



I've Got a Secret: Unveiling the Secret Sauce of Drafting a Delaware Trust

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Cook-Off Menu

A photograph of a wooden table with a bowl of vibrant green soup, a smaller bowl of white rice, and fresh basil leaves. The text 'Cook-Off Menu' is overlaid at the top.

- **Three Main Ingredients**
- **Key Sections of the Governing Agreement**

Case Study Overview – The Child Family

Guy Child wishes to create Dynasty trusts for his three children, Alton, Ina and Julia. Alton and Ina each have adult children while Julie's children are minors.

Guy intends to name a corporate Trustee but wants his brothers, Bobby and Ted, to be involved with making the investment and distribution decisions. The document is being drafted by his attorney, Alex, who Guy thinks should also play a role.

Under the terms of the governing agreement, Guy's children are to be considered as the primary beneficiaries. They are to receive the net income and discretionary HEMS distributions. However, principal distributions may additionally be made to or for the benefit of Alton's, Ina's and Julie's issue.

Each child will be given a testamentary limited power of appointment in favor of their issue.

Each trust will be funded with marketable securities and shares of Guy's knife manufacturing company, representing a 20% concentration. Other family assets include a family limited partnership, a golf course owned in an LLC, and several commercial real estate properties.



Three Main Ingredients

- Importance of being “technically practical”
- Grantor’s Intent
- Default Rules – What happens if you do not do anything?

Where do I find the ingredients?

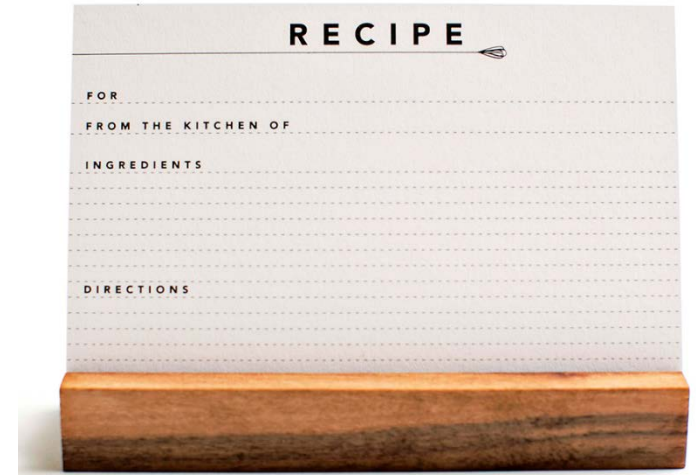


Statutory Provisions:

- Chapters 33, 35 and 61 of Title 12
- Rule Against Perpetuities – Chapter 5 of Title 25
- Tax Code – Title 30

Relevant case law will come from decisions of the Delaware Supreme Court and Court of Chancery.

Grantor's Intent is Paramount In Delaware



- Beneficiary's benefit vs. Grantor's intent
- 12 Del. C. §3303(a) – Fundamental Principle
- Echoed in other statutes
 - § 3302(e)
 - § 3586
 - § 3306
- Cases reinforcing this perspective
- Only a few things that cannot be overridden by the terms of a trust

Something to Remember.....

- Please remember - many of the techniques and protections available in Delaware are only available through the addition of specific terms to the trust.
- So, what happens if the Grantor fails to address something in the trust?

Default Rules: What Happens If You Do Not Do Anything?



The Delaware Default

Notice to Beneficiaries	All current and vested remainder beneficiaries must be given reasonable information.	<i>McNeil, 798 A. 2d 503, aff'g 792 A. 2d 190</i>
Duty to Diversify	Can be waived.	12 Del. C. § 3304
Dissenting Co-trustee	Possible from liability for failure to actively oppose majority, unless instrument exculpates.	12 Del. C. § 3304
Resignation	Court order needed if no path in the instrument.	12 Del. C. § 3326
Monitoring	Co-fiduciaries must keep each other informed.	12 Del. C. § 3317
Investments	Each Trustee responsible, under prudence person standard.	12 Del. C. § 3302
Life Insurance	Trustee responsible to monitor carrier, evaluate policy options.	12 Del. C. § 3302(d)
Investment positions	Diversification required.	<i>Estate of Hedge</i> 1984 Del. Ch. LEXIS 455
Multiple beneficiaries	Impartiality required.	<i>McNeil v. Bennett, 792 A.2d 190</i>
Transactions with Affiliates	Detailed disclosure rules.	12 Del. C. § 3312
Advisors' status	Fiduciaries.	12 Del. C. § 3313
Loans to beneficiaries	Must be for specified purposes.	12 Del. C. § 3325(19)
Discretionary distributions	Abuse of discretion.	12 Del. C. § 3315 <i>Merrill Lynch v. Campbell (2009)</i>

Co-Fiduciaries / Advisers



Co-Fiduciaries

- Define Trustee roles if there are multiple Trustees
 - “Trustee” versus “Trustees”
 - Independent versus Individual Trustee
 - Excluded Trustees - Administrative vs General (“Full”) Trustee
- Define roles potentially held by multiple parties (Advisers/Protectors)
 - “Distribution Fiduciary” and “Investment Fiduciary”
- Clarify where an Adviser or Special Trustee appointed for a specific situation or limited purpose
- Make it clear in directed trust language that all other language in the trust is subject to these provisions.
- Define the role as a fiduciary or non-fiduciary
- Establish the liability standards
- Define whether the role qualifies for compensation and the procedure for setting compensation

Allocation of Fiduciary Duties

- Define the allocation (cross reference versus broad provisions)
- Confirm the duty to keep co-fiduciaries informed – including the corporate Trustee
 - Define parameters and protocols
- Consider whether ancillary provisions should be allocated to other co-fiduciaries
 - Minors/ incapacity / GST provisions addressing source of distributions
 - Structuring loans as being investment or distribution related
 - Who has power/responsibility to insure an asset? Where do they get the value to be used for such insurance?
- Define how closely held assets will be administered
 - Power to create entities
 - Value closely held assets
 - Address the corporate Trustee's information requirements
- Define successor appointment and default provisions
 - Avoid circular patterns!



- There may be a lot of cooks in the kitchen – Be careful!
- With multiple fiduciaries, avoid inappropriate appointments, ambiguity, overlapping powers, power or duty gaps as well as potential conflicts.
- Let's discuss some examples...



Trustee Powers

Trustee Powers

- Defining the Trustee's powers
 - Should you limit to the governing instrument or should you state the terms are in addition to those provided by governing law?
- Define the permitted assets or investment strategies
 - Use broad or detailed language?
- Carve out key Trustee powers which should be retained, regardless if directed
 - Draft to reflect operational realities
 - Account for custody versus non-custody arrangements
 - What are the bare essentials for a trustee to retain?
- Confirming core Delaware Trustee responsibilities
- Setting compensation
- Establishing the liability standard

Dispositive Provisions



Highlighted Dispositive Provisions

- Remember Grantor's express intent will be given effect – take care when drafting these provisions.
 - The cases are instructive
 - Be absolutely clear “shall” vs “may”; “desire,” “wish,” or “hope” vs “intend”
- HEMS vs Absolute discretion
- Duty of impartiality
- Can external information or documents affect the interpretation of such language?

Legal & Tax Provisions



Highlighted Legal & Tax Provisions

- Define the termination provisions and who may trigger them
- Consider the extent to which administrative amendments may be made, and by which party
- Review situs considerations language and consider which parties should be given the ability to transfer situs
- Consider incapacity clauses applying to all parties, not just beneficiaries
- Consider language permitting the cost for accountings to be chargeable to the trust
- Consider which fiduciary will be responsible for tax provisions, filings and reporting (GST / QSST / ESBT / etc.)

Is an Excluded Tax Trustee a new role?

Notice Provisions



Notice Provisions - Considerations

- Judicial Accountings in Delaware are rare. Why?
 - In many instances the expense of such accounting will be borne by the Trustee.
 - *Res Judicata* is not assured even if one is filed.
 - Can an Adviser file an accounting?
 - What do you do if it's a quiet trust?
- Drafting suggestions:
 - Make it clear the “fiduciaries” are entitled to prepare and file accountings for judicial settlement (as well as any other action for construction or interpretation) at the expense of the trust.
 - Instruct that the trustee provide accounts in the form of statements to appropriate parties (beneficiaries, fiduciaries, designated representatives, and possibly the grantor)
 - Some will set out a period within which a beneficiary or those that represent them may object to the transactions reflected on the statement
 - If it is a quiet trust, consideration should be given to appointing a designated representative and it be made clear the designated representative may represent and bind the beneficiaries to whom they represent in any court proceeding, including an accounting.

Notice Provisions

Quiet Trust Provisions

- Remember express language is required
- Make clear this provision overrides all others
- Should be mandatory not permissive
- Time period needs to be addressed and should be reasonable
- Specifically address who shall receive information
 - Suggest the inclusion of a designated representative
- Address triggers for termination of quiet period
- Make sure no conflicts for those appointed

Miscellaneous Other Provisions

- Self dealing
 - § 3312 (c) affiliated investments
 - What about other self dealing (e.g. loans)?
 - Suggest a provision be added
 1. Tailored to the self dealing the grantor wishes to allow
 2. Address conflicts and self dealing for advisers as well
- Perpetuities
 - Express intent to be perpetual to fullest extent permitted by Delaware law
 - Add back up perpetuities provision (e.g. assets pouring over from another trust or real property).
- Spend thrift provision
 - Is *Garretson v Garretson*, 306 A.2d 737 (Del. 1973) applicable? Is any specialized drafting necessary? Any lessons learned from the *Mennen* decisions?

Miscellaneous Other Provisions

- Virtual Representation
 - Whether virtual representation is available through our statute (12 Del.C. § 3547) is not always clear.
 - Since some techniques and actions will hinge on whether virtual representation works, it is suggested that an express provision be included within the trust.

A close-up photograph of a thick, dark red sauce being poured from a glass bottle into a white bowl. The sauce is captured mid-pour, creating a smooth, continuous stream that falls into the bowl, forming a glossy, rounded puddle. The background is plain white, emphasizing the rich color and texture of the sauce.

What's your secret sauce?