

Directed Trusts: Delaware v. Florida
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Directed Trusts: An Overview

What is a Directed Trust?

- Bifurcation of duties.
 - With a Directed Trust, the settlor may assign investment, distribution and administrative duties amongst one or more trustees, investment advisors and trust protectors.
- Settlor may maintain a degree of control.
 - Oftentimes, the settlor may serve as investment advisor or will choose a third-party investment advisor to direct the administrative trustee as to the investment of trust assets.
- Distribution decisions may also be entrusted to a trust protector who directs the administrative trustee as to distributions of income and/or principal among one or more trust beneficiaries.

Why create a Directed Trust?

- Investment concerns.
 - Trust will be funded with “difficult assets” - family business, real estate.
 - Settlor wishes to retain concentrated positions in trust portfolio.
 - Settlor is a very sophisticated investor.
- Relationship issues.
 - Need for corporate trustee but preference for personal advisor.
 - Desire to maintain relationship with outside investment manager.

Development of Directed Trust Law

Second Restatement §185 (1959)

If under the terms of the trust a person has the power to control the action of the trustee in certain respects, the trustee is under a duty to act in accordance with the exercise of such power, unless the attempted exercise of the power violates the terms of the trust or is a violation of a fiduciary duty to which such person is subject in the exercise of the power.

Uniform Trust Code §808 (b) (2010)

If the terms of the trust confer upon a person other than the settlor of a revocable trust power to direct certain actions of the trust, the trustee shall act in accordance with an exercise of the power unless the attempted exercise is manifestly contrary to the terms of the trust or the trustee knows the attempted exercise would constitute a serious breach of a fiduciary duty that the person holding the power owes to the beneficiaries of the trust.

State Statutes

All but 14 states now have some form of directed trust statute.

2 states have adopted the Restatement approach.

Others, including Florida, have adopted the UTC approach.

20 states have adopted more protective statutes.

Delaware Law

- (a) Where 1 or more persons are given authority by the terms of a governing instrument to direct, consent to or disapprove a fiduciary's actual or proposed investment decisions, distribution decisions or other decision of the fiduciary, such persons shall be considered to be advisers and fiduciaries when exercising such authority provided, however, that the governing instrument may provide that any such adviser (including a protector) shall act in a nonfiduciary capacity.
- (b) If a governing instrument provides that a fiduciary is to follow the direction of an adviser, and the fiduciary acts in accordance with such a direction, then except in cases of wilful misconduct on the part of the fiduciary so directed, the fiduciary shall not be liable for any loss resulting directly or indirectly from any such act.
- (c) If a governing instrument provides that a fiduciary is to make decisions with the consent of an adviser, then except in cases of wilful misconduct or gross negligence on the part of the fiduciary, the fiduciary shall not be liable for any loss resulting directly or indirectly from any act taken or omitted as a result of such adviser's failure to provide such consent after having been requested to do so by the fiduciary.
- (d) For purposes of this section, "investment decision" means with respect to any investment, the retention, purchase, sale, exchange, tender or other transaction affecting the ownership thereof or rights therein and with respect to nonpublicly traded investments, the valuation thereof, and an adviser with authority with respect to such decisions is an investment adviser.

Del. Code Ann. tit 12, §3313

Delaware Law (continued)

(e) Whenever a governing instrument provides that a fiduciary is to follow the direction of an adviser with respect to investment decisions, distribution decisions, or other decisions of the fiduciary, then except to the extent that the governing instrument provides otherwise, **the fiduciary shall have no duty to:**

- 1. Monitor** the conduct of the adviser;
- 2. Provide advice** to the adviser or consult with the adviser; or
- 3. Communicate** with or **warn** or apprise any beneficiary or third party concerning instances in which the fiduciary would or might have exercised the fiduciary's own discretion in a manner different from the manner directed by the adviser.

Absent clear and convincing evidence to the contrary, **the actions of the fiduciary pertaining to matters within the scope of the adviser's authority (such as confirming that the adviser's directions have been carried out and recorded and reporting actions taken at the adviser's direction), shall be presumed to be administrative actions** taken by the fiduciary solely to allow the fiduciary to perform those duties assigned to the fiduciary under the governing instrument **and such administrative actions shall not be deemed to constitute an undertaking by the fiduciary to monitor the adviser or otherwise participate in actions within the scope of the adviser's authority.**

Del. Code Ann. tit 12, §3313

Florida Law

If the terms of a trust provide for the appointment of more than one trustee but confer upon one or more of the trustees, to the exclusion of the others, the power to direct or prevent specified actions of the trustees, the excluded trustees shall act in accordance with the exercise of the power. **Except in cases of willful misconduct on the part of the excluded trustee, an excluded trustee is not liable, individually or as a fiduciary, for any consequence that results from compliance with the exercise of the power.** An excluded trustee does not have a duty or an obligation to review, inquire, investigate or make recommendations or evaluations with respect to the exercise of the power. The trustee or trustees having the power to direct or prevent actions of the trustees shall be liable to the beneficiaries with respect to the exercise of the power as if the excluded trustees were not in office and shall have the exclusive obligation to account to and defend any action brought by the beneficiaries with respect to the exercise of the power. **The provisions of s. 736.0808(2) do not apply if the person entrusted with the power to direct the actions of the excluded trustee is also a co-trustee.**

Fla. Stat. § 736.0703(9) (as effective July 1, 2014)

Reasons for July 2014 Amendment to Fla. Stat. § 736.0703(9)

- Concerns about the protections for the excluded or directed trustee.
- The former Fla. Stat. § 736.0703(9) provided, in part:

Except in cases of willful misconduct on the part of the [directing trustee] of which the excluded trustee has actual knowledge, an excluded trustee is not liable, individually or as a fiduciary, for any consequence that results from compliance with the exercise of the power, regardless of the information available to the excluded trustee. (emphasis added)

- Concern that this actual knowledge language triggered an affirmative duty on the part of the excluded trustee to monitor the actions of the directing trustee.
 - In order for the excluded trustee to protect itself from liability, it had to determine if the directing trustee was engaging in acts of intentional misconduct.
- Were any individuals or trust companies willing to act as an excluded trustee? If so, were these fiduciaries willing to reduce their fees?

Differences Between Delaware and Florida Trust Laws

	Delaware	Florida
Duty to Inform and Account to Trust Beneficiaries	No, if express terms under trust agreement <i>Del. Code. Ann. tit. 12, §3303</i>	Yes. <i>Fla Stat. §736.0813</i> Grantor may designate a representative to receive information and accountings. <i>Fla. Stat. §736.0306</i>
Direction Investment Advisors and Direction Distribution Advisors	Yes, if express under trust agreement-directed trustee only liable in cases of his or her own willful misconduct <i>Del. Code. Ann. 12, §3313</i>	Yes for revocable trusts – directed trustee has no liability <i>Fla. Stat. §736.0808</i> For irrevocable trusts - directed co-trustee is relieved of liability for acts done in reliance on the direction of a co-trustee. <i>Florida Stat. §736.0703</i>
Prudent Investor Rule	Yes, but trustor may direct a different investment strategy policy than that authorized by the Prudent Investor Statute <i>Del. Code. Ann. tit. 12, §3302(e) and 3303 (a)</i> Additionally, trustee can be relieved from liability for life insurance policies held in trust if insured notified of trustee's limitation of responsibilities either under express terms of the trust agreement or in a separate writing <i>Del. Code. Ann. tit. 12 §3302(d)</i>	Yes
Self-settled Spendthrift Trust	Yes <i>Del. Code. Ann. tit. 12, §3570-3576</i>	No
Rule Against Perpetuities	No rule, with exception for real estate interests	360 Years

Differences Between Delaware and Florida Trust Laws

	Delaware	Florida
Who is a Directing Trustee	“Person”, who is presumed to be a fiduciary	Trustee
Liability Standard for the Excluded Trustee	“Willful Misconduct”	“Willful Misconduct”
Definition of “Willful Misconduct”	“intentional wrongdoing, not mere negligence, gross negligence or recklessness” <i>Del. Code Ann. tit 12, §3301(g)</i>	None
Definition of “Investment Decisions”	“The retention, purchase, sale, exchange, tender or other transaction affecting the ownership thereof or rights therein and with respect to nonpublicly traded investments, the valuation thereof.” <i>Del. Code Ann. tit 12, §3313(d)</i>	None
Duties of an Excluded Trustee	Excluded trustee has no duty to: <ul style="list-style-type: none"> • Monitor the conduct of the adviser • Provide advice to the adviser or consult with the adviser, or • Communicate with or warn or appraise any beneficiary or third-party concerning instances in which the fiduciary would or might have exercised the fiduciary’s own discretion in a manner different from the manner directed by the adviser 	Excluded trustee is relieved of any obligation to: <ul style="list-style-type: none"> • Review, • Inquire, • Investigate or • Make recommendations or evaluations with respect to the exercise of the power [to direct specified actions of the excluded trustees]

Differences Between Delaware and Florida Trust Laws

	Delaware	Florida
Presumption of Administrative Actions	Absent clear and convincing evidence, the actions taken by the excluded trustee that are otherwise outside of his scope of responsibilities are considered administrative actions only	None
Case Law	<u>Duemler v. Wilmington Trust Company</u> , 2004 Del. Ch. LEXIS 206 (upholding §3313 and finding that a trustee is not liable for investment losses when an acting investment adviser fails to direct the trustee).	None
Explicit Liability of Directing Trustee	None	Sole liability for directed actions, with the exclusive obligation to account and defend any actions brought by the beneficiaries related to those directions.
Default and Mandatory Rules	Terms of governing instrument control. <i>Del. Code Ann. tit 12 §3303</i>	Trustee's duty to act in good faith and in accordance with the terms and purposes of the trust and in the interests of the beneficiaries cannot be waived. <i>Fl. Stat. §736.0105(2)(b)</i>

Drafting Considerations for a Directed Trust

Identify Identity of Directing Party

- Delaware: Trust advisor need not be a trustee. Held to a fiduciary standard.
- Florida: To maximize the protections for a Florida excluded trustee, the direction power must be held by a co-trustee.
 - Fla. Stat. § 736.0808 provides that if the investment direction is held by a non-trustee (such as a trust adviser), the trustee must follow the direction “unless the attempted exercise is manifestly contrary to the terms of if the trust or the trustee knows the attempted exercise would constitute a serious breach of a fiduciary duty that the person holding the power owes to the beneficiaries of the trust”.
 - Greater burden is placed on the directed trustee.
 - No case law interpreting the language of this statute – specifically the definition of “manifestly contrary” and “serious breach of fiduciary duty”.

Drafting Considerations for a Directed Trust

Clarify Scope of Authority

- Clearly delineate powers that can only be exercised by direction.
- Identify assets subject to direction.
- Cross-reference general trustee powers specified in the governing instrument and statutory powers under the applicable law.
- Trust agreement should provide for a bifurcation of fiduciary duties, not simply a delegation of the investment management responsibilities to an agent.
 - Fla. Stat. § 518.112 provides that a trustee may delegate any or all of its investment management responsibilities, but must provide notice to the beneficiaries and must monitor the actions of the agent.
 - Courts have held excluded trustees to a greater level of scrutiny when acting under an Investment Direction Agreement. See Estate of John P. Saxton, 686 N.Y.S.2d 573 (Sur. Ct. 1998), modified, 712 N.Y.S.2d 225 (App. Div. 2000).

Drafting Considerations for a Directed Trust

Limit Liability of Directed Trustee

- Consider effect of exoneration clause. Be mindful of Fla. Stat. § 736.1011 and its limitations on exculpatory provisions for trustees.
- Ensure that directing party is held to a fiduciary standard.
- Directed trustee should have no duty to monitor the investment performance or the performance of the directing trustee, to warn the directing trustee or beneficiaries, and should be indemnified for any actions brought against it.
 - See Rollins v. Brach Bank & Trust Co. of Virginia, 56 Va. Cir. 147 (2001)(holding that a directed trustee has a duty to (1) keep informed as to the conditions of the trust and (2) fully inform beneficiaries of all facts relevant to the subject matter of the trust and which are material for the beneficiary to know for the protection of his interests; and the directed trustee cannot rid itself of this “duty to warn”).

Clarify Direction Power vs. Veto Power

- Directing trustee should be required to direct the actions of the excluded trustee, not to veto or consent to proposed investment decisions by the excluded trustee.
 - Liability of the excluded trustee can be greater when the directing trustee has only a veto or consent power. See Del. Code Ann. tit. 12, § 3313(c).
 - Avoids potential administrative burdens caused by the excluded trustee waiting on the consent or veto of the directing trustee.

Drafting Considerations for a Directed Trust

Define “Willful Misconduct”

- Unlike Delaware, Florida does not provide a statutory definition of willful misconduct.

Define “Investment Decisions”

- What does the grantor want the directing trustee to have responsibility over?
 - For example: if there is a family business held in the trust, grantor may wish the directing trustee be only responsible for those assets, with the responsibility for the marketable securities to be held by the directed trustee.
- What party must perform the administrative work of investments?
 - Consider including language identifying these tasks as administrative, absent clear and convincing evidence to the contrary.
- Who is responsible for valuation of assets?

Clarify mode of Communication

- How must the directing trustee communicate his directions to the excluded trustee?
 - Written directions, only, with no duty to confirm the authenticity of the written directions?

Drafting Considerations for a Directed Trust

Consider a provision to “turn off” the direction

- If the trust contains a unique asset that is later sold or distributed, consider allowing the directing trustee to authorize the excluded trustee to provide investment management services

Allow for Succession Provisions

- Include removal, replacement and succession provisions, if adviser is not a trustee.

Presenter's Biography

Gail E. Cohen, *Vice Chairman and General Trust Counsel*, is responsible for overseeing Fiduciary Trust Company's trust and estate services and client relationships. She has over 30 years of experience in the area of trusts and estates. Ms. Cohen is a member of Fiduciary Trust's Board of Directors and a member of the Management and Operating Committees. In 2010 and 2011, she was named one of the "Top 50 Women in Wealth," selected by AdvisorOne. She has been elected into the NAEPC Estate Planning Hall of Fame and awarded the Distinguished Accredited and Estate Planner® designation. Before joining Fiduciary Trust in 1994, Ms. Cohen was a trusts and estates attorney at the law firm of Debevoise & Plimpton. Previously, she was an associate at the law offices of Edward S. Schlesinger, P.C. Ms. Cohen is Immediate Past Chair of the New York Bankers Association, and sits on its investment committee. She has previously served as Chair, Vice Chair, and Treasurer. She currently sits on the Investment Committee of the New York City Bar Association and is a former member of that Bar Association's Committee on Estate and Gift Tax, which she chaired from 1998-2001. Ms. Cohen is a member of The Rockefeller University Committee on Trust and Estate Gift Plans and the Graham Windham Board. She teaches estate planning as an adjunct professor of law at Brooklyn Law School. Ms. Cohen received a B.A. from Mount Holyoke College and a J.D., *summa cum laude*, from Brooklyn Law School. She is admitted to the bar in New York and New Jersey.

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