Trusts, Estates & Tax Alert
August 1, 2016

Trust Act 2016 Legislative Update

On July 29, 2016, Delaware’s Governor, Jack Markell, signed new trust legislation into law that modifies Delaware’s nonjudicial settlement agreement (“NJSA”) statute, 12 Del. C. § 3338, to expand the utility and availability of Delaware NJSAs, and adds a new statute, 12 Del. C. §3342, that provides for modification of trusts if the trustor is living, upon consent or non-objection of all interested persons.

Section 3342 – Modification of Trust By Consent While Trustor Is Living.

New Section 3342 of Title 12 enables any trust, even an irrevocable trust, to be modified to include any provision that can be included in the governing instrument of a trust that is created upon the date of the modification upon the written consent or written non-objection of the trustor, all then living fiduciaries, and all beneficiaries. The interests of all beneficiaries must be adequately represented either directly or through virtual representation under 12 Del. C. § 3547. The statute applies to Delaware trusts even if there is a provision of law or a provision in the trust’s governing instrument limiting or prohibiting the amendment of the trust.

Modifications pursuant to Section 3342 can include any provision that trustors can include in the governing instrument of a trust that is created upon the date of the modification and there is no limitation on modifications that violate a material purpose of the trust. This means that modifications can include the addition or modification of virtually any provision of the trust’s governing instrument that is permitted under Delaware law. The modifications could include changes to beneficial interests as well as administrative provisions, and provisions that were not permitted at the time when the trust was originally created but are now permitted at the time of the consent modification.

This new statute is likely to become a very useful and powerful tool for trustors, beneficiaries and trustees of trusts. Some examples of things that parties wish to modify by consent may include the following:

• Converting a trust to a directed trust;
• Improving and clarifying problematic directed trust provisions;
• Including silent trust provisions;
• Including new provisions that take advantage of amendments to Delaware’s trust laws;
• Correcting drafting errors;
• Adding or changing beneficial interests;
• Granting powers of appointment;
• Changing grantor trust treatment or adding a trustor income tax reimbursement provision; and
• Including new provisions in an asset protection trust to take advantage of expanded capabilities under the Qualified Dispositions In Trust Act.

Section 3342 provides that a fiduciary shall not have a duty to consent to any proposed modification and shall not have any liability for failure to consent to a proposed modification absent willful misconduct. The question is sometimes raised by commentators whether trustees might be deemed to have an ongoing fiduciary duty to transfer trust situs or modify a trust in order to improve the administration of the trust. This provision is included in Section 3342 to protect fiduciaries from potential liability arising from lawsuits claiming that a fiduciary’s failure to modify a trust, or to recommend trust modifications, constitutes an actionable breach of trust.

Section 3342(c) provides that any person, including the trustor, may bring an action in the Delaware Court of Chancery to interpret, apply, enforce, or determine the validity of a modification under the Section, including, without limitation, a
determination regarding whether virtual representation is adequately satisfied under 12 Del. C. § 3547. Additionally, that subsection expressly provides that all parties to a consent modification may waive the right to contest the modification.

Delaware’s new consent modification statute is available to any trust administered under the laws of the state of Delaware. Pursuant to 12 Del. C. §§ 3332 and 3340, once a Delaware corporate trustee is appointed, the administration of the trust will be deemed to occur in Delaware, Delaware law will govern all matters pertaining to administration, and a trust can avail itself of all of the advantages of Delaware law that pertain to administration including, without limitation, Delaware’s new consent modification statute.

Section 3338 – Nonjudicial settlement agreements.

In addition to the new consent modification statute, the 2016 legislation also included amendments to Delaware’s NJSA statute, 12 Del. C. § 3338. Section 3338 of Title 12 of the Delaware Code permits the use of a NJSA for the resolution of matters arising with respect to the administration of a trust without the time and expense of court involvement. Subsection 3338(b) provides that interested persons may enter into a binding NJSA with respect to any matter involving a trust (with an exception relating to charitable trusts and noncharitable purpose trusts). Subsection 3338(d) provides a non-exclusive list of six matters that may be resolved by a NJSA: (1) interpreting or construing the terms of a trust; (2) approving the report or accounting of a trustee; (3) directing a trustee to refrain from exercising a power or granting a power to a trustee; (4) resignation, appointment, or determination of compensation of a trustee; (5) transferring the principal place of administration of a trust; and (6) determining the liability of a trustee for an action relating to the trust.

Prior to 2016, Subsection 3338(c) of Title 12 of the Delaware Code provided that a NJSA is only valid to the extent that it does not violate a material purpose of the trust and includes terms and conditions that could be properly approved by the Delaware Court of Chancery. The 2016 amendments to Subsection 3338(c) eliminated the restriction that a NJSA may only include terms and conditions that could be properly approved by the Court of Chancery. Additionally, Subsection 3338(c) now provides that the remaining limitation under that Subsection - that a NJSA cannot violate a material purpose - only applies in cases where the trustor is not living. In other words, if a NJSA under 12 Del. C. § 3338 involves a trust with a living trustor, then the trustor is a necessary party to the NJSA and the NJSA may violate a material purpose of the trust.