

HOUSE BILL REPORT

SB 5302

As Reported by House Committee On: Judiciary

Title: An act relating to the prudent investor rule for Washington state trusts, delegation of trustee duties by trustees of a Washington state trust, and standards for authorization and treatment of statutory trust advisors and directed trustees incident to the establishment of Washington state directed trusts.

Brief Description: Addressing the prudent investor rule for Washington state trusts, delegation of trustee duties by trustees of a Washington state trust, and standards for authorization and treatment of statutory trust advisors and directed trustees incident to the establishment of Washington state directed trusts.

Sponsors: Senators Benton and Mullet; by request of Washington State Bar Association.

Brief History:

Committee Activity:

Judiciary: 3/19/15, 3/26/15 [DP].

Brief Summary of Bill

- Amends trust laws to modify standards for the delegation of a trustee's powers and duties and standards for the investment of trust funds.
- Establishes a new chapter, the Washington Directed Trust Act, authorizing specific powers or duties relating to a trust to be vested in a "statutory trust advisor" and establishing standards relating to exercise of those powers and duties and the role and liability of the directed trustee in a directed trust.

HOUSE COMMITTEE ON JUDICIARY

Majority Report: Do pass. Signed by 13 members: Representatives Jinkins, Chair; Kilduff, Vice Chair; Rodne, Ranking Minority Member; Shea, Assistant Ranking Minority Member; Goodman, Haler, Hansen, Kirby, Klippert, Muri, Orwall, Stokesbary and Walkinshaw.

Staff: Edie Adams (786-7180).

This analysis was prepared by non-partisan legislative staff for the use of legislative members in their deliberations. This analysis is not a part of the legislation nor does it constitute a statement of legislative intent.

Background:

Trusts provide a means of transferring real or personal property. A trust is created by a trustor, who gives his or her property to a trustee. The trustee holds legal title to the property, but only manages the property for the benefit of other individuals specified by the trustor. The beneficiaries hold equitable title to the property, meaning the beneficiaries enjoy the property, but do not have control over the trustee or how the trustee manages the legal title. Trusts can be made revocable or irrevocable by the trustor. Revocable living trusts are commonly used as an alternative to traditional wills as a way to pass property when a person dies.

Washington statutes governing trust and estate law address a range of issues relating to trusts, including the requisites for creating and amending trusts, the duties and powers of trustees, trust administration, distribution of assets, liability issues, and the investment of trust funds. The Trust and Estate Dispute Resolution Act (TEDRA) provides procedures for resolving trust and estate disputes.

Trustee's Power to Delegate.

A trustee has a number of powers with respect to managing the property of the trust, including the power to employ third parties, such as lawyers, investment advisors, or accountants, to advise or assist the trustee in the performance of the trustee's duties or to perform any act. A trustee may not delegate all of the trustee's duties and responsibilities and must use reasonable care in selecting and retaining the person to whom duties are delegated. A trustee who delegates duties to a third person remains liable for the person's discretionary acts that, if done by the trustee, would result in liability to the trustee. A trustee or successor trustee may sue the person to collect damages suffered by the trust estate even though the trustee might not be personally liable for these damages.

Investment of Trust Funds.

A fiduciary managing trust property is required to use a total asset management approach, which requires consideration of the role that a particular investment or investment course of action plays within the overall portfolio of assets. Factors that a fiduciary must consider include:

- the probable income and safety of capital;
- marketability of investments;
- general economic conditions;
- length of the term of investment;
- duration of the trust
- liquidity needs;
- requirements of the beneficiaries;
- other assets and earning capacities of the beneficiaries; and
- effect of investments in increasing or diminishing liability for taxes.

In applying the total asset management approach, a fiduciary must exercise the judgment and care that persons of prudence, discretion, and intelligence exercise in the management of their own affairs. A fiduciary who has special skills or expertise is under a duty to use those skills or expertise.

Unless limited by the trust instrument, a fiduciary may acquire and retain any kind of property and every kind of investment, including debentures and other corporate obligations and stocks which persons of prudence, discretion, and intelligence acquire for their own account.

Summary of Bill:

Standards for the delegation of a trustee's duties to third parties and for the investment of trust funds are revised. A new chapter is created authorizing statutory directed trusts.

Trustee's Delegation of Powers and Duties.

The standards for a trustee's delegation of his or her powers or duties are revised. A trustee may delegate duties and powers that a prudent trustee of comparable skills could properly delegate under the circumstances. The trustee must exercise reasonable care, skill, and caution in selecting a delegate, establishing the scope and terms of the delegation, periodically reviewing the delegate's actions in order to monitor the delegate's performance and compliance with the terms of the delegation, and enforcing the delegate's duties. A trustee who complies with these requirements is not liable to the beneficiaries or to the trust for an action of the delegate.

A delegate owes a duty to the trustee to exercise reasonable care to comply with the terms of the delegation. A delegate, by accepting a delegation of powers or duties from the trustee, submits to the jurisdiction of the courts of this state.

Investment of Trust Funds.

A trustee must exercise reasonable care, skill, and caution to manage and invest trust assets as a prudent investor would, considering the purposes, terms, distribution requirements, and other circumstances of the trust.

A trustee must consider the following specified circumstances in investing and managing trust assets if relevant to the trust and beneficiaries:

- general economic conditions;
- possible effect of inflation or deflation;
- tax consequences of investment decisions;
- role each investment or course of action plays in the overall portfolio;
- expected total return from income and the appreciation of capital;
- other resources of the beneficiaries;
- needs for liquidity, regularity of income, and preservation or increase of capital; and
- an asset's special relationship or value to the trust or to one or more beneficiaries.

Decisions concerning an individual asset must be made considering the whole trust portfolio and the overall investment strategy having risk and return objectives appropriate for the trust.

Washington Directed Trust Act.

A new chapter is created establishing the Washington Directed Trust Act (WDTA), which allows a trustor to direct specific powers or duties to third parties, called "statutory trust

advisors," rather than having all powers and duties vested in the trustee. The WDTA applies to a trust only if the governing instrument expressly invokes the WDTA and the situs of the trust is in Washington. A governing instrument is the will, trust instrument, court order, exercise of power of appointment, or binding agreement that appoints, designates, or provides for a method of appointing a statutory trust advisor under the WDTA.

Powers and Duties of Statutory Trust Advisors. A statutory trust advisor is a person who under the terms of the governing instrument has a power or duty to direct, consent to, or disapprove an action, or who has a power or duty that would normally be required of a trustee. Unless otherwise provided in the governing instrument, the statutory trust advisor has the sole and absolute discretion regarding the exercise of a power, and his or her decisions are binding on all parties. The powers and duties of a statutory trust advisor include the power to:

- direct the acquisition, management, disposition, or retention of trust investments;
- direct a trustee to make or withhold distributions to beneficiaries;
- consent to a trustee's action or inaction relating to investments and distributions to beneficiaries;
- increase or decrease any interest of a beneficiary;
- grant, terminate, or amend a power of appointment to beneficiaries;
- modify or amend the governing instrument to achieve favorable tax status or respond to changes in tax laws or other laws affecting trust administration;
- appoint a successor trustee, trust advisor, or statutory trust advisor, or remove a trustee, trust advisor, or statutory trust advisor as allowed in the governing instrument; and
- change the governing law or principal place of administration of the trust.

A statutory trust advisor has a fiduciary duty with respect to each granted power to act in accordance with the term and purposes of the trust and solely in the interests of the beneficiaries. A statutory trust advisor who has any of the statutorily specified powers does not have a duty to monitor the administration of the trust to determine whether that power should be exercised unless requested by the trustee or a qualified beneficiary or required in the governing instrument. A governing instrument may not relieve a statutory trust advisor from his or her fiduciary duty or from the duty to act in good faith and with honest judgment.

Statutory Trust Advisor Appointment and Vacancies. Procedures are provided for a statutory trust advisor to accept or decline appointment, or resign as statutory trust advisor. A statutory trust advisor is entitled to reasonable compensation. By accepting appointment, a statutory trust advisor submits personally to the jurisdiction of Washington courts and may be made a party to any action relating to his or her decision, action, or inaction.

If there is a vacancy in the position of statutory trust advisor, the trustee has the power or duty that otherwise would be vested in the statutory trust advisor until a statutory trust advisor is appointed according to the governing instrument or by court order. A trustee is not liable for failing to exercise or assume a power or duty of the statutory trust advisor for 60 days from the date the trustee learns of the vacancy.

Remedies for Breach of Duty by Statutory Trust Advisor. A trustee or beneficiary of the trust may file an action in court when a statutory trust advisor breaches a fiduciary duty or

threatens to breach a fiduciary duty. The action may seek to compel the statutory trust advisor to perform his or her duties, enjoin the statutory trust advisor from committing a breach of duty, compel the statutory trust advisor to redress a breach of duty, require the trustee to assume responsibility for a power or duty given to the statutory trust advisor, remove the statutory trust advisor or reduce or deny compensation to the statutory trust advisor, impose an equitable lien or constructive trust on trust property, or trace wrongfully disposed of trust property to recover the property or its proceeds. A trustee or beneficiary may also seek any other remedy available by statute or common law, including damages.

A statutory trust advisor who breaches a fiduciary duty is liable for the greater of the amount required to restore the value of the trust property and distributions or the profit made by the statutory trust advisor as a result of the breach. The court may excuse a statutory trust advisor from liability if the advisor acted reasonably and in good faith under the circumstances known to the advisor.

A statutory trust advisor is protected from liability relating to any power, duty, or function granted or reserved exclusively to a trustee or another statutory trust advisor.

Statutory Trust Advisor's Duty to Report and Right to Information. A statutory trust advisor has a duty to: keep the trustee and qualified beneficiaries reasonably informed of the administration of the trust; provide the trustee with requested information relating to the administration of the trust; and provide a qualified beneficiary with requested information necessary for the qualified beneficiary to enforce his or her rights under the trust.

A statutory trust advisor may request from a trustee or beneficiary information that is reasonably necessary for the statutory trust advisor to perform his or her duties under the governing instrument. A statutory trust advisor may file an action under the TEDRA for determination of matters relating to the statutory trust advisor's duties or functions.

Directed Trustees. A "directed trustee" is a trustee that, with respect to a particular duty or function:

- must follow the direction of a statutory trust advisor, to the extent the trustee follows the direction;
- may not undertake the particular duty or function without direction from a statutory trust advisor, to the extent the trustee fails to undertake the duty or function due to absence of direction from the statutory trust advisor;
- must obtain consent or authorization of a statutory trust advisor, to the extent the trustee timely seeks but fails to obtain consent or authorization; or
- must obtain consent or authorization of a statutory trust advisor, to the extent the trustee obtains consent or authorization, but only if and to the extent the governing instrument indicates that the protections of directed trustee status are intended.

A directed trustee is not liable for any loss resulting from following directions of the statutory trust advisor actions taken with the statutory trust advisor's consent, or an action or inaction of the statutory trust advisor relating to any power of the statutory trust advisor. A directed trustee also is not liable for any loss resulting from a failure to take any action proposed by the directed trustee that requires the statutory trust advisor's prior consent, if the directed trustee sought but was unable to the consent.

A directed trustee when following the directions of a statutory trust advisor generally has no duty to monitor, advise, or consult with the statutory trust advisor, communicate with or warn any beneficiary concerning matters the directed trustee may have exercised in a different manner from the manner directed by the statutory trust advisor, or commence a proceeding against the statutory trust advisor. However, these limitations do not relieve a trustee of the duty to act in good faith and with honest judgment.

An action of a directed trustee relating to matters within the scope of the statutory trust advisor's authority are presumed to be administrative actions solely to allow the directed trustee to perform his or her duties, and the administrative actions do not constitute an undertaking by the directed trustee to monitor the statutory trust advisor or otherwise participate in actions within the scope of the statutory trust advisor's authority.

Other Provisions. Specified other chapters of law governing trusts are made applicable to a statutory trust advisor with respect to his or her powers, duties, or functions in the same manner as if the statutory trust advisor were acting as a trustee with respect to those powers, duties, and functions. The TEDRA is amended to apply to determinations of issues relating to the powers and duties of a statutory trust advisor or directed trustee under the WDTA.

Appropriation: None.

Fiscal Note: Not requested.

Effective Date: The bill takes effect 90 days after adjournment of the session in which the bill is passed.

Staff Summary of Public Testimony:

(In support) Trusts allow a trustor to transfer assets to a trustee for the benefit of a third party, and they are important in the wealth management field. The legislation is a joint effort between the Washington State Bar Association and the Department of Financial Institutions to improve our trust laws in light of modern trends, create more transparency and clearer expectations, and allow more flexibility for those creating trusts. The legislation will create a center for wealth management in the state, which will attract other investment businesses to the state. The changes in the legislation put Washington in line with other states. The standard for investment of trust assets comports with the prudent investor standard under the Uniform Prudent Investor Act. Trusts are becoming more specialized, requiring management by persons with specialized skills. The delegation provision will allow trustees to engage persons with specialized skills to help them manage their trusts.

(Opposed) None.

Persons Testifying: Mark Roberts, Washington State Bar Association; and Richard Riccobono, Department of Financial Institutions.

Persons Signed In To Testify But Not Testifying: None.