

NEW UNIFORM TRUST CODE IMPOSES TRUST REPORTING RULES ON TRUSTEES OF NEW HAMPSHIRE TRUSTS

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Overview

Effective October 1, 2004, New Hampshire has adopted a version of the *Uniform Trust Code* (“UTC”) as Chapter 564-B of the Revised Statutes Annotated (“RSA”). The statute generally is retroactive and applies to both existing and new trusts. The UTC is a comprehensive new trust law containing many new provisions which will provide clarity and certainty to an unsettled body of law and generally be welcomed by trust professionals and beneficiaries alike.

There are, however, certain aspects of the new law which may not be so welcome in some quarters. The potentially objectionable features include controversial ***mandatory and default rule trustee notification and disclosure requirements***. Trust settlors, trustees, beneficiaries and those who advise them must be aware of these new rules because (i) the mandatory disclosure notices must be sent to certain beneficiaries of irrevocable trusts ***on or before December 1, 2004***, and (ii) failure to provide the notice is a ***breach of the trustee’s fiduciary duty***. Trustees interested in taking advantage of the new limitations period on beneficiary claims may wish to make annual “reports” to beneficiaries and disclose prior trust transactions which might be questionable in any respect. Finally, attorneys and their privacy-minded clients should consider inserting provisions in new trusts, and making amendments to revocable trusts, which negate the application of all non-mandatory disclosure rules. Call Joe McDonald, Amy Kanyuk or Joy Riddell if you wish to discuss these implications for yourself or your clients.

New Hampshire made few changes to the UTC as adopted by the National Conference of Commissioners on Uniform State Laws (“NCCUSL”), and more information can be obtained from the UTC website at www.utcproject.org. This newsletter will focus primarily on the expanded reporting requirements for trustees of irrevocable trusts (defined to include revocable trusts whose settlors are incapacitated).

Important Definitions

➤ The UTC’s notice and disclosure requirements apply only to qualified beneficiaries. A ***“qualified beneficiary”*** is any beneficiary who is eligible now to receive either an income or principal distribution or who would be entitled to receive a distribution if all of the current beneficiaries died or if the trust terminated. This includes current discretionary beneficiaries, remainder beneficiaries, the takers in default under a testamentary power of appointment or an unexercised nontestamentary power of appointment, and appointees under an exercised lifetime power of appointment. Any

trustee who does not have the name, date of birth and current address of each such beneficiary should now begin gathering that information to meet the December 1, 2004 notification deadline.

➤ A “***nonqualified beneficiary***” is any person or entity who has any interest in the trust, vested or contingent, who is not a qualified beneficiary. Nonqualified beneficiaries might include, for example, the settlor’s siblings who receive the remainder interest in a credit shelter trust if both the settlor’s widow and child died. Those siblings are not “qualified” beneficiaries because if the widow died or the trust terminated now, the child, and not the siblings, would be entitled to the trust assets. Also, charities or the settlor’s intestate heirs named in the remote distribution provision (frequently called the “bomb” or “disaster” clause) are nonqualified beneficiaries.

➤ The notice requirements are among the UTC’s few “***mandatory rules***”. A mandatory rule is one which overrides any contrary provision of the trust itself, as contrasted with the more common “***default provisions***” which the UTC applies only in the absence of a relevant provision in the trust instrument.

Mandatory Rules

One of the UTC’s mandatory provisions requires that within 60 days of October 1, 2004, or thereafter within 60 days of when a trust becomes irrevocable or its settlor becomes incapacitated, the ***qualified beneficiaries of the irrevocable trust over the age of 21 must receive notice of the trust’s existence, the trustee’s name, address and telephone number, and be advised of their right to request a copy of the trust instrument and a trustee’s “report”*** -- essentially the equivalent of what most trustees know as an accounting (RSA 564-B:1-105(b)(8)). If a qualified beneficiary requests trustee reports, the reports must include “***trust property, liabilities, receipts and disbursements, including the source and amount of the trustee’s compensation, a listing of the trust assets and, if feasible, their respective market values***” (RSA 564-B:8-813). The trustee also must respond to a qualified beneficiary’s request for “***other information reasonably related to the administration of the trust***” (RSA 564-B:1-105(b)(9)). This language must be interpreted in light of the trustee’s duty to give a beneficiary any information he needs to protect his interest in the trust -- the overriding policy the UTC’s notice and disclosure requirements are designed to serve. Each notice should be sent via certified mail, return receipt requested.

Default Rules

New default provisions require that a ***full copy of the trust instrument*** be sent to all beneficiaries who request it, and that an ***annual report*** be sent to all permissible distributees and to ***any other beneficiary -- qualified or nonqualified -- who requests it***. ***Advance notice of any change in the trustee’s compensation or change in the principal place of administration*** of the trust also must be sent to all qualified beneficiaries and any nonqualified beneficiary who requests it. There is ***no mention of a minimum age of 21*** in the default rules.

Analysis

A. The Scope of the Trustee's Reporting Obligations. There is some ambiguous language in the mandatory rule which is non-specific concerning the form and frequency of trust reports and the trustee's obligation to send a beneficiary the entire trust instrument.¹ In some respects this will enable trustees to determine for themselves the extent of their disclosures to satisfy their obligations under the new law. If the default rules do not apply, the trustee might, for example, delete from one beneficiary's copy of the trust instrument the paragraphs containing a gift to another beneficiary who is the first beneficiary's adversary in a pending civil suit. Or the trustee might not prepare reports for an irrevocable life insurance trust on a regular basis.

The mandatory provisions of the new law are intended to strengthen the beneficiary's right to full disclosure on the one hand, balanced against administrative reasonableness and the rights of privacy of the settlor and other beneficiaries on the other. If the default rules apply, the statute resolves these questions in favor of disclosure.

All irrevocable trusts should be examined for language which bears on this "scope of reporting" issue. Few existing trusts are likely to have clear instructions on this point, and the default rules, as well as the mandatory reporting rules, normally will apply. However, new trusts drafted and amendments made to revocable trusts may have language providing, for example, that the trustee's duty to report to beneficiaries is limited to the qualified beneficiaries, or perhaps limited strictly to the mandatory rules of RSA 564-B:1-105(b)(8) and (9). We are recommending this latter approach to our privacy-minded clients who may wish to empower trustees -- especially surviving spouses -- and discourage harassment, threats or litigation by spendthrift or vexatious beneficiaries.

B. Some Immediate Implications. The new disclosure requirements will require immediate changes to many trustees' record-keeping and reporting practices and may stir the pot of trust litigation. For the first time, many widows and widowers will be reporting to the children or stepchildren how they, as trustees, have administered the QTIP and credit shelter trusts established upon the death of the deceased spouse. In these cases records may be fragmentary or even non-existent. The required reporting is likely to be unpopular with trustees who feel that the trust is "their money." They may simply refuse to report, or they may try to avoid the duty by seeking waivers from the beneficiaries who request reports or otherwise are entitled to them. Many trustees of

¹ NCCUSL's comments to UTC § 105 elaborate on this as follows: "Section 813 imposes a general obligation to keep the beneficiaries informed as well as several specific notice requirements. Subsections (b)(8) and (b)(9) specify limits on the settlor's ability to waive these information requirements. With respect to beneficiaries age 25 or older, a settlor may dispense with all of the requirements of Section 813 except for the duties to inform the beneficiaries of the existence of the trust, of the identity of the trustee, and to provide a beneficiary upon request with such reports as the trustee may have prepared. Among the specific requirements that a settlor may waive include the duty to provide a beneficiary upon request with a copy of the trust instrument (Section 813(b)(1)), and the requirement that the trustee provide annual reports to the qualified beneficiaries (Section 813(c)). The furnishing of a copy of the entire trust instrument and preparation of annual reports may be required in a particular case, however, if such information is requested by a beneficiary and is reasonably related to the trust's administration." [Note: New Hampshire changed the age 25 reference to age 21]. RSA 564-B:10-1005.

charitable remainder trusts and irrevocable life insurance trusts will be sending their first-ever reports to remainder beneficiaries. Because the statute will become effective October 1, 2004 and is retroactive, notices should be sent by December 1, 2004, and reporting should begin in 2005 for the year 2004. Some trustees will disclose the trust instrument and trustee information and will report for 2004 only. Others will be well advised to choose to report retroactively for all years of the trust to disclose past actions and obtain a shortened one year statute of limitations (see Paragraph C. below).

C. Enforcement; Potential Trustee Liability and Statutes of Limitation.

Failure to send required information is a breach of trust. Conversely, trustees who comply with these rules cannot be sued by a beneficiary who received or waived the report, unless the suit is filed within one year, if the report adequately discloses the transaction or issue which might give rise to the claim (RSA 564-B:10-1005). To make adequate disclosure, it might not be sufficient to merely report a prior sale of trust property -- for example, a self dealing transaction the purchase price paid by the trustee was unsupported by an appraisal or was below market value.

To address these uncertainties, we are encouraging our trustees to review annually the prior year's events, perhaps with us or other attorneys as trust client's counsel, to determine if in some cases something more than a "bare bones" accounting would be prudent. If an issue or questionable transaction is not adequately disclosed, any beneficiary who did not sign a waiver has two years to bring his lawsuit against the trustee for a breach of trust. That two year period is suspended until the trustee ceases to serve, or until the trust or the plaintiff/beneficiary's interest in the trust terminates, whichever comes first. By contrast, the one-year statute as to issues adequately disclosed starts to run as soon as the report is sent. The trust report must contain a clear statement of the one year statute of limitations so that a beneficiary receiving the report knows that his time for legal action is limited to one year.

D. Stay Tuned. Many of the jurisdictions enacting their own modified versions of the UTC have changed the beneficiary notification requirements from mandatory to default rules. There has been much criticism that mandatory disclosure will frustrate the settlor's intentions and contravene the general rule giving benefactors free reign in defining the scope of their largess -- a time honored principle in New Hampshire trust law embodied in, for example, the famous Dumaine case. Just last month NCCUSL responded by proposing amendments to the UTC which would effectively reverse the present bias which favors mandatory disclosure. The Drafting Committee expects to approve this important change at the NCCUSL meeting scheduled for August, 2004. We suspect that New Hampshire's ad hoc UTC Committee, which adopted the original version of the UTC virtually unchanged, will follow NCCUSL's lead and submit a bill adopting the default rule approach, perhaps retroactively effective as early as January 1, 2005, or even to the October 1, 2004 effective date. This cannot be guaranteed, however, and all prudent settlors, trustees and their advisors should proceed on the assumption that the disclosure rules will remain mandatory for the indefinite future.