THE ROBINS KAPLAN SPOTLIGHT

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ROBINS KAPLAN LLP

REWRITING THE ODDS

INSIDE THIS ISSUE

WELCOME

Welcome to the first edition of the Robins Kaplan Spotlight, a Trusts and Estates Newsletter. The Spotlight is the result of ongoing collaboration between our national trial practice and estate planning groups, with the goal of providing a forum to discuss the latest news and other issues impacting the trusts and estates community. Whether you are a trustee, beneficiary, trust officer, attorney, financial advisor, or other professional in this area, we hope that you will find this newsletter interesting, informative, and perhaps at times even a bit entertaining.

While the governing trust and estate authorities are often state-specific, we intend to provide content that relates to a national audience. There is inevitable variation in the trust and estate laws of each state, but the issues impacting the trusts and estates community extend far beyond state boundaries. We hope that you will find value in the topics, practice pointers, and other commentary presented, regardless of locale. Any comments or feedback on the newsletter, or suggestions about making it more useful, are always welcomed. Thank you for reading—and enjoy.

MINNESOTA'S NEW TRUST CODE

BY MATTHEW J. FRERICHS

During the 2015 session, the Minnesota legislature passed, and Governor Dayton signed into law, a bill enacting a new trust code. The new law, known as the Minnesota Trust Code, is codified as Minnesota Statutes § 501C.0101, *et seq.,* and replaces Minnesota Chapter 501B. The law became effective on January 1, 2016, and brings with it a number of changes in Minnesota trust law that will impact trust administration as well as estate planning. A few of these changes are highlighted below.

The new trust code provides increased flexibility to trustees with respect to administration and judicial proceedings.

- ***In personam* jurisdiction:** Previously, *in rem* jurisdiction (jurisdiction over trust property) was the only option for jurisdiction in court proceedings. Under the new law, a petitioner may choose either *in rem* or *in personam* as the basis of jurisdiction.

- **Decanting**: Decanting allows a trustee, under certain circumstances, to transfer assets from one trust to another trust. The extent of a trustee's ability to decant hinges on the discretion or authority the trustee has in the original trust as well as on other restrictions built into the law. The possible reasons for decanting are many. For example, a trustee may consider decanting in order to clarify an ambiguity in the trust or to extend the term of a trust (but not beyond what is permitted by the rule against perpetuities).

- **Modification and termination of trusts**: Article 4 of the Minnesota Trust Code contains several provisions relating to the modification and termination of trusts. For example, under the new law, a trust may be modified under certain circumstances to correct errors, to achieve the settlor's tax objectives, or to accommodate unanticipated circumstances. In addition, in specific situations, a trust may be terminated upon consent of the settlor and all beneficiaries or by court approval.

- **Non-judicial settlement agreements**: Under the new law, interested persons may enter into a binding non-judicial agreement as to any matter involving the trust, so long as the agreement does not violate a material purpose of the trust. The agreement does not need approval by a court. However, the terms and conditions of the agreement must be such that they *could* be properly approved by a court.

The new law will also afford estate planning attorneys new options for enhanced trust design and greater flexibility for clients.

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LITIGATE TRUST DISPUTES CONFIDENTIALLY IN SOUTH DAKOTA

BY BRENDAN JOHNSON AND SETH A. NIELSEN

When trust disputes surface, ample consideration should be given to the differences between trust jurisdictions and the impact of such differences on litigation. All too often, attorneys file lawsuits with little if any thought as to whether benefits may be realized by litigating in another jurisdiction. A situs change to a more litigation-friendly jurisdiction, such as South Dakota, may allow a trustee or beneficiary to benefit from the trust laws of another jurisdiction.

One important difference between trust jurisdictions is the ability and extent to which confidentiality of trust litigation may be maintained. As a general rule, court filings are a matter of public record and are easily accessible by the public. But in South Dakota, the court is required to seal court filings and orders relating to trust actions if requested by a living trustor or by any fiduciary or beneficiary. See SDCL §21-22-28. Once sealed, the documents are generally protected in perpetuity and will not be made available to the public. This ability to perpetually seal estate planning documents is a differentiating factor that has resulted in many trustors choosing to form their trusts under South Dakota law, and many others to change the situs of existing trusts.

In contrast, many jurisdictions do not permit sealed filings at all. Those that do generally permit sealing for a limited period of time, or allow sealing only at the court's discretion. Several jurisdictions commonly considered to have favorable trust laws do not have sealing statutes specific to trusts. Even Delaware, another state with favorable sealing laws, permits sealing of filed documents for only three years. See Del. Ch. Ct. R. 5(g).

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While the ability to litigate trust and estate disputes in a confidential manner is not necessary for all litigants, it is very important to many trustees and beneficiaries. This is frequently the case for wealthy or affluent families that may not want to disclose in public litigation family finances or less-than-ideal family dynamics. When confidentiality is of paramount concern to the trustor, when there are concerns that non-confidential litigation may further escalate a dispute, or when family dynamics drive the desire for privacy, prospective litigants should evaluate whether a situs change may benefit trust litigation efforts. If trustees or beneficiaries desire to litigate trust disputes in confidence, South Dakota's perpetual sealing statute makes litigating there an option worth considering.

AN EFFECTIVE STRATEGY FOR TESTAMENTARY TRUSTEES IN DISPUTES WITH BENEFICIARIES

BY ANTHONY A. FROIO AND MANLEEN SINGH

Administration of a trust requiring distributions to more than one beneficiary can be fraught with disputes between beneficiaries all seeking one general goal—a larger share of the trust estate. In an effort to resolve disputes, the trustee, however, may need to spend trust assets, whether to negotiate a settlement or, if negotiations fail, to hire outside counsel and/or initiate legal proceedings. With the resulting reduction of the trust estate's value, the trustee risks facing even more objections from beneficiaries, which cause additional cost and delay in distributions. How can a trustee administer the trust and make distributions with minimal cost to the trust estate when faced with beneficiaries who continue to object? The answer may lie in proactively initiating a proceeding in a court with the relevant expertise and experience.

DUTIES OF THE TRUSTEE

The law charges the trustee with carrying out the wishes of the settlor /decedent while complying with several duties. One important duty is to administer the trust reasonably and in good faith. An equally important duty is loyalty to all beneficiaries. In addition to prohibiting self-dealing, the duty of loyalty requires the trustee to treat all beneficiaries, and all classes or groups of beneficiaries, fairly and impartially. The trustee cannot favor one beneficiary or class of beneficiaries over another.

A TRUSTEE CATCH-22

But what if the trustee, while acting reasonably, is accused of violating her duty of loyalty? An example may best illustrate such a quandary. Frequently, a trustee must make decisions on how to allocate trust costs; how she allocates such costs directly affects the amount of distributions available to beneficiaries. Consider a trust comprising two classes of beneficiaries: Class A beneficiaries receive the net proceeds from the sale of certain property upon the death of the settlor, while Class B beneficiaries receive any and all remaining trust assets after specific distributions and trust expenses have been paid. How should the trustee allocate the costs associated with the sale of the property?

A trustee could reasonably decide to categorize such costs as general trust administration expenses, since the trust required her to sell the property and distribute the net proceeds to Class A beneficiaries. A general trust administration charge decreases the remainder of the trust assets and, likewise, decreases the amount distributed to Class B beneficiaries. Conversely, a trustee may reasonably charge the costs associated with the sale of the property against proceeds received from that sale, since the two are

intertwined. The inevitable result is a reduction in the amount distributed to Class A beneficiaries. In either scenario, the trustee has a reasonable basis for making her decision regarding allocation of the costs associated with the sale of the property. In either scenario, one class of beneficiaries could accuse the trustee of violating her duty to act impartially by favoring the other class, as shown by the resulting negative impact on their distributions. The classic catch-22.

A SEEMINGLY REASONABLE SOLUTION THAT CAN DRASTICALLY ERODE TRUST ASSETS

The trustee always has the option to preempt this issue outside of court through transparent and detailed communications with beneficiaries. At first blush, this may seem like the most reasonable, cost-efficient way to resolve the issue, but its success remains wholly dependent on the beneficiaries. For aggressive beneficiaries, however, whose only focus is their bottom line, this may simply mark the beginning of a long and difficult journey of trust administration tangled with conflict and dispute. In short order, the general trust administration costs could mushroom exponentially with the incurring of attorneys' fees and other costs and expenses on top of the previously accumulated costs. In their quest for larger distributions, these beneficiaries may not appreciate that their efforts can also simultaneously reduce their distributions because of the cumulative effect of increasing general trust administration costs that erode the trust assets. At the conclusion of litigation, all beneficiaries, objecting or not, may have been adversely impacted, and no one is satisfied.

GOING TO COURT EARLY MAY BE THE MOST EFFICIENT AND COST-EFFECTIVE RESOLUTION

One strategic alternative for a trustee to consider is seeking instruction from the court early. Promptly upon the death of a decedent, the testamentary trustee should open the lines of communication with all beneficiaries to keep them apprised of the assets of the trust, the progress of the trust administration process, and to establish a relationship of trust and credibility. Open communication allows the trustee to learn about the personalities and goals of each beneficiary. If the trustee foresees a catch-22 type dilemma, and the trustee has learned that at least one beneficiary (or class of beneficiaries) is unlikely to assent and may tend to object, the trustee should file a petition for instructions with the probate court, or other court specially designated to hear trust disputes, as soon as possible.

One strategic alternative for a trustee to consider is seeking instruction from the court early.

The advantages of filing a petition for instructions sooner rather than later are many. The act of filing the petition with the probate court effects jurisdiction over the trust with a court that has an intimate understanding of trust administration and the associated duties of a trustee. This forecloses the opportunity for an objecting beneficiary to initiate a proceeding in a court of general jurisdiction where experience and expertise in matters regarding trust administration may not be as robust. Second, the trustee transfers her decision-making power regarding the disputed issue over to the court via the petition for instructions. With the court order in hand dictating how the disputed issue must be resolved, the trustee has authority to proceed without fear of being accused of violating a fiduciary duty. Third, a court order conclusively determines the rights of all interested parties, absent fraud to beneficiaries. And fourth, early resolution of disputed issues by court order allows the trustee to minimize general trust administration costs that she incurred as a result of negotiating with an objecting beneficiary before ultimately going to, or being dragged into, court.

Even though the advantages of going to court early are plentiful, a trustee must avoid taking such formal action prematurely. Legal fees and costs, especially attorneys' fees, can grow quickly. While a trust typically covers such expenses, that coverage lasts only as long as the trustee acts reasonably. If a trustee seeks a court order before a dispute exists or before a trustee learns more about the beneficiaries and their likelihood to assent (or object), she risks facing an objection to the incurred legal expenses and losing that coverage. That risk can be reduced by ensuring there is a reasonable need to seek instructions from the court.

A trustee may feel trapped in a no-win situation when administering a trust with continually objecting beneficiaries. In such cases, seeking instructions from a court with the relevant area of expertise may be the trustee's best strategy to accomplish the goal of administering the trust to its closure, with minimal risk of liability, and ultimately accomplishing the goals and wishes of the settlor.

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- **Directed trusts** – A directed trust allows for the bifurcation of the trustee's powers and duties. For example, the settlor might appoint a trust protector and grant the protector certain powers—powers that the trustee does not have—such as the ability to direct the trustee with respect to investments, the ability to remove the trustee, or the ability to amend the trust to achieve a desired tax result. The settlor could also appoint other advisors, for example a distributions advisor or an investment advisor. In these ways, a directed trust can be far more flexible than a traditional trust.

- **Silent trusts** – Until now, Minnesota law has required trustees to keep beneficiaries reasonably informed regarding trust administration. Under the new law, the settlor can include a trust provision that limits this duty and allows the trustee to withhold information regarding the trust assets and trust administration.

- **Tangible personal property** – With regard to wills, the Minnesota probate statutes allow a testator to dispose of his or her tangible personal property via a separate list, which may be referenced in the will. Under the new law, a similar provision disposing of tangible personal property may now be included in a trust.

In future editions of the Spotlight, we will delve further into these topics, as well as other important aspects of the Minnesota Trust Code not mentioned here.

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