

SENATE BILL REPORT

SB 5302

As Reported by Senate Committee On:
Financial Institutions & Insurance, January 28, 2015

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: Financial Institutions & Insurance: 1/21/15, 1/28/15 [DP].

SENATE COMMITTEE ON FINANCIAL INSTITUTIONS & INSURANCE

Majority Report: Do pass.

Signed by Senators Benton, Chair; Angel, Vice Chair; Mullet, Ranking Minority Member; Darneille, Fain, Hobbs, Litzow and Pedersen.

Staff: Susan Jones (786-7404)

Background: A trust is a form of ownership of property that separates responsibility or control of the property from the benefits of ownership. A trust is created by a trustor, who transfers the property to a trustee. The trustee holds legal title to the property and manages the property for the benefit of the beneficiaries.

Delegation. A trustee has many powers provided in statute. In exercising these powers, the trustee may employ other persons (a delegate) to advise or assist the trustee or to perform any act. The trustee may not delegate all of the trustee's duties and responsibilities; must use reasonable care in selecting and retaining the delegate; and is not relieved from liability for the delegate's acts.

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.

Trust Investments. The trustee is a fiduciary with respect to a trust. In investing, a fiduciary must consider the role that the proposed investment or investment course of action plays within the overall portfolio of assets. In applying the total asset management approach, the fiduciary must exercise the judgment and care that a prudent person would exercise in the management of the fiduciary's own affairs and consider a number of factors.

Summary of Bill: Delegation by Trustee. A trustee may prudently delegate the trustee's duties and powers provided the trustee takes reasonable care, skill, and caution in (1) selecting a delegate, (2) establishing the scope and terms of the delegation, (3) reviewing and monitoring the delegate's performance, and (4) enforcing the delegate's duties. If the trustee acts with that reasonable care, the trustee is not liable for the delegate's actions. A delegate owes a duty to the trustee to exercise reasonable care and the trustee has a duty to require the delegate to account for the delegate's actions. By accepting the delegated duties, the delegate, wherever domiciled, is subject to the jurisdiction of Washington courts.

Washington Directed Trust Act – Opt In. The Washington Directed Trust Act (act) is created and applies to a trust only if (1) a will, trust instrument, court order, power of appointment, or agreement (the governing instrument) specifically calls for the act's application and (2) the trust situs is Washington State. The act allows a trustor to direct specific functions to third-parties – statutory trust advisors and directed trustees, rather than conferring all authority, duties, and liability upon the trustee.

Statutory Trust Advisor Defined – Powers, Duties, and Compensation. A statutory trust advisor (advisor) is as a person, including a trust advisor, special trustee, trust protector, or committee who is expressly called for under the terms of a governing instrument. The advisor has the power or duty to direct, consent to, or disapprove an action, or has the power or duty that would normally be required of a trustee. The advisor's powers and duties include the power to:

- direct 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;
- increase or decrease any interest of any beneficiary;
- grant, terminate, or amend a power of appointment to beneficiaries;
- modify or amend the governing instrument with respect to tax and other legal matters;
- appoint or remove a successor 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.

The advisor has the fiduciary duty to act in accordance with the trust terms and solely in the beneficiaries' interests, and must act in good faith and with honest judgment. The advisor has no duty to monitor the administration of the trust to determine whether the power should be exercised except upon request of the trustee or a qualified beneficiary. The advisor is entitled to reasonable compensation.

Remedies Against an Advisor – Court Matters. If an advisor breaches or threatens to breach a fiduciary duty, a trustee or beneficiary may file an action. An advisor who breached a duty is liable for the greater of (1) the amount lost because of the breach; or (2) the profit made from the breach. The court may excuse an advisor from liability if the advisor acted

reasonably and in good faith under the circumstances known to the advisor. The statute of limitations on claims against a statutory trust advisor is generally three years from when a report adequately disclosing the existence of a potential claim was delivered. By accepting the appointment the advisor submits to the jurisdiction of Washington courts even if the investment advisory or other agreements provide otherwise.

Vacancies – Duty to Inform and Report. If there is a vacancy, the trustee may act until a new advisor is appointed; however, a trustee is not liable for failing to act for 60 days from the date the trustee learns of the vacancy. The trustee may petition the court to fill the vacancy if required under the governing documents. The advisor must: (1) keep the trustee and the qualified beneficiaries reasonably informed; (2) provide the trustee with requested information; and (3) promptly provide a requesting qualified beneficiary with information reasonably necessary to enable the beneficiary to enforce their rights under the trust with respect to the advisor.

Directed Trustee – Defined, Liability, Statutory Trust Advisor Actions. A directed trustee is a trustee who, with respect to a particular duty or function, must follow the direction of a statutory trust advisor; may not undertake the duty or function without a statutory trust advisor's direction; or must obtain the consent of a statutory trust advisor. A directed trustee is not liable for any loss resulting from (1) following the statutory trust advisor's direction or from actions taken with the advisor's consent; (2) certain actions or inaction of the statutory trust advisor; or (3) 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 in timely fashion, but did not obtain the consent. A directed trustee has no duty to monitor, advise, or take other action with respect to the statutory trust advisor.

Trust Investments. The trustee's duties with respect to investment is modified to a Portfolio Management Theory. The trustee must invest and manage the assets as a prudent investor would, by considering the purposes, terms, distribution requirements, and other circumstances using reasonable care, skill, and caution. The decisions must be evaluated based on the entire trust portfolio and as part of an overall investment strategy with risk and return objectives reasonably suited to the trust. The trustee must consider a number of factors. The trustee must use reasonable efforts to verify certain facts.

Appropriation: None.

Fiscal Note: Not requested.

Committee/Commission/Task Force Created: No.

Effective Date: Ninety days after adjournment of session in which bill is passed.

Staff Summary of Public Testimony: PRO: The act is designed to improve Washington trust laws in light of modern trends; creates transparency; provides clearer laws and expectations for those who create trusts and to those whom duties are delegated, advisors, and beneficiaries; creates best practices; modernizes current prudent investment standards and other provisions based on uniform laws enacted in other states, including 29 states with directed trust legislation; and allows families to create more flexible trusts than would be

allowed under common law. Prudent investor language provides consistency with other states and may attract trust companies from other states. These update prudent inventor rules and protect beneficiaries while allowing for various types of investments trusts may hold. The Washington State Bar Association Real Property and Probate Section vetted the bill with the bar's Elder Law and Litigation sections. The act protects consumers, including trustors and beneficiaries. The act encourages and attracts other investment businesses to Washington.

Persons Testifying: PRO: Richard Riccobono, Dept. of Financial Institutions; Erik Strom, Russell Investments; Mark Roberts, WA State Bar Assn. Real Property Probate and Trust Section.