By **Trisha W. Hall** & **Gregory J. Weinig**

Serving as Trustee Without a Safety Net

When not obtaining a beneficiary's consent may be a fiduciary's best option

Serving as a trustee requires managing risk. That takes many forms—among them, requesting or requiring the consent of a trust's beneficiaries before a trustee performs a discretionary act (or, alternatively, a release of liability for doing so). This isn't to say that a trustee seeks consent to actions it knows would otherwise breach its fiduciary duties; prudent trustees won't perform a discretionary act if it clearly contravenes the trust's governing instrument or its duties to the beneficiaries. Rather, because trusts can seem complicated to a layperson, and trust and tax law even more so, trustees may fear that even if they take the prudent course in exercising discretion to act a certain way, one or more beneficiaries may not fully understand and might even sue. A trustee might also seek consents if the governing instrument's terms aren't entirely clear about the trustee's authority. Because the financial and reputational cost of a lawsuit far exceeds that of obtaining beneficiary consents, consents serve as an efficient risk management tool.

Some discretionary acts warrant a beneficiary's consent more than others—for example, decanting to a new trust, merging a trust into another, resigning as corporate trustee in favor of an individual trustee, terminating a trust and modifying a trust's terms. To be effective, a beneficiary's consent must be fully informed and not the product of misrepresentation, fraud or concealment. After a beneficiary provides an effective consent to a trustee's actions, that beneficiary will be barred from asserting a claim against the trustee for those actions.[1]

Obtaining a beneficiary's consent won't be problematic in these and most other situations involving a trustee's exercise of its discretion. But, there are times when a trustee may want to think twice before requesting a beneficiary's consent. Most of these considerations relate to the beneficiaries themselves and their particular circumstances. Others are tax-driven. Let's explore those occasions when a trustee might prefer to act without the safety net of consents.

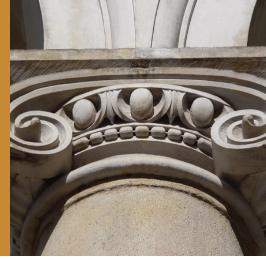
Potential Tax Consequences

A beneficiary may be treated as making a taxable gift when a non-beneficiary trustee exercises a power that increases or creates a new interest in a trust if the beneficiary fails to object to that exercise or certainly if the beneficiary affirmatively consents to it, especially when objecting to it would have prevented or reversed it.[2] It doesn't matter that the donees of the deemed transfer haven't yet been born.[3] Nor does it matter that the deemed transfer is difficult or impossible to value.[4]

This potential outcome could result from a decanting, as in the case of *Estate of Mayer*.[5] In *Mayer*, the trustees of a testamentary trust sought the court's approval to decant because New York's decanting statute allows a trustee to decant an irrevocable trust if he has "absolute discretion," and the trust's governing instrument authorized the trustee to distribute principal only for the limited purposes of health, education, maintenance and support. The court held that a beneficiary's consent to an unauthorized trustee decanting wouldn't make it valid and instead would be considered a gratuitous transfer by the beneficiary:

> The consents of the presumptive remaindermen

Trisha W. Hall and **Gregory J. Weinig** are partners at Connolly Gallagher LLP in Wilmington, Del.

> in this proceeding cannot enlarge the discretion of the trustee and thus bring the trust within the ambit of [the statute]. If affirmative consent of the remaindermen is determinative, then the appointment in further trust occurs by the beneficiaries' gratuitous transfer rather than the exercise of fiduciary discretion. Such a transfer presumably would be ineffectual to achieve the proposed transfer tax savings and, in any event, would be unauthorized by state law [internal citation removed].[6]

Other situations in which a beneficiary's consent to a trustee's discretionary decision may result in adverse transfer tax consequences to her are a distribution to other non-consenting beneficiaries via the trust's termination or a change of trust situs and governing law to a jurisdiction that changes the meaning of "descendants" to include adopted children when they weren't originally included,[7] both of which may result in gift tax being imposed on the deemed transfer from the consenting beneficiary to those who received distributions or were added to the trust.

Special Needs Beneficiary

If a trust's governing instrument authorizes the trustee to convert it into a supplemental needs trust that's currently subject to an ascertainable standard, the trustee would be wise not to seek the consent of the special needs beneficiary. If the beneficiary were to consent to that action, it could be construed as a transfer of an available resource under Medicaid regulations.

Divorcing Beneficiary

In *Ferri v. Powell-Ferri*, the Connecticut and Massachusetts courts confronted a trust for a divorcing spouse's sole benefit over which he had no rights of withdrawal, which had in turn been decanted from a predecessor trust over which he could withdraw up to 75 percent of the trust's principal (and which was soon to increase to the full trust balance during the divorce proceedings). The Supreme Court of Connecticut (where the divorce was occurring) certified certain trust-related questions to the Supreme Judicial Court of Massachusetts (whose law governed the trusts). The latter court upheld the decanting. In doing so, part of its analysis depended on its sister court's recitation of (in turn) the Connecticut trial court's finding that the beneficiary hadn't consented to (and hadn't even been informed of) the decision of the trustees (one of whom was the beneficiary's brother and business partner) to decant.[8] Had the beneficiary consented to the trustees' decision to decant, the result may well have been different in both states.

Some states, such as Delaware, allow a trust to be a "silent" trust with respect to the trust's beneficiaries with express language waiving the trustee's duty to provide information about the trust and its administration to the beneficiaries.

Confidentiality

Some states, such as Delaware, allow a trust to be a "silent" trust with respect to the trust's beneficiaries with express language waiving the trustee's duty to provide information about the trust and its administration to the beneficiaries.[9] Many silent trust instruments drafted within the last couple of years prohibit the trustee from providing such information to the beneficiaries and, in light of doing so, designate one or more individuals to represent such beneficiaries with respect to the trust. However, some silent trusts, especially older ones, don't provide such a clear prohibition. Instead, they may simply waive the duty—for example, "the trustee is under no duty to provide information about the trust or the administration of the trust to the beneficiaries who are

under the age of forty." Under such language, the trustee may be tempted to request the consent of one or more beneficiaries when exercising its discretion. Perhaps the trustee decides to diversify a concentrated portfolio after the death of the grantor's spouse, to whom the silent provisions don't apply, but because the family founded the company whose stock represents the largest holding, prefers to do so only after the now-current beneficiaries

In some cases, such as a dynasty trust on its third or fourth generation, the sheer number of beneficiaries may make obtaining consents from all of them too costly or unrealistic.

(who are all adults under the age of 40) consent. Seeking the beneficiaries' consents may violate the terms of the trust instrument, or certainly the grantor's intent, which may come back to bite the trustee.

In other cases, it may be that obtaining consents for a trustee action causes disharmony among the beneficiaries. For example, if a beneficiary receives a loan from the trust for a need that he wouldn't want his sibling co-beneficiaries to know about, requesting consents may cause ill-will among the family and directly against the trustee.

Practicalities

Often, it may be impractical to obtain consents from beneficiaries or cause more problems than it's worth. A beneficiary may be notoriously fickle, in which case his consent today may be the trustee's problem tomorrow—even if a court would uphold the action based on the consent, the beneficiary may become a nightmare to deal with. A beneficiary may be "off-the-grid"—a competent adult (by legal standards) whose whereabouts are known—but who won't engage with the trustee for any reason. In some cases, such as a dynasty trust on its third or fourth generation, the sheer number of beneficiaries may make obtaining consents from all of them too costly or unrealistic.

For beneficiaries who are minors, not yet born, incompetent or unascertainable, a virtual or designated representative named in the trust's governing instrument or provided for by state law may consent to a trustee's action.[10] However, if the trustee action places the individual who would represent that beneficiary in conflict with the interests of the other beneficiary she would be representing, virtual representation may either be unavailable or not clearly reliable.

In some cases, the beneficiary may be a competent adult whose whereabouts are known, but those whereabouts are a prison or other public or semi-public institution where she isn't allowed privacy. In this case, sending documentation to the beneficiary about informed consent for the trust may cause the beneficiary harm by alerting third parties to the trust as a potential resource of the beneficiary.

Consents may provide a trustee with some certainty that an exercise of its discretion won't prove costly. In most cases, this will indeed hold true. However, in some situations, the trustee's best course of managing risk will be to fly without a safety net and forgo consents altogether.

Endnotes

1. *Bogert's Trusts and Trustees,* Section 941, "Consent."
2. Treasury Regulations Section 25.2512-8. *See also* Revenue Ruling 81-264 (failure to demand payment on loan after statute of limitations expired deemed a gift because the donor relinquished control over the ability to enforce the note) and Rev. Rul. 84-105 (failure to object to an accounting that showed an underfunding of a testamentary trust by the executor was held to be a gift).
3. *See* Treas. Regs. Section 25.2511-2(a). *See also Robinette v. Helvering,* 318 U.S. 184 (1943) (taxpayer was treated as having made a gift of no ascertainable value to then non-existent grandchildren). *See also Smith v. Shaughnessy,* 318 U.S. 176, 180 (1943) (gift tax reaches property that's merely conceptual or contingent).
4. *See* Treas. Regs. Section 25.2511-1(e).
5. *Estate of Mayer,* 672 N.Y.S.2d 998 (N.Y. Sur. Ct. 1998).
6. *Ibid.,* at p. 1001.
7. *See* Private Letter Rulings 200917004 (April 4, 2009) and 9308032 (Nov. 30, 1992).
8. *Ferri v. Powell-Ferri,* 72 N.E.3d 541, 544 (Mass. 2017).
9. 12 Del. C. Section 3303(c).
10. *See, e.g.,* 12 Del. C. Sections 3339 (designated representatives) and 3547 (virtual representation).