accordance with the terms of the trust, by the Court on its own motion or on petition of a settlor, cotrustee, or beneficiary under Section 6-202.

(b) The Court may remove a trustee, or order other appropriate relief:

(1) if the trustee has committed a material breach of the trust;

(2) if the trustee is or becomes insolvent or otherwise unfit to administer the trust;

(3) if hostility or lack of cooperation among cotrustees impairs the administration of the trust;

(4) if the trustee fails or declines to act;

(5) if the trustee's compensation is excessive under the circumstances;

(6) for other good cause shown.

(c) If it appears to the Court that trust property or the interests of a beneficiary may suffer loss or injury pending a final decision on a petition for removal of a trustee, the Court may suspend the powers of the trustee, compel the trustee to surrender trust property to a cotrustee, receiver or temporary trustee, or order other appropriate relief.

**Comment.**

Source: CPC Section 15642.

Subsection (a) of this section is the same in substance as Section 107 of the Restatement (Second) of Trusts (1959) except that it gives the settlor of an irrevocable trust the right to petition for removal of a trustee. As to rights of a settlor of a revocable trust, see Sections 3-102 (revocation or modification), 3-103 (other rights of settlor). The right to petition for removal of a trustee does not give the settlor any other rights,



such as the right to an account or to receive information concerning administration of the trust.

The statement of grounds for removal of the trustee by the court is drawn from the Texas Trust Code and the Restatement. See Tex. Prop. Code Ann. Sec. 113.082(a) (Vernon 1984); Restatement (Second) of Trusts Section 107, comments b-d (1959). If a trustee is removed, another may be appointed to fill the vacancy as provided in Section 4-105.

The section does not attempt to catalog every conceivable ground for removal. Subsection (a)(6) instead permits the court to remove a trustee whenever there is good cause. Friction between a trustee and beneficiaries which interferes with the proper administration of the trust, indifference on the part of the trustee, or mediocre service or investment performance may all justify removal if in the best interests of the beneficiaries and not inconsistent with the purposes of the trust.

#### **SECTION 4-108. DELIVERY OF PROPERTY BY FORMER TRUSTEE.**

Unless a cotrustee remains in office, a former trustee, or if the trustee's appointment terminated because of death or disability, the former trustee's personal representative or guardian or conservator, is responsible for and has the powers necessary to protect the trust property and other powers essential to the trust's administration until the property is delivered to a successor trustee or a person appointed by the Court to receive the property.

#### **Comment.**

Source: CPC Section 15644; UPC Section 3-609.

This section clarifies that a trustee who has resigned or is removed has the powers needed to complete the trustee's remaining duties. Following the lead of the Uniform Probate Code, this section also imposes a similar obligation on the personal representative or guardian or conservator of a deceased or incapacitated trustee. However, the obligation to carry out residual duties of the former trustee applies only if no trustee remains in office. Whether or not a trustee remains in office, the former trustee remains liable for actions or omissions during the trustee's term of office until liability is barred.

Section 4-213 requires an accounting whenever there is a change of trustees. Section 4-603 protects third persons who deal in good faith with a former trustee without knowledge that the person is no longer a trustee. See also Sections 4-104 (vacancy

in office of trustee), and 4-502(4) (appointment of receiver or temporary trustee upon breach of trust).

#### **SECTION 4-109. COMPENSATION OF TRUSTEE.**

(a) If the terms of the trust do not specify the trustee's compensation, the trustee is entitled to compensation that is reasonable under the circumstances.

(b) If the terms of the trust specify the trustee's compensation, the trustee is entitled to be compensated as so provided, except that upon proper showing, the Court may allow more or less compensation:

(1) if the duties of the trustee are substantially different from those contemplated when the trust was created;

(2) if the compensation specified by the terms of the trust would be inequitable or unreasonably low or high; or

(3) in extraordinary circumstances calling for equitable relief.

(c) Unless the terms of the trust otherwise provide or all of the trustees otherwise agree, in the case of a trust with cotrustees, compensation must be apportioned among the cotrustees according to the value of the services rendered by each.

(d) In determining compensation, the Court may fix an amount to continue as long as the Court continues proper.

#### **Comment.**

Source: CPC Section 15680-15683.

Subsection (a) establishes a standard of reasonable compensation. For a list of factors relevant in determining reasonable compensation, see Restatement (Second) of Trusts Section 242 (1959). In setting compensation, the services actually performed and responsibilities assumed by the trustee should be closely examined. For example, an adjustment in

compensation may be appropriate if the trustee has delegated significant duties.

Subsection (b) permits the reasonable compensation standard to be overridden or clarified by the terms of the trust, subject to the court's inherent equity power to make adjustments downward or upward in appropriate circumstances.

Subsection (c) addresses apportionment of compensation between cotrustees. It is not intended to allow a double fee. Nor is an allocation based on time expended necessarily appropriate. Rather, compensation is to be apportioned among the cotrustees based on the value of the services rendered by each. Under this subsection, a cotrustee may be denied compensation if its services did not contribute to the administration of the trust.

Subsection (d) clarifies that the court may fix compensation prospectively.

Section 4-402(22) grants the trustee authority to fix and pay its compensation without the necessity of prior court review, but without precluding the right of a beneficiary to object to the compensation in a later proceeding.

**SECTION 4-110. NOTICE OF INCREASE IN TRUSTEE'S COMPENSATION.** Except as otherwise provided by the terms of the trust or unless all beneficiaries entitled to an account under Section 4-213(d) consent in writing:

(1) A trustee may increase its rate of compensation for administration of a trust only following the giving of at least 60 days' written notice of the increase to each beneficiary entitled to an account;

(2) If a beneficiary files a petition for review of an increase in the trustee's rate of compensation or for removal of the trustee and serves a copy of the petition on the trustee within the 60-day period, the increase does not take effect until ordered by the Court or the petition is dismissed. Failure of a beneficiary to file a petition for review does not preclude a beneficiary from objecting to the increase in a later proceeding.

**Comment.**

Source: CPC Section 15686.

See also Section 4-213(b) (duty of trustee to inform beneficiaries in advance of certain proposed sales).

**SECTION 4-111. REPAYMENT FOR EXPENDITURES.** A trustee is entitled to be repaid out of the trust property, with interest as appropriate, for:

(1) expenditures that were properly incurred in the administration of the trust; and

(2) to the extent that they benefitted the trust, expenditures that were not properly incurred in the administration of the trust.

**Comment.**

Source: CPC Section 15684.

A trustee has the authority to expend trust funds as necessary in the administration of the trust, including expenses incurred in the hiring of agents. See Sections 4-402(22) (trustee to pay expenses of administration from trust), and 4-402(26) (trustee may hire agents). Paragraph (1) clarifies that a trustee is entitled to reimbursement from the trust for incurring expenses within the trustee's authority. But a trustee is ordinarily not entitled to reimbursement for incurring unauthorized expenses. Such expenses are normally the personal responsibility of the trustee. Only if the unauthorized expenditures benefitted the trust, as provided in paragraph (2), is the trustee entitled to reimbursement. The purpose of paragraph (2), which is derived from Restatement (Second) of Trusts Section 245, is not to ratify the unauthorized conduct of the trustee, but to prevent the unjust enrichment of the trust. Given this purpose, a court, on grounds of equity, may delay or even deny reimbursement for expenses which benefitted the trust. For a list of factors which the court may wish to take into account in making this determination, see Restatement (Second) of Trusts Section 245 comm. g (1959).

Reimbursement under this section may include attorney's fees and expenses incurred by the trustee in defending an action. However, unless the court otherwise orders as provided in paragraph (2), a trustee is not entitled to attorney's fees and expenses if it is determined that the trustee breached the trust. See, e.g., *Estate of Gilmaker*, 38 Cal. Rptr. 270 (Ct. App. 1964); *Estate of Vokal*, 263 P.2d 64 (Cal. App. 1953).

## **PART 2.**

### **FIDUCIARY DUTIES OF TRUSTEE**

#### **Section**

- 4-201. Duty to Administer Trust; Alteration by Terms of Trust.**
- 4-202. Duty of Loyalty; Impartiality; Confidential Relationship.**
- 4-203. Standard of Prudence.**
- 4-204. Costs of Administration.**
- 4-205. Special Skills.**
- 4-206. Delegation.**
- 4-207. Directory Powers.**
- 4-208. Cotrustees.**
- 4-209. Control and Preservation of Trust Property.**
- 4-210. Separation and Identification of Trust Property.**
- 4-211. Enforcement and Defense of Claims and Actions.**
- 4-212. Predecessor Fiduciaries.**
- 4-213. Duty to Inform and Account.**
- 4-214. Duties with Regard to Discretionary Powers.**

#### **SECTION 4-201. DUTY TO ADMINISTER TRUST; ALTERATION BY TERMS OF TRUST.**

(a) On acceptance of a trust, the trustee shall administer the trust according to the terms of the trust and, except to the extent the terms of the trust provide otherwise, according to this [Act].

(b) The terms of the may expand, restrict, eliminate, or otherwise alter the duties prescribed by this [Part], and the trustee may reasonably rely on those terms, but nothing in this [Act] authorizes a trustee to act in bad faith or in disregard of the purposes of the trust or the interest of the beneficiaries.

#### **Comment.**

Source: CPC Section 16000.

Subsection (a) is drawn in part from Sections 164 and 169 of the Restatement (Second) of Trusts (1959). See also Sections 4-101 (acceptance of trust by trustee), 3-103 (duties owed to persons holding power to revoke), 3-104 (duties owed to persons with presently exercisable general power of appointment), 4-203

(trustee's standard of prudence in performing duties). For provisions permitting the beneficiaries to relieve the trustee from liability, see Section 4-506.

Subsection (b) clarifies that the trustee's duties prescribed by this Part may be altered by the terms of the trust. However, a trustee may never act in bad faith or without regard to the purposes of the trust or the interests of the beneficiaries. For other provisions on the effect of the terms of the trust, see Sections 4-214 (duties with regard to discretionary powers), 4-301 (prudent investor rule), 4-401 (general powers of trustee and fiduciary duties), and 4-505 (exculpation of trustee).

#### **SECTION 4-202. DUTY OF LOYALTY; IMPARTIALITY; CONFIDENTIAL RELATIONSHIP.**

(a) A trustee shall administer the trust solely in the interest of the beneficiaries, and shall act with due regard to their respective interests.

(b) Any transaction involving the trust which is affected by a substantial conflict between the trustee's fiduciary and personal interests is voidable by a beneficiary affected by the transaction unless (i) the transaction was expressly authorized by the terms of the trust; (ii) the beneficiary consented to or affirmed the transaction or released the trustee from liability as provided in Section 5-406; or (iii) the transaction is approved by the Court after notice to interested persons. A transaction affected by a substantial conflict between personal and fiduciary interests includes any sale, encumbrance, or other transaction involving the trust property entered into by the trustee, the spouse, descendant, agent, or attorney of a trustee, or corporation or other enterprise in which the trustee has a

substantial beneficial interest.

(c) A transaction not involving trust property between a trustee and a beneficiary which occurs during the existence of the trust or while the trustee retains significant influence over the beneficiary and from which the trustee obtains an advantage is an abuse of a confidential relationship unless the trustee establishes that the transaction was fair.

(d) This section does not apply to (i) an agreement between a trustee and a beneficiary relating to the appointment of the trustee; (ii) the payment of compensation to the trustee, whether by agreement, the terms of the trust, or this [Act]; and (iii) a transaction between a trust and another trust, decedent's or conservatorship estate of which the trustee is a fiduciary if the transaction is fair to the beneficiaries of the trust.

**Comment.**

Source: CPC Section 16002-16004.

Subsection (a) of this section, which recites the trustee's fundamental obligations of loyalty and impartiality, is based on Sections 170(1) and 232 of the Restatement (Second) of Trusts (1959). This section does not attempt to state all aspects of the trustee's duty of loyalty, nor does this Part seek to cover all duties that may exist. See Section 1-103 (common law of trusts).

Subsection (b), allowing an interested person to void certain transactions tainted by a conflict of interest, is based on Sections 3-713 and 5-421 of the Uniform Probate Code. Under this subsection, actual proof of a conflict of interest is not required if the transaction involving the trust property was entered into by the trustee or certain of the trustee's affiliates. For such transactions, the trustee will need to obtain the approval of the beneficiaries or the court unless the transaction was authorized by the terms of the trust.

Subsection (c) creates a presumption that certain transaction between a trustee and beneficiary outside of trust are an abuse of a confidential relationship by the trustee. But this section has a limited scope. If the trust has terminated, there must be proof that the trustee's influence with the beneficiary remains. Furthermore, whether or not the trust has

terminated, there must be proof that the trustee obtained an advantage from the relationship. The fact the trustee profited is insufficient to show an abuse if a third party would have similarly profited in an arm's length transaction.

Subsection (d) excepts from the general duty of loyalty sales or other transactions between two or more trusts that have the same trustee, or transactions with a decedent's or conservatorship estate of which the trustee is personal representative or conservator. See Restatement (Second) of Trusts Sec. 170, comm. r (1959). The trustee need not give advance notice of the transaction to the beneficiaries unless required by some other provision. See, e.g., Section 4-213(b) (duty to inform beneficiaries in advance of certain proposed sales). For provisions limiting the need to give notice, see Sections 3-103 (notice to beneficiary of revocable trust), 6-205 (virtual representation), and 6-301 et. seq. (nonjudicial settlement). For provisions permitting the beneficiaries to relieve the trustee from liability, see Section 4-506. For other fundamental duties of the trustee, see Sections 4-201(a) (duty to administer trust), and 4-203 (standard of prudence).

For a specific application of the duty of loyalty within the context of trust investment and management, see Section 4-305.

**SECTION 4-203. STANDARD OF PRUDENCE.** A trustee shall administer the trust with the reasonable care, skill, and caution as a prudent person would, by considering the purposes, terms, distribution requirements, and other circumstances of the trust.

**Comment.**

The duty to administer the trust with prudence is a fundamental duty of the trustee, which is not affected by whether the trustee receives compensation but which may be altered by the terms of the trust. See Section 4-201(b) (alteration of duties by terms of the trust). For a specialized application of this standard within the context of trust investment and management, see Section 4-301 (prudent investor rule). This section would be applicable to matters such as determining whether to make discretionary distributions, communicating with beneficiaries, and relations with creditors.

**SECTION 4-204. COSTS OF ADMINISTRATION.** A trustee may only incur costs that are reasonable in relation to the trust property, purposes, and other circumstances of the trust.

**Comment.**



Source: Unif. Prudent Investor Act Sec. 7.

This section is consistent with the rules concerning costs in Section 227(c)(3) of the Restatement (Third) of Trusts: Prudent Investor Rule (1992). For related rules concerning reimbursement and compensation of trustees, see Sections 4-109 and 4-111. The duty to minimize costs applies to delegation to agents as well as to other aspects of trust administration. In deciding whether and how to delegate, the trustee must be alert to balancing projected benefits against the likely costs. The trustee must also be alert to adjusting compensation for functions which the trustee has delegated to others in order to protect the beneficiary against "double dipping."

For a specific application of the duty to minimize costs within the context of trust investment and management, see Section 4-307.

#### **SECTION 4-205. SPECIAL SKILLS.**

(a) A trustee shall apply the full extent of the trustee's skills.

(b) If a settlor, in selecting a trustee, has relied on the trustee's representation of having special skills, the trustee shall comply with the standard of the skills represented.

#### **Comment.**

Source: CPC Section 16014.

Subsection (b) is similar to the last part of Section 7-302 of the Uniform Probate Code (1977) and the last part of Section 174 of the Restatement (Second) of Trusts (1959). Subsection (b) does not limit the duty provided in subsection (a). Thus, the nature of the trustee's representations to the settlor leading up to the selection of the trustee does not affect the trustee's duty to use the full extent of the trustee's skills.

#### **SECTION 4-206. DELEGATION.**

(a) A trustee may not delegate to an agent or cotrustee the entire administration of the trust or the responsibility to make or participate in the making of decisions with respect to discretionary distributions, but a trustee may otherwise delegate the performance of functions that a prudent trustee of comparable

skills might delegate under similar circumstances.

(b) The trustee shall exercise reasonable care, skill, and caution in:

- (1) selecting an agent;
- (2) establishing the scope and terms of a delegation, consistent with the purposes and terms of the trust;
- (3) periodically reviewing an agent's overall performance and compliance with the terms of the delegation; and
- (4) redressing an action or decision of an agent which would constitute a breach of trust if performed by the trustee.

(c) A trustee who complies with the requirements of subsections (a)-(b) is not liable to the beneficiaries or to the trust for the decisions or actions of the agent to whom a function was delegated.

(d) In performing a delegated function, an agent shall exercise reasonable care to comply with the terms of the delegation.

(e) By accepting the delegation of a trust function from the trustee of a trust that is subject to the law of this State, an agent submits to the jurisdiction of the courts of this State.

#### **Comment.**

This section, following the lead of the Uniform Prudent Investor Act, codified at Article 4, Part 3 of this Act, eliminates the traditional emphasis against delegation by a trustee and the often futile attempt to distinguish between specified ministerial functions, which were delegable, versus discretionary functions, which the trustee was required personally to perform. See Unif. Prudent Investor Act Sec. 9 comm.; and John H. Langbein, *Reversing the Nondelegation Rule of Trust-Investment Law*, 59 Mo. L. Rev. 105 (1994).

Under this section, the emphasis is instead placed on

encouraging and protecting the trustee in making delegations appropriate to the facts and circumstances of the particular trust. Under Subsection (a), the only functions which a trustee is absolutely forbidden to delegate is the entire administration of the trust and the obligation to make or participate, with a cotrustee, in the making of decisions with respect to discretionary distributions. Allowing for delegation of the entire administration would make the appointment of the trustee a useless gesture. Delegation of authority to make discretionary distributions is forbidden because this is the one function which more than any other is intrinsic to the office of trustee. However, while the trustee must make the final decision, the trustee may of course seek appropriate advice.

Whether other functions of the trustee are properly delegable is not based on some supposedly bright-line test between ministerial and discretionary functions but rather on whether it is a function that a prudent trustee might delegate under similar circumstances. For example, delegation of the trust accounting function might be proper and prudent for a family member trustee but improper for a corporate trustee which holds itself out as having expertise in and which is being compensated for this activity.

This section does not mandate delegation or hold a trustee liable for failing to delegate. However, such liability may be imposed under some other section if the trustee, due to the failure to delegate, is unable to perform in accordance with the required standards of a trustee. See, e.g., Sections 4-203 (trustee's standard of prudence in performing duties), 4-301 (prudent investor rule).

This section applies to delegation both to agents and cotrustees. In the case of delegation to a cotrustee, this section should be read together with Section 4-208, which requires a cotrustee to participate in trust administration and to take reasonable steps to prevent or redress a breach of trust committed by another trustee. Whether a trustee may delegate to a cotrustee functions which cannot be delegated to an agent and vice versa, will depend on the facts and circumstances of the particular trust.

Under subsection (b)(3), the duty to review the agent's overall performance includes the periodic evaluation of the continued need for and appropriateness of the delegation of authority. In particular circumstances, the trustee may need to terminate the delegation to comply with the duty under subsection (b)(1) (duty to use reasonable care, skill, and caution in selecting agent).

For provisions permitting beneficiaries to relieve the trustee from liability, see Section 4-506. See also Sections 4-103 (actions by cotrustees), 4-201 (duties subject to control by terms of the trust), 4-203 (trustee's standard of prudence in performing duties), 4-402(13) (trustee may give proxies to vote shares), 4-402(16) (authority to delegate to protective committee in a reorganization), 4-402(26) (power to hire agents of trust).

Delegation to a cotrustee is different than a cotrustee's assumption of duties due to a trustee's inability to perform the office. Under 4-103(3), a cotrustee, without a delegation, may assume the functions of another trustee who is unavailable to perform duties because of absence, illness, or other temporary incapacity.

#### **SECTION 4-207. DIRECTORY POWERS.**

(a) If the terms of the trust grant a person other than the trustee power to direct certain actions of the trustee, the trustee shall act in accordance with the exercise of the power unless an attempted exercise violates the terms of the trust or the trustee is aware that the attempted exercise violates a fiduciary duty which the person owes the beneficiaries of the trust.

(b) The holder of a power to direct the trustee who violates a fiduciary duty owed to the beneficiaries is liable for any loss which results.

#### **Comment.**

This section is based on Restatement (Second) of Trusts Section 185 and comments. Directory powers in trust instruments usually relate either to choice of investment or management of closely-held business interests. A directory power must be distinguished from a veto power. Under a directory power, action is initiated and is within the control of a third party and the trustee usually has no responsibility other than to carry out the direction when made. But if a third party holds a veto power, the trustee is responsible for initiating the decision, subject to the third party's approval. A trustee who administers a trust subject to a veto power occupies a position akin to that of a cotrustee and is responsible for taking appropriate action if the third party's refusal to consent would result in a breach of trust. See Restatement (Second) of Trusts Sec. 185 comm. g (1959); Section 4-208 (duties of cotrustees).

Directory powers take a variety of forms. Frequently, the person holding the power is directing the investment of the holder's own beneficial interest. Such self-directed accounts are particularly prevalent among trusts holding interests in employee plans or individual retirement accounts. But for the type of

donative trusts subject to this Act, the holder is frequently acting on behalf of others and may not even be a beneficiary of the trust. In that event, the holder, as provided in subsection (b), is under a fiduciary duty to the beneficiaries and liable for any loss due to the breach. Furthermore, the trustee, as provided in subsection (a), if aware that a breach of duty has occurred, is under an obligation not to honor the holder's direction.

In the case of a revocable trust, this section is subordinate to Section 3-103(5), which requires a trustee to follow the written direction of the holder of the power to revoke. This would require the settlor to follow a written direction of the holder which might be contrary to the direction of the person to whom the settlor has granted a directory power.

#### **SECTION 4-208. COTRUSTEES.**

(a) If a trust has more than one trustee, each trustee shall:

- (1) participate in the administration of the trust; and
- (2) take reasonable steps to prevent a cotrustee from committing a breach of trust or to compel a cotrustee to redress a breach of trust.

(b) A trustee who complies with subsection (a) is not liable to the beneficiaries or to the trust for the decisions or actions of a cotrustee.

#### **Comment.**

Source: CPC Section 16013.

This section codifies the substance of Sections 184 and 224 of the Restatement (Second) of Trusts (1959). Unlike the Restatement, however, this section combines in one place both the duties of the trustee and the provision on exemption from liability for the actions of a cotrustee. This section should be read in connection with Section 4-206, which permits a trustee to delegate certain functions to a cotrustee. At a minimum, however, a trustee must participate in decisions with respect to discretionary distributions. The exact extent to which a trustee must participate in administration beyond this minimum will depend on the facts of the particular case. This section is also subject to Section 4-201, which permits the settlor to allocate the functions of the cotrustees in the terms of the trust.

If a cotrustee is also a settlor under a revocable trust, a cotrustee who is not a settlor has a duty to follow the directions of the settlor-cotrustee. See Section 3-103(5). That duty supersedes the general duty under this section.

For provisions permitting beneficiaries to relieve the trustee from liability, see Section 4-506.

#### **SECTION 4-209. CONTROL AND SAFEGUARDING OF TRUST PROPERTY.**

A trustee shall take reasonable steps under the circumstances to take control of and to safeguard the trust property.

##### **Comment.**

Source: CPC Section 16006.

This section codifies the substance of Sections 175 and 176 of the Restatement (Second) of Trusts (1959). For provisions permitting the beneficiaries to relieve the trustee from liability, see Section 4-506. See also Sections 4-201 (duties subject to control by terms of the trust), 4-203 (trustee's standard of prudence in performing duties), 4-402(6) (power to abandon trust property), 4-402(19) (power to insure trust property).

#### **SECTION 4-210. SEPARATION AND IDENTIFICATION OF TRUST PROPERTY.** A trustee shall:

(1) keep the trust property separate from other property of the trustee; and

(2) cause the trust property to be designated in such a manner that the interest of the trust clearly appears.

##### **Comment.**

Source: CPC Section 16009.

This section is derived from Section 179 of the Restatement (Second) of Trusts (1959), except that this section permits the joint investment of trust funds with the funds of others, but not the trustee's own, as long as the interest of the trust clearly appears. For provisions permitting beneficiaries to relieve the trustee from liability, see Section 4-506. See also Sections 4-201 (duties subject to control by terms of the trust), 4-203 (trustee's standard of prudence in performing duties), and 4-402(17), which in conformity with this section, allows trustees to hold property in nominee form.

#### **SECTION 4-211. ENFORCEMENT AND DEFENSE OF CLAIMS AND**

**ACTIONS.** A trustee shall take reasonable steps to enforce claims that are part of the trust property and to defend against actions that may result in a loss to the trust.

#### **Comment.**

Source: CPC Section 16010-16011.

This section codifies the substance of Sections 177 and 178 of the Restatement (Second) of Trusts (1959). Under this section, it may not be reasonable to enforce a claim depending upon the likelihood of recovery and the cost of suit and enforcement. Depending on the circumstances of the case, it might also be reasonable to settle an action or suffer a default rather than to defend an action. For provisions permitting beneficiaries to relieve the trustee from liability, see Section 4-506. See also Sections 4-201 (duties subject to control by terms of the trust), 4-203 (trustee's standard of prudence in performing duties).

**SECTION 4-212. PREDECESSOR FIDUCIARIES.** A trustee shall take reasonable steps to (i) compel a former trustee or other fiduciary to deliver trust property to the trustee, and (ii) redress a breach of trust known to the trustee to have been committed by a predecessor trustee or other fiduciary.

#### **Comment.**

Source: CPC Section 16403.

This section is the same in substance as Section 223 of the Restatement (Second) of Trusts (1959), except that this section is written in terms of the affirmative duties of the trustee rather than in terms of negation from liability. Also, unlike the Restatement, this section applies not only to duties with respect to predecessor trustees, but also to personal representatives, conservators and agents under powers of attorney from whom the trustee received trust property.

This section is a specific application of Section 4-211 on the duty to enforce claims, which could include a claim against a predecessor trustee for breach of trust. In certain circumstances it may not be reasonable to enforce a claim against a predecessor trustee or other fiduciary, depending upon the likelihood of recovery and the cost of suit and enforcement. It should also be noted that the liability to beneficiaries does not include beneficiaries under revocable trusts during the time that the trust can be revoked. See Section 3-103 (rights of settlor of

revocable trust); see also Section 3-104 (holder of presently exercisable general power of appointment treated as settlor).

This section does not impose an affirmative duty on the part of a trustee to root out possible wrongdoing by a predecessor. Such a duty is negated because of the expense involved and the reluctance of many trustees to accept the office because of the possible liability. A trustee is liable, however, for breaches committed by a predecessor of which the trustee is aware and for which the trustee failed to take appropriate corrective action.

For provisions permitting a trustee to be relieved of liability for acts of a predecessor trustee or other fiduciary, see Section 4-506.

#### **SECTION 4-213. DUTY TO INFORM AND ACCOUNT.**

(a) A trustee shall keep the beneficiaries of the trust reasonably informed of the administration of the trust.

(b) A trustee shall inform the beneficiaries in advance of a proposed sale of trust property comprising a significant portion of the value of the trust and whose fair market value is not readily ascertainable.

(c) On reasonable request of a beneficiary, a trustee shall provide the beneficiary with a copy of the trust instrument and with information about matters of administration relevant to the beneficiary's interest.

(d) A trustee shall prepare an account of the trust property, liabilities, receipts, and disbursements at least annually, at the termination of the trust, and upon a change of a trustee, and shall send a copy of the account to each beneficiary, other than the trustee, to whom income or principal is required or authorized in the trustee's discretion to be currently distributed, and to each beneficiary who has filed with the trustee a written request for a copy of the account.



(e) An accounting on behalf of a former trustee shall be prepared by the former trustee, or if the trustee's appointment terminated by reason of death or incapacity, by the former trustee's personal representative or guardian or conservator.

**Comment.**

Source: CPC Section 16060-16062, 16064; S.D. Codified Laws Ann. Sec. 29A-3-715(b).

Subsection (a) is based on the first sentence of Section 7-303 of the Uniform Probate Code (1977). The trustee is under a duty to communicate to the beneficiary information about the administration of the trust that is reasonably necessary to enable the beneficiary to enforce the beneficiary's rights under the trust or to prevent or redress a breach of trust. See Restatement (Second) of Trusts Section 173, comment c (1959). Ordinarily, the trustee is not under a duty to furnish information to the beneficiary in the absence of a request for the information. See *id.*, comment d. Thus, the general duty provided in subsection (a) is ordinarily satisfied by complying with subsections (c) and (d) unless there are special circumstances requiring particular information to be reported to beneficiaries. However, if the trustee is dealing with the beneficiary on the trustee's own account, the trustee has a duty to communicate material facts in connection with the transaction that the trustee knows or should know. The trustee also has a duty to communicate material facts affecting the beneficiary's interest that the trustee knows the beneficiary does not know and that the beneficiary needs to know for protection in dealing with a third person. See *id.*

Furthermore, under subsection (b), the trustee must notify the beneficiary in advance of certain proposed sales. This subsection, which is based on a provision drawn from South Dakota law, is designed to codify but make more precise the fiduciary duty delineated in such cases as *Allard v. Pacific National Bank*, 663 P. 2d 104 (Wash. 1983), in which the court surcharged a trustee for failing to give the beneficiaries advance notice of the proposed sale of a parcel of real estate that was the sole asset of the trust. Cases subsequent to *Allard* have also extended this duty to the sale of an interest in a closely-held business, and this subsection extends the duty to sales of tangible personal property.

Subsection (c) is based in part on Section 7-303(b) of the Uniform Probate Code, although this subsection, unlike the UPC, obligates the trustee upon request to deliver a complete copy of the trust instrument. The UPC lets the trustee decide which portions of the trust instrument are relevant to the beneficiary's interest. The availability of information on request under this section does not negate the affirmative duty

of the trustee to provide information under the other subsections. During the time that a revocable trust can be revoked, the right to request information pursuant to this section does not belong to the beneficiaries but only to the settlor or other person having the power to revoke. See Section 3-103.

**SECTION 4-214. DUTIES WITH REGARD TO DISCRETIONARY POWERS.** A trustee shall exercise a discretionary power within the bounds of reasonable judgment and in accordance with any standard stated in the terms of the trust. Notwithstanding the use of such terms as "absolute," "sole," or "uncontrolled" in the grant of discretion, a trustee shall act in accordance with fiduciary principles and may not act in bad faith or in disregard of the purposes of the trust or the power. Absent an abuse of discretion, a trustee's exercise of discretion is not subject to control by a court.

**Comment.**

This section, which applies to both powers of management and powers granted with respect to distribution, is derived from Restatement (Second) of Trusts Section 187 (1959). Despite the breadth of discretion purportedly granted by the wording of the trust, a grant of discretion is never absolute. A grant of discretion establishes a range within which the trustee may act. The greater the grant of discretion, the broader the range. A trustee's action must always be in good faith, not induced by an improper motive, and to some extent reasonable, but with more flexibility in the concept of reasonableness the greater the discretion given. See Edward C. Halbach, Jr., Problems of Discretion in Discretionary Trusts, 61 Colum. L. Rev. 1425 (1961).

For the rights of creditors with respect to discretionary trusts, see Sections 2-303. For the remedies available for breach of trust, see Section 4-502.

**PART 3**

**UNIFORM PRUDENT INVESTOR ACT**

**Section**

- 4-301. Prudent Investor Rule.
- 4-302. Standard of Care; Portfolio Strategy; Risk and Return Objectives.
- 4-303. Diversification.
- 4-304. Duties at Inception of Trusteeship.
- 4-305. Loyalty.
- 4-306. Impartiality
- 4-307. Investment Costs.
- 4-308. Reviewing Compliance.
- 4-309. Delegation of Investment and Management Functions.
- 4-310. Language Invoking Standard of Prudent Investor Rule.

**PREFATORY NOTE**

Over the quarter century from the late 1960's the investment practices of fiduciaries experienced significant change. The Uniform Prudent Investor Act (UPIA) undertakes to update trust investment law in recognition of the alterations that have occurred in investment practice. These changes have occurred under the influence of a large and broadly accepted body of empirical and theoretical knowledge about the behavior of capital markets, often described as "modern portfolio theory."

This Act draws upon the revised standards for prudent trust investment promulgated by the American Law Institute in its Restatement (Third) of Trusts: Prudent Investor Rule (1992) [hereinafter Restatement of Trusts 3d: Prudent Investor Rule; also referred to as 1992 Restatement].

**Objectives of the Act.** UPIA makes five fundamental alterations in the former criteria for prudent investing. All are to be found in the Restatement of Trusts 3d: Prudent Investor Rule.

(1) The standard of prudence is applied to any investment as part of the total portfolio, rather than to individual investments. In the trust setting the term "portfolio" embraces all the trust's assets. UPIA § 2(b).

(2) The tradeoff in all investing between risk and return is identified as the fiduciary's central consideration. UPIA § 2(b).

(3) All categoric restrictions on types of investments have been abrogated; the trustee can invest in anything that plays an appropriate role in achieving the risk/return objectives of the trust and that meets the other requirements of prudent investing. UPIA § 2(e).

(4) The long familiar requirement that fiduciaries

diversify their investments has been integrated into the definition of prudent investing. UPIA § 3.

(5) The much criticized former rule of trust law forbidding the trustee to delegate investment and management functions has been reversed. Delegation is now permitted, subject to safeguards. UPIA § 9.

**Literature.** These changes in trust investment law have been presaged in an extensive body of practical and scholarly writing. See especially the discussion and reporter's notes by Edward C. Halbach, Jr., in Restatement of Trusts 3d: Prudent Investor Rule (1992); see also Edward C. Halbach, Jr., Trust Investment Law in the Third Restatement, 27 Real Property, Probate & Trust J. 407 (1992); Bevis Longstreth, Modern Investment Management and the Prudent Man Rule (1986); Jeffrey N. Gordon, The Puzzling Persistence of the Constrained Prudent Man Rule, 62 N.Y.U.L. Rev. 52 (1987); John H. Langbein & Richard A. Posner, The Revolution in Trust Investment Law, 62 A.B.A.J. 887 (1976); Note, The Regulation of Risky Investments, 83 Harvard L. Rev. 603 (1970). A succinct account of the main findings of modern portfolio theory, written for lawyers, is Jonathan R. Macey, An Introduction to Modern Financial Theory (1991) (American College of Trust & Estate Counsel Foundation). A leading introductory text on modern portfolio theory is R.A. Brealey, An Introduction to Risk and Return from Common Stocks (2d ed. 1983).

**Legislation.** Most states have legislation governing trust-investment law. This Act promotes uniformity of state law on the basis of the new consensus reflected in the Restatement of Trusts 3d: Prudent Investor Rule. Some states have already acted. California, Delaware, Georgia, Minnesota, Tennessee, and Washington revised their prudent investor legislation to emphasize the total-portfolio standard of care in advance of the 1992 Restatement. These statutes are extracted and discussed in Restatement of Trusts 3d: Prudent Investor Rule § 227, reporter's note, at 60-66 (1992).

Drafters in Illinois in 1991 worked from the April 1990 "Proposed Final Draft" of the Restatement of Trusts 3d: Prudent Investor Rule and enacted legislation that is closely modeled on the new Restatement. 760 ILCS § 5/5 (prudent investing); and § 5/5.1 (delegation) (1992). As the Comments to this Uniform Prudent Investor Act reflect, the Act draws upon the Illinois statute in several sections. Virginia revised its prudent investor act in a similar vein in 1992. Virginia Code § 26-45.1 (prudent investing) (1992). Florida revised its statute in 1993. Florida Laws, ch. 93-257, amending Florida Statutes § 518.11 (prudent investing) and creating § 518.112 (delegation). New York legislation drawing on the new Restatement and on a preliminary version of this Uniform Prudent Investor Act was enacted in 1994. N.Y. Assembly Bill 11683-B, Ch. 609 (1994),

adding Estates, Powers and Trusts Law § 11-2.3 (Prudent Investor Act).

**Remedies.** This Act does not undertake to address issues of remedy law or the computation of damages in trust matters. Remedies are the subject of a reasonably distinct body of doctrine. See generally Restatement (Second) of Trusts §§ 197-226A (1959) [hereinafter cited as Restatement of Trusts 2d; also referred to as 1959 Restatement].

**Implications for charitable and pension trusts.** This Act is centrally concerned with the investment responsibilities arising under the private gratuitous trust, which is the common vehicle for conditioned wealth transfer within the family. Nevertheless, the prudent investor rule also bears on charitable and pension trusts, among others. "In making investments of trust funds the trustee of a charitable trust is under a duty similar to that of the trustee of a private trust." Restatement of Trusts 2d § 389 (1959). The Employee Retirement Income Security Act (ERISA), the federal regulatory scheme for pension trusts enacted in 1974, absorbs trust-investment law through the prudence standard of ERISA § 404(a)(1)(B), 29 U.S.C. § 1104(a). The Supreme Court has said: "ERISA's legislative history confirms that the Act's fiduciary responsibility provisions 'codif[y] and mak[e] applicable to [ERISA] fiduciaries certain principles developed in the evolution of the law of trusts.'" *Firestone Tire & Rubber Co. v. Bruch*, 489 U.S. 101, 110-11 (1989) (footnote omitted).

**Other fiduciary relationships.** The Uniform Prudent Investor Act regulates the investment responsibilities of trustees. Other fiduciaries -- such as executors, conservators, and guardians of the property -- sometimes have responsibilities over assets that are governed by the standards of prudent investment. It will often be appropriate for states to adapt the law governing investment by trustees under this Act to these other fiduciary regimes, taking account of such changed circumstances as the relatively short duration of most executorships and the intensity of court supervision of conservators and guardians in some jurisdictions. The present Act does not undertake to adjust trust-investment law to the special circumstances of the state schemes for administering decedents' estates or conducting the affairs of protected persons.

Although the Uniform Prudent Investor Act by its terms applies to trusts and not to charitable corporations, the standards of the Act can be expected to inform the investment responsibilities of directors and officers of charitable corporations. As the 1992 Restatement observes, "the duties of the members of the governing board of a charitable corporation are generally similar to the duties of the trustee of a charitable trust." Restatement of Trusts 3d: Prudent Investor Rule § 379, Comment *b*, at 190 (1992). See also *id.* § 389,

Comment *b*, at 190-91 (absent contrary statute or other provision, prudent investor rule applies to investment of funds held for charitable corporations).

**Relationship to Uniform Trust Act.** The text of UPIA below is identical to that of the free-standing Act except for minor revisions to conform terminology.

#### **SECTION 4-301. PRUDENT INVESTOR RULE.**

(a) Except as otherwise provided in subsection (b), a trustee who invests and manages trust property owes a duty to the beneficiaries of the trust to comply with the prudent investor rule set forth in this [Part].

(b) The prudent investor rule, a default rule, may be expanded, restricted, eliminated, or otherwise altered by the provisions of a trust. A trustee is not liable to a beneficiary to the extent that the trustee acted in reasonable reliance on the terms of the trust.

#### **Comment.**

This section imposes the obligation of prudence in the conduct of investment functions and identifies further sections of the Act that specify the attributes of prudent conduct.

**Origins.** The prudence standard for trust investing traces back to *Harvard College v. Amory*, 26 Mass. (9 Pick.) 446 (1830). Trustees should "observe how men of prudence, discretion and intelligence manage their own affairs, not in regard to speculation, but in regard to the permanent disposition of their funds, considering the probable income, as well as the probable safety of the capital to be invested." *Id.* at 461.

**Prior legislation.** The Model Prudent Man Rule Statute (1942), sponsored by the American Bankers Association, undertook to codify the language of the *Amory* case. See Mayo A. Shattuck, *The Development of the Prudent Man Rule for Fiduciary Investment in the United States in the Twentieth Century*, 12 Ohio State L.J. 491, at 501 (1951); for the text of the model act, which inspired many state statutes, see *id.* at 508-09. Another prominent codification of the *Amory* standard is Uniform Probate Code § 7-302 (1969), which provides that "the trustee shall observe

the standards in dealing with the trust assets that would be observed by a prudent man dealing with the property of another . . . ."

Congress has imposed a comparable prudence standard for the administration of pension and employee benefit trusts in the Employee Retirement Income Security Act (ERISA), enacted in 1974. ERISA § 404(a)(1)(B), 29 U.S.C. § 1104(a), provides that "a fiduciary shall discharge his duties with respect to a plan solely in the interest of the participants and beneficiaries and . . . with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent man acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of like character and with like aims . . . ."

**Prior Restatement.** The Restatement of Trusts 2d (1959) also tracked the language of the *Amory* case: "In making investments of trust funds the trustee is under a duty to the beneficiary . . . to make such investments and only such investments as a prudent man would make of his own property having in view the preservation of the estate and the amount and regularity of the income to be derived . . . ." Restatement of Trusts 2d § 227 (1959).

**Objective standard.** The concept of prudence in the judicial opinions and legislation is essentially relational or comparative. It resembles in this respect the "reasonable person" rule of tort law. A prudent trustee behaves as other trustees similarly situated would behave. The standard is, therefore, objective rather than subjective. Sections 4-302 through 4-309 identify the main factors that bear on prudent investment behavior.

**Variation.** Almost all of the rules of trust law are default rules, that is, rules that the settlor may alter or abrogate. Subsection (b) carries forward this traditional attribute of trust law. Traditional trust law also allows the beneficiaries of the trust to excuse its performance, when they are all capable and not misinformed. Restatement of Trusts 2d § 216 (1959).

#### **SECTION 4-302. STANDARD OF CARE; PORTFOLIO STRATEGY; RISK AND RETURN OBJECTIVES.**

(a) A trustee shall invest and manage trust property as a prudent investor would, by considering the purposes, terms, distribution requirements, and other circumstances of the trust. In satisfying this standard, the trustee shall exercise

reasonable care, skill, and caution.

(b) A trustee's investment and management decisions respecting individual assets must be evaluated not in isolation but in the context of the trust portfolio as a whole and as a part of an overall investment strategy having risk and return objectives reasonably suited to the trust.

(c) Among circumstances that a trustee shall consider in investing and managing trust property are such of the following as are relevant to the trust or its beneficiaries:

- (1) general economic conditions;
- (2) the possible effect of inflation or deflation;
- (3) the expected tax consequences of investment decisions or strategies;
- (4) the role that each investment or course of action plays within the overall trust portfolio, which may include financial assets, interests in closely held enterprises, tangible and intangible personal property, and real property;
- (5) the expected total return from income and the appreciation of capital;
- (6) other resources of the beneficiaries;
- (7) needs for liquidity, regularity of income, and preservation or appreciation of capital; and
- (8) an asset's special relationship or special value, if any, to the purposes of the trust or to one or more of the beneficiaries.

(d) A trustee shall make a reasonable effort to verify



facts relevant to the investment and management of trust property.

(e) A trustee may invest in any kind of property or type of investment consistent with the standards of this [Act].

(f) A trustee who has special skills or expertise, or is named trustee in reliance upon the trustee's representation that the trustee has special skills or expertise, has a duty to use those special skills or expertise.

#### **Comment.**

This section is the heart of the Act. Subsections (a), (b), and (c) are patterned loosely on the language of the Restatement of Trusts 3d: Prudent Investor Rule § 227 (1992), and on the 1991 Illinois statute, 760 § ILCS 5/5a (1992). Subsection (f) is derived from Uniform Probate Code § 7-302 (1969).

**Objective standard.** Subsection (a) carries forward the relational and objective standard made familiar in the *Amory* case, in earlier prudent investor legislation, and in the Restatements. Early formulations of the prudent person rule were sometimes troubled by the effort to distinguish between the standard of a prudent person investing for another and investing on his or her own account. The language of subsection (a), by relating the trustee's duty to "the purposes, terms, distribution requirements, and other circumstances of the trust," should put such questions to rest. The standard is the standard of the prudent investor similarly situated.

**Portfolio standard.** Subsection (b) emphasizes the consolidated portfolio standard for evaluating investment decisions. An investment that might be imprudent standing alone can become prudent if undertaken in sensible relation to other trust assets, or to other nontrust assets. In the trust setting the term "portfolio" embraces the entire trust estate.

**Risk and return.** Subsection (b) also sounds the main theme of modern investment practice, sensitivity to the risk/return curve. See generally the works cited in the Prefatory Note to this Act, under "Literature." Returns correlate strongly with risk, but tolerance for risk varies greatly with the financial and other circumstances of the investor, or in the case of a trust, with the purposes of the trust and the relevant circumstances of the beneficiaries. A trust whose main purpose is to support an elderly widow of modest means will have a lower

risk tolerance than a trust to accumulate for a young scion of great wealth.

Subsection (b) follows Restatement of Trusts 3d: Prudent Investor Rule § 227(a), which provides that the standard of prudent investing "requires the exercise of reasonable care, skill, and caution, and is to be applied to investments not in isolation but in the context of the trust portfolio and as a part of an overall investment strategy, which should incorporate risk and return objectives reasonably suitable to the trust."

**Factors affecting investment.** Subsection (c) points to certain of the factors that commonly bear on risk/return preferences in fiduciary investing. This listing is nonexclusive. Tax considerations, such as preserving the stepped up basis on death under Internal Revenue Code § 1014 for low-basis assets, have traditionally been exceptionally important in estate planning for affluent persons. Under the present recognition rules of the federal income tax, taxable investors, including trust beneficiaries, are in general best served by an investment strategy that minimizes the taxation incident to portfolio turnover. See generally Robert H. Jeffrey & Robert D. Arnott, *Is Your Alpha Big Enough to Cover Its Taxes?*, *Journal of Portfolio Management* 15 (Spring 1993).

Another familiar example of how tax considerations bear upon trust investing: In a regime of pass-through taxation, it may be prudent for the trust to buy lower yielding tax-exempt securities for high-bracket taxpayers, whereas it would ordinarily be imprudent for the trustees of a charitable trust, whose income is tax exempt, to accept the lowered yields associated with tax-exempt securities.

When tax considerations affect beneficiaries differently, the trustee's duty of impartiality requires attention to the competing interests of each of them.

Subsection (c)(8), allowing the trustee to take into account any preferences of the beneficiaries respecting heirlooms or other prized assets, derives from the Illinois act, 760 ILCS § 5/5(a)(4) (1992).

**Duty to monitor.** Subsections (a) through (d) apply both to investing and managing trust assets. "Managing" embraces monitoring, that is, the trustee's continuing responsibility for oversight of the suitability of investments already made as well as the trustee's decisions respecting new investments.

**Duty to investigate.** Subsection (d) carries forward the traditional responsibility of the fiduciary investor to examine information likely to bear importantly on the value or the security of an investment -- for example, audit reports or records of title. E.g., *Estate of Collins*, 72 Cal. App. 3d 663, 139 Cal. Rptr. 644 (1977) (trustees lent on a junior mortgage on unimproved real estate, failed to have land appraised, and

accepted an unaudited financial statement; held liable for losses).

**Abrogating categoric restrictions.** Subsection (e) clarifies that no particular kind of property or type of investment is inherently imprudent. Traditional trust law was encumbered with a variety of categoric exclusions, such as prohibitions on junior mortgages or new ventures. In some states legislation created so-called "legal lists" of approved trust investments. The universe of investment products changes incessantly. Investments that were at one time thought too risky, such as equities, or more recently, futures, are now used in fiduciary portfolios. By contrast, the investment that was at one time thought ideal for trusts, the long-term bond, has been discovered to import a level of risk and volatility -- in this case, inflation risk -- that had not been anticipated. Accordingly, subsection (e) follows Restatement of Trusts 3d: Prudent Investor Rule in abrogating categoric restrictions. The Restatement says: "Specific investments or techniques are not per se prudent or imprudent. The riskiness of a specific property, and thus the propriety of its inclusion in the trust estate, is not judged in the abstract but in terms of its anticipated effect on the particular trust's portfolio." Restatement of Trusts 3d: Prudent Investor Rule § 227, Comment f, at 24 (1992). The premise of subsection (e) is that trust beneficiaries are better protected by the emphasis on close attention to risk/return objectives as prescribed in subsection (b) than in attempts to identify categories of investment that are per se prudent or imprudent.

The Act impliedly disavows the emphasis in older law on avoiding "speculative" or "risky" investments. Low levels of risk may be appropriate in some trust settings but inappropriate in others. It is the trustee's task to invest at a risk level that is suitable to the purposes of the trust.

The abolition of categoric restrictions against types of investment in no way alters the trustee's conventional duty of loyalty, which is reiterated in Section 4-305. For example, were the trustee to invest in a second mortgage on a piece of real property owned by the trustee, the investment would be wrongful on account of the trustee's breach of the duty to abstain from self-dealing, even though the investment would no longer automatically offend the former categoric restriction against fiduciary investments in junior mortgages.

**Professional fiduciaries.** The distinction taken in subsection (f) between amateur and professional trustees is familiar law. The prudent investor standard applies to a range of fiduciaries, from the most sophisticated professional investment management firms and corporate fiduciaries, to family members of minimal experience. Because the standard of prudence is relational, it follows that the standard for professional trustees is the standard of prudent professionals; for amateurs,

it is the standard of prudent amateurs. Restatement of Trusts 2d § 174 (1959) provides: "The trustee is under a duty to the beneficiary in administering the trust to exercise such care and skill as a man of ordinary prudence would exercise in dealing with his own property; and if the trustee has or procures his appointment as trustee by representing that he has greater skill than that of a man of ordinary prudence, he is under a duty to exercise such skill." Case law strongly supports the concept of the higher standard of care for the trustee representing itself to be expert or professional. See Annot., Standard of Care Required of Trustee Representing Itself to Have Expert Knowledge or Skill, 91 A.L.R. 3d 904 (1979) & 1992 Supp. at 48-49.

The UPIA Drafting Committee declined the suggestion that the Act should create an exception to the prudent investor rule (or to the diversification requirement of Section 4-303 in the case of smaller trusts. The Committee believes that subsections (b) and (c) emphasize factors that are sensitive to the traits of small trusts; and that subsection (f) adjusts helpfully for the distinction between professional and amateur trusteeship. Furthermore, it is always open to the settlor of a trust under Section 4-301(b) to reduce the trustee's standard of care if the settlor deems such a step appropriate. The official comments to the 1992 Restatement observe that pooled investments, such as mutual funds and bank common trust funds, are especially suitable for small trusts. Restatement of Trusts 3d: Prudent Investor Rule § 227, Comments *h*, *m*, at 28, 51; reporter's note to Comment *g*, *id.* at 83.

**Matters of proof.** Although virtually all express trusts are created by written instrument, oral trusts are known, and accordingly, this Act presupposes no formal requirement that trust terms be in writing. When there is a written trust instrument, modern authority strongly favors allowing evidence extrinsic to the instrument to be consulted for the purpose of ascertaining the settlor's intent. See Uniform Probate Code § 2-601 (1990), Comment; Restatement (Third) of Property: Donative Transfers (Preliminary Draft No. 2, ch. 11, Sept. 11, 1992).

**SECTION 4-303. DIVERSIFICATION.** A trustee shall diversify the investments of the trust unless the trustee reasonably determines that, because of special circumstances, the purposes of the trust are better served without diversifying.

**Comment.**

The language of this section derives from Restatement of Trusts 2d § 228 (1959). ERISA insists upon a comparable rule for pension trusts. ERISA § 404(a)(1)(C), 29 U.S.C. § 1104(a)(1)(C).

Case law overwhelmingly supports the duty to diversify. See Annot., Duty of Trustee to Diversify Investments, and Liability for Failure to Do So, 24 A.L.R. 3d 730 (1969) & 1992 Supp. at 78-79.

The 1992 Restatement of Trusts takes the significant step of integrating the diversification requirement into the concept of prudent investing. Section 227(b) of the 1992 Restatement treats diversification as one of the fundamental elements of prudent investing, replacing the separate section 228 of the Restatement of Trusts 2d. The message of the 1992 Restatement, carried forward in this section, is that prudent investing ordinarily requires diversification.

Circumstances can, however, overcome the duty to diversify. For example, if a tax-sensitive trust owns an underdiversified block of low-basis securities, the tax costs of recognizing the gain may outweigh the advantages of diversifying the holding. The wish to retain a family business is another situation in which the purposes of the trust sometimes override the conventional duty to diversify.

**Rationale for diversification.** "Diversification reduces risk . . . [because] stock price movements are not uniform. They are imperfectly correlated. This means that if one holds a well diversified portfolio, the gains in one investment will cancel out the losses in another." Jonathan R. Macey, An Introduction to Modern Financial Theory 20 (American College of Trust and Estate Counsel Foundation, 1991). For example, during the Arab oil embargo of 1973, international oil stocks suffered declines, but the shares of domestic oil producers and coal companies benefitted. Holding a broad enough portfolio allowed the investor to set off, to some extent, the losses associated with the embargo.

Modern portfolio theory divides risk into the categories of "compensated" and "uncompensated" risk. The risk of owning shares in a mature and well-managed company in a settled industry is less than the risk of owning shares in a start-up high-technology venture. The investor requires a higher expected return to induce the investor to bear the greater risk of disappointment associated with the start-up firm. This is compensated risk -- the firm pays the investor for bearing the risk. By contrast, nobody pays the investor for owning too few stocks. The investor who owned only international oils in 1973 was running a risk that could have been reduced by having configured the portfolio differently -- to include investments in different industries. This is uncompensated risk -- nobody pays the investor for owning shares in too few industries and too few companies. Risk that can be eliminated by adding different stocks (or bonds) is uncompensated risk. The object of diversification is to minimize this uncompensated risk of having too few investments. "As long as stock prices do not move exactly together, the risk of a diversified portfolio will be

less than the average risk of the separate holdings." R.A. Brealey, *An Introduction to Risk and Return from Common Stocks* 103 (2d ed. 1983).

There is no automatic rule for identifying how much diversification is enough. The 1992 Restatement says: "Significant diversification advantages can be achieved with a small number of well-selected securities representing different industries . . . . Broader diversification is usually to be preferred in trust investing," and pooled investment vehicles "make thorough diversification practical for most trustees." Restatement of Trusts 3d: Prudent Investor Rule § 227, General Note on Comments e-h, at 77 (1992). See also Macey, *supra*, at 23-24; Brealey, *supra*, at 111-13.

**Diversifying by pooling.** It is difficult for a small trust fund to diversify thoroughly by constructing its own portfolio of individually selected investments. Transaction costs such as the round-lot (100 share) trading economies make it relatively expensive for a small investor to assemble a broad enough portfolio to minimize uncompensated risk. For this reason, pooled investment vehicles have become the main mechanism for facilitating diversification for the investment needs of smaller trusts.

Most states have legislation authorizing common trust funds; see 3 Austin W. Scott & William F. Fratcher, *The Law of Trusts* § 227.9, at 463-65 n.26 (4th ed. 1988) (collecting citations to state statutes). As of 1992, 35 states and the District of Columbia had enacted the Uniform Common Trust Fund Act (UCTFA) (1938), overcoming the rule against commingling trust assets and expressly enabling banks and trust companies to establish common trust funds. 7 Uniform Laws Ann. 1992 Supp. at 130 (schedule of adopting states). The Prefatory Note to the UCTFA explains: "The purposes of such a common or joint investment fund are to diversify the investment of the several trusts and thus spread the risk of loss, and to make it easy to invest any amount of trust funds quickly and with a small amount of trouble." 7 Uniform Laws Ann. 402 (1985).

**Fiduciary investing in mutual funds.** Trusts can also achieve diversification by investing in mutual funds. See Restatement of Trusts 3d: Prudent Investor Rule, § 227, Comment m, at 99-100 (1992) (endorsing trust investment in mutual funds). ERISA § 401(b)(1), 29 U.S.C. § 1101(b)(1), expressly authorizes pension trusts to invest in mutual funds, identified as securities "issued by an investment company registered under the Investment Company Act of 1940 . . . ."

**SECTION 4-304. DUTIES AT INCEPTION OF TRUSTEESHIP.** Within a reasonable time after accepting a trusteeship or receiving

trust property, a trustee shall review the trust property and make and implement decisions concerning the retention and disposition of assets, in order to bring the trust portfolio into compliance with the purposes, terms, distribution requirements, and other circumstances of the trust, and with the requirements of this [Part].

**Comment.**

This section, requiring the trustee to dispose of unsuitable assets within a reasonable time, is old law, codified in Restatement of Trusts 3d: Prudent Investor Rule § 229 (1992), lightly revising Restatement of Trusts 2d § 230 (1959). The duty extends as well to investments that were proper when purchased but subsequently become improper. Restatement of Trusts 2d § 231 (1959). The same standards apply to successor trustees, see Restatement of Trusts 2d § 196 (1959).

The question of what period of time is reasonable turns on the totality of factors affecting the asset and the trust. The 1959 Restatement took the view that "[o]rdinarily any time within a year is reasonable, but under some circumstances a year may be too long a time and under other circumstances a trustee is not liable although he fails to effect the conversion for more than a year." Restatement of Trusts 2d § 230, comment *b* (1959). The 1992 Restatement retreated from this rule of thumb, saying, "No positive rule can be stated with respect to what constitutes a reasonable time for the sale or exchange of securities." Restatement of Trusts 3d: Prudent Investor Rule § 229, comment *b* (1992).

The criteria and circumstances identified in Section 4-302 as bearing upon the prudence of decisions to invest and manage trust assets also pertain to the prudence of decisions to retain or dispose of inception assets under this section.

**SECTION 4-305. LOYALTY.** A trustee shall invest and manage the trust property solely in the interest of the beneficiaries.

**Comment.**

The duty of loyalty is perhaps the most characteristic rule of trust law, requiring the trustee to act exclusively for the beneficiaries, as opposed to acting for the trustee's own interest or that of third parties. The language of Section 4 of this Act derives from Restatement of Trusts 3d: Prudent Investor Rule § 170 (1992), which makes minute changes in Restatement of

Trusts 2d § 170 (1959).

The concept that the duty of prudence in trust administration, especially in investing and managing trust assets, entails adherence to the duty of loyalty is familiar. ERISA § 404(a)(1)(B), 29 U.S.C. § 1104(a)(1)(B), extracted in the Comment to Section 1 of this Act, effectively merges the requirements of prudence and loyalty. A fiduciary cannot be prudent in the conduct of investment functions if the fiduciary is sacrificing the interests of the beneficiaries.

The duty of loyalty is not limited to settings entailing self-dealing or conflict of interest in which the trustee would benefit personally from the trust. "The trustee is under a duty to the beneficiary in administering the trust not to be guided by the interest of any third person. Thus, it is improper for the trustee to sell trust property to a third person for the purpose of benefitting the third person rather than the trust." Restatement of Trusts 2d § 170, comment *q*, at 371 (1959).

No form of so-called "social investing" is consistent with the duty of loyalty if the investment activity entails sacrificing the interests of trust beneficiaries -- for example, by accepting below-market returns -- in favor of the interests of the persons supposedly benefitted by pursuing the particular social cause. See, e.g., John H. Langbein & Richard Posner, *Social Investing and the Law of Trusts*, 79 Michigan L. Rev. 72, 96-97 (1980) (collecting authority). For pension trust assets, see generally Ian D. Lanoff, *The Social Investment of Private Pension Plan Assets: May it Be Done Lawfully under ERISA?*, 31 Labor L.J. 387 (1980). Commentators supporting social investing tend to concede the overriding force of the duty of loyalty. They argue instead that particular schemes of social investing may not result in below-market returns. See, e.g., Marcia O'Brien Hylton, "Socially Responsible" Investing: Doing Good Versus Doing Well in an Inefficient Market, 42 American U.L. Rev. 1 (1992). In 1994 the Department of Labor issued an Interpretive Bulletin reviewing its prior analysis of social investing questions and reiterating that pension trust fiduciaries may invest only in conformity with the prudence and loyalty standards of ERISA §§ 403-404. Interpretive Bulletin 94-1, 59 Fed. Regis. 32606 (Jun. 22, 1994), to be codified as 29 CFR § 2509.94-1. The Bulletin reminds fiduciary investors that they are prohibited from "subordinat[ing] the interests of participants and beneficiaries in their retirement income to unrelated objectives."

**SECTION 4-306. IMPARTIALITY.** If a trust has two or more beneficiaries, the trustee shall act impartially in investing and managing the trust property, taking into account any differing



interests of the beneficiaries.

**Comment.**

The duty of impartiality derives from the duty of loyalty. When the trustee owes duties to more than one beneficiary, loyalty requires the trustee to respect the interests of all the beneficiaries. Prudence in investing and administration requires the trustee to take account of the interests of all the beneficiaries for whom the trustee is acting, especially the conflicts between the interests of beneficiaries interested in income and those interested in principal.

The language of Section 6 derives from Restatement of Trusts 2d § 183 (1959); see also *id.*, § 232. Multiple beneficiaries may be beneficiaries in succession (such as life and remainder interests) or beneficiaries with simultaneous interests (as when the income interest in a trust is being divided among several beneficiaries).

The trustee's duty of impartiality commonly affects the conduct of investment and management functions in the sphere of principal and income allocations. This Act prescribes no regime for allocating receipts and expenses. The details of such allocations are commonly handled under specialized legislation, such as the Revised Uniform Principal and Income Act (1962) (which is presently under study by the Uniform Law Commission with a view toward further revision).

**SECTION 4-307. INVESTMENT COSTS.** In investing and managing trust property, a trustee may only incur costs that are appropriate and reasonable in relation to the property, the purposes of the trust, and the skills of the trustee.

**Comment.**

Wasting beneficiaries' money is imprudent. In devising and implementing strategies for the investment and management of trust assets, trustees are obliged to minimize costs.

The language of Section 7 derives from Restatement of Trusts 2d § 188 (1959). The Restatement of Trusts 3d says: "Concerns over compensation and other charges are not an obstacle to a reasonable course of action using mutual funds and other pooling arrangements, but they do require special attention by a trustee. . . . [I]t is important for trustees to make careful cost comparisons, particularly among similar products of a specific type being considered for a trust portfolio." Restatement of Trusts 3d: Prudent Investor Rule § 227, comment *m*, at 58 (1992).

**SECTION 4-308. REVIEWING COMPLIANCE.** Compliance with the prudent investor rule is determined in light of the facts and circumstances existing at the time of a trustee's decision or action and not by hindsight.

**Comment.**

This section derives from the 1991 Illinois act, 760 ILCS 5/5(a)(2) (1992), which draws upon Restatement of Trusts 3d: Prudent Investor Rule § 227, comment *b*, at 11 (1992). Trustees are not insurers. Not every investment or management decision will turn out in the light of hindsight to have been successful. Hindsight is not the relevant standard. In the language of law and economics, the standard is *ex ante*, not *ex post*.

**SECTION 4-309. DELEGATION OF INVESTMENT AND MANAGEMENT FUNCTIONS.**

(a) A trustee may delegate investment and management functions that a prudent trustee of comparable skills could properly delegate under the circumstances. The trustee shall exercise reasonable care, skill, and caution in:

- (1) selecting an agent;
- (2) establishing the scope and terms of the delegation, consistent with the purposes and terms of the trust; and
- (3) periodically reviewing the agent's actions in order to monitor the agent's performance and compliance with the terms of the delegation.

(b) In performing a delegated function, an agent owes a duty to the trust to exercise reasonable care to comply with the terms of the delegation.

(c) A trustee who complies with the requirements of subsection (a) is not liable to the beneficiaries or to the trust

for the decisions or actions of the agent to whom the function was delegated.

(d) By accepting the delegation of a trust function from the trustee of a trust that is subject to the law of this State, an agent submits to the jurisdiction of the courts of this State.

#### **Comment.**

This section reverses the much-criticized rule that forbade trustees to delegate investment and management functions. The language of this section is derived from Restatement of Trusts 3d: Prudent Investor Rule § 171 (1992), discussed *infra*, and from the 1991 Illinois act, 760 ILCS § 5/5.1(b), (c) (1992).

**Former law.** The former nondelegation rule survived into the 1959 Restatement: "The trustee is under a duty to the beneficiary not to delegate to others the doing of acts which the trustee can reasonably be required personally to perform." The rule put a premium on the frequently arbitrary task of distinguishing discretionary functions that were thought to be nondelegable from supposedly ministerial functions that the trustee was allowed to delegate. Restatement of Trusts 2d § 171 (1959).

The Restatement of Trusts 2d admitted in a comment that "There is not a clear-cut line dividing the acts which a trustee can properly delegate from those which he cannot properly delegate." Instead, the comment directed attention to a list of factors that "may be of importance: (1) the amount of discretion involved; (2) the value and character of the property involved; (3) whether the property is principal or income; (4) the proximity or remoteness of the subject matter of the trust; (5) the character of the act as one involving professional skill or facilities possessed or not possessed by the trustee himself." Restatement of Trusts 2d § 171, comment *d* (1959). The 1959 Restatement further said: "A trustee cannot properly delegate to another power to select investments." Restatement of Trusts 2d § 171, comment *h* (1959).

For discussion and criticism of the former rule see William L. Cary & Craig B. Bright, *The Delegation of Investment Responsibility for Endowment Funds*, 74 Columbia L. Rev. 207 (1974); John H. Langbein & Richard A. Posner, *Market Funds and Trust-Investment Law*, 1976 American Bar Foundation Research J. 1, 18-24.

**The modern trend to favor delegation.** The trend of subsequent legislation, culminating in the Restatement of Trusts 3d: Prudent Investor Rule, has been strongly hostile to the nondelegation rule. See John H. Langbein, *Reversing the*

Nondelegation Rule of Trust-Investment Law, 59 Missouri L. Rev. 105 (1994).

**The delegation rule of the Uniform Trustee Powers Act.** The Uniform Trustee Powers Act (1964) effectively abrogates the nondelegation rule. It authorizes trustees "to employ persons, including attorneys, auditors, investment advisors, or agents, even if they are associated with the trustee, to advise or assist the trustee in the performance of his administrative duties; to act without independent investigation upon their recommendations; and instead of acting personally, to employ one or more agents to perform any act of administration, whether or not discretionary . . . ." Uniform Trustee Powers Act § 3(24), 7B Uniform Laws Ann. 743 (1985). The Act has been enacted in 16 states, see "Record of Passage of Uniform and Model Acts as of September 30, 1993," 1993-94 Reference Book of Uniform Law Commissioners (unpaginated, following page 111) (1993).

**UMIFA's delegation rule.** The Uniform Management of Institutional Funds Act (1972) (UMIFA), authorizes the governing boards of eleemosynary institutions, who are trustee-like fiduciaries, to delegate investment matters either to a committee of the board or to outside investment advisors, investment counsel, managers, banks, or trust companies. UMIFA § 5, 7A Uniform Laws Ann. 705 (1985). UMIFA has been enacted in 38 states, see "Record of Passage of Uniform and Model Acts as of September 30, 1993," 1993-94 Reference Book of Uniform Law Commissioners (unpaginated, following page 111) (1993).

**ERISA's delegation rule.** The Employee Retirement Income Security Act of 1974, the federal statute that prescribes fiduciary standards for investing the assets of pension and employee benefit plans, allows a pension or employee benefit plan to provide that "authority to manage, acquire or dispose of assets of the plan is delegated to one or more investment managers . . . ." ERISA § 403(a)(2), 29 U.S.C. § 1103(a)(2). Commentators have explained the rationale for ERISA's encouragement of delegation:

ERISA . . . invites the dissolution of unitary trusteeship. . . . ERISA's fractionation of traditional trusteeship reflects the complexity of the modern pension trust. Because millions, even billions of dollars can be involved, great care is required in investing and safekeeping plan assets. Administering such plans--computing and honoring benefit entitlements across decades of employment and retirement--is also a complex business. . . . Since, however, neither the sponsor nor any other single entity has a comparative advantage in performing all these functions, the tendency has been for pension plans to use a variety of specialized providers. A consulting actuary, a plan

administration firm, or an insurance company may oversee the design of a plan and arrange for processing benefit claims. Investment industry professionals manage the portfolio (the largest plans spread their pension investments among dozens of money management firms).

John H. Langbein & Bruce A. Wolk, Pension and Employee Benefit Law 496 (1990).

**The delegation rule of the 1992 Restatement.** The Restatement of Trusts 3d: Prudent Investor Rule (1992) repeals the nondelegation rule of Restatement of Trusts 2d § 171 (1959), extracted supra, and replaces it with substitute text that reads:

§ 171. Duty with Respect to Delegation. A trustee has a duty personally to perform the responsibilities of trusteeship except as a prudent person might delegate those responsibilities to others. In deciding whether, to whom, and in what manner to delegate fiduciary authority in the administration of a trust, and thereafter in supervising agents, the trustee is under a duty to the beneficiaries to exercise fiduciary discretion and to act as a prudent person would act in similar circumstances.

Restatement of Trusts 3d: Prudent Investor Rule § 171 (1992). The 1992 Restatement integrates this delegation standard into the prudent investor rule of section 227, providing that "the trustee must . . . act with prudence in deciding whether and how to delegate to others . . . ." Restatement of Trusts 3d: Prudent Investor Rule § 227(c) (1992).

**Protecting the beneficiary against unreasonable delegation.** There is an intrinsic tension in trust law between granting trustees broad powers that facilitate flexible and efficient trust administration, on the one hand, and protecting trust beneficiaries from the misuse of such powers on the other hand. A broad set of trustees' powers, such as those found in most lawyer-drafted instruments and exemplified in the Uniform Trustees' Powers Act, permits the trustee to act vigorously and expeditiously to maximize the interests of the beneficiaries in a variety of transactions and administrative settings. Trust law relies upon the duties of loyalty and prudent administration, and upon procedural safeguards such as periodic accounting and the availability of judicial oversight, to prevent the misuse of these powers. Delegation, which is a species of trustee power, raises the same tension. If the trustee delegates effectively, the beneficiaries obtain the advantage of the agent's specialized investment skills or whatever other attributes induced the trustee to delegate. But if the trustee delegates to a knave or an incompetent, the delegation can work harm upon the beneficiaries.

This section is designed to strike the appropriate balance between the advantages and the hazards of delegation. This section authorizes delegation under the limitations of subsections (a) and (b). Subsection (a) imposes duties of care, skill, and caution on the trustee in selecting the agent, in establishing the terms of the delegation, and in reviewing the agent's compliance.

The trustee's duties of care, skill, and caution in framing the terms of the delegation should protect the beneficiary against overbroad delegation. For example, a trustee could not prudently agree to an investment management agreement containing an exculpation clause that leaves the trust without recourse against reckless mismanagement. Leaving one's beneficiaries remediless against willful wrongdoing is inconsistent with the duty to use care and caution in formulating the terms of the delegation. This sense that it is imprudent to expose beneficiaries to broad exculpation clauses underlies both federal and state legislation restricting exculpation clauses, e.g., ERISA §§ 404(a)(1)(D), 410(a), 29 U.S.C. §§ 1104(a)(1)(D), 1110(a); New York Est. Powers Trusts Law § 11-1.7 (McKinney 1967).

Although subsection (c) exonerates the trustee from personal responsibility for the agent's conduct when the delegation satisfies the standards of subsection (a), subsection (b) makes the agent responsible to the trust. The beneficiaries of the trust can, therefore, rely upon the trustee to enforce the terms of the delegation.

**Costs.** The duty to minimize costs that is articulated in Section 4-307 applies to delegation as well as to other aspects of fiduciary investing. In deciding whether to delegate, the trustee must balance the projected benefits against the likely costs. Similarly, in deciding how to delegate, the trustee must take costs into account. The trustee must be alert to protect the beneficiary from "double dipping." If, for example, the trustee's regular compensation schedule presupposes that the trustee will conduct the investment management function, it should ordinarily follow that the trustee will lower its fee when delegating the investment function to an outside manager.

#### **SECTION 4-310. LANGUAGE INVOKING PRUDENT INVESTOR RULE.**

The following terms or comparable language in the provisions of a trust, unless otherwise limited or modified, authorizes any investment or strategy permitted under this [Act]: "investments permissible by law for investment of trust funds," "legal

investments," "authorized investments," "using the judgment and care under the circumstances then prevailing that persons of prudence, discretion, and intelligence exercise in the management of their own affairs, not in regard to speculation but in regard to the permanent disposition of their funds, considering the probable income as well as the probable safety of their capital," "prudent man rule," "prudent trustee rule," "prudent person rule," and "prudent investor rule."

**Comment.**

This provision is taken from the Illinois act, 760 ILCS § 5/5(d) (1992), and is meant to facilitate incorporation of the Act by means of the formulaic language commonly used in trust instruments.

**PART 4.**

**POWERS OF TRUSTEES**

**Section**

**4-401. General Powers; Fiduciary Duties.**

**4-402. Specific Powers.**

**SECTION 4-401. GENERAL POWERS; FIDUCIARY DUTIES.**

(a) A trustee, without authorization by the Court, may exercise:

- (1) the powers conferred by the terms of the trust;
- (2) except as limited by the terms of the trust, powers conferred by this [Act].

(b) This [Part] does not affect the power of the Court to relieve a trustee from restrictions in the terms of the trust on the exercise of powers, to confer on a trustee additional powers whether or not authorized by the terms of the trust, or to

restrict the exercise of a power otherwise given to the trustee by the terms of the trust or this [Act].

(c) The grant of a power to a trustee, whether by the terms of the trust, this [Act], or the Court, does not in itself govern the exercise of the power. In exercising a power, the trustee shall act in accordance with fiduciary principles.

#### **Comment.**

Source: CPC Section 16200-16202.

Subsection (a) is drawn from Sections 2(a) and 3(a) of the Uniform Trustee's Powers Act (1964). The introductory clause clarifies that the trustee has the powers as provided in this section without the need to obtain court authorization. However, if the trustee desires court approval before exercising a power or desires court review after exercise of a power, the procedure provided in Section 6-202 *et seq.* is available.

Subsection (a)(2) gives the trustee the powers listed in Section 4-402 or provided elsewhere in the Act without the need to incorporate them. See, e.g., Section 4-301 (prudent investor rule).

The exercise of powers by the trustee is subject to various important limitations as recognized in this section and as stated elsewhere in the Act. Most importantly, subsection (c) clarifies that the exercise of powers is subject to the trustee's fiduciary duties. See Section 4-201 *et seq.* (fiduciary duties of trustee); Section 4-301 *et seq.* (Uniform Prudent Investor Act). In addition, subsection (a)(2) provides that the exercise of statutory powers is subject to limitations provided in the trust. See also Section 2-201(b) (powers after trust terminates).

Subsection (b) is based on Restatement (Second) of Trusts Section 167 (1959), and UPC Section 5-425. For a provision permitting the court to modify a trust due to unanticipated circumstances, see Section 2-204.

Subsection (c) recognizes that a power granted to the trustee from any source does not necessarily permit the exercise of the power, nor does it prevent the exercise of a power in a manner that conflicts with a general duty if the terms of the trust so direct, or the trustee is directed so to act by a person holding the power to revoke the trust (see Section 3-103(5)). For example, the terms of the trust may give the trustee discretion to favor one beneficiary over the others, in apparent conflict with the general duty to deal with beneficiaries impartially under Section 4-202(a).



**SECTION 4-402. SPECIFIC POWERS OF TRUSTEES.** A trustee may:

(1) collect, hold, and retain trust property received from a settlor or any other person; and the property may be retained even though it includes property in which the trustee is personally interested;

(2) accept additions to the property of the trust from a settlor or any other person;

(3) continue or participate in the operation of a business or other enterprise that is part of the trust property and affect an incorporation, dissolution, or other change in the form of the organization of the business or enterprise;

(4) deposit trust funds in an account in a financial institution, including a financial institution operated by the trustee;

(5) acquire or dispose of property, for cash or on credit, at public or private sale, or by exchange;

(6) manage, control, divide, develop, improve, exchange, partition, change the character of, or abandon trust property;

(7) encumber, mortgage, or pledge trust property for a term within or extending beyond the term of the trust in connection with the exercise of a power vested in the trustee;

(8) make ordinary or extraordinary repairs, alterations, or improvements in buildings or other trust property; demolish improvements; and raze existing or erect new party walls or buildings;

(9) subdivide or develop land; dedicate land to public use;

make or obtain the vacation of plats and adjust boundaries; adjust differences in valuation on exchange or partition by giving or receiving consideration; and dedicate easements to public use without consideration;

(10) enter into a lease for any purpose as lessor or lessee with or without the option to purchase or renew and for a term within or extending beyond the term of the trust;

(11) enter into a lease or arrangement for exploration and removal of gas, oil, or other minerals or geothermal energy, and enter into a community oil lease or a pooling or unitization agreement;

(12) grant an option involving disposition of trust property or take an option for the acquisition of property, including an option that is exercisable beyond the duration of the trust;

(13) with respect to shares of stock of a domestic or foreign corporation, any membership in a nonprofit corporation, or other property;

(i) vote in person, and give proxies to exercise, any voting rights with respect to the shares, memberships, or property;

(ii) waive notice of a meeting or give consent to the holding of a meeting; and

(iii) authorize, ratify, approve, or confirm any action that could be taken by shareholders, members, or property owners;

(14) pay calls, assessments, and any other sums chargeable or accruing against or on account of securities;

(15) sell or exercise stock subscription or conversion rights;

(16) consent, directly or through a committee or other agent, to the reorganization, consolidation, merger, dissolution, or liquidation of a corporation or other business enterprise, and participate in voting trusts, pooling arrangements, and foreclosures, and in connection therewith, deposit securities with and transfer title and delegate discretion to any protective or other committee as the trustee considers advisable;

(17) hold a security in the name of a nominee or in other form without disclosure of the trust so that title to the security may pass by delivery;

(18) deposit securities in a securities depository;

(19) insure the property of the trust against damage or loss and insure the trustee against liability with respect to third persons;

(20) borrow money for any trust purpose to be repaid from trust property;

(21) pay or contest any claim; settle a claim by or against the trust by compromise, arbitration, or otherwise; and release, in whole or in part, a claim belonging to the trust;

(22) pay taxes, assessments, reasonable compensation of the trustee and of employees and agents of the trust, and other expenses incurred in the collection, care, administration, and protection of the trust;

(23) make loans out of trust property to a beneficiary on

terms and conditions the trustee considers to be fair and reasonable under the circumstances; and guarantee loans to the beneficiary by encumbrances on trust property;

(24) pay an amount distributable to a beneficiary, whether or not the beneficiary is under a legal disability, by paying the amount to the beneficiary or by paying the amount to another person for the use or benefit of the beneficiary;

(25) make a distribution of property and money in divided or undivided interests, pro rata or non-pro-rata, and adjust resulting differences in valuation;

(26) employ accountants, attorneys, investment advisers, appraisers or other persons, even if they are associated or affiliated with the trustee, to advise or assist the trustee in the performance of administrative duties;

(27) inspect or investigate property that the trustee has been asked to hold, or property owned or operated by an entity in which the trustee holds or has been asked to hold an interest for the purpose of determining the application of environmental law with respect to the property; and take action to prevent, abate, or otherwise remedy any actual or potential violation of any environmental law affecting property held directly or indirectly by the trustee;

(28) to establish for any asset a reserve for depreciation, depletion or obsolescence, and to decide, in accordance with rules of law, how and in what proportions any receipts or disbursements shall be credited, charged or apportioned as

between principal and income;

(29) execute and deliver instruments that are useful to accomplish or facilitate the exercise of the trustee's powers;

(30) prosecute or defend an action, claim, or proceeding in order to protect trust property and the trustee in the performance of the trustee's duties; and

(31) perform all other actions necessary to accomplish the proper management, investment, and distribution of the trust.

### **Comment.**

Source: CPC Section 16220-16249.

Most of the powers listed in this section are drawn from Section 3 of the Uniform Trustee's Powers Act (1964). Paragraphs (27), (28), and (31) are new, however. In addition, several of the provisions of the Trustee's Powers Act have been modified.

Paragraph (3) authorizes the trustee to continue or incorporate a business. Any such decision by the trustee must be made in light of the standards of prudent investment stated in Part 3 of this article. The authority under this paragraph is broader than that granted under Section 3(c)(3) of the Uniform Trustee's Powers Act. Under the Trustee's Powers Act, a trustee may continue a business only if authorized by the terms of the trust or court order.

Paragraph (5) authorizes a trustee to acquire or dispose of property, for cash or on credit, at public or private sale, or by exchange. Under the Restatement, a trustee may sell on credit only if security is given. Restatement(Second) of Trusts Section 190, comment j (1959).

Paragraph (21) authorizes a trustee to release claims. The determination of when to release a claim depends upon the duties imposed on the trustee. As a general matter, the trustee should be able to release a claim not only when it is uncollectible, but also when it is uneconomical to attempt to collect it. See also Sections 4-211 (duty to enforce claims and defend actions).

Paragraph (22) authorizes a trustee to pay compensation without prior court approval. For other provisions relating to trustees' compensation, see Section 4-109. See also Sections 4-111 (repayment to trustees for expenses incurred), 4-402 (26) (power to hire agents).

Paragraph (23) allows a trustee to make loans to or guarantee loans of a beneficiary upon such terms and conditions the trustee considers fair and reasonable. The determination of what is fair and reasonable must be made in light of the fiduciary duties of the trustee and purposes of the trust. If the

trustee requires security for the loan to the beneficiary, adequate security under this paragraph may consist of a charge on the beneficiary's interest in the trust. See Restatement (Second) of Trusts Section 255 (1959). The interest of a beneficiary that is subject to a spendthrift restraint may not be used for security for a loan under this paragraph. See Section 2-301 *et seq.* (spendthrift protection).

Paragraph (24) allows a trustee to make payments to another person for the use or benefit of the beneficiary. In an appropriate case, a distribution may be made to a custodian under the Uniform Transfers to Minor Act.

Paragraph (25) allows a trustee to make non-pro rata distributions and distribute undivided interests. The trustee also has the power to sell property in order to make the distribution. This paragraph recognizes the authority to take gains and losses into account for tax purposes when making distributions. This power provides needed flexibility and avoids the possibility of a taxable event arising from a non-pro rata distribution.

Paragraph (26) authorizes the hiring of agents. If the trustee is in doubt concerning the propriety of hiring an agent, the judicial procedure under Section 6-202 for obtaining instructions is available. An agent with a close relationship with the trustee or an insider may be hired when it is in the best interests of the trust, taking into account the duty of loyalty and duty to avoid conflicts of interest (see Section 4-202), and particularly as to routine matters, but in situations involving substantial matters, it is best to hire outside agents. The trustee has a duty to inform certain beneficiaries of agents hired, their relationship to the trustee, if any, and their compensation. See also Sections 4-205 (duty to use special skills), and 4-206 (delegation).

Paragraph (27), which addresses possible liability for violations of environmental law, is based on the Texas Trust Code.

Paragraph (30) authorizes a trustee to prosecute or defend an action. As to the propriety of reimbursement for attorney's fees and other expenses of an action or proceeding, see Section 4-111 and comment. See also Sections 4-211 (duty to defend actions), 4-401(c) (exercise of powers subject to fiduciary principles), 4-603 (protection of persons dealing with trustees).

## **PART 5.**

### **LIABILITY OF TRUSTEES TO BENEFICIARIES**

#### **Section**

- 4-501.      Violations of Duties; Breach of Trust.**
- 4-502.      Breach of Trust; Actions.**
- 4-503.      Breach of Trust; Liability.**
- 4-504.      Limitation of Action Against Trustee Following Final Account.**
- 4-505.      Exculpation of Trustee.**

**4-506. Beneficiary's Consent, Release, or Affirmance;  
Nonliability of Trustee.**

**SECTION 4-501. VIOLATIONS OF DUTIES; BREACH OF TRUST.**

(a) A violation by a trustee of a duty the trustee owes a beneficiary is a breach of trust.

(b) The remedies of a beneficiary for breach of trust are exclusively equitable.

**Comment.**

Source: CPC Section 16400, 16421.

Subsection (a) is drawn from Section 201 of the Restatement (Second) of Trusts (1959). While a trust is revocable, the trustee owes duties to the person holding the power to revoke and not to the named beneficiaries. See Section 3-103; see also Section 3-104 (holder of presently exercisable general power of appointment treated as settlor).

Subsection (b) is drawn from Section 197 of the Restatement (Second) of Trusts (1959). For a list of equitable remedies, see Section 4-502. See also Section 4-503 (measure of liability for breach of trust).

**SECTION 4-502. BREACH OF TRUST; ACTIONS.** To remedy a breach of trust which has occurred or may occur, a beneficiary or cotrustee of the trust may request the Court to:

- (1) compel the trustee to perform the trustee's duties;
- (2) enjoin the trustee from committing a breach of trust;
- (3) compel the trustee to redress a breach of trust by payment of money or otherwise;
- (4) appoint a receiver or temporary trustee to take possession of the trust property and administer the trust;
- (5) remove the trustee;
- (6) subject to Section 4-603, nullify an act of the trustee;
- (7) reduce or deny compensation to the trustee;

(8) subject to Section 4-603, impose an equitable lien or a constructive trust on trust property;

(9) subject to Section 4-603, trace trust property wrongfully disposed of and recover the property or its proceeds.

#### **Comment.**

Source: CPC Section 16420.

This section codifies in general terms the remedies available to a beneficiary or cotrustee when a trustee has committed a breach of trust or threatens to do so. The list of remedies is not necessarily exclusive and is not intended to prevent resort to any other appropriate remedy. This section provides a general list of remedies and does not attempt to set out the refinements and exceptions developed over many years by the common law. The availability of a particular remedy listed in this section, and its application under the circumstances, are governed by the common law. See Section 1-103 (common law of trusts). The petitioner may seek any one or more of the remedies listed as is appropriate in the circumstances of the case.

Paragraph (1) is consistent with Restatement (Second) of Trusts Section 199(a) (1959). Paragraph (2) is consistent with Restatement (Second) of Trusts Section 199(b) (1959).

The reference to payment of money in paragraph (3) includes liability that might be characterized as damages, restitution, or surcharge. For the measure of liability, see Section 4-503. The characterization of monetary liability does not affect the fact that the remedies for breach of trust are exclusively equitable, as provided in Section 4-501(b). In certain circumstances, rather than ordering the payment of money, it may be appropriate for the court to order the trustee to transfer tangible property as a remedy for breach of trust. See also Restatement (Second) of Trusts Section 199(c) (1959).

Paragraph (4) makes explicit the authority to appoint a receiver. See also Restatement (Second) of Trusts Section 199(d) (1959). This paragraph also permits appointment of a temporary trustee if appointment of a receiver would be appropriate. See Section 4-105 (appointment of trustee to fill vacancy).

As to paragraph (5), see Restatement (Second) of Trusts Section 199(e) (1959). For provisions governing removing trustees, see Section 4-107 (grounds for removal).

The authority under paragraph (6) to set aside wrongful acts of the trustee is a corollary of the power to enjoin a threatened breach as provided in paragraph (2). As recognized in the introductory clause of paragraph (6), the wrongful acts of the trustee may not be set aside if to do so would impair the rights of bona fide purchasers. See also G. Bogert, *The Law of Trusts and Trustees* Sec. 861, at 16-17 (rev. 2d ed. 1982).

Paragraph (7) is drawn from Section 243 of the Restatement



(Second) of Trusts (1959).

The introductory clauses of paragraphs (6), (8), and (9) recognize that this remedy is limited by the rights of a bona fide purchaser as provided in Section 4-603. See also Restatement (Second) of Trusts Section 202 (1959).

A successor trustee may also have standing to sue for a breach of trust. As to standing generally, see Restatement (Second) of Trusts Section 200.

**SECTION 4-503. BREACH OF TRUST; LIABILITY.** A beneficiary may charge a trustee who commits a breach of trust with the amount required to restore the value of the trust property and trust distributions to what they would have been had the breach not occurred, or, if greater, the amount of profit that the trustee made by reason of the breach.

**Comment.**

This section is based on Restatement (Third) of Trusts-Prudent Investor Rule Section 205 (1992).

If a trustee commits a breach of trust, the beneficiaries may either affirm the transaction or, if a loss has occurred, hold the trustee liable for the amount necessary to fully compensate for the consequences of the breach. This may include lost income, capital gain, or appreciation that would have resulted from proper administration. Even if a loss has not occurred, the trustee may not be allowed to benefit by reason of the trustee's improper action, and is thus accountable for any profit which the trustee may have made by reason of the breach. For extensive commentary on the determination of damages, with numerous specific applications, see Restatement (Third) of Trusts-Prudent Investor Rule Sections 204-213 (1992).

The court is not precluded from reducing or excusing damages if equitable to do so. See Restatement (Second) of Trusts Section 205, comment g (1959).

As to defenses of the trustee, see Sections 4-504 to 4-506.

The remedies provided in this section do not preclude resort to other remedies provided by this Act or available under the common law. See Sections 1-103 (common law of trusts), and 4-502 (breach of trust; actions).

**SECTION 4-504. LIMITATION OF ACTION AGAINST TRUSTEE  
FOLLOWING FINAL ACCOUNT.**

(a) Unless previously barred by adjudication, consent, or other limitation, a claim against a trustee for breach of trust is barred as to a beneficiary who has received a final account or other report adequately disclosing the existence of the claim unless a proceeding to assert the claim is commenced within two years after the latter of (i) the receipt of the account or report, or (ii) the termination of the trust relationship between the trustee and beneficiary. An account or report adequately discloses the existence of a claim if it provides sufficient information so that the beneficiary knows of the claim or reasonably should have inquired into its existence.

(b) For the purpose of subsection (a), a beneficiary is deemed to have received an account or report:

(1) In the case of an adult who is reasonably capable of understanding the account or report, if it is received by the adult personally.

(2) In the case of an adult who is not reasonably capable of understanding the account or report, if it is received by the adult's legal representative, including a guardian ad litem or other person appointed for this purpose.

(3) In the case of a minor, if it is received by the minor's guardian or conservator or, if the minor does not have a guardian or conservator, if it is received by a parent of the minor who does not have a conflict of interest.

**Comment.**

Source: CPC Section 16460.

This section is drawn in substantial part from Section 7-307

of the Uniform Probate Code. For provisions governing consent, release, and affirmance by beneficiaries to relieve the trustee of liability, see Section 4-506. The reference in the introductory clause to claims previously barred also includes principles such as estoppel and laches that apply under the common law. See Section 1-103 (common law of trusts). During the time that a trust is revocable, the person holding the power to revoke is the one who must receive the account or report in order to commence the running of the limitations period provided in this section. See Sections 3-103 (limits on rights of beneficiary of revocable trust).

Subsection (b) provides special rules concerning who must receive the account or report for it to have the effect of barring claims based on the information disclosed. Under subsection (b)(2) it may be appropriate to seek the appointment of a guardian ad litem or some other person to receive accounts and reports if no guardian or conservator has been appointed for the person and there is serious doubt that the beneficiary can understand the account or report. See Section 6-206 (appointment of guardian ad litem).

For the provisions relating to the duty to report information and account to beneficiaries, see Section 4-213.

**SECTION 4-505. EXCULPATION OF TRUSTEE.** A provision in the terms of the trust relieving a trustee of liability for breach of trust is unenforceable to the extent that it:

(1) relieves a trustee of liability for breach of trust committed intentionally, with gross negligence, in bad faith, or with reckless indifference to the interest of the beneficiary, or for any profit derived by the trustee from the breach; or

(2) was inserted as the result of an abuse by the trustee of a fiduciary or confidential relationship to the settlor.

**Comment.**

Source: CPC Section 16461.

This section is the same in substance as Section 222 of the Restatement (Second) of Trusts (1959), except that the reference to gross negligence does not appear in the Restatement. There is a distinction between an exculpatory provision and the negation of a duty. While the terms of the trust may negate a duty (see Section 4-201(b)), if the trustee is required under the terms of the trust or this Act to perform the duty, the trustee may not be

totally absolved from liability for a breach. See Restatement (Second) of Trusts Section 222 comments b & c (1959).

#### **SECTION 4-506. BENEFICIARY'S CONSENT, RELEASE, OR**

**AFFIRMANCE; NONLIABILITY OF TRUSTEE.** A beneficiary may not hold a trustee liable for a breach of trust if the beneficiary (i) consented to the conduct constituting the breach, (ii) released the trustee from liability for the breach , or (iii) affirmed the transaction constituting the breach unless:

(1) the beneficiary at the time of the consent, release, or affirmance did not know of the beneficiary's rights and of the material facts the trustee knew or should have known and the trustee did not reasonably believe that the beneficiary knew; or

(2) the consent, release, or affirmance of the beneficiary was induced by improper conduct of the trustee.

#### **Comment.**

Source: CPC Section 16463-16465.

This section is drawn from Sections 216 to 218 of the Restatement (Second) of Trusts (1959). When one beneficiary has consented but others have not, courts give a remedy to the nonconsenting beneficiaries. Restatement (Second) of Trusts Section 216, comment h. But consent by the settlor of a revocable trust binds all the beneficiaries under Section 3-103. See also Section 3-104 (consent by holder of a presently exercisable general power of appointment).

Restatement (Second) of Trusts Section 218, comment d, states that its rule relating to affirmance applies only to breaches which give beneficiaries the option to affirm or disaffirm, but that in other cases the trustee may be protected by laches.

### **PART 6. RIGHTS OF THIRD PERSONS**

#### **Section**

**4-601. Personal Liability; Limitations.**

**4-602. Dissenting Cotrustees.**

- 4-603.      **Protection of Third Persons.**
- 4-604.      **Certification of Trust.**
- 4-605.      **Liability for Wrongful Taking, Concealing of Disposing  
                 of Trust Property.**

**SECTION 4-601.    PERSONAL LIABILITY; LIMITATIONS.**

(a) Except as otherwise provided in the contract or in this [Part], a trustee is not personally liable on a contract properly entered into in the trustee's fiduciary capacity in the course of administration of the trust unless the trustee fails to reveal the representative capacity or identify the trust in the contract.

(b) A trustee is personally liable for obligations arising from ownership or control of trust property or for torts committed in the course of administering a trust only if the trustee is personally at fault.

(c) A claim based on a contract entered into by a trustee in the trustee's representative capacity, on an obligation arising from ownership or control of trust property, or on a tort committed in the course of administering a trust may be asserted against the trust by proceeding against the trustee in the trustee's representative capacity, whether or not the trustee is personally liable on the claim.

(d) A question of liability as between the trust and the trustee personally may be determined in a proceeding under Section 6-202.

**Comment.**

Source: CPC Section 18000-18002, 18004-18005.  
This section is drawn from Section 7-306 of the Uniform

Probate Code (1977). However, unlike the Uniform Probate Code, this section excuses the trustee from personal liability on a contract if *either* the trustee's representative capacity or the identity of the trust is revealed in the contract. Under this section, it is assumed that either one of these statements in a contract puts the person contracted with on notice of the fact that the other person is a trustee. The protection afforded the trustee by this section applies only to contracts that are properly entered into in the trustee's fiduciary capacity, meaning that the trustee is exercising an available power and is not violating a duty. This section does not excuse any liability the trustee may have for breach of trust. To fall within the rule of subsection (a), either the trustee's status or the identity of the trust must be revealed.

Under subsection (b), a trustee is "personally at fault" when the trustee, either intentionally or negligently, acts, or fails to act, or commits a tort either intentionally or negligently. Restatement (Second) of Trusts Section 264 makes a trustee liable regardless of fault, including liability for acts of agents under respondeat superior.

Subsection (c) alters the case law rule that the trustee could not be sued in a representative capacity if the trust estate was not liable.

Under subsection (d), ultimate liability between an estate and trustee need not be determined before the third person's claim can be satisfied. It is permissible, and may be preferable, for judgment to be entered against the trust without determining the trustee's ultimate liability until later. If judgment is entered against the trustee individually, the question of the trustee's right to reimbursement may be settled informally with the beneficiaries or in a separate proceeding in the probate court. For rules governing indemnification of trustees, see Section 4-111. See also Section 6-201 *et seq.* (proceedings against trustee by beneficiary).

#### **SECTION 4-602. DISSENTING COTRUSTEES.**

(a) A cotrustee who does not join in exercising a power is not liable to a third person for the consequences of the exercise of the power.

(b) A dissenting cotrustee who joins in an action at the direction of the majority cotrustees is not liable to a third person for the action if the dissenting cotrustee expresses the dissent in writing to any other cotrustee at or before the action is taken.

(c) This section does not excuse a cotrustee from liability for failure to discharge a cotrustee's duties as a trustee.

**Comment.**

Source: CPC Section 18003.

This section is drawn from Section 114.006(a) of the Texas Trust Code. See Tex. Prop. Code Ann. Sec. 114.006 (Vernon 1984).

As to the duties of cotrustees, see Sections 4-208. Under Section 4-103, cotrustees may act by majority vote unless otherwise provided by the terms of the trust.

**SECTION 4-603. OBLIGATIONS OF THIRD PERSONS.**

(a) With respect to a third person dealing with a trustee or assisting a trustee in the conduct of a transaction, if the third person acts in good faith and for a valuable consideration and without knowledge that the trustee is exceeding the trustee's powers or improperly exercising them:

(1) A third person is not bound to inquire as to whether a trustee has power to act or is properly exercising a power and may assume without inquiry the existence of a trust power and its proper exercise;

(2) A third person is fully protected in dealing with or assisting a trustee, as if the trustee has and is properly exercising the power the trustee purports to exercise.

(b) A third person who acts in good faith is not bound to ensure the proper application of trust property paid or delivered to the trustee.

(c) If a third person acting in good faith and for a valuable consideration enters into a transaction with a former trustee without knowledge that the person is no longer a trustee,

the third person is fully protected as if the former trustee were still a trustee.

**Comment.**

Source: CPC Section 18100.

This section is drawn from Section 7 of the Uniform Trustees' Powers Act (1964).

**SECTION 4-604. CERTIFICATION OF TRUST.**

(a) A trustee may present a certification of trust to any person in lieu of providing a copy of the trust instrument to establish the existence or terms of the trust.

(b) The certification must contain a statement that the trust has not been revoked, modified, or amended in any manner which would cause the representations contained in the certification of trust to be incorrect and must contain a statement that it is being signed by all of the currently acting trustees of the trust.

(c) A certification of trust need not contain the dispositive provisions of the trust which set forth the distribution of the trust estate.

(d) A person may require that the trustee offering the certification of trust provide copies of those excerpts from the original trust instrument and amendments thereto which designate the trustee and confer upon the trustee the power to act in the pending transaction.

(e) A person who acts in reliance upon a certification of trust without knowledge that the representations contained therein are incorrect is not liable to any person for so acting



and may assume without inquiry the existence of the facts contained in the certification. Knowledge may not be inferred solely from the fact that a copy of all or part of the trust instrument is held by the person relying upon the trust certification. A transaction, and a lien created thereby, entered into by the trustee and a person acting in reliance upon a certification of trust is enforceable against the trust assets.

(f) A person making a demand for the trust instrument in addition to a certification of trust or excerpts shall be liable for damages, including attorney's fees, incurred as a result of the refusal to accept the certification of trust or excerpts in lieu of the trust instrument if the Court determines that the person acted in bad faith in requesting the trust instrument.

(g) This section does not limit the rights of beneficiaries to obtain copies of the trust instrument or rights of others to obtain copies in a proceeding concerning the trust.

**Comment.**

Source: CPC Section 18100.5.

**SECTION 4-605. LIABILITY FOR WRONGFUL TAKING, CONCEALING OF DISPOSING OF TRUST PROPERTY.** A person who, in bad faith, wrongfully takes, conceals, or disposes of trust property is liable for twice the value of the property, recoverable in an action by a trustee for the benefit of the trust.

**Comment.**

Source: CPC Section 16249(b).

## ARTICLE 5. CHARITABLE TRUSTS.

### Section

- 5-101. Charitable Purposes.
- 5-102. Application of Cy Pres.
- 5-103. Trust with Uneconomically Low Value.
- 5-104. Interested Persons; Proceedings.

**SECTION 5-101. CHARITABLE PURPOSES.** A charitable trust may be created for the relief of poverty, the advancement of education or religion, the promotion of health, or any other purpose the accomplishment of which is beneficial to the community. If the terms of the trust do not indicate a particular charitable purpose or beneficiaries, the trustee may select one or more charitable purposes or beneficiaries.

### **Comment.**

The purpose of this Article is to substantially broaden the authority of courts and trustees to make charitable gifts more effective. Many of the concepts expressed in this Article are not new, but reflect the views of commentators. See, e.g., Report, Cy Pres and Deviation: Current Trends and Application, 8 Real Prop. Prob. & Trust J. 391 (1971); Roger G. Sisson, Relaxing the Dead Head's Grip: Charitable Efficiency and the Doctrine of Cy Pres, 74 Va. L. Rev. 635 (1988); Kenneth L. Karst, The Efficiency of the Charitable Dollar: An Unfulfilled State Responsibility, 73 Harv. L. Rev. 433 (1960); Joseph A. DiClerico, Jr., Cy Pres: A Proposal for Change, 47 B.U.L. Rev. 153 (1967). A liberalizing trend is also apparent in a number of the state statutes, with the reforms in Wisconsin, from which this Article borrows extensively, being the most notable. See Wis. Stat. Ann. Sec. 701.10.

Section 5-101, unlike the remainder of the Article, does not break significant new ground, but merely restates the well-established categories of charitable purposes listed in Restatement (Second) of Trusts Section 368 and ultimately derived from the Statute of Charitable Uses, Eliz. I, c.4 (1601).

This section also ratifies a common estate planning technique whereby the trustee is granted discretion to distribute the trust property for any charitable purpose or beneficiary. See Restatement (Second) of Trusts Section 396 (1959).

**SECTION 5-102. APPLICATION OF CY PRES.** Unless the terms of the trust provide expressly to the contrary:

(1) A charitable trust does not fail, in whole or in part, if a particular purpose for which the trust was created becomes impracticable, unlawful, or impossible to fulfill;

(2) If a particular charitable purpose for which a trust was created becomes impracticable, unlawful or impossible to fulfill, the Court may modify the terms of the trust or direct that the property of the trust be distributed in whole or in part to one or more charitable entities. If an administrative provision of a charitable trust becomes impracticable, unlawful, impossible to fulfill or otherwise impairs the effective administration of the trust, the Court may modify the provision. Before modifying or terminating a charitable trust the Court shall consider the current and future community needs in the general field of charity for which the trust was created, the settlor's other charitable interests, and the value of the available trust property.

**Comment.**

This section codifies the court's inherent authority to apply cy pres. The power may be applied to modify an administrative or dispositive provision. The court may order the trust terminated and distributed to other charitable entities. Partial termination may also be ordered if the trust property is more than sufficient to satisfy the trust's current purpose. Cy pres under the Act is a default rule. The court's authority is subject to the settlor's right to specify an alternate disposition.

This section also modifies the doctrine of cy pres. Under traditional doctrine, if a specific charitable purpose becomes impossible to fulfill, the courts embark on an elusive hunt to determine whether the settlor had a general charitable intent.

If so, the trust property is diverted to other charitable purposes. But if not, the trust fails. This section is built on the assumption that in the great majority of cases the settlor would prefer that the gift be used for other charitable purposes rather than fail. Consequently, unless the terms of the trust provide expressly to the contrary, a charitable trust does not fail in whole or in part if the particular purpose for which the trust was created becomes impracticable, unlawful, or impossible to fulfill.

The court must consider several factors when applying cy pres. The list is by no means exclusive. The application of cy pres involves a difficult balancing of the needs of society against an assessment of the settlor's probable intent. In determining the settlor's probable intent, the court must consider the current and future community needs in the general field of charity for which the trust was created, the settlor's other charitable interests, and the value of the available trust property.

#### **SECTION 5-103. TRUST WITH UNECONOMICALLY LOW VALUE.**

(a) If the value of the trust property of a charitable trust falls to less than [\$50,000], the trustee may terminate the trust and distribute the trust property to any alternate takers designated by the terms of the trust, or if none, to one or more charitable entities in the general field of charity for which the trust was created or which reflect the settlor's other charitable interests.

(b) On petition by a trustee or other interested person, if the Court determines that the value of the trust property is insufficient to justify the cost of administration involved, the Court may appoint a new trustee or modify or terminate the trust.

#### **Comment.**

Subsection (a) strives to make charitable gifting more effective by permitting the nonjudicial termination of small charitable trusts, thereby avoiding the expense of a judicial termination proceeding. Nonjudicial termination is allowed if the value of the trust property falls to less than \$50,000. While

the creation of small charitable trusts is not encouraged, subsection (a) does not interfere with the right of a settlor to create such a trust. Under this subsection, the trustee may not terminate a charitable trust which has never exceeded \$50,000 in value.

Subsection (b) authorizes the court to terminate a charitable trust. Unlike subsection (a), there is no dollar limit. In order to reduce administrative costs in relation to the size of the trust, the court, instead of terminating the trust, may appoint a new trustee. Upon termination of the trust, the trust property is to be distributed as provided in Section 5-102.

For the comparable provision on termination of small noncharitable trusts, see Section 2-205.

**SECTION 5-104. INTERESTED PERSONS; PROCEEDINGS.** The settlor, the trustee, the attorney general, and any charitable entity to which trust property must be distributed under the terms of the trust shall be interested persons in any proceeding brought under this section.

**Comment.**

This section modifies the definition of "interested person" but only in the context of charitable trusts. See Section 1-102(10) ("interested person" defined). This section, which authorizes a settlor to enforce a charitable trust, is contrary to the common law. Compare Restatement (Second) of Trusts Section 391 (1959).

**ARTICLE 6. PROCEEDINGS CONCERNING TRUSTS**

**Part**

- 1. Jurisdiction and Venue.**
- 2. Judicial Proceedings Concerning Trusts.**
- 3. Nonjudicial Settlement.**

**PART 1. JURISDICTION AND VENUE**

**Section**

- 6-101. Subject Matter Jurisdiction.**
- 6-102 Principal Place of Administration of Trust.**
- 6-103. Jurisdiction Over Trustees and Beneficiaries.**
- 6-104. County of Venue.**
- 6-105. Transfer of Jurisdiction.**

**SECTION 6-101. SUBJECT MATTER JURISDICTION.**

(a) The Court has exclusive jurisdiction of proceedings concerning the internal affairs of a trust.

(b) The Court has concurrent jurisdiction of actions and proceedings to determine the existence of a trust; actions and proceedings by or against creditors or debtors of trusts; and other actions and proceedings involving trustees and third persons.

**Comment.**

Source: CPC Section 17000.

Subsection (a) of this section is drawn from the first sentence of Section 7-201(a) of the Uniform Probate Code. This section provides for exclusive jurisdiction in the court in matters involving the internal affairs of trusts. Subsection (b) is drawn from Section 7-204 of the Uniform Probate Code.

**SECTION 6-102. PRINCIPAL PLACE OF ADMINISTRATION OF TRUST.**

(a) The principal place of administration of a trust is the usual place where the day-to-day activity of the trust is carried on by the trustee or the trustee's representative who is primarily responsible for the administration of the trust.

(b) If the principal place of administration of the trust cannot be determined under subsection (a), it must be determined as follows:

(1) If the trust has one trustee, the principal place of administration of the trust is the trustee's residence or usual place of business.

(2) If the trust has more than one trustee, the principal place of administration of the trust is the residence

or usual place of business of any of the cotrustees as agreed upon by them or, if not, the residence or usual place of business of any of the cotrustees.

**Comment.**

Source: CPC Section 17002.

Section 6-105 governs transfers of trusts to and from other jurisdictions.

**SECTION 6-103. JURISDICTION OVER TRUSTEES AND BENEFICIARIES.**

(a) By accepting the trusteeship of a trust having its principal place of administration in this State, the trustee submits personally to the jurisdiction of the Court.

(b) To the extent of their interests in the trust, all beneficiaries of a trust having its principal place of administration in this State are subject to the jurisdiction of the Court.

**Comment.**

Source: CPC Section 17003.

This section, which is intended to facilitate the exercise of the court's power, is drawn from Section 7-103 of the Uniform Probate Code. As recognized by the introductory clause, constitutional limitations on assertion of jurisdiction apply to the exercise of jurisdiction under this section. Consequently, appropriate notice must be given to a trustee or beneficiary as a condition of jurisdiction under this section. See, e.g., *Mullane v. Central Hanover Bank & Trust Co.*, 339 U.S. 306 (1950). This section does not limit the jurisdiction of the court over the trust, trust property, or parties to the trust. See also Sections 4-101 (methods of trustee acceptance), 3-103 (notice to beneficiary of revocable trust).

A state continues to have jurisdiction over a trustee who moves to another state. See Restatement (Second) of Trusts Section 199, comment f.

**SECTION 6-104. COUNTY OF VENUE.**

(a) A proceeding under this [Act] shall be commenced in the [county] in which the trust's principal place of administration

is or is to be located, and if the case trust is created by will, in the [county] in which the decedent's estate is administered.

(b) If a trust not created by will has no trustee, a proceeding for appointing a trustee shall be commenced in the [county] in which either a beneficiary resides or the trust property, or some portion of the trust property, is located.

(c) Except as otherwise provided in subsections (a) and (b), a proceeding under this [Act] shall be commenced in accordance with the rules applicable to civil actions generally.

#### **Comment.**

Source: CPC Section 17005, 17452.

See Section 6-102 (principal place of administration of trust).

Subsection (b) applies only to appointment of a trustee for a trust not created by will. Proceedings to appoint a trustee for a trust created by will that has no trustee are commenced in the county where the decedent's estate is administered. See subsection (a).

Subsection (c), which is drawn from Section 7-204 of the Uniform Probate Code, provides venue rules applicable in cases not covered by subsections (a) and (b). This would include cases where jurisdiction over a trust, trust property, or parties to a trust is based on a factor other than the presence of the principal place of administration in this state. When the principal place of administration of a trust is in another state, but jurisdiction is proper in this State, the general rules governing venue apply.

#### **SECTION 6-105. TRANSFER OF JURISDICTION.**

(a) The Court may transfer the place of administration of a trust to or from this State or transfer some or all of the trust property to a trustee in or outside this State if it finds that:

(1) the transfer of the trust property to a trustee in this or another jurisdiction, or the transfer of the place of administration of the trust to this or another jurisdiction, will



promote the best interest of the trust and those interested in it, taking into account the economical and convenient administration of the trust;

(2) the transfer does not violate the terms of the trust;

(3) any new trustee to whom the trust property is to be transferred is qualified, willing, and able to administer the trust or trust property under the terms of the trust; and

(4) if the trust or any portion of the trust property is to be transferred to another jurisdiction and if approval of the transfer by the other court is required under the law of the other jurisdiction, the proper court in the other jurisdiction has approved the transfer.

(b) If a transfer is ordered, the Court may direct the manner of transfer and impose terms and conditions as may be just, including a requirement for the substitution of a successor trustee in any pending litigation in this State. A delivery of property in accordance with the order of the Court is a full discharge of the trustee with respect to all property embraced in the order.

(c) If the Court grants a petition to transfer a trust or trust property to this State, the Court shall require the trustee to give a bond, if necessary under the law of the other jurisdiction or of this State, and may require bond as provided in Section 4-102.

**Comment.**

Source: CPC Sections 17401, 17404, 17405, 17451, 17455-17457.

This section is not limited to transfers to or from other states, but may include a transfer to or from different countries. See also Section 6-101 (subject matter jurisdiction of court).

This section provides a method whereby the court can indicate its willingness to accept jurisdiction over a trust administered in another jurisdiction if the law of the other jurisdiction requires appointment of a trustee in the proposed new place of administration before approving the transfer. See, e.g., Mass. Gen. Laws Ann. ch. 206, Sec. 29 (West 1969).

If appropriate to facilitate transfer of the trust property or the place of administration of a trust to this State, the Court may issue a conditional order appointing a trustee to administer the trust in this State and indicating that transfer to this State will be accepted if transfer is approved by the proper court of the other jurisdiction.

Under this section a transferred trust is treated the same as a trust that was created in this State, and so is governed by this Act. This section is not intended to provide choice of law rules. A trust that was subject to judicial supervision in another state will not be subject to continuing court jurisdiction unless the terms of the trust so provide and the court so determines in the order accepting transfer to this state.

## **PART 2. JUDICIAL PROCEEDINGS CONCERNING TRUSTS**

### **Section**

- 6-201. Judicial Intervention Intermittent**
- 6-202. Petitions; Purposes of Proceedings.**
- 6-203. Beneficiaries Request for Special Notice.**
- 6-204. Reformation; Tax Objectives.**
- 6-205. Virtual Representation; Notice of Proceeding.**
- 6-206. Appointment of Guardian Ad Litem.**

**SECTION 6-201. JUDICIAL INTERVENTION INTERMITTENT.** The administration of trusts shall proceed expeditiously and free of judicial intervention, except to the extent the jurisdiction of the Court is invoked by interested parties or otherwise exercised as provided by law.

### **Comment.**

Source: CPC Section 17209.

Uniform Probate Code Section 7-201(b) contains similar language. See also Section 4-401. As to the jurisdiction of the court, see Part 1 of this article.

**SECTION 6-202. PETITIONS; PURPOSES OF PROCEEDINGS.**

(a) Except as otherwise provided in Section 3-103, a trustee or beneficiary of a trust may petition the Court under this [Part] concerning the internal affairs of the trust or to determine the existence of the trust.

(b) Proceedings concerning the internal affairs of a trust include proceedings to:

- (1) construe and determine the terms of a trust;
- (2) determine the existence of any immunity, power, privilege, duty or right;
- (3) determine the validity of a trust provision;
- (4) ascertain beneficiaries and determine to whom property shall pass or be delivered upon final or partial termination of the trust;
- (5) settle accounts and pass upon the acts of the trustee, including the exercise of discretionary powers;
- (6) instruct the trustee;
- (7) compel the trustee to report information about the trust or account to the beneficiary;
- (8) grant powers to the trustee;
- (9) fix or allow payment of the trustee's compensation or review the reasonableness of the compensation;
- (10) appoint or remove a trustee;
- (11) accept the resignation of a trustee;

- (12) compel redress of a breach of trust by any available remedy;
- (13) approve or direct the modification or termination of the trust;
- (14) approve or direct the combination or division of trusts;
- (15) authorize or direct transfer of a trust or trust property to or from another jurisdiction;
- (16) determine liability of a trust for debts or the expenses of administration of the estate of a deceased settlor;
- (17) determine any other issue that will aid in the administration of the trust.

**Comment.**

Source: CPC Section 17200(a).

The introductory clause of this section has the effect of giving the right to petition concerning the internal affairs of a revocable trust to the settlor (or other person holding the power to revoke) instead of the beneficiaries during the time that the holder has capacity. See Section 3-103 and comment.

The items listed in subsection (b) are illustrative and not exclusive. The court has jurisdiction to hear any matter involving the administration of the trust. See Section 6-101. The procedure provided in this Part is available to determine matters concerning the administration of trusts notwithstanding a purported limitation or exclusion in the terms of the trust.

**SECTION 6-203. BENEFICIARIES REQUEST FOR SPECIAL NOTICE.**

(a) If proceedings involving a trust are pending, a beneficiary of the trust may file with the clerk of the court in which the proceeding is pending a written request stating that the beneficiary desires special notice of the filing of petitions and motions in the proceeding and giving an address for receiving

notice by mail. A copy of the request must be personally delivered or mailed to the trustee or the trustee's attorney. If personally delivered, the request is effective when it is delivered. If mailed, the request is effective when it is received. The original of the request must be filed with the court clerk, and be accompanied by a written admission or proof of service. A request for special notice may be modified or withdrawn in the same manner as provided for the making of the initial request.

(b) A request for special notice made by a beneficiary whose right to notice is restricted by Section 3-103 is not effective.

**Comment.**

Source: CPC Section 17204.

Subsection (b) makes clear that the restrictions on rights of beneficiaries of revocable trusts apply to the right to request special notice. Sections 6-205 and 6-301 *et. seq.* limit the need to give notice to certain beneficiaries with future interests but do not restrict the right of such beneficiaries to request special notice.

**SECTION 6-204. REFORMATION; TAX OBJECTIVES.**

(a) The terms of a trust shall be liberally construed to conform to the settlor's intent.

(b) The terms of a trust may be reformed to conform to the settlor's intention if the failure to conform was due to a mistake of fact or law and the settlor's intent can be established.

(c) The terms of a trust may be construed or modified, in a manner that does not violate the settlor's probable intention, to achieve the settlor's tax objectives.

**Comment.**

This section is based in part on Restatement (Third) of Property-Donative Transfers Section 12.1-12.2 (Tent. Draft No.1, 1995).

**SECTION 6-205. VIRTUAL REPRESENTATION; NOTICE OF PROCEEDING.**

(a) In proceedings involving trusts, and in judicially supervised settlements, persons are bound by orders binding others as follows:

(1) Orders binding the sole holder or all coholders of a power of revocation or a presently exercisable general power of appointment, including one in the form of a power of amendment, bind other persons to the extent their interests (as objects, takers in default, or otherwise) are subject to the power.

(2) To the extent there is no conflict of interest between the representor and those represented: (i) orders binding a conservator bind the person whose estate the conservator controls; (ii) orders binding a guardian bind the ward if no conservator of the ward's estate has been appointed; (iii) orders binding a trustee bind beneficiaries of the trust; (iv) orders binding a personal representative bind the persons interested in the undistributed assets of the decedent's estate; and (v) orders binding a sole holder or all co-holders of a general testamentary power of appointment bind other persons whose interests (as objects, takers in default, or otherwise) are subject to the power. If there is no conflict of interest and no conservator or guardian has been appointed, a parent may represent and bind a minor child.

(3) Unless otherwise represented, a minor or an incapacitated, unborn, or unascertained person is bound by an order to the extent the person's interest is adequately represented by another party having a substantially identical interest in the proceeding.

(b) Notice shall be given to every interested person or to one who can bind an interested person as described in subsection (a)(1) or (2). Notice may be given to a person and to another who may bind the person. Notice is given to unborn or unascertained persons, who are not represented under subsection (a)(1) or (2), by giving notice to all known persons whose interests in the proceedings are substantially identical to those of the unborn or unascertained persons.

**Comment.**

Source: Unif. Probate Code Sec. 1-403(1)-(3).

**SECTION 6-206. APPOINTMENT OF GUARDIAN AD LITEM.** At any point in a judicial proceeding, a Court may appoint a guardian ad litem to represent the interest of a minor, an incapacitated, unborn, or unascertained person, or a person whose identity or address is unknown, if the Court determines that representation of the interest otherwise would be inadequate. If not precluded by conflict of interest, a guardian ad litem may be appointed to represent several persons or interests. The Court shall set out its reasons for appointing a guardian ad litem as a part of the record of the proceeding. In approving a judicially supervised settlement, a guardian ad litem may consider general family

benefit.

**Comment.**

Source: Unif. Probate Code Sec. 1-403(4).

**PART 3. NONJUDICIAL SETTLEMENT.**

**Section**

- 6-301. Nonjudicial Settlement; Definition and Applicability.**
- 6-302. Representation By Holders of Powers**
- 6-303. Representation By Fiduciaries and Parents.**
- 6-304. Representation of Future Interests.**
- 6-305. Appointment of Special Representative.**

**SECTION 6-301. NONJUDICIAL SETTLEMENT; DEFINITION AND APPLICABILITY.**

(a) For purposes of this [Part], a "fiduciary matter" includes any item listed in Section 6-202(b).

(b) Without approval of Court, persons interested in a fiduciary matter may agree to a nonjudicial settlement and may represent and bind other persons interested in the fiduciary matter as provided in this [Part].

(c) This [Part] does not apply to the extent the terms of the trust indicate a contrary intent.

**SECTION 6-302. REPRESENTATION BY HOLDERS OF POWERS.**

The holders or all coholders of a power of revocation or presently exercisable general power of appointment, including one in the form of a power of amendment, may represent and bind the



persons whose interests (as objects, takers in default, or otherwise) are subject to the power. Person whose interests are subject to a general testamentary power of appointment may be represented and bound by the holder or holders of the power but only to the extent there is no conflict of interest with respect to the fiduciary matter between the holders and the persons represented.

**SECTION 6-303. REPRESENTATION BY FIDUCIARIES AND PARENTS.** To the extent there is no conflict of interest between the representor and those represented with respect to the fiduciary matter:

(1) a conservator may represent and bind the estate the conservator controls;

(2) a guardian may represent and bind the ward if no conservator of the ward's estate has been appointed;

(3) a trustee may represent and bind the beneficiaries of the trust;

(4) a personal representative may represent and bind the persons interested in the estate; and

(5) if no conservator or guardian has been appointed, a parent may represent and bind a minor child.

**SECTION 6-304. REPRESENTATION OF FUTURE INTERESTS.** Unless otherwise represented, and to the extent there is no conflict of interest between them and the persons represented with respect to the fiduciary matter;

(1) a beneficiary currently entitled or eligible to receive

income or principal of the trust may represent and bind the person or persons who may succeed to the trust property in whole or in part upon termination of that beneficiary's interest;

(2) an adult and ascertained beneficiary with capacity may represent and bind a minor, incapacitated, unborn or unascertained person who is a beneficiary of the same class gift;

(3) if an interest is in a class none of whose members are yet ascertained, the person or class of persons who would be entitled to the interest if the event making the interest future in enjoyment had occurred immediately before the nonjudicial settlement may represent and bind those class members and potential class members who are not so entitled; and

(4) a beneficiary of an interest which is conditioned on the occurrence of a future event or combination of future event may represent and bind the person or persons who would succeed to that interest, in whole or in part, upon the occurrence of an additional event or combination of events.

**SECTION 6-305. APPOINTMENT OF SPECIAL REPRESENTATIVE.** In connection with a nonjudicial settlement, the Court may appoint a special representative to represent the interests of designated parties. If not precluded by conflict of interest, a special representative may be appointed to represent several persons or interests. In approving a settlement, a special representative may consider general family benefit.

## **ARTICLE 7. TRANSITIONAL PROVISIONS**

### **Section**

#### **7-101. General Rule Concerning Application of [Act].**

#### **SECTION 7-101. GENERAL RULE CONCERNING APPLICATION OF [ACT] .**

(a) This [Act] takes effect on \_\_\_\_\_.

(b) On and after the effective date, this [Act] applies to all trusts regardless of whether they were created before, on, or after its effective date.

(c) This [Act] applies to all proceedings concerning trusts commenced on or after its effective date.

(d) This [Act] applies to all proceedings concerning trusts commenced before its effective date unless the Court finds that application of a particular provision of this [Act] would substantially interfere with the effective conduct of the proceedings or the rights of the parties or other interested persons, in which case the particular provision of this [Act] does not apply and prior law applies.

#### **Comment.**

Source: CPC Section 15001.

This section provides the general rule governing the application of this Act to administration of existing trusts and pending proceedings involving trusts. For a comparable provision, see Section 8-101 of the Uniform Probate Code.

For effective dates applicable to particular matters under California law but not reproduced in this draft, see California Probate Code Sections 15401(e) (rules governing method of revocation by settlor), 16042 (interpretation of the trust terms concerning legal investments), 16062 (application of duty to account annually to beneficiaries), 16203 (application of rules governing trustees' powers), 16401(c) (application of rules

governing trustees' liability to beneficiary for acts of cotrustee), 16403(c) (application of rules governing trustees liability to beneficiary for acts of predecessor trustee), 18000(b) (application of rule governing personal liability of trustee to third persons on contracts).