

TRUSTS

1) Requirements for a trust

a) There are 3 things using the name trust:

i) Express trust

(1) This is the only real trust. The others are just equitable remedies.

ii) Resulting trust

iii) Constructive trust

b) Express trust

i) Definition: a legal device that allows an owner of property to make transfers of property and to have those assets managed on behalf of someone else, rather than have the beneficiary manage the money himself.

ii) Types:

(1) Lifetime trust or intervivos trust– set up during the lifetime of the person who created the trust (the settlor).

(2) Testamentary trust – set up in the settlor's will.

iii) Requirements for a valid trust (Note: no consideration is required to create a trust.)

(1) **Settlor** – creator – who makes a...

(a) Can be anyone 18 or older, with the capacity to enter into contracts.

(2) **Delivery** of legal title to...

(a) Titled assets must be formally transferred to a trustee for delivery to be valid.

(b) Example: S signed a trust agreement naming Tom as trustee and her children A and B as beneficiaries. The trust agreement was properly notarized. The agreement recited the property of the trust as shares of stock in various corporations and recited that the trustee acknowledged receipt of the shares. The stock certificates were handed over to T by S at time trust document was signed and acknowledged. Before the shares could be re-registered in T's name, S died. Is this trust valid?

(i) No. There was no delivery with formal transfer of the title in the stock. Physically handing over the stock is not enough.

(3) **Property** – res, corpus, or principal – to a...

(a) This can be almost anything but it must be property that the settlor owns, not just an expectancy of future ownership.

(i) Example: S's mom, T, executed a will leaving her farm to S. S was thrilled that he would get the farm on T's death and he decided to create a trust. He executed a trust naming himself as trustee and his sons as beneficiaries. S executed a deed to himself, as trustee, with the income to be paid to his sons for life with the principal then going to his granddaughter. T approved of this because she

loved her granddaughter and thought this would preserve the farm for her granddaughter to own one day. Is this a valid trust?

1. No. S has only an expectancy of property ownership. He has no present interest in the farm. T might someday change her will and change the disposition.

(b) The property must be identified, not subject to future determination.

- (i) Example: S created a trust to be funded with “whatever money that I may choose to contribute to the trust over the next 10 years.” Is this a valid trust?

1. No, because the property must be identified, that the settlor owns.

(4) **Trustee** who holds legal title for the benefit of a...

(a) Lifetime trust

- (i) Almost anyone can be a trustee since no court involvement is needed for such trusts.

(b) Testamentary trust

- (i) Created under court supervision, anyone can be a trustee except for those who are:
 1. Under 18
 2. Judicially declared incompetent
 3. Convicted felons
 4. Those incapable because of drunkenness, dishonesty, want of understanding, or improvidence.

(c) A non-resident alien can serve as trustee only if:

- (i) That person is related to decedent; and
 1. Either decedent’s spouse, grandparent or descendant of the grandparent of decedent, or descendant decedent’s spouse, or the spouse of any of them.
- (ii) A NY resident serves as co-fiduciary.

(d) A failure to name a trustee in the trust does not matter as the court can appoint someone to be trustee.

(5) **Beneficiary** with...

- (a) Beneficiaries must be definite and ascertainable. No ambiguity.
- (b) If there is ambiguity, the trustee holds in a resulting trust for the residuary beneficiary of a will (or intestate heirs in absence of a valid will).
 - (i) Example: S's will created a trust, giving \$4million of IBM stock to T as trustee, to pay the income for life "to all my good friends" and to pay the remainder to "my very best friend of all." The residuary beneficiary of S's will was his sister.
 - 1. Does the trust fail?
 - a. Yes. The beneficiaries "my good friends" and "my very best friend" are not definite and ascertainable.
 - 2. Does T get to keep the money/.
 - a. No. He holds it in a resulting trust for sister, who is the residuary beneficiary of the will.
- (c) Exception:
 - (i) A beneficiary listed as someone's "family" or "next of kin" is definite and ascertainable and the trust does not fail.
 - 1. Consult the intestacy statutes for the names of persons who fit the description in the trust.
 - (ii) Example: S's will created a trust, giving \$4million of IBM stock to T as trustee, to pay the income "to my family" and to pay the remainder to his sister. Is this ok?
 - 1. Yes. Family can be determined by looking to the intestacy statute.

(6) **Intent** to create a trust for...

- (a) Settlor must intend to create an enforceable obligation.
 - (i) Precatory (non-binding) language is not enough. Settlor's language must create a binding obligation.
- (b) Trustee must be given duties to perform. If the trustee has not duties to perform, it is called a passive trust, which is not trust at all.
 - (i) Example: June gives \$250k in cash to her daughter Mary in trust with the statement "I would like the trust income to be paid to my youngest Son for life, with the remainder going to Son's son Charles." Is this a valid trust?
 - 1. No. The language "would like" is precatory language and does not impose an enforceable obligation.
- (c) Note: just using the word "trust" does *not* show intent to create a trust. Look at all of the language and all of the facts to determine intent.
 - (i) If the circumstances show that settlor did not intend trust, then there is no trust.

- (ii) Example: S purchased Whiteacre in 2005 and the deed was made “to S in trust for S1.” At the time deed was executed, S and S1 agreed in writing that S1 would live on Whiteacre and pay \$1k per month in rent to S. Is this a valid trust?
 - 1. No. All facts indicate that S really intended a landlord-tenant relationship with S1.

(7) A **lawful purpose...**

- (a) So a trust cannot:
 - (i) Call for commission of a crime.
 - (ii) Call for destruction of property.
 - (iii) Have a condition against public policy.
- (b) Exam tip: watch for trusts restricting marriage or promoting divorce.
 - (i) Example: R created a testamentary trust in his will and he directed the trustee to pay income to his daughter “until she divorced her worthless husband and upon her divorce that trust shall terminate and all principal shall be distributed to daughter. If daughter does not divorce him then on her death the trustee shall distribute the principal to the Red Cross.” Is this a valid trust?
 - 1. No because it promotes divorce.
- (c) But if a purpose can be found that is *not* offensive to public policy then it is valid.
 - (i) I.e., a trust that gives income to a spouse until that spouse remarries is ok.
 - (ii) Example: In his will, J set up a testamentary trust with income going to his wife for life or until she remarries and upon his wife’s death or remarriage to his son. Is this a valid trust?
 - 1. Yes, because the underlying purpose is valid – to provide for his widow during her widowhood.
- (d) Marriage restrictions to members of a certain religion or ethnic group *are valid* as permissible partial restraints on marriage.
 - (i) Example: in his will, J set up a testamentary trust with the principal going “to my son providing he marries a Jewish woman within 7 years after my death. If he does not do so the trust principal shall be paid to the state of Israel.” Is this a valid trust?
 - 1. Yes because he still has a fairly wide choice. His options are not unduly restricted.

(8) In a **validly executed** document.

- (a) Must be in writing;
- (b) Signed by both settlor and trustee; **and either**
 - (i) Acknowledged by a notary public; or
 - (ii) Signed by 2 witnesses.

2) **Types of trusts**

a) All trusts are considered irrevocable unless stated otherwise.

b) **Revocable lifetime/intervivos trusts**

i) There must be at least one beneficiary who is not the settlor.

(1) The settlor cannot be the sole beneficiary when also named the sole trustee
(to ensure a true fiduciary relationship).

ii) Settlor:

(1) Can be a trustee.

(2) Can be the income beneficiary for life.

(3) Settlor's estate can be one of the beneficiaries of the principal so long as there is at least one other beneficiary.

(4) Can retain the power to terminate or amend the trust.

iii) Reasons to have a revocable lifetime/intervivos trust:

(1) Manages assets efficiently, particularly using a professional trustee.

(2) Helps plan for possible incapacity by avoiding guardianship.

(a) Trustee has title to property, so no need for guardian appointment.

(3) Avoids probate

(a) No part of the principal of a trust goes through the settlor's estate in probate.

iv) Reasons not to have a revocable lifetime/intervivos trust:

(1) Does not avoid taxes.

(2) If a settlor keeps an income interest, or keeps a power to revoke, the full trust assets will be included in the settlor's gross estate for federal estate tax purposes.

c) **Pour-over gifts**

i) Testamentary gifts (gifts made in a will) to an existing revocable trust.

(1) This is ok.

(2) Such gifts avoid will formalities in the trust.

(3) Trusts can be changed during the lifetime of the settlor in ways that are somewhat easier than changing a will.

ii) Requirements for a pour-over gift to a trust to be valid:

(1) Trust must be in existence, or

(a) Trust need not be created by settlor, but it can be any existing trust, including those executed by other persons.

(b) Pour-over gift is valid even if the trust was unfunded or only partially funded during settlor's lifetime.

(2) Executed concurrently with the will.

(a) Example: R executed his will on 1/3/2004. In his will, he provided that the bulk of his estate would go to a trust that would pay the income "to his daughter for life, with the principal then paid to her Son." His lawyer drafted the trust document the week before and failed to have R execute it at the time of the will execution. When R's lawyer discovered that R did not execute the trust document at the time of the will execution, he called R and had him return to execute the trust document. The trust document was executed on 1/10/2004. Is the pour-over gift to the trust valid?

(i) No. The trust was not executed before or concurrently with the will.

iii) **Life insurance proceeds**

(1) Ways an insured can make life insurance proceeds payable to a trust:

(a) Insured can create an unfunded revocable insurance trust and name the trustee of the trust as policy beneficiary.

(b) Have the trust be a testamentary trust and have the insurance policy contract name "the trustee named in my will" as the life insurance beneficiary.

(2) Proceeds of savings accounts or pension plans can be handled in this same way.

d) **Totten trust**

i) Also called a bank account trust.

(1) The Totten trust is a bank account in the depositor's name "as trustee for" a named beneficiary.

(a) Example: M opened a bank account at First National Bank and the account name is "M as Trustee for J."

(i) This is a Totten trust.

ii) Remember:

(1) Depositor makes deposits and withdrawals as he wishes during depositor's lifetime.

(2) Beneficiary has no interest in it is the depositor's lifetime but gets whatever is in the account when the depositor dies.

iii) No particular words are needed to create a Totten trust.

(1) Example: depositor opened an account entitled "J ITF ["in trust for"] R." Is this a Totten trust account?

(a) Yes. ITF is enough to indicate "in trust for" and thereby create a Totten trust account.

iv) Revoking a Totten trust:

- (1) Withdraw all money from the account.
- (2) Express revocation made during lifetime by depositor.
 - (a) Needs a writing
 - (b) Naming the beneficiary and the financial institution, and
 - (c) Having revocation notarized and delivered to the bank.
 - (i) If any of these are missing, the whole attempted revocation is invalid.
- (3) Revocation in a will.
 - (a) Must comply with the same requirements for revocation during lifetime.
 - (b) Example: D died leaving the bulk of his funds in 2 accounts at Bank. The names of the accounts were "D in trust for N" and "D in trust for N1." He also left a will, which had the provision "I revoke all 'in trust' bank accounts that I have at Bank and give the amounts on deposit to my new friend F." Does F get the money?
 - (i) No. This is not a valid revocation because no beneficiaries of the Totten trust accounts are named in the will.
- (4) Death of the beneficiary
 - (a) Revokes the Totten trust and the money in the account goes free and clear to the depositor.
 - (i) Example: D opened an account at Bank in the name of "D in trust for B." 1 year later, B was killed in car crash leaving a son and daughter as survivors. On her death there was a balance in the account of \$57k. B's son and daughter claimed that they had an immediate right to claim the \$57k as heirs to B's estate or should be replaced as beneficiaries to Totten trust. Can they get either?
 1. No. When beneficiary dies, the money in the account goes free and clear to depositor D and beneficiary's heirs get nothing.

v) Changing beneficiaries

- (1) Can be made by depositor but it must be done the same way as a revocation.
- (2) Notarized statement send to the financial institution that names the old beneficiary and the new one.

vi) Creditors of the depositor can always reach Totten trust account balance, either before or after depositor's death, since it is a form of revocable trust revoked partially each time a withdrawal is made.

- (1) Example: D opened an account at Bank called "D in trust for B." D closed all her other bank accounts and placed the money in this Totten trust. D made deposits regularly over the years and withdrew little money from the account. She financed her living expenses mostly to charges on

her credit cards. When she maxed out her cards, she told the credit card companies that she had no money and no assets in her name except for the Totten trust account, in which she was merely a trustee for B. The companies sought to reach all the money in the Totten trust account. Who wins?

(a) The credit card companies because the creditors of the depositor can always access the Totten trust balance.

e) **Joint bank accounts that are not Totten trusts** [“John and Jane with right of survivorship”]

i) Issue: when one of the parties of the account dies, can anyone block the money from going to the survivor of the joint tenancy?

(1) Sometimes

(a) Example: H opened an account in the names of himself and his son, Hjr. Name of the account was “H depositor and Hjr depositor, payable to either, or to the survivor of them.” [rights of survivorship] When H died he was survived by his son Hjr and his daughter. He had no assets at death except for \$200k in the joint account. Daughter sued to get half of the amount in the account, asserting that H opened the account only to allow Hjr to pay H’s bills and never intended that Hjr should get the entire account on H’s death. She introduced several letters from H to her indicating that she would get half of the account on his death and that he did not understand the meaning of the words “or survivor of them.”

(i) Can daughter successfully challenge the survivorship provision of the account?

1. Perhaps.

(2) If clear and convincing evidence shows that a survivorship was not intended when the account was established, and that the account was opened only as a matter of convenience to the depositor, then the survivorship language can be set aside.

(a) This is a hard requirement to satisfy.

ii) Each joint account holder owns $\frac{1}{2}$ of the joint account, no matter who deposits the money.

(1) If one person makes the entire deposit it is considered a gift of $\frac{1}{2}$ to the other account holder.

(2) Example: H opened an account in the names of himself and his son, Hjr. Name of the account was “H depositor and Hjr depositor, payable to either, or to the survivor of them.” H opened the account with a deposit of \$100k.

(a) Who owns the \$100k during the lifetimes of H and Hjr?

(b) H owns \$50k and Hjr owns \$50k as a gift from H.

- (3) Example: What if Hjr knows H is very ill, goes to bank and withdraws all the money, an amount that has grown to \$200k. Then H dies. H's executor under his will sues Hjr to recover the money Hjr took from the account before H's death.
 - (a) Can Hjr be forced to return any of the money he withdrew?
 - (i) Yes. He severed the joint tenancy by unilateral and unauthorized withdrawal of the entire amount.
 - (ii) He could be made to return \$100k, the amount that he removed that is in excess of what was his lifetime gift.
 - (b) If Hjr had not withdrew any money, he would have gotten all of it through rights of survivorship.

iii) **NY Uniform Transfers to Minors Act (UTMA)** – [ripe for testing]

- (1) Reasons to make a gift to a minor under UTMA:
 - (a) It avoids guardianship proceedings.
 - (b) It avoids a trust and government supervision over trusts.
 - (c) It qualifies for the \$13k/donee annual exclusion from federal and state gift tax.
- (2) Gifts under UTMA must be made to a custodian (not a trustee) and it must specify that it is made under the NY UTMA.
- (3) UTMA gifts can be made in a will so long as the same required statutory language is used.
- (4) Duties of a UTMA custodian:
 - (a) Hold, manage, and invest the property under a prudent person standard;
 - (b) Pay over to the minor or for the minor's needs what part of the property that the custodian deems advisable; and
 - (c) Pay what is left of the property to the minor when minor turns 21 (with a post-1996 gift) or 18 (with a pre-1997 gift).
- (5) UTMA does not create a trust. It is a special statutory conservatorship, where the custodian does not hold legal title to the property. The minor holds that.
- (6) Tax consequences:
 - (a) If donor names himself as custodian, then the amount of the gift is includible in the custodian's gross estate for federal and state estate taxes.
 - (b) If donor names someone else as custodian, then the amount of the gift is not includible.

f) **Charitable trusts**

i) Things to remember:

(1) The charitable trust must have indefinite beneficiaries and they must be a reasonably large group.

(a) Cannot have specific, named persons as beneficiaries for a charitable trust.

(i) Example: Settlor created a trust to pay income for the health care and costs of education to “all of my children” for life and on death distribute principal to “all my grandchildren” to improve their health and education. Is this a valid charitable trust?

1. No, because the beneficiaries are a small group of identifiable beneficiaries.

(ii) Example: Settlor created a trust “to provide scholarships for the benefit of the descendant of the settlor.” Is this a valid charitable trust?

1. No, same reason. This is not a large enough group.

(iii) Example: Settlor created a trust “to benefit all orphans in Syracuse.” Is this a valid charitable trust?

1. Yes because this group is potentially large enough to qualify.

(iv) Example: Settlor created a trust to benefit all orphans attending Syracuse University. Is this a valid charitable trust?

1. Unclear, because the class needs to be not so narrowly defined that just a few people benefit. It falls between the rules.

(v) Example: Settlor created a trust “to benefit all orphans living next door to me at 815 Albany Ave.” Is this a valid charitable trust?

1. No. The group is too small.

(b) Exception: a trust for **Masses** for relatives is ok.

(i) Example: Settlor created a trust “to pay for the costs of Masses for the repose of souls of the testator, his deceased parents, and other relatives.” Is this a valid charitable trust?

1. Yes, it qualifies under the Masses exception.

(2) Charitable trusts must be for a charitable purpose.

(a) Health, education, and religion are the most common.

(3) Charitable trusts may be perpetual.

(a) They are not subject to the rule against perpetuities (RAP), which indirectly limits the duration of trusts.

(4) Cy Pres can be used to change the trust.

(a) If the stated purpose of the charitable trust can no longer be accomplished, or the designated charity goes out of existence, the court may use this to make the trust be as near as possible to what the settlor wanted.

- (5) The Attorney General (AG) has the duty of representing the beneficiaries of charitable trusts in the state.
 - (a) The AG is an indispensable party to any suit on construction or enforcement of a charitable trust.
 - (b) The AG and donor have standing to sue to enforce the trust's terms.

g) **Non-trusts**

- i) These are called trusts, but they are *not* trusts.
- ii) **Honorary trusts** – where no human being is beneficiary of a private trust.
 - (1) The trustee is on his honor to perform the duties – there is no beneficiary to enforce. A private trust must have a human beneficiary.
 - (2) Example: S's will attempted a testamentary trust by giving \$10k to her Friend as trustee "to use the trust income to care for my beautiful rose garden."
 - (a) Is it a valid trust?
 - (i) No. Gardens are not human beings and no human is beneficiary.
 - (b) What happens to the \$10k?
 - (i) It falls into the residuary estate.
 - (3) Exceptions:
 - (a) Pet trusts
 - (i) This is a statutory exception that is valid for the lifetime of the pet.
 - (ii) Someone is either designated in the will or appointed by the court, who can enforce the trust and make sure the trust's purposes are carried out.
 - (iii) Example: S's will bequeaths \$50k to her Sister, as trustee, to use the income to care for her Dog. Is this a valid trust?
 - 1. Yes, by virtue of NY's Pet Trust Statute.
 - (b) Cemetery trusts
 - (i) Trusts for perpetual care and maintenance of cemeteries are categorized as charitable trusts and are OK even though there are no human beneficiaries.
 - (ii) There is also no RAP problem with these, since they are called charitable trusts.
- iii) **Constructive trusts**
 - (1) This is a flexible equitable remedy designed to disgorge unjust enrichment that results from wrongful conduct.
 - (2) The trustee's only duty is to convey the property to the person who, in equity, should have the property.

(3) Example in a will hypo:

- (a) In 1992, testator M executed a will that devised all her property to her brothers Mel and Marvin. By 2005, M lost confidence in Mel and Marvin and thought they were out for her money. She decided to change her will and left her property to the Girl Scouts. When M told Lawyer of her plans and asked him for a new will, L told Mel that he and Marvin were cut out of new will. When M went to sign the new will, Mel and Marvin were waiting for her to convince her that changing the will was a bad idea. M refused to change her mind to sign the new will, Mel and Marvin caused a disturbance in L's office and prevented M from signing the new will. In the new will was a provision revoking the old ill. M suffered stroke in L's office and died the next day.
- (i) The question of who gets M's property is complicated by the wills rule that requires all wills to be signed by the testator before 2 witnesses.
- (ii) Can you probate the new will leaving property to Girl Scouts?
1. No. The new will was not signed and witnessed.
- (iii) Was the old will validly revoked by the new will?
1. No. The new will was not signed and witnessed.
- (iv) Do Mel and Marvin win as beneficiaries of the old will?
1. No. They hold title on a constructive trust and they have a duty to transfer title to the Girl Scouts because otherwise they would be unjustly enriched by their wrongful conduct.

(4) Example to an intestacy hypo:

- (a) J has 2 children, R1 and R2. R1 has 2 children, M1 and M2. In a fit of anger, R1 shoots J to death. J died intestate (without preparing a will). Intestacy statute would give J's property to his 2 children in equal shares. Who gets J's estate?
- (i) Intestacy statute says $\frac{1}{2}$ to R1 and $\frac{1}{2}$ to R2.
- (ii) But R1 killed J, which is wrongful conduct, which would result in unjust enrichment to R1.
- (iii) Result is a constructive trust and the property would go as if the wrongdoer had predeceased J. R1's $\frac{1}{2}$ would go to his children, M1 and M2.

iv) **Resulting trust**

(1) This is an equitable remedy.

(2) PMRT = purchase money resulting trust.

(a) This is NOT recognized in NY.

(i) On exam, tell them that NY does NOT recognize this.

(b) A PMRT only arises when the purchaser buys property and has title put in someone else's name (who is not a relative). Later, purchaser claims no gift was intended and asks title holder for title to be returned and the title holder refuses.

(c) Most states would find a PMRT in this case, which would allow the purchaser to compel the title holder to give up title.

(i) But not in NY.

(d) Example: M bought beach house but wanted to conceal the purchase from her Husband. M made down payment using money she earned by doing neighbor's laundry. She had title taken in name of her Friend. A few years later, upon divorcing her husband, M asked F to transfer title to her. F refused. M sued F to force the conveyance of the property from F to M on grounds that the oral understanding between them justified a resulting trust that would compel the transfer of the property to M. F argued that the parol evidence rule bars any testimony contradicting the deed. Who wins?

(i) In most states: M because of the PMRT.

(ii) In NY: F because there is no PMRT in NY.

(3) NY exception to the no-PMRT rule:

(a) If there is clear and convincing evidence that the grantee had expressly or impliedly promised to reconvey the land to the purchaser, then a constructive trust can be imposed to benefit the purchaser. (because of fraud or deceit)

(b) Example: M had title taken in F's name, assuming that F would transfer title to her when M asked. F refused when M asked. In NY, can M sue to force F to transfer title?

(i) No. There is no PMRT in NY, and because there is no clear and convincing evidence of a promise to reconvey the title to the property.

(c) Example: M had title taken in F's name. At the closing in the Lawyer's office, F promised M that she would transfer title to M whenever M asked. This comment was heard by the purchaser, M, M's lawyer, F's lawyer, and Mother Teresa, who were all in the room at the same time. In NY, can M sue to force F to transfer title?

(i) Yes. There is clear and convincing evidence that F promised to convey to M when asked.

- h) **Statutory spendthrift rule and protection from creditors**
- i) Protects a trust beneficiary's interest from creditors by prohibiting voluntary or involuntary transfer of the beneficiary's interest.
 - (1) I.e., creditors cannot demand payment from the trust.
 - (2) Creditors are kept at bay until income is paid to the income beneficiary.
 - ii) In NY, there is automatic spendthrift protection unless you specifically state otherwise. (you must opt out)
 - (1) In other states, you have to actively put a spendthrift clause in.
 - (2) NY has a special statutory rule that protects all income interests in trusts with spendthrift protection even if the trust does not contain the clause, **but** this only applies to income from trust, not principal.
 - (3) To provide spendthrift protection to the remainder beneficiary (i.e., the one who gets the principal) then the spendthrift clause must be expressly stated in the trust.
 - (4) Example: J created a trust "to pay income for life to J1 and then on J1's death the principal of the trust is to be transferred to P."
 - (a) Who can the spendthrift clause protect?
 - (i) J1 as the income beneficiary, or P as the remainder beneficiary, or both.
 - (b) In NY, who gets the protection automatically?
 - (i) J1, the income beneficiary.
 - iii) Typical language for a spendthrift clause:
 - (1) "No beneficiary of this trust shall have the power to assign his interest, nor shall such interest be reachable by the beneficiary's creditors by attachment, garnishment, or other legal process."
 - iv) Exceptions to the spendthrift clause:
 - (1) Creditors who furnish necessities.
 - (a) Food, clothing, shelter.
 - (2) Child support and alimony.
 - (3) Federal tax liens.
 - (4) Excess income beyond that needed for support and education.
 - (a) A last resort remedy: have to show all other possible remedies have been exhausted.
 - (b) What is needed for support is based on the life style of the beneficiary.
 - (5) The 10% levy provided by CPLR 5205(e).
 - (a) This is available to all judgment creditors.
 - (b) All creditors together share the levy; it is not 10% per creditor.

- (c) Example: Party Patty was the income beneficiary under a trust. Because of irresponsible spending patterns she had many debts and 4 of her creditors sued and gained judgments against her. The trust was subject to the NY spendthrift rule. Can the creditors reach any or all of P's income interest under the trust?
 - (i) Yes. They can use the 10% levy even if the trust income is subject to a spendthrift clause.

v) Limitation on spendthrift clause:

- (1) Self-settled trust rule (created by settlor for benefit of settlor)
 - (a) Spendthrift protection does not apply to any interest retained by the settlor.
 - (i) Example: Settlor created a valid lifetime trust with provision "trustee shall pay the income for life to S and on S's death, the trustee shall distribute the trust principal to S's son, Sjr. 5 years later, while S was alive, a creditor obtained a judgment against S for \$250k. Can creditor reach the income interest of S even though the trust is subject to the spendthrift rule?
 - 1. Yes because there is no spendthrift protection to any interest retained by the settlor.
 - (ii) Example: what if S had put an express spendthrift clause in the trust that would extend to his income interest and to the remained interest as well
 - 1. Is income interest protected?
 - a. No. Any interest retained by the settlor is not protected by a spendthrift clause, whether it is statutory spendthrift clause or an express clause.
 - 2. Is the principal protected?
 - a. Yes. Settlor is not the remainder beneficiary.
 - (b) So settlor can protect other beneficiaries, but they cannot hide from their own creditors.
 - (i) All revocable trusts are available to settlor's creditors. Even if the settlor has no immediate financial interest in the trust, but settlor retains the power to revoke, then the trust offers no protection at all against creditors of the settlor.

3) **Modification and termination of trusts** [law is reluctant to make changes to settlor's intent]

- a) Trust modification by trustees and/or beneficiaries:
 - i) Is appropriate only when the objectives of the trust would be defeated or substantially impaired if it is not modified.
 - (1) The purpose of the trust comes first, overriding any specific directions in the trust.

- ii) Example: Pulitzer, a newspaper publisher, established a trust to provide income to his wife, children, and grandchildren. He directed the trustee to keep and not sell the principal trust asset, stock in his newspaper. Over the years, losses at the newspaper resulted in virtually no income to be paid to the income beneficiaries. Trustee petitioned the court to allow the sale of the newspaper stock so the funds could be more broadly diversified and thus provide income to the beneficiaries. Could the trustee sell the stock, notwithstanding the direction of the settlor that the stock not be sold?
 - (1) Yes. The primary purpose of the trust was to provide income to the Pulitzer family and retention of the stock was just incidental to that.
- b) 2-level modification test
- i) Find out the **primary intent** of the settlor regarding trust purposes.
 - ii) Look at **specific directions** in the trust instrument to determine whether, because of changes in circumstances, those specific directions in trust would now frustrate the primary intent of the trust. **If so**, then those directions can be changed by the court.
 - (1) Example: H established a trust consisting of his large mansion which was never to be sold, but which his wife would be allowed to live in during her lifetime and on her death, pass to his daughter. Over the years, neighborhood changed and became a heavy manufacturing area. All houses in the area except for settlor's were torn down and replaced with factories. Trustee petitioned to have the restriction on the sale of the house removed so it could be sold and proceeds used to buy the widow a house in a more suitable neighborhood. Should the petition be granted?
 - (a) Yes. Primary purpose is to provide a house to wife and give house to daughter. The specific direction was to keep this house, but changed conditions frustrates that intent.
 - iii) The court can authorize the invasion of the principal if the income is not enough to carry out the settlor's purpose of the trust.
 - (1) Example: G died in 2000, leaving a will that created a trust. Income was to his Wife for life, remainder to his Son. W was 80-years old and ill. W wanted to move into a retirement home that would cost \$5k/month. The trust corpus was producing only \$45k/year in income. That, plus SS would not pay for the retirement home. W petitioned the court to make annual distributions of principal to supplement her income. S objected, pointing out that the trust did not give the trustee any power to distribute principal and that any such distribution would be taking away his money. Can the court authorize invasions of principal on W's behalf?
 - (a) Yes, by statute the court can authorize distribution of principal to carry out the settlor's trust purposes.

- c) Trust termination by the settlor
 - i) Trusts are **irrevocable** and **unamendable** unless the power to revoke and amend is expressly reserved in the trust instrument.
 - ii) Exception: a settlor can terminate an irrevocable trust if all beneficiaries in being consent.
 - (1) This is often impossible because no one can give consent for any beneficiary who is a minor or who is incompetent.
 - (2) Beneficiaries must be alive to count: a child in gestation is not regarded as a person for trust termination.
 - (3) If a trust gives property to **heirs or next of kin**, that interest is not considered a beneficial interest and thus no consent need be obtained from them (as they cannot be ascertained until the decedent's death).
 - (a) Note: a living person has no heirs or next of kin. Heirs or next of kin are people entitled to another's property by intestate distribution at the time of a death of a decedent who failed to leave a valid will.
 - iii) Example: In 2000, N created a valid irrevocable lifetime trust "income to N for life and on her death, the principal goes to N's daughter O; but if O is not then living to O's then living children. N now wants to terminate the trust and O, with 2 minor children, agrees. Should the court allow the trust to be terminated?
 - (1) No. No one can consent for O's minor children. (not even their mother)
 - iv) Example: What if O has no children but is 6 months pregnant? Can the trust be terminated?
 - (1) Yes. For purposes of trust termination, a child in gestation is not considered a person whose consent is required.
 - v) Example: In 1999, Jim created a valid irrevocable trust "income to Jim for life, then to his Daughter for life and on D's death, the principal shall go to D's heirs at law." Can Jim now terminate the trust if D agrees?
 - (1) Yes. The remainder gift is to D's heirs and that is not considered a beneficial interest requiring consent.

4) **Trust administration**

- a) Trustee's powers
 - i) Controlled by NY Fiduciary Powers Act (FPA).
 - (1) Sets out powers that can be exercised by a trustee without court order and without express authorization in the trust.
 - (2) The FPA also controls what an executor or administrator of a decedent's estate can do.

- ii) General approach to trustee's powers in NY
 - (1) Trustee can do almost anything, with some clearly defined specific exceptions.
 - (2) Trustees **can**:
 - (a) **Sell** any real or personal property
 - (b) **Mortgage** property
 - (c) **Lease** property
 - (d) Make **ordinary repairs**
 - (e) **Contest, compromise, or settle** claims
 - (f) Do almost anything needed to **manage** the corpus of the trust.
 - (3) Trustees **cannot**:
 - (a) **Engage in self-dealing**
 - (b) **Borrow money** on behalf of trust
 - (c) Continue a **business**
 - (i) Trustee is liable for losses incurred by the business unless trustee has court approval to continue the business.
- b) Self-dealing
 - i) **Prohibitions on self-dealing**
 - (1) Trustee cannot buy or sell trust assets to himself
 - (a) This is an absolute rule.
 - (b) Example: T desired to buy stock held by the trust because he thought that the stock would greatly increase in value. He purchased the stock paying the trust \$110/share. The trading value of the stock on the day of the purchase was \$96/share. Was this a prohibited transaction?
 - (i) Yes. A trustee cannot buy or sell trust assets on his own behalf.
 - (2) Trustee cannot borrow trust funds
 - (a) This is an absolute rule.
 - (b) Example: Trustee was in desperate need of funds. He could sell several bonds to raise money but he did not want to do so. He borrowed \$5k from the trust, giving as security a \$10k treasury bond. He promised to pay the trust an annual interest rate of 9%. The current interest rate was 7.5%. Was this a prohibited transaction?
 - (i) Yes. A trustee cannot borrow money from a trust.
 - (3) Trustee cannot lend money to the trust
 - (a) This is an absolute rule.
 - (b) Any interest earned on such a loan must be returned to the trust and any security given for the loan is invalid.

- (4) Trustee cannot profit from serving as trustee (except for appropriate trustee fees)
 - (a) Trustee cannot take advantage of confidential information received while trustee.
 - (5) Corporate trustee cannot buy its own stock as a trust investment
- ii) **Affirmative duties on self-dealing**
 - (1) Duty to segregate trust assets from personal assets.
 - (a) Remedy for violation of this duty:
 - (i) If commingled funds are used to buy an asset and the assets goes down in value, the conclusive presumption is that personal funds were used.
 - (ii) If the asset goes up in value, the conclusive presumption is that trust funds were used.
 - (2) Duty to earmark trust assets by titling them in trustee's name
 - (a) I.e., "John Jones, Trustee" not just "John Jones"
- c) **Remedies for breach of fiduciary responsibilities**
 - i) Beneficiary can sue to remove the trustee
 - ii) Beneficiary can ratify the transaction and waive the breach
 - (1) Example: Trustee sells the trust stock in T's Gold Mine. At time of sale the trust paid T \$20/share over the trading price of the stock on that date. By the time the beneficiary learned of the transaction the stock in T's Gold Mine had skyrocketed to \$600/share, 6x what the trust paid T for it.
 - (a) Was this a prohibited transaction? Yes.
 - (b) Does the beneficiary want to rescind the purchase? No, beneficiary can ratify the transaction.
 - iii) Beneficiary can sue for any loss
 - (1) **Surcharge action** – action to recover losses to the trust.
- d) **No further inquiry rule**
 - i) Breach of a fiduciary duty by engaging in self-dealing is an automatic wrong and no further inquiry need be made. The trustee loses.
 - (1) Good faith is not a defense.
 - (2) Reasonableness is not a defense.
- e) Actions against a third party when trustee engages in self-dealing
 - i) If trustee engages in a prohibited transaction (such as self-dealing) and sells trust property to a 3rd party, the beneficiary cannot sue the purchaser of property from the trustee if that purchaser was a bona fide purchaser (BFP) for value without notice.

(1) Example: A testamentary trust named T as trustee. T borrowed \$250k from the trust, giving the trust a 6-month note at 10% interest. The then-prevailing rate was 9%. T took the money and bought a rental property with the \$250k. 6 months later he sold the property to T1 for \$300k.

(a) Was the transaction by T acceptable?

(i) No. Trustee is not allowed to borrow money.

(b) Can the beneficiary sue T1?

(i) No, if she did not know that she was dealing with a self-dealing trustee (BFP).

ii) To keep purchaser from being a BFP and thus making the purchaser liable to the beneficiary, the purchaser not only has to know that she was dealing with a trustee, but that the trustee was engaged in self-dealing.

f) **Indirect self-dealing**

i) Self-dealing rules also apply to loans or sales to a relative of the trustee, or to a business of which the trustee is an officer, employee, partner, or principal shareholder.

(1) Example: From above, what if T1 was T's sister? T1 did not know that T bought the property with improperly borrowed money from the trust. Is T1 protected from suit by the beneficiary?

(a) No because the self-dealing rules apply to relatives or businesses associated with the trustee.

g) **Exculpatory clauses** (one who purports to relieve trustee of liability)

i) Cannot be used to shield trustee from liability for breach of a fiduciary duty in a testamentary trust because relieving an executor or testamentary trustee from liability for negligence is void as against public policy.

ii) Can be used in a lifetime/inter vivos trust.

5) **Liability of trustee in contract and tort**

a) Personal liability of trustee in contract:

i) How trustee signed the contract is key to determining liability,

(1) If trustee signed only on behalf of the trust, no personal liability.

(2) If trustee signed personally and merely mentioned the trust, then trustee has personal liability.

(3) Example: T signed contract as "Mary, Trustee of the Jones trust."
Personal liability of trustee?

(a) Yes, because she just noted that she was trustee of the Jones trust.

(4) Example: T signed a contract as "Jones Trust, by Mary, Trustee."
Personal liability of trustee?

(a) No because the language shows that the contract was with the trust, not the trustee.

- (5) Example: T signed a contract as “Mary, as Trustee of the Jones trust and not individually.” Personally liability of trustee?
 - (a) No because the contract is with the trust.
- ii) Even if there is no personal liability, the trustee will be reimbursed by the trust if:
 - (1) The contract was within the powers of the trustee, **and**
 - (2) The trustee was acting in the course of proper administration of the trust.
- b) Personal liability of trustee in tort:
 - i) Trustee is personally liable for all torts by the trustee of the trustee’s employees.
 - (1) This is an absolute rule.
 - (2) Trustee should buy liability insurance to protect against this and charge the cost to the trust.
 - ii) Trustee can get reimbursement from the trust for any tort claims if:
 - (1) Trustee must have been acting within the powers of the trustee’s powers (when the tort was committed), **and**
 - (2) The trustee was not personally at fault.
 - iii) Example: Trustee’s employee was negligently driving a truck carrying trust files to a storage facility when truck collided with Plaintiff. P was seriously injured and sued T for negligence of his employee and received a judgment of \$1million. Can T get reimbursement from the trust for the judgment?
 - (1) Apply 2-part test:
 - (a) Was the trustee acting within his powers when the tort was committed? Yes, trust files were being taken to storage.
 - (b) Was trustee personally at fault? No, negligence was trustee’s employee.
 - (2) Reimbursement is justified because both requirements are met.
 - iv) Example: Same facts, except now T was driving the truck that struck P. Can T get reimbursement from the trust for this judgment?
 - (1) No, because T was personally at fault.
- c) Trustee’s investment power
 - i) Trustee must manage the property of the trust on behalf of the beneficiary.
 - (1) This means the investment of the corpus of the trust.
 - ii) NY has adopted the Uniform Prudent Investor Act (UPIA).
 - (1) This gives broad latitude to trustees to choose investments.
 - iii) Trustee can pursue what UPIA calls the modern portfolio theory of investment where the trustee creates a custom-tailored investment strategy for this particular trust.

- iv) Remember:
 - (1) Trustee must consider the role each investment plays within the overall trust portfolio.
 - (2) Trustee must consider the expected total return from income and capital gain.
- v) Trustee does not have to justify the prudence of each investment by itself. He can balance off risky speculative investments against safe, conservative investments.
- vi) Specific things to remember:
 - (1) Prudence is not measured by hindsight.
 - (a) Look at decision to invest when it was made, not later. Trustee does not need to have a crystal ball.
 - (2) Trustee can exercise adjustment power and allocate capital gains to income.
 - (a) Can do this if necessary to protect the income beneficiary, and vice versa.
 - (b) The end goal is fairness to all beneficiaries.
- vii) The key to UPIA is **flexibility** [exam likes this term] to shape the investment strategy for maximum total return, along with flexibility to adjust income between the income and remainder beneficiaries to be fair to each of them.

6) Rule against perpetuities (RAP)

- a) Rule: no interest is valid if it could vest later than any life in being at the time of the creation of the interest + 21 years.
 - i) An interest is vested when there is no condition that has to be satisfied and the exact identity of the taker is known.
 - ii) If there is any possibility that an interest could vest later than lives in being +21 years, it is void.
- b) NY has a perpetuities reform statute that automatically reduces all age contingencies to 21 years, thus saving the gift.
- c) Example: J conveyed Blackacre to his Son for life, remainder to the first of S's children to reach 30 years. Does the gift over to the first of S's kids to reach 30 violate RAP?
 - i) So this vests when S's children reaches 30. Until then, the interest is contingent.
 - ii) MBE answer: Yes. Vesting could take longer than the RAP timeframe.
 - (1) S is the life in being (measuring life). S can have a child after the conveyance and S can die. Child ___ make it to 21 years past S's death.
 - iii) NY answer for NY essays: No because the NY RAP reform statute automatically reduces the age contingencies to 21.

- d) RAP and trusts
 - i) Example: J conveyed Blackacre to his Son for life, remainder to the Bank in trust, to pay the income to Grandson for life, and then to pay the principal to any child of G who reaches 30.
 - (1) Does the income interest of G violate RAP?
 - (a) No. Interest is vested now. G is alive and no conditions need to be satisfied.
 - (2) Does the principal interest in a child of G who reaches 30 violate RAP?
 - (a) MBE: Yes.
 - (b) NY: No.
- e) **NY Rule Against Suspension of the power of Alienation** [applied in addition to RAP]
 - i) Any interest is void if it suspends the power of alienation for a period longer than lives in being + 21 years, that is, when there are no persons who could, together, transfer fee simple title.
 - (1) No beneficiaries alive who can agree and join to transfer a fee simple, power of alienation is suspended, if period is longer than LIB + 21 years, then it is void.
 - ii) Suspension of alienation is a concern when either:
 - (1) Spendthrift income interests are in the trust, **or**
 - (2) A life estate is created in an unborn person, or in an open class that may possibly include unborn persons.
 - iii) Example: O to A and his heirs so long as no liquor is consumed on the premises and if liquor is ever consumed then to B and her heirs.
 - (1) Is the suspension rule violated by this grant?
 - (a) No because A and B together could agree to transfer a fee simple within their own lifetimes + 21 years.
 - (2) Does the gift over to B violate RAP?
 - (a) Yes because the vesting in B's interest might take place beyond the RAP period of A & B's lifetimes + 21 years.
 - iv) Example: J created a trust that provided income to her Sister for life, then on S's death to pay the income to S's children for their respective lives and at the death of S's children, remainder to B. At J's death, S, who is 30 years old, has one child, S1.
 - (1) So S's children's interest vest at S's death. We will know who S's children are at her death, which is well within the RAP period.
 - (2) Is RAP violated? No, B's remainder is vested.
 - (3) Is the suspension rule violated?
 - (a) Yes because upon creation of the trust, S could joint the other beneficiaries to transfer a fee simple absolute, since the class gift to S's children includes potential unborn children who cannot give consent in an unborn state and who will not have a life in being to validate the duration of their spendthrift income interest.

- f) Recap RAP and suspension rule
 - i) RAP:
 - (1) Deals with vesting only
 - (2) Just says for an interest to be valid, it must vest within lives in being at time of grant + 21 years.
 - (3) Look at facts to make sure there is no way the vesting could come outside the time period of the rule. If there is a chance, then the interest is void.
 - ii) Suspension rule:
 - (1) Does not deal with vesting. It is only concerned with the possible suspension of the ability to transfer a fee simple.
 - (2) Look for facts to make sure there are persons identified and alive who could together convey a full fee simple. If you cannot find such persons who could do this during LIB + 21 years, then the interest is void.
 - (3) Remember that the perpetuities reform statute provision reducing age contingencies to 21 years also apply for saving gifts from suspension rule violations,
 - (4) [look for contingent remainder to children of named person, an open class who may include unborn who may ____]