

Trust Protectors 101

Irrevocable Trusts can be impacted by changes in the law and lives of beneficiaries. Trust Protectors watch over a trust for the length of the trust administration to mitigate problems that may arise.

Trust Protector Powers

A trust protector is an individual, or in some cases, a company, who is provided specific authority in the trust document.

Typically, a trust protector is granted the ability to:

- Remove or replace a trustee
- Change situs and governing law
- Correct errors or ambiguities
- Request accountings
- Interpret trust provisions
- Decant the trust into a new trust
- Grant a beneficiary a general power of appointment to allow for a step-up in basis

Somewhat less common powers include authority to:

- Add or remove beneficiaries
- Modify the trust
- Veto trustee decisions
- Direct the trustee

It's critical to review possible challenges that could arise during trust administration to understand how a trust protector could respond. A trust protector is most useful when its powers are very broad. In a general sense, the trust protector's chief responsibility is to safeguard the grantor's intentions and the welfare of the beneficiaries. The grantor's intentions or the beneficiaries' best interests could be compromised when an unforeseen change in the law or other challenge occurs, which is when a trust protector can take action.

Trust Modification Options

Legislative changes, declining health or unexpected disability of a beneficiary, and similar circumstances could prompt the need for trust modification. When a trust is established, the trust document is drafted to preserve the intent of the grantor, which generally includes serving the best interests of the beneficiaries. In order for trust administration to follow through with this intent, trust modification might be the solution.

Traditionally, modification of an irrevocable trust can be handled in a few different ways dependent upon the circumstances surrounding the trust, provisions in the trust document, and the jurisdiction where the trust is administered. Generally, courts must be petitioned to modify the trust. Other methods like decanting into a new trust may be possible, but not all trusts are eligible for decanting. Also, only certain states have statutes for decanting. Decanting is the process of creating a new trust with more favorable terms and transferring the assets of the old trust (or trusts) into the new one.

Two trust modifications options that bypass the need for court involvement are non-judicial settlement agreements and use of a trust protector. Non-judicial settlement agreements require unanimous approval by the grantor and all trust beneficiaries. Non-judicial settlements are not provided for by law in every state. Trust protectors, however, can be granted wide authority over trust modification. The trust protector can amend the trust as needed with no requirement for court approval.

Since some trusts may be in effect for multiple generations, the need for trust modification could arise several times. Unilateral action by a trust protector could save considerable legal and court fees.

Trustee Complications

In an ideal situation, the trust grantor selects a responsible trustee who properly administers the trust, maintains accurate accountings, and actively responds to changes in life and in the law that could impact trust beneficiaries. Trustees should have no conflict of interest with regard to trust assets or the beneficiaries. Several possibilities could disrupt trust administration, such as if the trustee:

- Misappropriates trust funds
- Makes negligent investment decisions
- Fails to provide distributions to beneficiaries
- Fails to provide accurate accountings
- Misses important tax deadlines
- Develops an addiction, disability, or health condition that prevents them from administering the trust
- Dies during the term of the trust

When any of the above or a similar event occurs, trustee removal is likely necessary. Provisions for removal and replacement of a trustee are usually in more modern trust documents. If a successor trustee has been named in the document, and the named party is able and willing to take over, the process may not be too complicated. However, in most cases action by a trust protector would be most expeditious, avoiding the need to coordinate action by multiple beneficiaries.

However, many older trusts lack any provisions for removal and replacement of trustees, or the power is limited; e.g., only a corporate trustee may be named. If removal power is not vested in the beneficiaries or a trust protector, court action is necessary.

Trust Protectors Over Time

Offshore trusts were the first tools that included trust protectors. Protectors first came into domestic use after Alaska passed legislation in 1997.

- Pre-1997 - Use in foreign trusts, primarily for increased asset protection
- 1997 - Alaska becomes the first state to recognize the use of trust protectors in domestic asset protection legislation. (Alaska Trust Act, ALASKA STAT. §§ 34.40.110, 13.36.370 Trust Protector). Delaware passed similar legislation on July 1, 1997.
- 1998 - 2016 - Nearly two dozen states enact or clarify legislation pertaining to trust protectors

Trust protectors are now often used in the United States by astute trust lawyers. As their benefits become more widely known, more jurisdictions are starting to formally recognize trust protectors.

Who Can Serve as Trust Protector?

A trust protector can be an individual, group of individuals, or an entity. Choosing a trust protector should be done with great care and consideration to the party's, experience, abilities, and character. Trust protectors must make decisions with respect to the law, tax and finance; therefore selecting a party with detailed knowledge of applicable law and asset management is the best practice. The chosen party should have no conflict of interest with the trust assets or individuals with interest in the trust.

The issue of whether a trust protector must serve in a fiduciary capacity has surfaced in recent years. While trustees are always held to fiduciary standards, not all trust protectors are regarded as fiduciaries. It depends on state law and the terms of the trust. A fiduciary must act in the best interest of the beneficiaries and has an ongoing duty to monitor the trust and act when prudent. If a trust protector serves in a non-fiduciary capacity, there is generally no ongoing duty. This makes acting as trust protector less risky and therefore holds down fees and induces more persons to serve. Learn more about fiduciary concerns associated with trust protectors and schedule time with an attorney to discuss more.

A trust protector can be an individual, entity, or committee. Depending on the goal of the trust maker, having multiple people on a committee of varying areas of expertise may prove beneficial.

Overall Benefits of Trust Protector Services

A trust protector can help minimize long-term costs and reduces time needed for the resolution of many administrative matters. Additionally, the role offers:

- **Avoidance of problems in old trusts.** In addition to legislative change, original trust terms may not be ideal after unforeseen life changes of beneficiaries or trustees, or simply be outdated.
- **Peace of mind.** Appointing a trust protector helps alleviate concern about establishing an irrevocable trust. A

trust protector can ensure a trustee acts as expected, that legal and financial changes are addressed, and the trust document remains current.

- **Flexibility.** Trust protector powers are defined in the trust documents. The grantor decides how much or little power the protector has and over which specific matters.
- **Privacy.** Grantors who select a non-familial party to serve as trust protector can help preserve the confidentiality of family trusts. This can help prevent hostility or resentment among family members.
- **Long-term protection.** A negligent trustee could embezzle or waste trust assets that the grantor may have worked his or her entire life to build. A beneficiary could develop an addiction that eats up all of their trust distributions. The trust protector works quickly to implement trust changes in response to these situations, whereas court action could take weeks or months.
- **Risk management.** Leaving an outright inheritance carries considerable risk. The heirs could be targets of a lawsuit, divorce claims, or start excessively spending their inheritance. Using a trust with a trust protector protects the grantor's legacy and ensures assets are available as intended. If a beneficiary develops financial or other trouble, a trust protector can modify the trust to provide additional protection.
- **Trustee support.** Trust protectors can counsel trustees and/or verify the trustees are acting in accordance with their duty under the law and the terms of the trust. The trust protector can help the trustee notice and avoid potential pitfalls and make decisions in line with the goals of the trust. The trust protector can also help the trustee proactively address changes in trust or tax laws that affect the trust, so that beneficiaries receive the best possible outcome. If it becomes necessary to remove a trustee, a trust protector will typically have the power to do so. Then, the beneficiaries are spared the need to go to court and ask for a removal, saving time and money, while reducing or eliminating emotional stress.
- **Easier dispute resolution.** Trust protectors can also potentially resolve a wide range of disputes. For instance, the grantor can specify that the trust protector will act as mediator in disputes between co-trustees, between a trustee and a beneficiary, or between the beneficiaries. By giving the trust protector the "final say" in these disputes, the grantor can help avoid the expense, hassle, and uncertainty of litigation. Simply giving the trust protector decision-making authority can shorten some disputes even further. For example, beneficiaries do not need to spend time and effort arguing that a trustee should be removed if the trust protector provides oversight and has the power to remove a trustee. The trust protector can also be given the power to sue or to defend lawsuits that involve the trust assets. By doing so, the grantor helps ensure that someone who understands their goals and intentions as they relate to the trust is present during the case to advocate on behalf of those goals and to center them in pursuit of the lawsuit's resolution.

Replacing a Trust Protector

Over time it may be necessary to replace a trust protector. Provisions for a successor may be included in the trust. However, these terms are not always present. In some situations, trust documents may have terms that allow for the beneficiaries or another named party to appoint a new protector. Learn more about replacing a trust protector.

Implementing Trust Protectors in New or Existing Trusts

Trust protectors can be included in both domestic and foreign trusts, and are easily added to existing and new revocable trusts as well as new irrevocable trusts.

When adding trust protector provisions to a new trust, consider having an attorney draft the terms with respect to clarity and fiduciary duty (see above section on Who Can Serve as Trust Protector). Ambiguous terms could invalidate a trust protector, while confusion over fiduciary status could cause conflicts over time.

Trust protectors can be added to some irrevocable trusts if the trust grantor is living. Different methods allow for this, including decanting. An attorney can advise whether including trust protector provisions would help to achieve the grantor's goals.

Conclusion

TrustCounsel recommends trust protectors in virtually all long-term trusts. We serve as trust protector through an affiliated company, TrustProtector, LLC, as well as offer counsel to trust protectors, trustees and beneficiaries. TrustCounsel, with 25 years of trust experience in trust administration, and TrustProtector, LLC, with 10 years of service as trust protector, stand ready to assist you with your trust.