

finals

LAW SCHOOL EXAM SERIES

TRUSTS

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INTRODUCTION

FINALS is a new law school preparatory series. It is designed to provide students with all the ammunition needed to succeed on their law school exams. Remember that **FINALS** is not simply another commercial outline series. Rather, each edition consists of several integrated sections. This edition contains a substantive outline, capsule summary outlines, diagnostic true-false questions, objective law school exam questions, essay exam questions, and fully detailed explanatory answers.

FINALS is designed to be used as a pre-exam study aid. You should be aware that most law schools are now implementing objective AND essay questions on their final examinations. In the past, virtually all law school exams were written solely in an essay format. No longer is this the case. Now the modern trend is to test students with objective and subjective types of questions. Why? There are two reasons.

First, objective questions on exams eliminate the subjectivity of essay grading. All too often, students complain about the lack of uniformity in the grading of law school essay exams. There are constant charges of favoritism, fraternizing, and “brown nosing.” Obviously, objective exam questions provide a uniform and reliable grading scheme.

Second, law schools are beginning to realize that it is necessary to start exposing students to objective-style questions as early as possible in preparation for the Multistate Bar Examination (commonly referred to as the “MBE”). The MBE is a uniform, national, 200-question multiple choice exam covering the six subject areas of Torts, Contracts, Real Property/Future Interests, Evidence, Constitutional Law, and Criminal Law/Procedure.

Forty-eight states have adopted the MBE as part of their exams. In fact, the MBE is now more important than the essays on most state bar examinations. Because of the increasing importance of the MBE, law schools are recognizing the need to start exposing students to an objective exam format.

Because **FINALS** is designed as a national law school study aid, many of the questions and answers follow the majority rule of law in effect in most jurisdictions. That’s why many of the explanations and rationales in **FINALS** refer

to the “Multistate,” or national, norm. Thus, **FINALS** can be used by students all across the country without taking into account regional differences.

This edition of **FINALS** includes three types of questions of varying difficulty. The true-false questions merely require the student to know the black letter law. These questions might be appropriate for a student to complete over lunch or on the bus, as they can be done in a short period of time and require less reasoning. The multiple-choice questions require knowledge of the black letter law and some legal reasoning skills. Therefore, students might want to do a few of these each day during the weeks leading up to final exams. Finally, the essay questions require deep thought and extensive legal reasoning. In order to thoroughly prepare for exams, students will want to do a number of each type of question.

Best of luck . . . and we’re sure that you will find **FINALS** to be a very valuable study aid in preparation for your law school exams.

TRUSTS

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TRUSTS

I. TRUST ELEMENTS

A. DESCRIPTION OF TRUST: A trust is a fiduciary relationship concerning specific property. Trusts typically arise when someone (the trustor or settlor) transfers legal title to property to another (the trustee), with directions for the latter to hold and distribute these assets for the benefit of others (the beneficiaries). Thus, it is often stated that, while the trustee holds legal title to the trust *res* (i.e., ownership stands in his name), equitable title (i.e., the beneficial interests) in that property is owned by the beneficiaries.

Once an effective transfer of property has been made to the trustee, the trustor is no longer the owner of those assets. The trustee is obligated to adhere to the terms of the trust with respect to the preservation, enhancement and distribution of the trust *res* to the beneficiaries. The trustee's responsibilities are ordinarily embodied in a writing (frequently called the "trust instrument"). Additionally, a trustee owes numerous implied obligations and responsibilities to the beneficiaries. Nevertheless, provided the trustee complies with the trust instrument, the beneficiaries cannot ordinarily affect or alter the trust.

B. ELEMENTS NECESSARY FOR A TRUST TO EXIST. The basic elements necessary for a trust to be created are described below.

1. **Trust intent.** The trustor must manifest, via words or conduct, a present intention to create a trust relationship. The trustor's intention is determined from the language utilized, his relationship with the parties involved, and any other appropriate circumstances.

a. **No special language.** No particular words (i.e., "trust") or actions are necessary to manifest the trustor's intention to create a trust.

Example: X conveys "Blackacre to Y, to hold and manage for Alice, Carole and Ted." If X has exhibited a special fondness for these three persons, a trust relationship would probably be found to exist. Y is the trustee, holding Blackacre (the trust *res*) in trust for Alice, Carole and Ted (the beneficiaries).

b. **Precatory language.** Where the trustor "suggests" or expresses only a "hope" that the property being transferred be utilized for the benefit of another, the requisite intent is usually deemed to be lacking. In certain contexts, however, precatory language has been interpreted as evidencing an intention to create a trust. For example, courts are likely to find a trust intent, despite precatory language, where the recipient of the property stood in a pre-existing fiduciary relationship with the trustor; the recipient of the property would not normally be an object of the trustor's bounty, but the alleged beneficiary is such a person; or the instructions to the recipient concerning the trustor's intentions with regard to use of trust property are detailed and specific.

Example: X gives \$10,000 to his friend Paul. At the time of the gift, X tells Paul that he "hopes" the latter will use the money for his daughter Pam's college education. This grant

would probably be viewed as a gift to Paul. Thus, Paul could use the \$10,000 in any manner he chose.

Example: X gives \$100,000 to A, her accountant. She advises A that she hopes he will use the income to pay \$1,000 a month to X's widowed sister, W, until such time as W remarries. The rest of the income is to be used for the support of X's son in some "sensible" career, other than practicing law. Under these circumstances, although X uses precatory (as opposed to mandatory) language, X probably intends to create a trust.

Example: X conveys "Blackacre to Z, with the expectation that Z will use the income for Ann's support and maintenance". While the language might be precatory, if X had previously assisted in Ann's support, a court might find that a trust relationship existed.

- c. **Gratuitous promises.** Where a purported trustor gratuitously promises to create a trust at some future point in time, the present intention to create a trust is lacking.

Example: T writes a letter to Y, in which he states, "I'm going to establish a trust for you as soon as I see my attorney". T's statement shows merely an unenforceable intention to create a trust in favor of Y at some future point in time.

- d. **Postponing elements.** If the trustor purports to create a trust, but designates certain prerequisites (i.e., delivery of the trust *res*, description of the beneficiaries, etc.) to be completed in the future, no "present" trust intent exists. However, if the trustor subsequently manifests a present intent when the missing element is furnished, the trust is effective as of the latter date.

Example: T transfers \$500,000 "to Joe, as trustee, for such persons as I shall name at a later point in time." No express trust has been formed at this time. Without beneficiaries, T lacks the present intent to create a trust. However, if T later hands Joe a paper that states, "The beneficiaries of the trust are Ann and Sally," a trust has probably been created as of the later date. T's intent to establish a trust at the later time is shown by the writing which he handed to Joe.

- e. **No requirement of communication.** The words or conduct manifesting a present trust intent do not have to be communicated to the beneficiary. However, the failure to inform anyone of the trust arguably shows that the trustor lacked the present intent to create a trust relationship.

Example: T executes a deed to Blackacre, naming himself "as trustee for A and B." T then inserts the deed into an envelope, which he puts into his desk drawer. Under these facts, it could be contended that a trust relationship has been created. On the other hand, T's failure to record the deed or inform the beneficiaries about the trust suggests that T lacked the requisite present trust intent. Thus, the outcome of this issue must be resolved by the fact-finder.

2. **Trust Res.** A trust cannot exist without property which is the subject of the trust relationship. A trustor may use several methods to place title to the trust *res* in the trustee, including the following:

- (1) the trustor can make an *inter vivos* transfer of title to the trustee,
- (2) the trustor can declare himself the trustee over particular property standing in his name,
- (3) the trustor can, in a valid will, direct the executor to distribute property to a trustee (i.e., a testamentary trust), or
- (4) a trustor can enter into an enforceable contract with another person who thereby becomes obligated to transfer property to a trustee for the purpose of establishing a trust.

Whichever method of creation is used, however, no trust can be established until the trustee has legal title to the trust *res*. In general, any identifiable property right which is transferable and capable of ownership may constitute a trust *res*.

- a. **Property Rights.** Property interests which can serve as a trust *res* include: (a) vested possessory interests, (b) contingent, non-possessory, future interests, (c) contract rights, and (d) equitable interests in another trust.

As a general matter, the following interests may not be used as the *res* of a trust:

- (1) the mere expectancy that a person has in the prospective estate at death of a living person as his heir or under the will,
- (2) expectations of future earnings which are unsupported by an enforceable contract, and
- (3) a debt or obligation owed by the trustee.

Example: X properly executes a deed which conveys, "Blackacre to Belle for life, remainder to Z in trust for Mary and John". Although the *res* is not a present possessory interest, the vested future interest conveyed to Z is nevertheless an effective trust *res*. Z, the trustee, has present duties (i.e., to verify that Belle refrains from dissipating, or causing permanent damage to Blackacre during her life estate).

- b. **Alienable.** Generally, the trustor must be capable of conveying to the trustee the property which is to serve as the trust *res*.
 - c. **Identifiable.** The trust *res* must be capable of being identified.
 - i. **Vague descriptions.** A description of a trust *res* such as "most of the money in my bank account at ABC Bank" would be too indefinite.
 - ii. **Fractional interests.** A gift of an undivided fractional interest in specific property (i.e., "one-half of the land which I presently own") is usually adequate. The trustee is a tenant-in-common with the other owner.
3. **Beneficiaries.** Except with respect to charitable trusts, a trust must have identifiable beneficiaries, whose interests will vest or fail within a period of time which is not violative of the Rule Against Perpetuities. Any natural or artificial person may be a beneficiary, as long as s/he can legally own property.

- a. **Identifiable beneficiaries.** The trust beneficiaries must be (i) presently ascertainable (i.e., either specifically named or capable of being determined without undue difficulty), or (ii) ascertainable at a future time (within the Rule Against Perpetuities) when their interests are to vest.
- b. **Class Gifts.** The beneficiaries of a trust may be a designated class of persons, if (i) the class is sufficiently definite, and (ii) all of its members are ascertainable within the period of time prescribed by the Rule Against Perpetuities.
- i. **Time when interest vests.** The members of a class are usually determined at the time when their interests are to vest, rather than when the trust was created. If X creates a trust, to benefit Y for life, and then to Y's children, "Y's children" are determined as of Y's death (rather than when X created the trust).
 - ii. **Interpretation problems.** There must be some reasonably objective basis for determining the members of the class. A trust which has as its beneficiaries a class comprised of "X's children" is clearly permissible. On the other hand, a trust established by T for "all of my friends," without naming these persons or otherwise providing a formula through which they can reasonably be identified, would be impermissibly vague. Where a class of beneficiaries is described as the trustor's "family", "relatives", "relations" or "kindred", courts often treat the vague language as evidencing an intent to create a trust for the benefit of the trustor's heirs.
 - iii. **Determination of class by trustee.** The trustee is often empowered to (i) select from members of a class for distribution from the trust *res*, or (ii) determine the amount of each recipient's distribution. However, the class within which the trustee is to make his selection must be sufficiently definite. Thus, a trust established for five of the trustor's "friends" should fail (even if the trustor was obviously fond of the persons subsequently chosen by the trustee), since a group denominated as "friends" is arguably too indefinite.
 - iv. **Rule Against Perpetuities.** Beneficial interests in a trust (including class gifts) which are violative of the Rule Against Perpetuities ("No interest is good unless it must vest, if at all, not later than twenty-one years after some life in being at the creation of the interest") are void.
 - (a) **"No interest is good"** means that any contingent interest which does not conform to the rule is void ab initio.
 - (b) **"Must vest"** means that the contingent interest must become a vested interest (or fail) within the period of the rule.

Example: If A establishes a trust for B and C (who are born and ascertainable) to pay for their college education, the rule is satisfied, because they will go to college, if at all, within the period of the rule.
 - (c) **"If at all"** means that if the contingent interest is absolutely certain either to "vest" or "fail" entirely within the period of the rule, it is valid.

(d) **“Not later than 21 years after some life in being”** includes within the period, (1) lives in being, provided they are not so numerous as to prevent practical determination of the time when the last one dies, plus (2) 21 years, plus (3) such actual periods of gestation as come within the proper purpose of the rule.

(e) **“At the creation of the interest”** means that in the ordinary case the period of the rule begins when the creating instrument (e.g., trust or will) takes effect.

(f) **Rule directed against remoteness of vesting:** The rule is directed entirely against remoteness of vesting, i.e., the sole test being, must the interest vest (or fail) within the period of the rule. If it may vest beyond the maximum period permitted by the rule, it is void.

(1) **Purpose:** While the rule is directed toward remoteness of vesting, its ultimate purpose is to prevent the clogging of titles beyond reasonable limits in time by contingent interests and to keep land freely alienable in the market places.

(g) **Interests subject to rule:**

(1) contingent remainders

(2) executory interests

(3) options to purchase land not incident to a lease

(4) powers of appointment

(5) class gifts

(6) rights of first refusal

(h) **Interests not subject to the rule:**

(1) present interests in possession

(2) reversions

(3) vested remainders

(4) possibilities of reverter

(5) powers of termination

(6) charitable trusts

(7) resulting trusts

(i) The **“measuring life”**:

Under the rule, lives in being must be:

- (1) human lives, not the lives of any of the lower animals or lives of corporations;
 - (2) the lives in being must precede, they cannot follow, the 21 years;
 - (3) every human being is conclusively presumed capable of having children during her lifetime;
 - (4) the lives in the measuring group or class must *not be so numerous* or so situated that the survivor cannot be practically determined by the ordinary evidentiary processes, e.g., if the lives in being were all the persons now living in the state of California, or in Great Britain, the interest would be void.
- (j) The time for vesting is generally calculated from the time the creating instrument takes effect. In the case of a will, it is *date of the testator's death*.

Example: A, being fee owner, devises Blackacre in trust "to the children of my son, B, who reach the age of 25." At A's death, B has four sons ranging in age from 14 to 22. B dies 10 days after the death of A, leaving no other children. Is the trust for the children valid under the Rule Against Perpetuities? The answer is no.

Analysis: The validity of an interest created by a will must be determined as of the date when the will takes effect, that is in our case at A's death. Looking forward from that date these possibilities, and we are dealing with possibilities not probabilities, must be observed. First, as long as B lives he is conclusively presumed capable of having more children. Second, it is possible that he will have other children after A's death. Third, it is possible that all of B's four sons living at A's death will die before any one of them arrives at the age of 25. Fourth, then it is possible that the only one, if any, of B's children who will arrive at the age of 25 will be a child who is born after A's will took effect. Fifth, it is possible that such child may be born posthumously, that is, after the death of B, and that it will take 25 more years for him to arrive at the required age for an interest in Blackacre to vest in him. In conclusion, it is possible that any interest in B's children will vest at a time later than any life in being and 21 years after the will of A took effect. Consequently, the trust in favor of B's children who reach the age of 25 violates the rule and is void ab initio.

- (k) **Common statutory modifications of the Rule Against Perpetuities.** Most jurisdictions have modified the common law Rule in some way.
- (1) **"Wait and See" Statutes.** With this type of modification, the court simply waits out the perpetuities period to see whether the future interests will vest. The requirement of initial certainty is overcome. Under this type of statute, the interest is not sure to be invalid until the death of all lives in being plus 21 years.
 - (2) **"Cy Pres" Statutes.** In jurisdictions with cy pres statutes, courts look to the grantor's intent and attempt to meet the grantor's wishes as closely as possible by altering the grant slightly to fit the Rule.

(3) **“Patch Up” Statutes.** If a grant would fail at common law under absurd circumstances, the court may ignore these obscure possibilities and modify the grant to fit the Rule.

(4) **Alternative Perpetuities Periods.** Although statutes with alternative perpetuities periods still require initial certainty, they use another – usually longer – specified period to give future interests a chance to vest.

v. **Interpretation to avoid application of Rule Against Perpetuities preferred.** Where the trustor’s intent as to the identity of the beneficiaries of a trust is subject to more than one meaning, an interpretation which avoids application of the Rule Against Perpetuities is ordinarily preferred.

Example: X conveys funds to Y, “in trust, for the maintenance and support of team members of the New York Yankees.” Whether X intended a gift to the Yankees as constituted at the time of the transfer to the trustee, or to whomever might subsequently become members of that group, is determined by the trustor’s intent. However, the former interpretation avoids invalidation of the entire trust under the Rule Against Perpetuities and would therefore be preferred.

c. **Minors and incompetents.** A minor or legally incompetent person may be a beneficiary. Any claims which they might have against the trustee can be asserted by legal guardians appointed to act on their behalf.

d. **Business organizations.** Modernly, unincorporated non-charitable associations may benefit from a trust. However, if the trustor indicates that the support of such an organization is to be on-going indefinitely, the trust may fail under the Rule Against Perpetuities.

Example: Susan establishes a trust for the benefit of her book group, the Reading Rebels. If she indicates that the group should be funded for “all perpetuity”, the trust will fail, as it will be unclear as to whether the interest will vest within 21 years of Susan’s life (or even that of the other book club members).

e. **Non-Beneficiaries.** The fact that one is incidentally benefited in the context of a trust relationship does not result in that person being a beneficiary of the trust.

Example: X creates a trust, pursuant to which Y, as trustee, is instructed to purchase Cadillacs for X’s children. X’s children, not Cadillac dealers in the area, are the beneficiaries. If Y fails to perform the terms of the trust, local Cadillac dealers could not compel him to do so.

4. **Trustee.** Legal title to, and responsibility for the management of the trust *res*, resides in the trustee.

a. **Capacity.** A trustee must have the mental capacity to administer the trust. She cannot be a minor or mentally incompetent person. Modernly, corporations are allowed to be trustees. However, many states have statutes prohibiting corporations from engaging in trust activities, unless the corporate entity is incorporated under the laws of their jurisdiction.

- b. **Acceptance by trustee.** The trustee's acceptance of the trusteeship is presumed, unless she promptly disclaims it when informed of the trust. Once accepted, the trustee's acceptance ordinarily relates back to inception of the trust relationship.
 - c. **Failure to designate or appoint a qualified trustee.** If no trustee is designated, or he (a) is incompetent, (b) fails to survive the trustor, or (c) otherwise fails to qualify, courts will ordinarily appoint a new trustee. However, where the trustor's selection of the trustee was obviously "personal" and exclusive in nature, the trust will fail if the specifically designated person refuses to accept the trusteeship.
 - d. **Co-trustees.** Where two or more persons are named as co-trustees, they are ordinarily considered co-tenants. If a co-trustee dies or becomes incapacitated, no new trustee is appointed until the survivor dies or is disqualified. However, if the trust instrument expressly requires a specified number of co-trustees, a court will appoint additional trustees, as necessary. In the absence of a trust provision stating otherwise, the actions of co-trustees of a private trust must be unanimous. In contrast, co-trustees of a charitable trust may generally undertake action by majority vote.
5. **Valid trust purpose.** Trusts may be created for virtually any purpose, except for one which is (i) illegal, (ii) for the purpose of perpetrating a fraud, or (iii) contrary to public policy.
- a. **Trust provisions affecting marriage.** A trust provision which encourages a beneficiary to (1) refrain from marrying, or (2) obtain a divorce, is invalid (except that restraints upon *remarriage* by the trustor's spouse are ordinarily upheld). A trust condition which excludes a beneficiary if he subsequently becomes divorced is usually valid.
- Example:** T deeds Blackacre to X, as trustee, to distribute the income to Sonny (T's son) for life, and then to deliver the real property to the Red Cross at Sonny's death. However, the trust instrument also provides that Sonny's income interest is extinguished if he ever marries. The condition subsequent pertaining to marriage is probably invalid.
- Example:** T deeds Blackacre to X, as trustee, to distribute the income to W (T's wife) for her life, and then to deliver the remainder of the trust property to the Red Cross at W's death. However, the trust instrument provides that if W remarries after T's death, her income interest is extinguished. This provision is probably effective.
- b. **Consequences of an invalid provision.** Whenever possible, courts attempt to merely delete an objectionable provision, and retain the balance of the trust. However, where this result would frustrate the trustor's *overall purposes*, the entire trust is invalidated.

C. CREATION OF EXPRESS INTER VIVOS TRUSTS.

- 1. **Delivery.** Legal title to the trust *res* must be transferred to the trustee of the trust. Where the trust *res* is real property, transfer is effectuated by:
 - (1) execution of a deed conveying title to the trustee, and
 - (2) delivering that document to the trustee (or his agent).

Where the trust *res* is personal property, transfer may be made by:

- (1) physical delivery (i.e., delivering actual possession of the item),
- (2) symbolic delivery (i.e., executing a deed or gift or instrument of title in favor of the trustee, and delivering that document to the trustee or his agent), or
- (3) constructive delivery (i.e., delivery to the trustee or his agent of an object which represents or gives access to the property, such as delivering the key to a car with the intention of transferring ownership of the car itself).

2. **Declaration of Trust.** A trustor may create a trust by declaring (ordinarily, in a written instrument), that henceforth he holds legal title to the subject property as trustee for the beneficiary. The trustor, in effect, continues *to hold legal title to the property, while transferring equitable title to the beneficiaries*. The trustor may also manifest an intent to create a trust by (i) declaring himself trustee, and (ii) earmarking particular assets as the trust *res*. The trustor's marking an envelope "held for James" with the requisite intent would probably constitute a sufficient declaration of trust. The envelope's contents would be the trust *res*.

Example: T declares that he is putting 20 head of cattle from his herd into a trust for B. However, T fails to separate or otherwise designate which animals are subject to the trust and continues to treat all of his cattle in a similar manner. *No* effective transfer has occurred. However, a gift of a fractional interest in a known quantity of items of a particular asset is valid. Thus, T's declaration that he holds 20% of his stamp collection in trust for B would probably be upheld. Under these circumstances, T, as trustee, would hold the stamp collection in a tenancy in common with the trustor, individually.

3. **Statute of Frauds.** *Inter vivos* transfers of personal property to a trust *are not subject to the Statute of Frauds*. However, where an *inter vivos* conveyance of an interest in real property is made, the requirements of the Statute of Frauds must be met, or the trust *is not enforceable* against an unwilling trustee. The Statute of Frauds requires that a trust of real property be evidenced by a writing which is signed by the party to be charged (i.e., the party who, at the time of the transfer, had the power to create a trust upon that property).

Example: T deeds Blackacre to himself, "as trustee, for X and Y." Since the conveyance is memorialized in a signed writing (i.e., the deed), there has been compliance with the Statute of Frauds.

Example: T verbally advises several people that he is holding Blackacre in trust for X and Y. Since the purported change in the legal title of Blackacre from T, personally, to T as trustee of a trust in favor of X and Y, is *not* memorialized in a signed writing, T could repudiate the purported trust if X or Y sought to enforce it.

- a. **Trust not void, only unenforceable.** Failure to comply with the Statute of Frauds does not preclude voluntary performance of the trust by a willing trustee. Notwithstanding the Statute of Frauds, *an oral trust involving real property* may be performed by the trustee. If the trustee voluntarily chooses to carry out the terms of the trust, or to execute a writing sufficient under the Statute of Frauds, no one (e.g., the trustee's creditors) has standing to contest the trust.

b. **Equitable part performance/estoppel.** When the trustee permits the alleged beneficiary to be *in possession of the land, and* the beneficiary:

- (1) makes substantial improvements to the property, or
- (2) otherwise relies upon the trust to his substantial detriment,

lack of compliance with the Statute of Frauds can be overcome under the equitable part performance doctrine.

Additionally, where a trustee's own actions clearly and objectively indicate, despite title standing in his name (personally) a trust relationship, a trustee *may be equitably estopped* to deny the existence of the trust.

- c. **Constructive Trusts.** Constructive trusts are *not subject to the Statute of Frauds*. In certain contexts (i.e., promissory fraud based upon a promise which the trustor never intended to perform, breach of promise in the context of a pre-existing fiduciary relationship, etc.), a trustee's refusal to carry out an oral trust relating to real property may be grounds for imposition of a constructive trust upon the land.
- d. **Bona fide purchasers.** If a bona fide purchaser ("BFP") acquires trust property while it stands in the trustee's name (without any reference to the trust relationship), the beneficiaries' rights in the asset are extinguished. The acquisition of property by a BFP cuts off any hidden equities in that asset. In this situation, the sole recourse of the beneficiaries is against the trustee for breach of his fiduciary duties (presuming, of course, the beneficiaries can prove the existence of an enforceable trust).
- e. **Secret and semi-secret trusts.** The analysis which is made where a trustor-grantor makes an *inter vivos* conveyance of property that omits any reference to a trust relationship should *not* be confused with secret and semi-secret trusts pertaining to a decedent's estate (discussed in the context of a *testamentary trust*, immediately below).

D. TESTAMENTARY TRUSTS.

1. **Description.** A testamentary trust is created by the testator's will. Its essential terms are described in, or incorporated by reference into, a valid will. The "present intent" element is satisfied, since a will "speaks as of the testator's death" and it was the trustor's intent that the trust take effect at that time.
2. **Secret and Semi-Secret Testamentary Trusts.**
 - a. **Secret trust.** A secret trust situation arises where property is devised to another *without reference* in the will to the fact that the devisee promised the trustor-decedent, or (expressly or impliedly) agreed, to hold the property received under the will in trust for another. A secret trust also arises where a decedent refrains from making a will based upon promises by his intestate heirs to, at his death, hold the estate in trust for specific beneficiaries. If the devisees/trustees refuse to perform the secret trust, extrinsic evidence is admissible to prove its existence. In most states, a constructive trust may be imposed upon the secret trust *res* in favor of the beneficiaries.

Example: In his will, T leaves "\$50,000 to X." After T dies, Mel claims that X had promised T to hold the money *in trust* for him (Mel). In most states, Mel can introduce extrinsic evidence of X's alleged promise to T. If Mel prevails on this issue, a constructive trust will be imposed upon X's devise in Mel's favor. A new trustee will be appointed to take control of the property and perform the trust. In a minority of jurisdictions, if a secret trust is proven, the devise is held in a constructive trust for T's estate. The rationale of these cases is that enforcement of a "secret" trust is inconsistent with the Statute of Wills, since it permits extrinsic evidence to contradict the provisions of a will or codicil (i.e., to prevent unjust enrichment, X must be divested of the property, but the asset need *not* be given to Mel to remedy the wrongdoing).

Example: T advises Sonny (T's only child) that he wants the latter to hold property passing to him (Sonny) under intestacy principles in trust for T's elderly sister. Sonny does not expressly promise to do so, but acknowledges T's request by responding, "Understood". If, when T dies intestate, Sonny refuses to hold his intestate share in trust for T's sister, the latter may succeed in imposing a constructive trust upon the property in her favor.

- b. **Semi-Secret Trusts.** Where a testator indicates in his will that property is being devised to a trustee "in trust" but fails to identify the beneficiaries, a semi-secret trust results. In a majority of jurisdictions, semi-secret trusts are void. The trustee holds the property in a resulting trust for the trustor's estate. In a minority of jurisdictions, assuming the terms of the trust can be proven, a constructive trust can be imposed upon the property for the benefit of the beneficiaries if the trustee refuses to perform the trust.

Example: T's will contains a provision which states, "I devise Blackacre, in trust, to Bill, as trustee." The terms of the trust and the beneficiaries *are not stated* in the will, nor in any documents incorporated by reference into the will. In a majority of jurisdictions, the trust fails and Blackacre passes via the residuary clause of T's will (or, if there is no residuary provision, under intestacy principles).

- c. **Pour-over provisions.** Wills frequently contain provisions which direct the transfer of the decedent's property into a trust established by either the testator or another person.
- i. In jurisdictions that have adopted the "incorporation by reference" doctrine, pour-over provisions are usually valid. Even in these jurisdictions, however, the will must direct the pour-over of assets into a preestablished (i.e., *inter vivos*) trust. Furthermore, the terms of the trust must be irrevocable and unamendable.

E. TRUSTS ARISING BY CONTRACT.

1. **Specific performance.** A person can create a trust by entering into an enforceable contract with another who, by virtue of the agreement, is obliged to (i) become a trustee of certain property which he owns, or (ii) transfer title to property to another person as trustee. If the promisor fails to perform his obligations, the promisee or beneficiaries can often compel specific performance.

Example: Bill promises to give Harry his antique car, in exchange for Harry's promise to convey Blackacre, in trust, to George, pursuant to a trust arrangement whereby Bill and Mary (his wife) would receive the income from that property for their lives. If Bill transfers the car

to Harry, but the latter fails to create the trust, Bill and Mary might be able to obtain an order compelling Harry to carry out the trust arrangement.

2. **Trust *res* subsequently acquired.** When the promisor fails to perform his obligation to establish a trust because he does not own the asset which is to serve as the trust *res*, a trust relationship automatically arises when the asset is subsequently acquired by the promisor.

Example: N, in consideration for the sum of \$50,000 received from Alan, promises to create a trust relating to Blackacre for the benefit of Alan's children. N does not presently own Blackacre, but expects to inherit it under the will of her father, Frank. If N subsequently inherits or otherwise acquires Blackacre, the contracted for trust automatically arises.

- F. **TOTTEN TRUSTS.** When a person opens a bank account *in his own name*, as trustee for other parties, it is often unclear as to whether he intends to create a trust relationship pertaining to the deposited funds and subject himself to the fiduciary duties of a trustee. If he executes a trust instrument pertaining to the deposit or otherwise indicates he is creating a formal trust relationship (e.g., delivering the passbook to the beneficiary, making accountings, etc.), an *inter vivos* trust arises. If, however, the depositor's intention was merely tentative (i.e., he intended the beneficiaries to have no rights in the account until he died), in most jurisdictions the arrangement is viewed as a "Totten" trust.

A Totten trust is a hybrid creation of the courts which melds both will and trust characteristics. Totten trusts are created like trusts and do not have to comply with the formalities of a will. However, Totten trusts are similar to wills in that:

- (1) they are revocable by the depositor at any time,
- (2) the beneficiary has no interest in the account until the depositor dies,
- (3) the beneficiary must survive the depositor to receive the account,
- (4) the depositor owes no fiduciary duties to the beneficiary, and
- (5) the deposit is subject to the claims of the depositor's creditors.

II. CHARITABLE TRUSTS

- A. **DISTINGUISHING CHARACTERISTICS.** Charitable trusts have certain characteristics which distinguish them from the express, private trusts previously discussed. Four differing aspects are: (1) the trust must have a *charitable purpose*, (2) the beneficiaries must be *indefinite*, (3) charitable trusts may have a perpetual existence (i.e., the Rule Against Perpetuities has limited application to charitable trusts), and (4) the *cy pres* doctrine.

1. Charitable purposes.

- a. **Description.** The major categories of charitable purposes are:

- (1) the relief of poverty,
- (2) the advancement of education,
- (3) the advancement of religion,
- (4) the promotion of health, and
- (5) the performance of governmental and municipal purposes (e.g., maintenance of parks, etc.).

In addition, under the Restatement (Second) of Trusts other purposes may be found charitable if they are “sufficiently beneficial to the community to justify permitting property to be devoted forever to their accomplishment” (e.g., prevention of cruelty to animals).

A charitable purpose can be broad as long as the trustee is constrained to use the trust exclusively for that objective. For example, a trust established simply “for charity” is permissible, but courts have sometimes refused to sustain trusts established for the attainment of “benevolent”, “philanthropic”, “liberal” or “worthy” purposes (although the modern trend is to construe these terms as synonymous with “charity” whenever possible).

- b. **Distinguish purpose from motive.** The objective of a charitable trust must be to benefit the public, but the *subjective motive* of the trustor for establishing the trust may be selfish in nature. Thus, a trustor may create a valid charitable trust for the advancement of education, even though the predominant reason for this action is to reduce his taxes, gain notoriety, or achieve some similar personal objective.
2. **Indefinite Beneficiaries.** The fact that there is a *limited number of persons* actually receiving funds *does not cause a charitable trust to fail* if the recipients are to be chosen from a sufficiently large and indefinite group. For example, a trust to provide college scholarships for up to five needworthy children whose fathers were policemen killed while on duty is valid. Although it might conceivably be possible to ascertain all of the children of policemen killed while performing their duties, the difficulty inherent in this task would probably result in the class being sufficiently “indefinite.”
3. **Rule Against Perpetuities.** A charitable trust may be of perpetual duration. However, where *the charitable trust is preceded by a non-charitable estate*, the charitable interest *must vest* within the period of time prescribed by the Rule Against Perpetuities.

Example: T creates a testamentary trust. It provides that, upon his death, a trust of \$1,000,000 is to be established. The income from this trust is to be distributed (i) to his children during their lives, and (ii) after the death of his last child, the property is to be held by the trustee in perpetuity with the income therefrom to be used for the advancement of medical research. Since the charitable interest vests within 21 years of a life in being (T’s children, as determined at the time of his death), the charitable remainder trust to advance medical research is valid.

4. **Mixed Trusts.** A mixed trust has *both charitable and private purposes*. The characteristics of charitable and private trusts are *mutually exclusive* in that (1) a charitable trust must have

indefinite beneficiaries, and (2) a private trust must have *ascertainable beneficiaries*. A trust which has both charitable and private purposes will fail, unless the private and public purposes can be segregated (either proportionally or at different points in time), into separate trusts.

Example: T creates a trust pursuant to which X (the trustee) is to distribute the income to A for life, and thereafter to use the income to purchase reference books for the local public library. The latter purpose is charitable, since it represents a gift for the advancement of education. The trust is valid. While there are both private and charitable purposes, the periods of time during which each is operative are distinct. There are actually two trusts, a private trust of a life estate, followed by a charitable trust of the remainder.

Example: T creates a testamentary trust, under the terms of which the trustee is to use the income of the trust “for the support of trustor’s wife and children, or for the maintenance of Central Park.” The trust will fail in its entirety. As a whole, it neither qualifies as a private or charitable trust. Furthermore, there is no objective standard by which the trust might be divided into *two distinct components*, so that each could separately qualify as a valid trust.

Example: T creates a trust, designating “X as trustee, to use the income as President of Elk’s Lodge #57 *and* support veterans of the U.S. Armed Forces.” The trust could be viewed as having mixed purposes: supporting Elk’s Lodge #57, which constitutes a private purpose, and supporting U.S. Armed Forces veterans, which is a charitable purpose. If this is the situation, the entire trust fails.

However, the gift can arguably be bifurcated into two separate trusts (one for Elk’s Club #57, and the other for veterans of the U.S. Armed Forces). Alternatively, it could be contended that the trust is entirely charitable in nature, if the “and” (italicized above) is construed as meaning “for.” Under this interpretation, the words “President of Elk’s Lodge #57” are viewed as merely assisting in the identification of X (rather than constituting a distinct trust purpose).

5. **The “Cy Pres” Doctrine.** Under this doctrine, where (1) the trustor’s specific charitable purpose with respect to a valid charitable trust becomes impossible, impracticable or illegal to carry out, *and* (2) the trustor had, in addition to this specific charitable purpose, *a general charitable intent* (i.e., the trustor’s specific charitable purpose was not intended to be exclusive), a court may modify the trust to allow the trustee to carry out a *substantially similar* charitable purpose instead. If a charitable trust cannot be performed as intended and the cy pres doctrine is *not* applicable, the trust terminates and a resulting trust in favor of the trustor’s estate arises.

a. **Determining the trustor’s intent.** Generally, the court will infer from the making of a charitable trust that the trustor *had a general charitable intent*. However, where the trust instrument makes clear that the trustor would have preferred the trust to terminate rather than be used in a manner other than that which he had indicated, the cy pres doctrine *cannot* be utilized. If the trustor has provided for a “gift over” in the event that the charitable purpose cannot be accomplished, this is ordinarily viewed as indicating that the trustor *lacked* a general charitable intent. (In the typical “gift over” situation, unless the transfer is to another charitable trust, the gift is often violative of the Rule Against Perpetuities.)

- b. **Effect of language in trust instrument.** Language in a trust instrument that the trust *res* is to be used “only” for the stated charitable purpose *is not dispositive* on the question of whether the trustor had a general charitable intent. While such language indicates that the trustor intended the trust to be used only for the specific charitable purpose while possible to accomplish it, it does not necessarily show that the trustor would have preferred the trust to terminate, rather than be used for a similar charitable purpose if the original charitable purpose was no longer possible to accomplish.

Example: T creates a charitable trust to support medical research to develop a cure for a rare disease which primarily afflicts children. If a complete cure for that malady is later discovered, under the cy pres doctrine the trustee could be instructed to carry out the trust for a different disease which has a disproportionately high impact upon children.

Example: T creates a charitable trust to support medical research to develop a cure for a certain disease which primarily afflicts children. T established this trust because one of his daughters had died of this disease. If a complete cure for this malady is later discovered, the cy pres doctrine would not be applied if the court determines that T was interested only in mitigating the effects of the particular disease which took his child’s life. Consequently, any remaining assets in the trust would be held by the trustee as a resulting trust for T’s estate.

Remember, the cy pres doctrine can be used only to modify an already valid, existing charitable trust. This doctrine *cannot be used to (i) turn a private trust into a charitable trust, or (ii) reform an invalid trust.*

Example: T creates a testamentary trust to care for his cat. Even in those few jurisdictions that permit “honorary trusts,” — trusts that do not meet the requirements for either charitable or private trusts — this trust violates the Rule Against Perpetuities. Additionally, since not originally a *valid charitable trust*, the cy pres doctrine *is not applicable* to turn this trust into a charitable one (i.e., for the prevention of cruelty to animals). Thus, the trust for T’s cat fails and the trustee holds the *res* in a resulting trust for T’s estate.

III. THE TRUSTEE’S POWERS AND RESPONSIBILITIES

A. **SOURCES OF THE TRUSTEE’S POWERS.** A trustee’s powers are derived from:

- The trust instrument (either expressly or by implication), and
- Powers which are (i) granted by statute, or (ii) implied-in-law as necessary or appropriate to accomplish the trust’s purposes.

1. **Trust instrument.** In addition to those powers which are specifically delegated to the trustee in the trust instrument, she is also authorized to undertake those acts which are by implication necessary or convenient to accomplish the trust’s purposes. If a trustee is unclear as to whether or not contemplated action is permitted under a trust instrument, clarifying instructions may be obtained from a proper court.

2. **Powers implied-in-law.** Unless expressly precluded by the trust instrument, a trustee has the power to:
- (1) make improvements to trust property,
 - (2) sell or lease trust assets, and
 - (3) incur reasonable expenses which are necessary to maintain trust property.

However, the trustee has *no implied power* to:

- (1) mortgage or otherwise encumber trust property, or
 - (2) invade trust principal for a beneficiary who has merely the right to receive income from the trust.
3. **Standard of review.** A trustee's actions pertaining to matters *within his discretion are not subject to attack*, unless he has abused his discretion in undertaking the conduct in question. The trustee's exercise of discretion is ordinarily reviewed under an objective standard (i.e., he must act reasonably under the circumstances). Where the trustee is given "sole" or "absolute" discretion under the trust instrument, his actions are reviewed under a good faith standard (i.e., they are not improper unless undertaken in bad faith).

B. DUTY OF LOYALTY. A trustee owes a duty of utmost good faith and loyalty to the beneficiaries in carrying out her obligations under the trust.

1. **General rule.** A trustee is (i) prohibited from self-dealing, in any manner (even if done in good faith) with trust assets, and (ii) ordinarily precluded from obtaining *any personal benefit* (other than the agreed upon or statutory fees) as a consequence of his position.
 - a. **Self-dealing.** Examples of prohibited self-dealing include the trustee, or persons under his control (a) buying assets from, or selling assets to the trust (even if the sales are for fair market value or occur at a public auction), or (b) borrowing money from, or loaning money to the trust.
 - b. **Self-employment.** A trustee is permitted to receive reasonable compensation from services rendered to the trust beyond those normally required of a trustee, *provided* those services are necessary and an extension of his ordinary trust duties. Nevertheless, trustees who are also insurance agents, stockbrokers or real estate agents have been precluded from receiving their usual commissions for services involving trust property. However, attorney-trustees rendering legal services on behalf of the trust have been able to recover when the courts have accepted the rationale that these services were a necessary extension of the trustee's ordinary trust duties.
 - c. **Dealings with beneficiaries.** The trustee is *not absolutely prohibited* from entering into transactions with *beneficiaries* of the trust she is administering. However, she is viewed as having a fiduciary relationship with these beneficiaries, and must therefore disclose *all* pertinent facts known by her with respect to the transaction. Additionally, the transaction must be "fair" when viewed objectively.

- d. **Dealings with third parties.** The *trustee cannot obtain any personal benefit from a third party* with respect to dealings involving the trust estate. Thus, for example, obtaining a personal commission, bonus, finder's fee or other benefit for placing trust business with others is strictly prohibited.

Example: The XYZ Bank, to attract new depositors, offers free television sets to anyone procuring a certificate of deposit of \$5,000 or more. T, a trustee, deposits \$5,000 into the XYZ Bank, and *personally* receives the advertised television set. T would be obliged to deliver the item, or its fair market value to the trust.

- e. **Conflicts of interest.** The trustee is precluded from permitting himself to be in *an apparent conflict of interest* with respect to the trust and third parties. Thus, a corporate or bank trustee should *not* purchase its own shares or deposit trust funds into an account at its institution. There is even a question as to whether a corporate or bank trustee can retain its own shares when they are already part of the trust estate, or must promptly sell that stock and re-purchase different assets.
- f. **Identification of trust assets.** The trustee is ordinarily expected to segregate trust assets from his own assets, and earmark or otherwise identify trust property. Corporate fiduciaries are, however, generally permitted to utilize pooled or common trust funds (i.e., funds in which the assets of various trusts are combined, in order to make more diversified and desirable investments).
2. **Exceptions.** The trust instrument may expressly permit specified acts of self-dealing. For example, the trustee may be authorized to loan money to, or purchase assets from, the trust. Even in these instances, however, the trustee must act in good faith and with the "utmost fairness" in transactions involving trust property.

C. AFFIRMATIVE DUTIES WITH RESPECT TO TRUST ASSETS. A trustee has an affirmative duty to preserve and enhance trust property.

1. **Standard of care.** The trustee's actions are examined under *an objective standard of care*. He must exercise that degree of care, skill and prudence with respect to trust assets as would a reasonably prudent businessperson with respect to his own affairs and property. However, where a trustee possesses superior business expertise or is a professional fiduciary (i.e., a trust company or bank), a higher standard is applied. He is held to the care, skill and prudence of an individual or entity possessing those capabilities.
2. **Duty to collect and preserve trust assets.** The duty of care incumbent upon a trustee includes the obligation to take reasonable steps to protect and preserve the trust estate (i.e., obtain necessary insurance, satisfy trust obligations as they become due, maintain trust assets to prevent untimely deterioration and assure that no one is injured on the premises, defend the trust when subjected to legal attack by creditors of the trustor, prevent trust property from being stolen or otherwise appropriated, etc.).
3. **Duty to make trust property productive.** The trustee is obliged to attempt to utilize trust property in a productive manner; subject, at all times, to the obligation to be prudent (i.e., invest only in a conservative manner). Thus, land should be leased and personal property

utilized, if possible, to produce income for the trust. Where cash is a trust asset, it should be invested, consistent with the trust's overall liquidity needs.

a. **Prudent investor rule.** Almost all jurisdictions follow the "prudent investor rule." Under this doctrine, a trustee is permitted to invest trust assets as would a prudent investor, considering both the interests of life beneficiaries and remaindermen (i.e., the trustee must consider both the investment's ability to produce a reasonable rate of income and the safety of the principal). Under this standard, the trustee must also seek to diversify the investments, so that all of the trust's "eggs are not placed in one basket."

b. **Permissible investments.** The following types of investments are generally appropriate for trust assets:

(1) government and highly rated corporate bonds,

(2) first trust deed mortgages (assuming they are adequately secured), and

(3) "blue chip" common and preferred stock.

Impermissible investments include unsecured loans, "penny" stocks and commodities futures. Courts are divided on the appropriateness of mutual funds (but in no event may investments be made in speculative funds). Investments in land for resale are ordinarily improper (being viewed as too speculative).

c. **Non-productive assets/wasting assets.** Unless expressly instructed otherwise by the trust instrument, a trustee must generally seek to dispose of wasting (i.e., most frequently, mines, oil wells, etc.) or non-productive (i.e., most frequently vacant land) assets expeditiously and for a reasonably fair price.

4. **Duty to account.** The trustee has the duty to maintain a clear, accurate accounting with respect to all transactions which he enters into on behalf of the trust.

5. **Delegation and professional advice.** In deciding whether to undertake, or refrain from undertaking, action for or on behalf of the trust, the trustee may seek the advice of professionals.

a. **Discretionary functions.** A trustee may not ordinarily delegate *discretionary functions*. For example, a trustee may (and if he lacks the necessary background to make a reasonably competent decision, must) consult with investment counselors concerning the investment of trust property. However, the trustee must nevertheless make an informed ultimate decision concerning these matters. He is *not permitted* to unthinkingly follow the advice of others.

b. **Ministerial functions.** A trustee is permitted to delegate purely ministerial duties (painting a structure, collecting rent, etc.), and minor discretionary functions (exclusive of investment decisions) to the extent that a reasonably prudent trustee would employ others to assist him in similar circumstances. Even when a delegation of trust duties is appropriate, if the trustee fails to exercise adequate care in the selection and supervision of his delegates, he is a guarantor of effective performance, (notwithstanding whether the actions of the trustee were otherwise improper or not).

D. TRUSTEE'S LIABILITY. A trustee stands in a fiduciary relationship with respect to the beneficiaries of his trust. Thus, when duties owed to the beneficiaries are breached, any questions of liability are typically resolved *against the trustee*. Only the beneficiaries (or their guardians ad litem) can commence an action against the trustee for breach of the duties which are owed to them. The trustor, except where he is also a beneficiary, ceases to have any interest in the trust once delivery of the trust *res* has occurred.

1. **Breach of Duty of Loyalty.** Where a trustee breaches his duty of loyalty, the beneficiaries have several potential actions and remedies.

a. **Use of trust funds for personal purposes.** Where the trustee has utilized trust funds for his own purposes, the court may:

(1) compel the trustee to convey to the trust any property which he obtained with those funds, or

(2) recover any profits made by the trustee with those monies.

Example: T, the trustee of a trust, uses \$5,000 of trust funds to personally acquire title to particular land. If the land subsequently increases in value, the beneficiaries are entitled to have a constructive trust in their favor imposed upon the real property. Thus, the entire benefit resulting from this transaction will accrue to the beneficiaries of the trust.

b. **Use of commingled funds for personal purposes.** Where a trustee uses both trust property and his own funds to undertake a personal activity, he is liable to the beneficiaries for *any* appreciation or profits derived from those commingled monies.

Example: T, the trustee of a trust, combines \$5,000 of trust funds with \$5,000 of his own monies to purchase an antique car, personally taking title to this asset. The automobile appreciates in value to \$15,000. The beneficiaries can compel T to sell the vehicle and return \$10,000 (i.e., the initial \$5,000, plus the \$5,000 of appreciation) to the trust.

c. **Recovery of any losses, including interest.** Where property removed from the trust has been dissipated or can no longer be identified, the trustee is liable for (i) its value, and (ii) any interest which could have been earned on those funds.

d. **Possibility of punitive damages.** Since a trustee's breach of the duty of loyalty is ordinarily intentional (rather than as a consequence of negligence or inadvertence), punitive damages may be recoverable. The deliberate breach of one's fiduciary duties is arguably conduct which should be discouraged.

e. **Removal of trustee.** A trustee's breach of the duty of loyalty may serve as a basis for removing him from his trusteeship.

2. **Breach of investment duties.** The trustee is liable to the beneficiaries for any damages or losses resulting from (i) improper investments, or (ii) his failure to take reasonable steps to make trust assets productive.

- a. **“No offset” rule.** Where a trustee makes an *imprudent investment* which results in a loss, he cannot offset these losses against profits made from other improper transactions; *except* where the losses and gains are attributable to a single transaction or one substantially related to the breach of the trustee’s duties.

Example: T, a trustee, makes two concurrent investments which are violative of the “prudent investor” rule. In the first, T purchases \$50,000 worth of ABC Company stock (a corporate entity whose securities are *not* highly rated and which has *not* paid dividends in recent years). In the second, T purchases land for speculation. The first investment is unsuccessful, and the stock is presently worth only \$25,000. The second investment, however, realizes appreciation of \$50,000. T *cannot* offset the \$25,000 loss against the \$50,000 gain. T is liable to the beneficiaries for the \$25,000 stock loss, while the real property remains an asset of the trust.

Example: T, as trustee, uses \$10,000 of trust assets to purchase one hundred acres of rural land for the trust as a speculative investment. A few years later, ten acres of this land is condemned to build a freeway. The governmental entity pays the trust \$35,000 for the ten acres, and the remaining ninety acres are now worth \$5,000 each. Although the trustee breached his duty of care in making a speculative investment, a court would most likely view this as a single breach. Since the improper investment was a profitable one, the beneficiaries would probably ratify it.

- b. **Lost earnings or interest.** The trustee is liable to the beneficiaries for lost interest or other income which would have been earned in the absence of the failure to perform his duties.

Example: T creates a trust for B, naming X as trustee and transferring \$100,000 in cash and 1,000 shares of ABC company stock to the trust. The trust instrument prohibits the sale of ABC stock, except under certain specified, limited circumstances. Despite the directive in the trust instrument, and without any other justification, X sells the ABC stock for \$500,000 (its fair market value at that time). X then utilizes these proceeds, plus the original \$100,000 and places the entire sum in a safe deposit box. When X’s actions become known, 1,000 shares of ABC stock are worth \$1,000,000. Under these circumstances the beneficiary, B, can hold X liable for the income and interest that would have been earned if the trustee had not breached his duty, (i.e., the full appreciation on the ABC stock that was wrongfully sold, including any dividends paid in the interim, plus interest on the \$100,000 at the rate of interest which would have probably been earned if X had properly invested it).

3. **Liability of successor trustee for breach of former trustees’ duties.** A trustee ordinarily has no liability for breaches of duty by the trustee whom he succeeds, except where the successor trustee:

(1) knew, or should have become aware of the prior trustee’s breach, and failed to undertake appropriate action to minimize its effects or to pursue the appropriate remedies on behalf of the beneficiaries, or

(2) was negligent in failing to obtain a complete accounting and delivery of trust property from the preceding trustee.

4. **Recovery of trust assets from third parties.** Where the trustee has transferred trust property (or identifiable proceeds from trust assets) to persons who are not bona fide purchasers, the beneficiaries can often have a constructive trust imposed upon it. Constructive trusts are described in the final chapter of this outline.

5. **Trustee's Defenses to Liability.** Where an action is brought against the trustee by the beneficiaries, the former may assert equitable and legal defenses against the latter. The most important of these defenses are discussed below.

a. **Express authorization.** Occasionally, the trust instrument expressly authorizes the trustee to undertake certain actions which would otherwise be improper. In these specified instances, the trustee's acts are *not deemed wrongful* or in breach of the trust, as long as he acts within the scope of the instrument's authorization.

b. **Exculpatory clauses.** An exculpatory clause is a provision in the trust instrument which relieves the trustee of liability for potentially wrongful acts (e.g., "the trustee shall not be liable for negligence or errors of judgment with respect to his activities involving the trust estate"). When the trustee's conduct falls within the purview of this clause, he is ordinarily relieved of liability (i.e., a trustee's acts are generally not wrongful or in breach of the trust), as long as within the scope of the instrument's authorization. Thus, the trustee incurs no liability in these circumstances (unless his acts would be violative of the state's public policy).

i. **Ineffective with respect to intentional conduct or gross negligence.** An exculpatory clause is ineffective to the extent that it purports to relieve the trustee of liability for acts of bad faith and intentional misconduct, recklessness or gross negligence. Permitting its application in these situations is viewed as being violative of public policy.

ii. **Narrow construction.** Exculpatory clauses are narrowly construed by the courts. A provision relieving the trustee from liability for "errors in judgment" would probably be construed as applying only to mistakes in judgment; rather than providing him with a defense where, for example, he failed to exercise any judgment, at all.

c. **Consent.** Where a beneficiary has full knowledge of the material facts, and expressly approves of the complained of action by the trustee, he may be deemed to (i) *have waived the trustee's breach*, or (ii) *be estopped from asserting an action*.

E. REMOVAL AND RESIGNATION OF TRUSTEES. The circumstances pursuant to which trustees may be removed or can resign are discussed below.

1. **Removal.** A trustee may be removed by court order where he has:

- (1) In a material manner, failed or refused to perform his duties under the trust agreement, or
- (2) Become unable to adequately perform his duties (i.e., is incapacitated, has relocated to another area, etc.).

Courts are more reluctant to remove a trustee who was designated by the trustor, than a person who was judicially appointed to their position.

2. **Resignation.** Once a trustee has accepted the appointment to his position, he cannot resign *unless* authorized to do so by the trust instrument, (ii) all of the beneficiaries consent to this action, or (iii) he obtains a court order permitting this action.
 - a. **No appointment of successor.** Where a trustee is permitted to resign, he *cannot* (unless expressly authorized to do so by the trust agreement) appoint a successor. This must usually be accomplished by a court order.
 - b. **Resignation effective.** Where a trustee is permitted to resign, he cannot to do so until a successor has been properly appointed. The trustee cannot avoid his responsibilities by transferring the trust *res* back to the trustor or to another individual. The transferee under these circumstances would hold only “constructive” legal title to the assets and the original trustee would remain liable for any breach of the legal title holder’s trust duties.

F. TRUSTEE’S LIABILITY TO THIRD PARTIES. Although the trustee is performing trust duties, he may incur *personal* liability to those with whom he interfaces on behalf of the trust. In certain situations, the trustee can obtain indemnification from the trust to the extent of his personal liability.

1. **Tort Liability.** A trustee is ordinarily personally liable for the torts which he or his agents commit in the course of performing trust duties. A trustee may, however, obtain reimbursement from the trust where he was *not personally at fault*. For example, a trustee is entitled to be indemnified by the trust where:

- (1) the tort was a normal incident to an activity in which the trustee was properly engaged on behalf of the trust,
- (2) the tort is based on strict liability, or
- (3) liability is based upon respondeat superior principles and the trustee did *not* make an improper delegation of discretionary functions to the agent or violate his duty to exercise reasonable care in the selection and supervision of the agent.

Example: T is the trustee of a trust. His trust responsibilities include the operation of a bank. Thomas, one of T’s employees, embezzles \$20,000 from a depositor’s account. Ordinarily, T is entitled to reimbursement from the trust for the amount he is obliged to repay the depositor (i.e., T did not *personally* cause the loss). However, if T failed to exercise reasonable care in (i) hiring Thomas, or (ii) supervising the activities of Thomas, T would *not* be entitled to reimbursement from the trust.

Example: T is the trustee of a trust. His trust responsibilities include the operation of a newspaper. If T is successfully sued for defamation as a consequence of an article published in the newspaper, he could obtain reimbursement from the trust. The tort involved in this instance is a normal incident to operating and publishing a newspaper.

2. **Contractual Liability.** In most states, a trustee is personally liable on a contract entered into on behalf of the trust *unless* he specifically and explicitly disclaims and limits liability in writing. However, where a contract exceeds the trustee’s authority or is otherwise improper, *only* the trustee (personally) is ordinarily liable for that obligation.

- a. **Right of Reimbursement.** The trustee has an *implied right of reimbursement and indemnification against the trust* where the contract was for the benefit of the trust and within his authority. Where a right of reimbursement exists, the trustee can pay any contractual obligation (including reasonable attorneys' fees) directly from trust assets. If the trust *res* is not sufficient to pay the claim, however, the trustee remains personally liable.
- b. **Rights of creditors.** Where only the trust is liable on a contractual obligation (i.e., the contract was a proper one and the trustee correctly limited his liability), creditors must proceed directly against the trust. Where, however, the trustee is personally liable, but has a right of reimbursement from the trust, creditors can proceed against trust assets only after their efforts to obtain payment from the trustee have been exhausted. Finally, where the contract was *not* a proper one, the trustee (personally) is generally the *only party* liable under it, even if he purported to limit liability.

IV. ALIENABILITY OF TRUST BENEFICIARIES' INTERESTS AND CREDITORS' RIGHTS

A. BENEFICIARIES' INTERESTS.

1. **General rule/voluntary alienation.** In the absence of a restrictive provision to the contrary, a trust beneficiary may freely assign (gratuitously or for consideration) his right to receive income or principal from a trust.
 - a. **Writing Requirement.** Where the trust estate is comprised of an interest in land (including leasehold interests), the Statute of Frauds is applicable. Thus, an assignment of this type of interest by the beneficiary must be evidenced by a writing which is signed by the beneficiary. In the absence of a written memorandum, the assignment is unenforceable.
 - b. **Notice to trustee.** Except where expressly required by the trust instrument, notice to the trustee is not necessary for an assignment by the beneficiary to be effective. However, the trustee ordinarily has no liability to an assignee for refusing to honor a purported assignment if (i) there is no writing evidencing the assignment, and (ii) the beneficiary contends that no assignment has been made.
 - c. **Death of beneficiary.** Unless the trust agreement provides for a gift over in case of the beneficiary's death (i.e., the beneficiary only has a life estate), a beneficiary's interest in a trust can be devised by will or pass pursuant to intestacy principles.
 - d. **Multiple assignments of same trust interest.** Where a beneficiary makes multiple assignments of his interest in a trust, the "first-in-time, first-in-right" rule will usually apply. However, where (i) an earlier transferee neglects to inform the trustee of the assignment, and (ii) a subsequent assignee pays consideration to the beneficiary-assignor for the assignment after inquiring of the trustee as to the existence of any previous assignments and receiving a negative response, the latter assignee is often given priority.

Example: T creates a trust with Art as trustee. Mary and Sal are the beneficiaries, who receive the income from the trust until they attain the age of 35, at which point the

principal is to be distributed to them in equal shares. Sal assigns his interest to Gus. Subsequently, however, Sal assigns the same interest to Peter. Ordinarily, once an interest is assigned, the assignor no longer has anything additional to convey. If, however, (i) Gus neglected to inform Art of the assignment, and (ii) Peter loaned money to Sal upon the basis of the assignment and Art's statement that Sal's interest had not previously been assigned, Peter might be given priority.

2. **General rule/rights of creditors.** In the absence of a restrictive provision in the trust instrument to the contrary, creditors can ordinarily attach and foreclose upon a beneficiary's interest in a trust. If this occurs, the trustee must deliver the beneficiary's interest to the successful purchaser (to the extent of the beneficiary's obligation) at the foreclosure sale.
3. **Exceptions to general rule of alienability: discretionary, support and spendthrift trusts.** Where a beneficiary's interest in a trust is restricted by a valid discretionary, support or spendthrift provision (discussed below), she cannot assign that interest.
 - a. **Support trusts.** A support provision is one in which the trustee is directed to provide only so much income and/or principal of the trust as is necessary for the latter's "education, maintenance and support," and for no other purpose. A support provision is not merely an expression of the trustor's motive for creating the trust. It actually limits the beneficiary's interest to amounts necessary for her support. Any trust property in excess of what is necessary for the beneficiary's support must be distributed as otherwise provided in the trust instrument.
 - i. **Non-alienability by beneficiary.** Where a support provision exists, a beneficiary cannot transfer her interest in the trust.
 - ii. **Rights of creditors.** Creditors cannot ordinarily attach a beneficiary's interest in a support trust.
 - b. **Discretionary Trusts.** A discretionary provision is one in which payment to the beneficiary (even for a stated purpose) is to be made, if at all, at the trustee's absolute discretion. The hallmark of a discretionary provision is the trustee's ability to prevent a beneficiary from receiving anything under the trust, if the trustee believes this is appropriate.
 - i. **Alienability by beneficiary.** Where a discretionary provision exists independent of a support clause, the beneficiary can assign his interest in the trust. However, an assignee's right is of no marketable value, unless and until the *trustee determines* that a distribution to the assignor-beneficiary is to be made.
 - ii. **Rights of creditors.** Creditors may *attach* a beneficiary's interest in a discretionary trust. However, that interest has *no* marketable value until the *trustee determines* that a contribution to the beneficiary should be made.
 - iii. **Liability of trustee.** If the trustee makes a distribution to the beneficiary *after being notified* of an assignment (by the beneficiary) or attachment (by a creditor), he is liable to the assignee or creditor for the amount of that distribution.

- c. **Spendthrift trusts.** A spendthrift provision is one *which precludes (i) a beneficiary from voluntarily transferring his interest in the trust, and (ii) creditors from reaching that interest.* No specific language is necessary to accomplish this result. Whether the trustor intended to create a spendthrift trust is a factual issue, determined from all of the circumstances.
- i. **Alienability by beneficiary.** Where, despite a valid spendthrift provision, the beneficiary attempts to voluntarily assign her interest, the trustee *may* (if she chooses to do so) comply with the transferee's demand, unless the beneficiary has expressly notified the trustee to disregard the assignment.
 - ii. **Rights of creditors.** Where the spendthrift provision prevents alienation by the beneficiary *and* attachment by creditors, creditors *cannot* ordinarily reach the beneficiary's interest.
 - iii. **Restraints upon creditors only.** A spendthrift provision which precludes creditors from reaching a beneficiary's interest, *but does not limit the beneficiary's right of transfer, is probably not effective.* However, these provisions are sometimes construed as *also* impliedly prohibiting voluntary transfers by the beneficiary. In the latter event, the spendthrift provision limiting creditors is valid.
 - iv. **Restraints upon voluntary transfers only.** Spendthrift provisions which limit only the beneficiary's right of alienation are valid. In this situation, creditors of the beneficiary are *not* prevented from reaching his interest in the trust.
4. **Limitations upon the enforceability of spendthrift, support and discretionary trusts.** In certain situations, creditors of a beneficiary can reach the latter's interest in a trust, despite a valid support, discretionary or spendthrift clause.
- a. **Trust distributions.** Once the trustee has actually made a distribution to the beneficiary, the latter's creditors can attach that property through the same means that are applicable to any debtor-owned assets.
 - b. **Trustor-created trusts.** A trustor is *not permitted* to insulate his own property from creditors by means of spendthrift, support or discretionary provisions. Where a person creates a trust, or furnishes consideration to another person to establish a trust in which *he is a beneficiary*, his creditors can reach the maximum portion of the trust that could have been distributed to him (despite a valid support, discretionary or spendthrift provision).
- Example:** T and X enter into an agreement. T conveys Blackacre to X. In return, X establishes a spendthrift trust for \$200,000. The trust instrument provides that (i) T will receive the income for life, and (ii) the principal will pass to the persons designated in T's will. Creditors of T can invade the trust established by X to satisfy obligations owed to them by T.
- c. **Claims for child or spousal support.** In most states, a beneficiary's interest in a trust is subject to the claims of spouses, ex-spouses and his children for alimony or support, notwithstanding a spendthrift clause.

- d. **Reimbursement for necessary services or supplies.** In most jurisdictions, persons or entities which furnish necessities of life (i.e., food, clothing, emergency medical attention, etc.) to a beneficiary are entitled to reimbursement from the trust, despite a valid support or spendthrift clause.

Example: Mickey, the beneficiary under a discretionary, spendthrift trust, was taken care of at a state hospital for the mentally ill. In most states, the state is permitted to reach Mickey's interest in the trust to obtain reimbursement for the services and supplies provided to him while he was a patient at the hospital.

- e. **Reimbursement for preserving a beneficiary's interest.** The Restatement (Second) of Trusts provides that a beneficiary's interest, even though protected by a spendthrift provision, is subject to the claims of creditors who "preserve the interest" of that beneficiary. For example, an attorney who, on behalf of the beneficiary of a spendthrift trust, performs services which protect or preserve the trust interest of that otherwise impecunious beneficiary, is able to collect his fees from the beneficiary's interest in the trust.
- f. **Tax claims.** A trust can be invaded by the U.S. or a state governmental entity to satisfy tax claims against a beneficiary.

5. Rights of the Trustor's Creditors.

- a. **General rule.** As previously described, any beneficial interest (i.e., a life estate) retained by the trustor in a trust is subject to the claims of his creditors.
- b. **Fraudulent conveyances.** Where the trustor creates a trust in favor of others, (i) as a consequence of which, he is, or will be rendered, insolvent (i.e., his liabilities exceed his assets, or he will be unable to pay his debts as they become due), or (ii) for the purpose of hindering or defrauding his creditors, the creditors can reach the trust *res* to satisfy their claims against the trustor.
- c. **Revocable trusts.** In most jurisdictions, the fact that an *inter vivos* trust is revocable by the trustor **does not permit** his creditors to attach the trust's assets to satisfy their claims against him (unless the trust **also constitutes a fraudulent conveyance**). Nevertheless, if the trustor is placed into bankruptcy, the court may exercise his power of revocation.

Example: T creates a trust, making himself (or another) the trustee, and conveying Blackacre to the trust. The income is to be distributed to Joe and Jan for life, and the principal to their children. Assuming T is not rendered insolvent by the transfer of Blackacre to the trust, if he subsequently incurs obligations which he cannot pay, T's creditors **cannot invade the trust corpus** to satisfy his obligations to them. But, if T declares, or is forced into, bankruptcy and he has not previously renounced his power of revocation, the trustee-in-bankruptcy may exercise this power, causing title to Blackacre to be returned to T, and thereby subject that realty to the claims of T's creditors.

V. MODIFICATION OR TERMINATION OF TRUSTS

- A. BY TRUSTOR.** The majority rule prohibits a trustor from modifying or terminating an *inter vivos* trust, ***unless she has expressly reserved this right*** under the terms of the trust instrument. The minority rule states that an *inter vivos* trust is amendable and revocable by the trustor, **unless she has expressly waived or limited this right in the trust instrument.**

Example: T creates an *inter vivos* trust. The trust document is silent on the question of whether the trustor may modify or revoke the trust. Under the majority rule, T may not do so.

- B. TERMINATION OF A TRUST BY MERGER.** If a sole trustee becomes the only beneficiary (i.e., holder of all of the beneficial interests of the trust), the trust ceases to exist and he (personally) becomes the owner of the trust assets.

Example: T creates an *inter vivos* trust of which she is the sole trustee. The beneficiaries are herself, X, and Y, as joint tenants with right of survivorship. Unfortunately, X and Y are killed in a common accident. Since T has become the sole trustee and beneficiary, (i) the trust is extinguished, and (ii) T owns the trust property outright (i.e., free of the trust).

Example: T creates a trust with himself as trustee. The income is to be paid to T and his wife during their lives, and the principal passes to T's children at his death. If T's wife dies, the trust continues to exist, since additional beneficiaries (T's children) are still alive. The fact that T's children hold only a future interest in the trust is not significant.

- C. TERMINATION BY OPERATION OF LAW.** A trust is terminated by operation of law where:

- (1) accomplishment of the material purposes of the trust have become illegal, impossible or impractical,
- (2) the trust *res* has been consumed, destroyed or lost, or
- (3) the trust's purposes have been fully accomplished.

Example: T creates a trust to provide for the special tuition and costs associated with his daughter Debra's training to become a concert violinist. Shortly thereafter, Debra is involved in a car accident which damages the nerves in her fingers. As a result, any future prospects of her becoming a performing musician are terminated. Under these circumstances, a court could find that the trust is terminated by operation of law.

- D. ADMINISTRATIVE DEVIATIONS.** Where exact compliance with the ***administrative provisions*** of the trust would, as a result of unforeseen circumstances, frustrate or substantially impair a ***material purpose*** sought to be accomplished by the trust, the court, on petition of the trustee, may allow deviance from those administrative provisions, as necessary to accomplish the trustor's purposes. The administrative deviance doctrine ***may not, however, be used to change the beneficial interests in the trust.***

Example: T creates a trust under which Blackacre (which used to be his farm) is the main asset. The trust instrument states that the farm is ***not*** to be sold, and that the income is to be distributed

to Sue and Jeffrey. Nevertheless, if farming in that locale becomes unprofitable, the trustee may be able to obtain a court order permitting the sale of the land (rather than have the property depreciate in value to the point where it is virtually worthless).

E. TERMINATION OR MODIFICATION OF THE TRUST BY THE BENEFICIARIES. A trust may be terminated or modified where: (1) *all of the beneficiaries are legally competent* and join in the action, *and* (2) *the material purposes of the trustor in creating the trust will not be frustrated.*

1. **All Beneficiaries.** All persons who presently are, or could become, beneficiaries of the trust must consent. It does not matter if a person's beneficial interest is vested or not, or even whether they are in existence or presently ascertainable. Consequently, if a beneficiary is a (i) minor, or (ii) potential member of a class which has not yet closed, it would be impossible to obtain the consent of all of the beneficiaries. However, in a growing number of jurisdictions, a guardian ad litem may be appointed for the purpose of giving consent for minors and potential beneficiaries.

2. **Material purposes.** The trustor's "material purposes" are determined from all of the possible evidence (i.e., the trust instrument, statements by the trustor, circumstances surrounding the creation of the trust, etc.). Beneficiaries are not permitted to terminate a trust where the relationship was created to protect them from their own wastefulness or lack of maturity (i.e., a spendthrift trust). If the trustor joins in the petition, the trust may be terminated or modified by consent of all of the beneficiaries, notwithstanding that a material purpose of the trust would be defeated. The trustor's consent is viewed as waiving the "material purpose" restriction.

F. NATURAL EXPIRATION. Where the trust was to be in operation for a specified number of years or until the occurrence of a prescribed event, and that period of time has elapsed or the incident has occurred, the trust ordinarily terminates in accordance with the instrument's terms.

VI. TRUSTS ARISING BY OPERATION OF LAW

A. RESULTING TRUSTS. There are two main types of resulting trusts: (1) those which arise where an express trust fails after property has been conveyed to the trustee, and (2) purchase money trusts.

1. **Failed express trusts.** Where an express trust, partially or completely, fails, or is terminated by operation of law, and there is no alternative disposition for the trust's assets, a resulting trust ordinarily arises. Typical situations are where:

- (1) The trust no longer has beneficiaries (i.e., they have died, cannot be located or identified, or disclaim their trust interests),
- (2) No provision has been made for a portion of the trust *res*, or where a trust designated for a specific purpose is invalid, insufficient or excessive,
- (3) The trust purpose was never described or is unclear, **or**

(4) Carrying out the material purposes of the trust has become impractical or illegal.

Example: T conveys Blackacre to Y, as trustee, with instructions to hold the land in trust for beneficiaries which T will name later. However, T fails to name any beneficiaries prior to his death. At T's death, Y holds Blackacre in a resulting trust for (i) the residuary devisees of T's will, or (ii) if T's will did not contain a residuary clause or T died intestate, T's heirs.

Example: T transfers \$100,000 to X, as trustee, to use the income from this amount to support Elmer (T's brother). If T fails to designate how the principal should be utilized after Elmer dies, at Elmer's death the remainder is held by X in a resulting trust for T's estate.

Example: T's will leaves \$50,000 in trust to support the activities of the local Boy's Club. However, the Boy's Club has insufficient other resources and is obliged to close. If the cy pres doctrine is not applicable, the principal and unexpended interest are held in a resulting trust for T's estate.

Example: T transfers one million dollars to X, as trustee, to build a small playground for children on a parcel of land which T had previously conveyed to the city. Assuming the cy pres doctrine is not applicable, if it takes only a portion of this sum to complete the playground, X would hold the balance in a resulting trust for T (or, if T has died, his estate).

Example: T, in his will, devises \$500,000 to X, as trustee, to pay the income to Z until she reaches 35 years of age, and then to distribute the principal to her. If Z fails to reach 35, and no alternative disposition has been provided for in the trust, X holds the principal in a resulting trust for T's estate.

2. **Purchase money resulting trusts.** If a party pays (or obligates himself to pay) the original *purchase price* of property, but directs that title to the asset be placed *in another's name*, then (unless the payor and grantee stand in a certain, close familial relationship), there is a *rebuttable presumption* that the grantee holds the property in a *resulting trust* for the payor. Where the payor is the grandparent, parent, or (sometimes) spouse of the person in whose name title is taken, *there is a rebuttable presumption that a gift was intended*. Generally, other familial relationships have *not* been deemed to raise a presumption of gift. Thus, where a brother provides the purchase money and directs title to be taken in the name of his sister, there is a rebuttable presumption that the grantee holds title to the property in trust for her brother. Courts are divided on which presumption applies when a spouse is the payor and directs that title be taken in the other spouse's name. However, the emerging view under these circumstances is to presume that an outright gift was intended.

Example: T pays owner \$50,000 for Greenacre, but directs that Josh be named as grantee upon the deed. Assuming T and Josh do not stand in a close familial relationship, there is a rebuttable presumption that Josh holds Greenacre in a resulting trust for T.

3. **Pro rata purchase money resulting trust.** Purchase money resulting trusts also arise where one or more persons provide all or part of the purchase money for property, and (ii) title is taken in the name of another, or in the names of the payors in shares different from the proportions in which the purchase money was provided. In such cases, there is a rebuttable presumption that the takers of title (unless standing in a certain, close familial relationship with the payor) hold the property in trust for the payor and in conformity with the share of purchase money each contributed.

Example: T and X each contribute \$25,000 toward the purchase of Greenacre, but the owner of the parcel is instructed to designate X as the sole grantee in the deed. Since T paid one-half of the purchase price, there is a rebuttable presumption that X owns an undivided *one-half interest* in the land and holds the balance in a resulting trust for T. Thus, X, individually, and X as resulting trustee for T, are tenants-in-common.

Example: T pays \$50,000 to Owner for Blackacre and directs that title be taken in Al's name. If T claimed that Al held Blackacre in a resulting trust for him (T), Al could rebut the presumption by showing that he (Al) had (i) borrowed the money from T, and (ii) directed T to pay the proceeds from the loan to Owner. In this situation, while Al is liable to T for repayment of the loan, he would *not* be obliged to convey Blackacre to T. No resulting trust occurs, since the funds used to purchase the land actually belonged to Al (i.e., he acquired ownership of the funds by borrowing them from T). Under these circumstances, T might have an equitable lien against Blackacre for the amount of his loan to Al.

4. **Duties of the Trustee Under a Resulting Trust.** As a general matter the trustee of a resulting trust has the same duties and obligations as other trustees. Primary among his responsibilities, however, are to:

- (1) convey the trust *res* back to the trustor (or her estate) or payor (where a purchase money trust is involved), and
- (2) account for any income traceable to the trust from the time that it arose.

B. **Constructive Trusts.** A constructive trust is an *equitable remedy*, whereby trust-like responsibilities are imposed upon the holder of specific property to redress wrongdoing or prevent unjust enrichment. It is typically imposed when property has been wrongfully obtained (i.e., acquired by fraud or undue influence). The purpose of a constructive trust is to oblige the holder of property to divest himself of it and transfer it to the person entitled to that asset.

Example: X verbally promises T that, if the latter will convey Blackacre to him, he will hold it in trust for Darryl until Darryl reaches 30 years of age. Subsequently, X refuses to transfer the land to Darryl. If it can be shown that X never intended to convey Blackacre to Darryl (i.e., that X had *fraudulently* obtained title to Blackacre via a fraudulent promise), a court could impose a constructive trust upon the land in favor of Darryl.

Example: X promises T that if T will convey Blackacre to him (X), he will hold it in trust for Z until the latter reaches 30 years of age. T conveys Blackacre to X, but X subsequently refuses to transfer Blackacre to Z. If T *cannot* prove that X never intended to convey the land to Z (i.e., X's promise was not fraudulent), X has only broken a promise which he had originally intended to perform. Nevertheless, a breach of promise in the context of a *pre-existing confidential relationship* is considered adequate grounds for imposing a constructive trust. Under these facts, a court could require X to hold Blackacre in a constructive trust for Z.

C. **Rights of a Bona Fide Purchaser ("BFP").** Where wrongfully acquired property, which might otherwise be subject to a constructive trust, is sold for value to someone who is unaware of the wrongdoing (i.e., the purchaser of the property is a BFP), the aggrieved party's rights to impose a constructive trust on that asset are foreclosed. Hidden equities in an asset are extinguished when acquired by a BFP. However, any assets the wrongdoer-seller obtained in exchange for the property transferred to the BFP may be subject to a constructive trust.

Example: X owns a substantial art collection. He is also the trustee of a trust established for the benefit of B. The *res* of B's trust includes two valuable paintings. X sells one of these paintings to P, who pays the fair market value for it and has no reason to suspect that X is not the item's owner. X uses the proceeds from this sale to purchase a home. X donates the second painting to the State Art Museum ("Museum") in an effort to ingratiate himself with the board of directors of that entity. Museum accepts the donation, unaware that the painting is not owned by X. Shortly thereafter, X's wrongdoing is discovered. Although B cannot impose a constructive trust on the painting sold to P, he may be able to have a constructive trust imposed on the one donated to the Museum and on X's new home (via tracing principles).

TRUSTS

QUESTION BY QUESTION CAPSULE SUMMARY OUTLINE TRUE-FALSE QUESTIONS

1. Title to the trust
2. Language necessary to form a trust
3. Precatory language
4. Gratuitous promises as evidence of intent
5. Future intention to form a trust
6. Communication requirement
7. Expectancy interests
8. Identifiable beneficiary requirement
9. Time for identification of beneficiaries
10. Strict interpretation of the Rule Against Perpetuities
11. Minors as beneficiaries
12. Corporations as trustees
13. Failure to appoint a trustee
14. Restrictions against marriage
15. Applicability of the Statute of Frauds
16. Present intent in testamentary trusts
17. Semi-secret trusts
18. Totten trusts
19. Selfish motive for charitable trusts
20. Indefinite beneficiaries – charitable trusts
21. Perpetuity requirement for charitable trusts
22. Specific purpose for a charitable trust
23. Sources of trustee power
24. Encumbering trust assets
25. Standard of review for trustee actions
26. Compensation of trustees
27. Transactions between trustee and beneficiaries
28. Duties of the trustee
29. Who may bring suit against the trustee
30. Availability of punitive damages
31. Offset of losses

32. Breaches of duty by predecessor trustees
33. Removal of the trustee by the beneficiaries
34. Resignation of the trustee
35. Assignment by beneficiary
36. Devising of interest in trust by beneficiary
37. Attachment by creditors
38. Administrative provisions of a trust
39. Termination or modification by the beneficiaries
40. Trusts for the benefit of a pet
41. Trusts arising by operation of law
42. Trusts terminating by operation of law
43. Support trusts
44. Discretionary trusts
45. Spendthrift trusts

DIAGNOSTIC TRUE-FALSE QUESTIONS

(Circle Correct Answer)

1. T F Title to a typical trust is held by both the trustee and the beneficiaries.
2. T F No particular words or actions are necessary to manifest the trustor's intent to create a trust.
3. T F Precatory language may be interpreted as evidence of a trustor's intention to create a trust.
4. T F A gratuitous promise to create a trust at some future point in time is evidence of the present intention to create a trust.
5. T F A trustor may create a trust and define the class of beneficiaries at a later date.
6. T F A trustor must generally inform a trust beneficiary of the existence of the trust.
7. T F If a person knows himself to be beneficiary under a will, he may create a trust using the prospective inheritance as the trust res.
8. T F The Rule Against Perpetuities applies to trusts.
9. T F When a class of people is designated as the beneficiaries of a trust, all of its members must be ascertainable at the time the trust is created.
10. T F Where the trustor's intent as to the identity of the beneficiaries of a trust is subject to more than one meaning, an interpretation which avoids application of the Rule Against Perpetuities is ordinarily preferred.
11. T F Minors may be beneficiaries of trusts.
12. T F Corporations may serve as trustees.
13. T F Failure to appoint a trustee generally causes a trust to fail.
14. T F A parent who is concerned about a child may set up a trust which only becomes effective if the child refrains from marrying her high school sweetheart.
15. T F Violation of the Statute of Frauds renders an inter vivos trust void.
16. T F The present intent element is satisfied in a testamentary trust.
17. T F In most states, semi-secret trusts are void.
18. T F Totten trusts do not have to comply with the formalities of a will.
19. T F A trustor may create a charitable trust even if his predominate motivation is selfish in nature.
20. T F The beneficiaries of a charitable trust must be definite.
21. T F A charitable trust may be of perpetual duration.
22. T F If a trustor specifies a particular purpose, and that charitable trust becomes impossible to carry out, the trust must fail.
23. T F The sole source of a trustee's powers is the language of the trust instrument.
24. T F A trustee may mortgage trust property in order to obtain cash for a beneficiary.
25. T F If a trustee has absolute discretion about a trust, his actions are reviewed under a good faith standard.
26. T F A trustee may be compensated for actions he takes in his role as trustee.
27. T F A trustee may enter into transactions with beneficiaries of the trust she is administering.
28. T F While a trustee has an affirmative duty to preserve trust property, he has no duty to enhance it.
29. T F A trustor may sue a trustee for breach of the trustee's duties to the beneficiaries.
30. T F Punitive damages are available against a trustee who has breached the duty of loyalty.

31. T F If a trustee makes an imprudent investment, he may offset the losses against the profits he has made from other prudent investments of the trust.
32. T F A trustee may be liable for breaches of duty by the trustee who preceded him.
33. T F A trustee may be removed by the beneficiaries.
34. T F A trustee may freely resign from his position as trustee.
35. T F A trust beneficiary may assign his right to receive income or principal from a trust.
36. T F A beneficiary may devise his interest in a trust to anyone he pleases.
37. T F If an *inter vivos* trust is revocable by the trustor, a creditor may attach the trust's assets to satisfy its claims against the trustor.
38. T F Administrative provisions of a trust must always be followed to the letter.
39. T F A trust may be terminated or modified by all of the beneficiaries to the trust.
40. T F A trustor may establish a testamentary trust for the benefit of his pet.
41. T F A trust may arise by operation of law.
42. T F A trust may terminate by operation of law.
43. T F The trustee of a support trust has the discretion to distribute more assets to the beneficiaries than are necessary for their support.
44. T F Under a discretionary trust, the trustee may prevent the beneficiaries from receiving anything at all.
45. T F When there is a provision in a spendthrift trust that only limits the beneficiary's right of alienation, creditors of the beneficiary are prevented from reaching his interest in the trust.

ANSWERS TO DIAGNOSTIC TRUE-FALSE QUESTIONS

1. True. While the trustee holds legal title to the trust *res*, equitable title in that property is owned by the beneficiaries.
2. True. The trustor may manifest intent through words or conduct. The trustor's intention is determined from the language utilized, his relationship with the parties involved, and any other appropriate circumstances.
3. True. While the requisite intent is usually deemed to be lacking where the trustor merely suggests or expresses a hope that the property be utilized for the benefit of another, courts are likely to find trust intent, despite precatory language, in several situations: where the recipient of the property stood in a preexisting fiduciary relationship with the trustor, where the recipient of the property would not normally be an object of the trustor's bounty, but the alleged beneficiary of such a person; or where the instructions to the recipient concerning the trustor's intentions with regard to use of trust property are detailed and specific.
4. False. Where purported trustor gratuitously promises to create a trust at some future point in time, the present intention to create a trust is lacking.
5. False. If the trustor purports to create a trust but designates certain prerequisites to be completed in the future, no present trust intent exists. However, if the trustor subsequently manifests a present intent when the missing element is furnished, the trust is effective as of the later date.
6. False. The words or conduct manifesting a present trust intent do not have to be communicated to the beneficiary. However, the failure to inform anyone of the trust arguably shows that the trustor lacked the present intent to create a trust relationship.
7. False. A person who has a mere expectancy in the respective estate at death of a living person may not use that future inheritance as the *res* of a trust.
8. True. Except with respect to charitable trusts, a trust must have identifiable beneficiaries whose interests will vest or fail within a period of time which is not violative of the Rule Against Perpetuities.
9. False. Members of a class are usually determined at the time when their interests are to vest, rather than when the trust is created.
10. True. If the trust may be upheld and saved under the Rule, a court will generally do so.
11. True. However, most minors have legal guardians who act on their behalf with respect to the trusts.
12. True. However, many states require corporations that serve as trustees to be incorporated under the laws of their jurisdictions.

13. **False.** If no trustee is designated, courts will ordinarily appoint a new trustee. The same is true if the trustee is incompetent, fails to survive the trustor, or otherwise fails to qualify. However, where the trustor's selection of the trustee was obviously personal and exclusive in nature, the trust will fail if the specifically designated person refuses to accept the trusteeship.
14. **False.** A trust provision which encourages a beneficiary to refrain from marrying is invalid except that restraints upon remarriage by the trustor's spouse are ordinarily upheld.
15. **False.** Failure to comply with the Statute of Frauds does not preclude voluntary performance of the trust by a willing trustee. Notwithstanding the Statute of Frauds, an oral trust involving real property may be performed by the trustee. If the trustee voluntarily chooses to carry out the terms of the trust, or to execute a writing sufficient under the Statute of Frauds, no one has standing to contest the trust.
16. **True.** The present intent element is satisfied in a testamentary trust because a will speaks as of the testator's death (in accordance with the testator's wishes).
17. **True.** In a semi-secret trust situation, the trustee holds the property in a resulting trust for the trustor's estate. Note that a semi-secret trust results where a testator indicates in his will that the property is being devised to a trustee in trust but fails to identify the beneficiaries.
18. **True.** A Totten trust is a hybrid creation of the courts which melds both will and trust characteristics. Totten trusts are created like trusts and do not have to comply with the formalities of a will. However, Totten trusts are similar to wills in that they are revocable by the depositor at any time, the beneficiary has no interest in the account until the depositor dies, the beneficiary must survive the depositor to receive the account, the depositor owes no fiduciary duties to the beneficiary, and the deposit is subject to the claims of the depositor's creditors.
19. **True.** The objective of a charitable trust must be to benefit the public, but the subjective motive of the trustor for establishing the trust may be selfish in nature. Therefore, as long as the trust advances some charitable purpose, the predominate reason for the trustee's action may be to reduce his taxes, gain notoriety, or achieve some similar personal objective.
20. **False.** In fact, charitable trusts differ from other types of trusts in that the beneficiaries must be indefinite. In other words, the recipients must be chosen from a large and indefinite group.
21. **True.** Charitable trusts may have a perpetual existence, and the Rule Against Perpetuities thus has limited application to charitable trusts. Where the charitable trust is preceded by a non-charitable estate, an interest must vest within the period of time prescribed by the Rule Against Perpetuities.

22. **False.** Under the "cy pres" doctrine, where a specific charitable purpose with respect to a valid charitable trust becomes impossible, impracticable or illegal to carry out, a court may modify the trust to allow the trustee to carry out a substantially similar charitable purpose instead if the trustor had a general charitable intent. If the trustor did not have a general charitable intent, however, the trust terminates, and a resulting trust in favor of the trustor's estate arises. Note that the court will generally infer from the making of a charitable trust that the trustor had a general charitable intent.
23. **False.** Not only may the trust instrument expressly state a trustee's powers, but these powers may be implied. Furthermore, powers which are granted by statute or implied in law as necessary or appropriate to accomplish the trust's purposes are also part of the trustee's powers. A trustee may undertake acts which are necessary or convenient to accomplish the trust's purposes. Furthermore, a trustee may make improvements to the trust property, sell or lease trust assets and incur reasonable expenses which are necessary to maintain the trust property.
24. **False.** The trustor has no implied power to mortgage or otherwise encumber trust property.
25. **True.** Where the trustee is given sole or absolute discretion in the trust instrument, his actions will not be improper unless undertaken in bad faith. Furthermore, the trustee's exercise of discretion is ordinarily reviewed under an objective standard. Therefore, unless he abuses his discretion, his actions pertaining to matters within his discretion are not subject to attack.
26. **True.** A trustee may be paid agreed upon or statutory fees. Furthermore, a trustee is permitted to receive reasonable compensation for services rendered to the trust beyond those normally required of a trustee, provided that those services are necessary and an extension of his ordinary trust duties. However, a trustee may not engage in self-dealing or accept commissions for services provided.
27. **True.** The trustee is not absolutely prohibited from entering into transactions with beneficiaries of the trust she is administering. However, she is viewed as having a fiduciary relationship with these beneficiaries, and she must therefore disclose all pertinent facts known by her with respect to the transaction. Additionally, the transaction must be fair when viewed objectively.
28. **False.** A trustee has an affirmative duty both to preserve and to enhance trust property. However, the trustee is under an obligation to be prudent. Therefore, a trustee is obligated to seek to derive income from the trust, but any investments made must be safe and diversified. Furthermore, a trustee must dispose of non-productive assets so as to maximize the value of the trust.
29. **False.** Only the beneficiaries can commence an action against the trustee for breach of the duties which are owed to them. The trustor, except where he is also a beneficiary, ceases to have any interest in the trust once delivery of the trust *res* has occurred.
30. **True.** Since a trustee's breach of the duty of loyalty is ordinarily intentional, punitive damages may be recoverable.

31. **False.** Where a trustee makes an imprudent investment which results in a loss, he cannot offset those losses against profits made from other improper transactions, except where the losses and gains are attributable to a single transaction or one substantially related to the breach of the trustee's duties.
32. **True.** If the new trustee knew or should have become aware of the prior trustee's breach and failed to undertake appropriate action to minimize its effects or pursue the appropriate remedies on behalf of the beneficiaries, or was negligent in failing to obtain a complete accounting and delivery of trust property from the preceding trustee, a trustee may be liable for breaches of duty by a preceding trustee.
33. **False.** A trustee may only be removed by a court order, and only where he has in a material manner failed or refused to perform his duties under the trust agreement, or become unable to adequately perform his duties. Furthermore, a court is more reluctant to remove a trustee who was designated by the trustor than a person who is judicially appointed to his position.
34. **False.** In fact, once a trustee has accepted the appointment to his position, he cannot resign unless authorized to do so by the trust instrument, allowed to do so by all of the beneficiaries, or allowed to do so by a court order. Furthermore, where a trustee is permitted to resign, he cannot do so until a successor has been properly appointed.
35. **True.** Unless there is a restrictive provision in the trust to the contrary, a trust beneficiary may freely assign (gratuitously or for consideration) his right to receive income or principal from a trust. If the interest is an interest in land, an assignment of this type of interest must be evidenced by a writing which is signed by the beneficiary.
36. **True.** Unless the trust agreement provides for a gift-over in case of the beneficiary's death, a beneficiary's interest in a trust may be devised by will or passed pursuant to intestacy principles.
37. **False.** In most jurisdictions, the fact that an *inter vivos* trust is revocable by the trustor does not permit his creditors to attach the trust's assets to satisfy their claims against him unless the trust also constitutes a fraudulent conveyance.
38. **False.** Where exact compliance with the administrative provisions of the trust would, as a result of unforeseen circumstances, frustrate or substantially impair a material purpose sought to be accomplished by the trust, the court, on petition of the trustee, may allow deviance from those administrative provisions as necessary to accomplish the trustor's purpose. The administrative deviance doctrine may not, however, be used to change the beneficial interests in the trust.
39. **True.** A trust may be terminated or modified where all of the beneficiaries are legally competent and join in the action and the material purposes of the trustor in creating the trust will not be frustrated.
40. **False.** This trust violates the Rule Against Perpetuities and is not a valid charitable trust.

41. **True. Both resulting trusts and constructive trusts arise by operation of law.**
42. **True. A trust is terminated by operation of law where: (1) accomplishment of the material purposes of the trust have become illegal, impossible or impractical; the trust *res* has been consumed, destroyed or lost; or the trust's purposes have been fully accomplished.**
43. **False. Any trust property in excess of what is necessary for the beneficiaries' support must be distributed as otherwise provided in the trust instrument.**
44. **True. A discretionary provision is one in which payment to the beneficiary (even for a stated purpose) is to be made, if at all, at the trustee's absolute discretion. The trustee may actually prevent the beneficiary from receiving anything at all under the trust if the trustee believes this to be appropriate.**
45. **False. There are two types of spendthrift provisions: ones that preclude a beneficiary from voluntarily transferring his interest in the trust, and ones that keep creditors from reaching that interest. There is a provision that limits the creditors from reaching the trust, but does not limit the beneficiary's right of transfer, this provision is probably ineffective. However, when there is a provision in a spendthrift trust that only limits the beneficiary's right of alienation, creditors of the beneficiary are prevented from reaching his interest in the trust.**

TRUSTS

QUESTION BY QUESTION CAPSULE OUTLINE MULTIPLE CHOICE EXAM QUESTIONS

1. Language necessary to create a trust
2. Precatory language
3. Communication requirement
4. Distribution of the trust assets
5. Types of trusts
6. Secret and semi-secret trusts
7. Extrinsic evidence to prove the existence of a trust
8. Semi-secret trusts
9. Testamentary trusts
10. Totten trusts
11. Revocability of Totten trusts
12. Beneficiaries' rights to take money out of the trust
13. Duration of charitable trusts
14. Trust to care for pets
15. Distribution of the trust assets
16. Mixed trusts
17. Exercise of discretion by the trustee
18. Termination of a trust
19. Appropriate trustee actions
20. Duties of the trustee
21. People who may bring a claim against the trustee
22. Breach of contract by a trustee
23. Reimbursement from trust in contract action
24. Torts committed by a trustee
25. Reimbursement from trust in tort action
26. Assignment of right to receive income or principal
27. Devise of interest in a trust
28. Natural expiration of a trust
29. Trust distribution
30. Termination by operation of law

MULTIPLE CHOICE EXAM QUESTIONS

Questions 1 through 5 refer to the following fact pattern.

Shaquille "Big Deal" O'Deal is an extremely successful professional basketball player. Each year, he earns at least three million dollars in salary, bonuses and endorsements, and he has been playing basketball for more than 10 years.

Shaquille has three living grandparents, all of whom are retired and living on fixed incomes. Two of them have chronic health problems, and Shaquille regularly contributes to all of their bank accounts to insure that they are comfortable. However, recognizing that he is often on the road and sometimes forgets to send checks out, he decides to set up an account for them. In addition, he writes a letter that says, "I am setting up a bank account to be used for the care and support of my grandparents. Because I travel a great deal and my grandparents are old and sick, I hereby appoint my brother, Sean, to manage this bank account for their benefit."

1. Has Shaquille created a valid trust?
 - (A) No, because the beneficiaries, not named, are indefinite.
 - (B) No, because he has not used special trust language.
 - (C) Yes, because the words he uses are sufficient to create a trust.
 - (D) Yes, if the bank account is in his grandparents' names.
2. Assume for purposes of this question only that the letter Shaquille writes instead states that the bank account is being established in Sean's name and that Shaquille "hopes" that Sean will use the account for the benefit of his grandparents. Will the language be construed as intending to create a trust?
 - (A) Yes, because Shaquille had a pre-existing financial relationship with his grandparents.
 - (B) Yes, because precatory language is generally enforceable in trust situations.
 - (C) No, because Shaquille did not state that Sean had to use the money to take care of the grandparents.
 - (D) No, because precatory language is not generally enforceable in trust situations.
3. Assume for purposes of this question only that Shaquille does not tell anyone about the bank account. Has a trust been created?
 - (A) Yes, because there is no communication requirement for trusts.
 - (B) Yes, because the grandparents count on Shaquille's money.
 - (C) No, because failure to tell anyone can show that the trustor did not have a present intent to create a trust.
 - (D) No, because if Sean does not know about the trust, he can't administrate it.
4. Assume for purposes of this question that, six months after Shaquille establishes the bank account, one of his grandparents dies. How will the rest of the money be distributed?
 - (A) The other two grandparents will continue to receive payments.
 - (B) The other two grandparents will split the deceased grandparent's share of the capital and continue to receive payments on the rest.
 - (C) The trust will terminate.
 - (D) We don't have enough information to answer the question.
5. If the account that Shaquille has set up is a trust, what type of trust is it most likely to be?
 - (A) A charitable trust.
 - (B) A spendthrift trust.
 - (C) A Totten trust.
 - (D) A regular inter vivos trust.

Questions 6 through 9 refer to the following fact pattern.

Bob Steinberg is the director of a very successful bar review company. He has built the company from the ground up and now has a following of tens of thousands of students across the country, all of whom use his bar review practice questions and study methods.

In building a business, Bob has learned that one should keep his cards close to his chest. Therefore, while an open and friendly guy, Bob does not give out information to people that he doesn't feel they need. He is especially private about his personal finances.

Bob has two teenage children, Giles and Margaret. He wishes to create a trust for them, but he doesn't want them to know about it, and he's afraid even to tell his estates attorney about his intention to establish the trust. He's concerned that the attorney, a real "pull themselves up by their bootstraps" type of guy, will discourage him from setting up the trust. Therefore, Bob tells his attorney

to draft his will leaving gifts to his wife and children and a large sum of money to his brother, Evan. Unbeknownst to the attorney, Bob has had a conversation with Evan in which Evan has promised to hold the money he is to receive under the will in trust for Giles and Margaret.

After the will has been properly signed and executed, Bob has a heart attack in the middle of teaching a bar review seminar and dies. His death is mourned by his family, his employees, and by bar review students everywhere.

6. Does Bob's agreement with Evan constitute a trust?
 - (A) Yes, it is a secret trust.
 - (B) Yes, it is a semi-secret trust.
 - (C) No, because Bob did not indicate in his will that he was creating a trust.
 - (D) No, because Evan's promise to hold the money in trust is unenforceable.
7. Assume for purposes of this question only that Evan refuses to perform under the agreement. Assume also that Edna, Evan's wife, and Pat, Bob's wife, also knew of the agreement between Bob and Evan. Is the agreement enforceable?
 - (A) No, because Evan had all the discretion about whether to keep the money or hold it in trust.
 - (B) No, because Bob has given his children gifts under the will.
 - (C) Yes, and Edna and Pat may testify to the agreement's existence and terms.
 - (D) Yes, because of the close family relationship between Bob and Evan.
8. Assume for the purposes of this question only that Bob does tell his estates attorney that he is setting up a trust with Evan as trustee, but he still refuses to tell the attorney (or anyone else except Evan) who the beneficiaries are. The attorney therefore drafts a clause in Bob's will that states, "To my brother, Evan, one trillion dollars, in trust for beneficiaries known to Evan." What will happen to the one trillion dollars?
 - (A) It will be held in trust for Giles and Margaret.
 - (B) It will be held in trust for Bob's estate.
 - (C) Evan will keep the money.
 - (D) It will be put into a trust, but Evan will not be allowed to be the trustee.
9. May a trust be created in a will (as Bob purports to do here)?
 - (A) Yes.
 - (B) No, because there is no present intent to create a trust.
 - (C) No, because the beneficiaries are necessarily indefinite.
 - (D) No, because we don't allow people to control their estates from their graves.

Questions 10 through 12 refer to the following fact pattern.

Lisa and Steve are the parents of Chloe, a beautiful 11 month-old girl. Lisa and Steve are very concerned that Chloe should always be provided for. Therefore, they open a bank account in order to save money for Chloe's future. At the time that they open the bank account, they intend that Chloe (or her guardian) be able to use the money if something happens and Lisa and Steve meet an untimely demise. However, they keep their names on the bank account, as they want to control the funds in the account until their deaths.

10. Have Lisa and Steve created a trust?
 - (A) Yes, they have created a testamentary trust.
 - (B) They have created a Totten trust.
 - (C) No, because they do not have the present intent to create a trust.
 - (D) No, because Chloe has no rights in the account until and unless Steve and Lisa predecease her.
11. If Steve and Lisa change their minds and decide to use the money to pay for Chloe's preschool expenses, may they validly withdraw the money from the account?
 - (A) Yes, because the decision to keep the bank account for Chloe's support after her parents' deaths was a revocable one.
 - (B) Yes, because the preschool expenses fall within the category of expenses for which the account was intended.
 - (C) No, because the decision to keep the bank account for Chloe's support after her parents' deaths was not a revocable one.
 - (D) No, because only Chloe can withdraw funds from the account.
12. If Chloe turns 21 and Steve and Lisa are still living, may she withdraw funds from the account?
 - (A) No, unless she uses the funds for college.
 - (B) No, because she has no interest in the account until Steve and Lisa die.
 - (C) Yes, because the account was created for her benefit.
 - (D) Yes, because she is now a legal adult.

Questions 13 through 15 refer to the following fact pattern.

Lake Warren is a beautiful lake in Southern New Hampshire. The lake is very quiet; very few houses are located on the lake, and there is almost no water skiing or motor boating. All of the residents love the lake and want to keep it pristine.

Not only people live on the lake. Lake Warren is also home to a number of rare species of geese. The lake seems to be a particularly fertile breeding ground for the geese, who migrate south for the winter but return in gaggles each spring for the summer months. One species in particular, the Great Geese, is quite endangered.

Katherine Hepburg, a retired actress, has made her home on Lake Warren for 20 years, ever since she left the glamour of Hollywood life for the simpler pleasures of a lake community. Katherine is particularly devoted to the Great Geese and wants to do everything she can to save them.

13. Katherine approaches you, her estates attorney, to ask you what she can do to save the geese. She is thinking of establishing a trust to protect the Great Geese for all perpetuity. May she do so?
- (A) Yes, because the Rule Against Perpetuities does not apply to charitable trusts.
- (B) Yes, if she limits the duration of the trust to her lifetime.
- (C) No, because such a trust would be violative of the Rule Against Perpetuities.
- (D) No, because protecting the geese is not a charitable purpose.
14. Assume for the purposes of questions 14 and 15 only that Katherine wishes to establish the trust to care for, not all Great Geese, but her personal pet goose, Gander. The trust is to go into effect upon her death and is to be used to feed, clothe, and pamper Gander for the remainder of his natural life. Will this trust be valid?
- (A) Yes, as a charitable trust.
- (B) Yes, as a private trust.
- (C) No, because it is neither a charitable trust nor a private trust.
- (D) No, because trusts may not be created to care for animals.
15. Upon Katherine's death, how should the money Katherine has designated for Gander's care be distributed?
- (A) It should be used to care for Gander for the remainder of his natural life.
- (B) It should be used to care for all Great Geese.
- (C) It should be used to care for animals in danger of extinction.
- (D) It should be held in a general trust for Katherine's estate.

Questions 16 through 18 refer to the following fact pattern.

Simon and Simone are the parents of ten year-old Sarah and five year-old Jonathan. Simon and Simone are also both medical doctors who specialize in treating people with HIV disease. Even before they had children, both Simon and Simone agreed that they would always put the support and care of their children first, but that any extra resources they possessed would be dedicated to helping people with HIV disease. Accordingly, they wish to establish a trust.

16. Which of the following language would NOT form a valid trust?
- (A) "Upon our deaths, the trust res should be used for the care and support of Sarah and Jonathan until each reaches the age of 21. When Jonathan has reached the age of 21, the remainder of the trust res should be used for AIDS research." (Simon and Simone are still living).
- (B) "From this day forward, the trust res should be used for the care and support of Sarah and Jonathan or for the care and support of people with HIV disease." (Simon and Simone are still living).
- (C) "For Sarah and Jonathan's college educations; when each has completed an undergraduate degree, the remainder of the trust res should be used to care for people with HIV disease."
- (D) "For Sarah and Jonathan for life, thereafter for the care of people with HIV disease."
17. If Simon and Simone succeed in establishing a trust, and the time has come to use the trust assets for people with HIV disease, which of the following would NOT be a valid action by the trustee?
- (A) The trustee allocates a percentage of the trust's income to a reputable scientific non-profit organization that is attempting to develop a cure for AIDS.
- (B) The trustee finds an AIDS hospice which is desperately in need of funds. He makes a yearly donation from the trust to the hospice.
- (C) The trustee learns of a political organization that is lobbying for more access to experimental drugs for people with HIV disease. He pledges a percentage of the trust's income to the organization, to be paid over a five-year period.
- (D) The trustee learns that schizophrenia has become a large problem in the inner-city of New City, where Simon and Simone spent a great deal of time. He commits yearly donations to a public health organization in New City.

18. Assume for the purposes of this question only that, 10 years after Simon and Simone set up a valid trust with the aforesaid objectives, a cure for AIDS is found. All AIDS cases are subsequently cured, and there are no more people with HIV disease. The Center for Disease Control announces and declares that HIV has been eradicated and that the only remaining small amount of the virus is locked safely away in a vault in Switzerland. What will happen to the trust?

- (A) Because Simon and Simone are particularly devoted to caring for people with HIV disease, the trust will probably terminate.
- (B) Unless Simon and Simone used specific language indicating that they only wanted the assets to be used for HIV disease, the trust will probably be allocated to help people with other medical problems.
- (C) The trust will remain on hold in case there's a future outbreak of HIV; after all, no one knows exactly where it came from in the first place.
- (D) None of the above.

19. Which of the following would be an inappropriate action for the trustee of a trust?

- (A) Leasing real estate in order to obtain income for the trust.
- (B) Investing trust assets in blue chip stocks.
- (C) Selling land that stands vacant.
- (D) Making an unsecured loan to a friend of the trustor.

20. Which of the following is NOT a duty that a trustee has to the beneficiaries?

- (A) A duty to account to the beneficiaries.
- (B) A duty to collect and preserve trust assets.
- (C) A duty personally to carry out all trust functions.
- (D) A duty to make trust property productive.

21. If a trustee breaches any of his duties, who may bring a claim against him?

- (A) The trustor only.
- (B) The trustor and/or the beneficiaries.
- (C) The beneficiaries only.
- (D) The trustee is immune from actions against him.

Questions 22 through 25 refer to the following fact pattern.

Tom Trustee is the trustee of a large trust, which he administers on behalf of all of the grandchildren of Stan Walton, a mega-businessman from humble beginnings. Stan was responsible for starting Wall-Market, a national chain of discount stores. In trust for the grandchildren is Wall-Market's stock as well as other assets. Wall-Market is still a privately-held company, and the trust owns 100% of its stock.

Because individual Wall-Market stores are owned by franchisees, Tom routinely makes investments on behalf of the trust and enters into contracts with franchisees, who purchase assets from the trust's holdings and return a percentage of their earnings to the trust company.

In July, 1999, Frankie Franchisee brings a contract action against Wall-Market, Tom, and the trust, saying that Tom promised to allow Frankie to keep 100% of the revenues of his store but is now demanding a 1% contribution to the company. Frankie claims that Tom is trying to take away his franchise because Frankie refuses to pay the 1% contribution. Other franchisees routinely pay the company 1% of revenues.

Frankie produces a contract signed "Tom Trustee, on behalf of the Wall-Market/Walton trust." The contract contains a clause stating that Frankie may keep 100% of his store's revenues. It also contains a clause stating that Tom disclaims any liability relating to claims arising from the contract.

22. Will Frankie prevail against Tom?

- (A) No, because Tom specifically disclaimed liability.
- (B) No, because the other franchisees pay 1% of their revenues to the company.
- (C) Yes, because Tom, as trustee, is personally liable for contracts he enters into on behalf of the trust.
- (D) Yes, because Tom is in breach of contract.

23. Will Tom be entitled to reimbursement from the trust if Frankie recovers damages from him?

- (A) Yes, because Tom entered into the contract on behalf of the trust.
- (B) Yes, because he disclaimed liability in writing.
- (C) No, because he did not act for the benefit of the trust.
- (D) No, because the trust is also a defendant in the action.

24. Assume for purposes of this question only that, when interviewed by the press about Frankie Franchisee's lawsuit, Tom Trustee tells The New York Times that Frankie Franchisee is "a stinking idiot who failed basic arithmetic in second grade."

Frankie sues Tom, the trust, and Wall-Market for defamation. As evidence for his position, Frankie produces affidavits from his wife and gym buddies that he showers on a daily basis and uses deodorant. He also produces a copy of his second-grade report card, which reflects a grade of B+ in arithmetic. The report card does show that Frankie failed social studies and language arts. Will Frankie prevail against Tom for defamation?

- (A) No, the trust would be liable, not Tom.
 - (B) No, Wall-Market would be liable, not Tom.
 - (C) Yes, because as trustee, Tom is personally liable for torts he commits in the course of performing trust duties.
 - (D) Yes, because Tom's statements were untrue.
25. If Frankie succeeds in his defamation action against Tom, will Tom be entitled to reimbursement from the trust for any damages he has to pay Frankie?
- (A) Yes, because the statement was a normal incident to an activity in which Tom was properly engaged on behalf of the trust.
 - (B) Yes, because Tom was speaking on behalf of the trust.
 - (C) No, because the trust is also a defendant in the action.
 - (D) No, because he was personally at fault.
26. May a beneficiary assign his right to receive income or principal from a trust?
- (A) Yes, under limited circumstances.
 - (B) Yes, gratuitously or for consideration.
 - (C) No, because the trustor intended the trust to benefit that particular beneficiary only.
 - (D) No, because the right to receive income or principal from a trust is not alienable.
27. May a beneficiary devise his interest in a trust?
- (A) No, because trusts and wills are not interrelated.
 - (B) No, because a trust ends on the death of the beneficiary.
 - (C) Yes, because an interest in a trust is an asset which is freely devisable.
 - (D) Yes, because the trustor has no control over what a beneficiary does with his interest in a trust.

Questions 28-30 refer to the following fact pattern.

The 2000 Summer Olympics are to be held in Sydney, Australia, and the Singer family is very excited. Susan and Sidney Singer are the parents of five children, four of whom are entering the Olympic trials in various events. Sam Singer is a high-jumping high jumper, Sally Singer is a champion swimmer, Solomon Singer is proficient on horseback, and Sarah Singer is the world's best on the balance beam.

In order to pay for training, lessons, competitions, costumes, and sports therapy, Susan and Sidney have set up a trust for the benefit of these little athletes. The trust is intended to pay for athletic-related expenses until the conclusion of the Sydney games, at which point the family has agreed that the children will retire from sports and the family will begin having dinner together every night, going to the amusement park, and doing things that other families do.

The Olympic trials come and go, and, much to the disappointment of the Singer family, none of the children qualify for the Olympic team.

28. What happens to the trust?
- (A) It naturally expires at the end of the Olympics.
 - (B) It remains in effect in case one or more of the children want to resume an athletic career.
 - (C) It is given to the fifth Singer child, Sasquatch, because he didn't get any benefits from the trust while the others were competing in athletics.
 - (D) The trustors may modify it to use for other purposes.
29. Assume for purposes of this question only that Solomon and Sarah make the Olympic team but the other children do not. What happens to the trust?
- (A) It will be used for Solomon and Sarah's athletic expenses until the conclusion of the Sydney games.
 - (B) It will be used for Solomon and Sarah's athletic expenses for as long as they choose to continue athletic competition.
 - (C) It will be used for any child who wishes to compete in athletics for as long as they wish to do so.
 - (D) It will terminate because all four children are not competing in Sydney.

30. Assume for purposes of this question only that all four children qualify for the Olympic team. The Singers are ecstatic and can hardly wait to take the whole family to Sydney for the competition. However, two weeks before the Olympics, Australia invades New Zealand and holds all blue-eyed New Zealanders in concentration camps. President Clinton therefore boycotts the Sydney Olympics, and none of the athletes are sent to the games to represent the U.S. What happens to the trust?
- (A) It remains in effect for future Olympics.
 - (B) It terminates by operation of law.
 - (C) It goes to Sasquatch, who has not otherwise benefited from the trust.
 - (D) Susan and Sidney may decide whether or not the trust should continue.

ANSWERS TO MULTIPLE CHOICE EXAM QUESTIONS

1. (C) Shaquille's words are probably sufficient to create a trust. No specific trust language is required; rather, the trustor's intention is determined from the language utilized, his relationship with the parties involved, and any other appropriate circumstances. Shaquille has been supporting his grandparents for years, and he has a close relationship with them. (B) is therefore incorrect. (A) is incorrect because the grandparents are easily ascertainable individuals. (D) is incorrect because the bank account does not have to be in the names of the grandparents in order to constitute a trust.
2. (A) Shaquille has been supporting his grandparents for some time. Therefore, even though he only uses precatory language (as opposed to mandatory language), a court would probably decide that intent was present. (C) is therefore wrong. (B) is an incorrect statement of law. (D) is a correct statement of law, but this situation would probably constitute an exception.
3. (C) The beneficiaries of a trust do not have to know of its existence, but the failure to inform anyone of the existence of a trust arguably shows that the trustor lacked the requisite intent to create a trust relationship. (A) is therefore wrong. (B) is irrelevant if Shaquille does not possess the requisite intent. (D) is a correct statement of fact, but the legal reason is better laid out in (C).
4. (D) While (A) is probably correct to some degree and (B) and (C) are probably incorrect (Shaquille's intent does not seem to be that the grandparents receive capital or that all three are living), we probably do not know exactly whether the payments to the living grandparents will increase or stay the same upon the death of the one grandparent.
5. (D) (A) is incorrect because the beneficiaries are definite and Shaquille's grandparents are not a charity. There is no language in the trust instrument stating that the beneficiaries may not transfer their portion of the trust. Therefore, (B) is incorrect. A Totten trust is one in which the trustee sets up a bank account for someone else's benefit but retains control over it. Here, control is given to Sean. Therefore, (C) is incorrect. This is a regular *inter vivos* trust.
6. (A) A secret trust arises where a trustor devises money to a trustee but does not state in the will that the money is for a trust. That is exactly the situation that Bob has set up with Evan here. (B) and (C) are therefore incorrect. (D) is incorrect because promises to hold money in trust are enforceable.
7. (C) Extrinsic evidence is admissible to prove the existence of a secret trust, so Edna and Pat may testify to the trust's existence and terms. (A) is incorrect because Bob was specific about the use of the money, and he did not give Evan broad discretion about how to use the money. (B) is entirely irrelevant. Bob may both set up a trust for the children AND leave them outright gifts in his will. (D) is an incorrect statement of law. The trust is enforceable because of Bob's intent and because of the agreement between Bob and Evan, not because of the family relationship between Bob and Evan.

8. (B) The "trust" established in this question is a semi-secret trust, which would be unenforceable in most jurisdictions. Where a semi-secret trust is unenforceable, the court imposes a constructive trust in favor of the trustor's estate. (A) and (C) are therefore wrong. (D) is incorrect because it is not the identity of the trustee that is at issue, but rather the nature of the trust.
9. (A) A trust may absolutely be created in a will. Such a trust is called a "testamentary trust." (B) is incorrect because the requisite intent is considered to be present where a testator creates a testamentary trust. (C) is incorrect because we consider the identity of the beneficiaries at the time their interests vest. Here, their identities (probably already certain), will be absolutely certain upon Bob's death. (D) is clearly incorrect under any theory of Trusts and Estates!
10. (B) A Totten trust arises where the trustor opens a bank account in his/her own name and intends that the beneficiary have no rights in the account until their deaths. Such is the case here. (D) is therefore incorrect. It is not a testamentary trust, (A), because it is not created in a will.
11. (A) Totten trusts are much like wills in that they are revocable at any time. Unless Lisa and Steve formalize their intentions with a written document, the trust will remain an informal, Totten trust. (C) is therefore incorrect. (B) is irrelevant because Lisa and Steve have retained the right to make decisions about and control the bank account. (D) is therefore incorrect.
12. (B) Totten trusts are also similar to wills in that the beneficiary has no rights in the trust until the testator dies. (A), (C), and (D) are therefore incorrect.
13. (A) Katherine's trust will qualify as a charitable trust, and such trusts are not subject to the Rule Against Perpetuities. (B), (C) and (D) are therefore incorrect.
14. (C) This trust is neither a charitable trust nor a private trust, and the cy pres doctrine would not apply since it is not a charitable trust. Furthermore, the trust violates the Rule Against Perpetuities. (A) and (B) are therefore incorrect. (D) is incorrect because trusts may be established to care for animals as an indefinite group, but they may not be created to care for a specific pet.
15. (D) Katherine's money should be held in trust for her estate. Because this is not a charitable trust, the cy pres doctrine can not apply. (B) and (C) are therefore incorrect. (A) is incorrect for the reasons stated in the previous answer.
16. (B) This language creates neither a private trust nor a charitable trust. There are not distinct time periods for each gift stated, and the gifts are not clearly distinguished from one another. Therefore, it is unclear how much money should go to each party and when it should be distributed. (A), (C) and (D) all divide the money clearly and thus are valid.
17. (D) Simon and Simone have been specific in designating the funds' use — they want it to help care for people with HIV disease. (A), (B) and (C) are all arguably consistent

with that purpose. (D) has nothing to do with HIV disease, and the trustee will therefore not be permitted to use the funds for that purpose.

18. (A) Simon and Simone are particularly concerned about HIV disease – they have made their careers in that area. Therefore, if HIV is cured, the trust will probably terminate. Had they been doctors who were simply interested in chronic or terminal illness, the trust could be converted to help people with different illnesses, and (B) would have been correct. (C) and (D) are clearly incorrect.
19. (D) All of the others are within the trustee's powers and duties.
20. (C) A trustee may delegate ministerial and minor discretionary functions. All of the others are duties of the trustee.
21. (C) Only the beneficiaries may bring a claim against a trustee, who certainly is not immune! The trustor's standing to bring such a claim terminates with the creation of the trust and the appointment of the trustee.
22. (D) (D) is correct because, although Tom disclaimed liability, he is still personally liable for contracts he enters into on behalf of the trust where his actions exceed his authority or are improper. Because all of the other franchisers pay the company 1% of revenues, Tom probably does not have the authority to make a different deal with Frankie. Furthermore, the deal with Frankie is harmful to the trust, because the trust will not get earnings that it normally would receive under the terms of the typical franchisee contracts. (A) is incorrect because, although Tom would be free from personal liability in ordinary circumstances if he disclaimed liability in writing, such is not the case where he exceeds his authority. (B) is completely irrelevant. (C) is a true statement but does not take into account the breach or the disclaimer.
23. (C) Tom would be entitled to reimbursement if he had acted for the benefit of the trust and within his authority. However, as we saw in the previous answer, such is not the case. (A) is therefore wrong. As we saw in #22, the disclaimer (B) is ineffective under these circumstances. (D) is entirely irrelevant to the question at hand.
24. (C) (C) is the best answer because Tom will be personally liable for torts he commits in the course of performing trust duties unless he is not personally at fault. Tom's temper got him into trouble here, and this is definitely his fault! (A) and (B) are therefore incorrect. (D) is a correct statement, but only addresses an element of defamation, not Tom's position as trustee. (C) is therefore the best answer.
25. (D) As we saw in #24, Tom cannot be protected by his position as trustee where he did not act for the benefit of the trust or where the tort was not a normal incident to an activity in which the trustee properly engaged. Defaming a franchisee is definitely not a proper activity for a trustee! (A) and (B) are therefore wrong. (C) is irrelevant to the question at hand.
26. (B) A beneficiary may freely assign his rights to receive income or principal from a trust and may do so gratuitously or for consideration.

27. (C) Unless there is a pour-over provision which provides that, on the beneficiary's death, the trust will go to another, a beneficiary may freely devise his interest in a trust. (A) is a silly statement. (B) is incorrect because, while a trust may end on the death of a beneficiary, the trustor must explicitly state that this should happen. (D) is incorrect because a trustor may set up parameters for the trust when the trust is established.
28. (A) Where a trust is to be in operation for a specified number of years or until the occurrence of a prescribed event, and that period of time has elapsed or the incident has occurred, the trust ordinarily terminates in accordance with the instrument's terms. Here, the Singers have established a trust for athletic-related expenses to be used until the end of the Sydney games. The trust will therefore expire at the conclusion of the games. (B) is incorrect because it is inconsistent with the terms of the trust. (C) is ridiculous as it is inconsistent with the terms and nature of the trust. (D) is incorrect because, in the majority of states, a trustor may not modify an *inter vivos* trust after it is established unless he has specifically reserved the right to do so under the terms of the trust instrument.
29. (A) This is the only answer that is consistent with the terms of the trust.
30. (B) The material purposes of the trust have become impossible. Therefore, the trust will terminate. (A) and (C) are therefore incorrect. (D) is incorrect because, in the majority of states, a trustor may not modify an *inter vivos* trust after it is established unless he has specifically reserved the right to do so under the terms of the trust instrument.

ESSAY EXAM QUESTIONS

Note to students: Because the subject Trusts necessarily includes elements of Wills, Property, and other areas of the law, you will find that you may need to address non-Trusts issues in fully answering these essay questions. The same will probably be true on your law school exams and on the bar exam.

Questions 1 and 2 refer to the following fact pattern.

Bill, a widower, duly executed a will, dated February 1, 1987. It reads as follows:

ONE: I leave my stamp collection to those persons whose names appear from time to time on a memo that can be found in the drawer of my night table in my home.

TWO: I leave the balance of my estate to the Trustees of The Bill Revocable Trust, dated January 31, 1987, between myself, as grantor, and the Faithful Trust Company, as Trustee to hold in trust thereunder.

Under the terms of Bill's Revocable Trust, income is payable to Bill for life, remainder to Bill's children, Tilly and Rita, in equal shares. Bill died on December 30, 1988. Tilly predeceased Bill, having died on October 15, 1988. Her son, Allan, age three, survived Bill.

Under the terms of Tilly's will, she bequeathed all of her property to her distant cousin, Calvin. Tilly's will was executed before Allan was born. On Allan's first birthday, Tilly gave him \$10,000. The asset value of Tilly's estate, without taking account of Bill's trust, is \$150,000.

An unsigned and undated memo was found in Bill's home leaving his entire stamp collection, valued at \$150,000, to his cousin, Nellie. In addition, Bill left stocks and bonds valued at \$350,000.

Rita, Allan, Calvin, and Nellie survive Bill.

What rights, if any, does each of the survivors have in the estates of:

1. Bill? Discuss.
2. Tilly? Discuss.

Question 3. Describe an *inter vivos* trust and give a detailed example.

Question 4. Describe a testamentary trust and give a detailed example.

Question 5. Describe a secret trust and give a detailed example.

Questions 6 and 7 refer to the following fact pattern.

A was the owner in fee simple of a parcel of real property on which there was a building housing five tenants who carried on separate businesses in the building. In 1980, A entered into a new 10-year written lease with B, one of those tenants. In the lease, A covenanted to keep the leased premises "in good repair and condition throughout the term of this lease." Part of the property to the rear of the building consisted of a parking lot exclusively controlled and maintained by A for the convenience of his tenants and their customers.

A died in 1982, devising his entire estate to T in trust for the benefit of N's daughters, who survived him. During the administration of the estate, B's leased premises fell into disrepair, and although B demanded of N's executor that repairs be made, nothing was done. In 1984, administration of N's estate was completed and T undertook administration of the trust. B demanded that T make repairs; T refused. B then spent \$1500 on repairs to the leased premises.

After T became trustee, the surface of the parking lot developed several severe cracks, making use of the lot hazardous. Tenants complained to T about the parking lot, but T refused to repair it. C, a customer of one of the tenants, fell because of the hazardous condition of the parking lot and suffered permanently disabling injuries.

B sued T individually and as trustee for breach of covenant to repair leased premises. C sued T individually and as trustee in a personal injury action seeking damages that far exceeded the total of the trust assets.

6. What should the result be in each of these actions? Discuss.
7. Is T entitled to indemnification from the trust estate for any damages recovered against him individually? Discuss.

Question 8. Describe a semi-secret trust and give a detailed example.

Question 9. Describe a Totten trust and give a detailed example.

Question 10. Describe a charitable trust and its purposes and give a detailed example.

Question 11 refers to the following fact pattern.

Bill, a widower, had one child, his daughter June. Bill purchased a \$100,000 farm (Blackacre), bought a single payment life insurance policy on his own life (face amount \$50,000), and maintained a large balance in a checking account (usually \$100,000). Titles to the farm and the account were always in Bill's name only. June was named originally as beneficiary of the insurance policy, but Bill reserved the power to change the designation of his beneficiary.

A few years before his death, Bill requested the insurance company to make Joe, his neighbor, sole policy beneficiary. After the company informed Bill the change had been made, Bill wrote Joe: "I have named you my insurance beneficiary. You are to collect the proceeds and divide them three ways. You are one; the others I shall name later." Joe replied: "Sure, I'll do what you want."

In June 1995, Bill executed a deed conveying Blackacre to an old friend, Pete. The day of this execution, Bill mailed a signed letter to Pete directing him to "rent my farm, pay the net income to June yearly, and when she dies, convey the farm to my church." Pete received and read the letter. A few days later, Bill attempted to deliver the deed to Pete but found out from Pete's housekeeper that Pete was on a three-month sailing trip in the South Pacific. Bill gave the housekeeper the deed and told her to give it to Pete when he returned.

In July 1995, Bill suffered a heart attack and while hospitalized, executed a valid will which left "all property I own to my daughter, June, and I recommend that she look out after my 90-year-old Aunt Selma, as long as she lives, making such gifts and provisions for her as she, June, thinks best."

The day after executing this will, Bill wrote the following on a separate piece of paper: "To Joe: the other two beneficiaries are Tom Allen and his wife."

Bill died the following day. Two days after Bill's death, Pete's housekeeper handed Pete the deed.

11. Who is entitled to the assets and why? Discuss.

Question 12. Describe a support trust and give a detailed example.

Question 13. Describe a discretionary trust and give a detailed example.

Question 14. Describe a spendthrift trust and give a detailed example.

Question 15 refers to the following fact pattern.

In 1992, Agatha loaned \$300,000 to her brother George. George died in 1995. His will provided that if Agatha forgave the \$300,000 debt, a \$300,000 trust would be created for her under his will ("Trust E1"). Agatha forgave this debt in exchange for the trust interest. Under this trust, Agatha receives the income for life, and upon her death the corpus is to be distributed to Betty, Agatha's daughter.

George's residuary estate passed into Trust E2 for the benefit of five named beneficiaries. Agatha was not named as a beneficiary of this trust.

Each of the trusts created by George's will contained a spendthrift provision stating that creditors could not reach income in the trustee's hands. Nancy, George's accountant, was designated trustee of Trust E1, and Agatha was designated trustee of Trust E2. Each trustee was authorized to sell trust assets.

In 1998, Agatha defaulted on a \$10,000 loan from John made in 1991. She relied on the spendthrift clause to shield her income interest in Trust E1 from John's claim for the debt. However, to discharge her debt, she offered to sell John 100 shares of T stock from the corpus of Trust E2 for \$10,000 less than its fair market value. John agreed and purchased the stock from Trust E2 on the offered terms.

In 1999, John gave the T stock to his nephew Larry as a wedding present. Larry had no notice of the prior transactions and still has possession of the T stock.

15. What are the rights and liabilities of John, Agatha, and Larry? Discuss.

Question 16. During his lifetime, Ted establishes a trust to provide for the education of his children. What type of trust is being established? What are the characteristics of this type of trust?

Question 17. In his will, Joe establishes a trust for his daughter, Margo, and any other surviving children. What type of trust is being established? What are the characteristics of this type of trust?

Question 18. Courtney devises her bank account at Wells Fargo Bank to her sister, Susan. Although it is not so stated in Courtney's will, Susan has promised to use this money for the benefit of Courtney's niece and nephew, Susan's children, Andrea and Charles. What type of trust is being established? What are the characteristics of this type of trust?

Question 19. A client comes to you and asks you to draft a trust for her. What kinds of questions would you want to ask her to insure that her trust adequately serves her needs?

Question 20. Your client has answered your questions. What clauses should you be sure to include in her trust?

Question 21. Courtney devises all of the money in her bank account at Wells Fargo Bank to her sister, Susan, "in trust". What type of trust is being established? What are the characteristics of this type of trust?

Question 22. Jonathan creates a trust for the benefit of his daughter, Miranda, and includes a provision which states that Miranda may not transfer her interest in the trust and that creditors may attach her interest in the trust. What type of trust is being established? What are the characteristics of this type of trust?

Question 23. A new client calls for an appointment with you. When he comes in for a meeting, he tells you that he had his prior attorney draft a trust. He tells you that he is concerned that the trust may not meet all of the legal requirements for a trust. He asks you to analyze the trust instrument and suggest any modifications that should be made.

Here is the trust language that the prior attorney drafted:

"I, Willy Wonka, give the value of 25,000 chocolate bricks to my friend, the Wicked Witch. I hope that the Wicked Witch will use the trust to benefit chocolate lovers everywhere. Furthermore, I promise my friend, Stuart Little, that I will create a similar trust in his favor at some point in the future, but no later than the year 2002. I intend that that trust will be in effect for all perpetuity."

What advice would you give to your new client about revisions?

Question 24. Cynthia creates a trust for "the promotion of health and the elimination of AIDS in sub-Saharan Africa". What type of trust is being established? What are the characteristics of this type of trust?

Question 25. Andrea creates a trust "for all of the people who like Alfred Hitchcock movies". The assets of the trust are to be used to provide money for weekly screenings of Alfred Hitchcock movies. What type of trust is being established? What are the characteristics of this type of trust?

ANSWERS TO ESSAY EXAM QUESTIONS

1. What rights, if any, does each of the survivors have in Bill's estate?

ANSWER A

A. Nellie

The first issue to be determined is whether Nellie ("N") has a right to Bill's ("B") stamp collection by virtue of Paragraph 2 of B's will and/or the memo found in B's home. There are several theories under which N could assert her claim.

(1) The memo was integrated into the will: This argument will not be successful because the memo was not found in the same place as the will, and there is nothing in the facts indicating that the memo was physically present when B executed his will.

(2) The memo was incorporated by reference into the will: Under incorporation by reference, a pre-existing document, which is not itself valid as a testamentary instrument and is not integrated, may nevertheless be used as part of a will if it is sufficiently identified and was in existence at the time the will was executed and has not since been altered.

N may assert that the reference to "a memo that can be found in the drawer of my night table" sufficiently identifies the memo as an existing document that is incorporated by reference.

However, there are several problems with this argument. First, the facts do not indicate exactly where the memo was found — it may have been someplace in B's home other than his nightstand drawer. Second, the memo is undated and gives no hints of when it was written, so it may very well not have been in existence when B executed his will. Finally, the fact that B referred to "those persons whose names appear from time to time" indicates that it was exactly his intention to alter or replace the memo after he executed his will.

Therefore, the memo should not be held to be incorporated by reference.

(3) The memo may be valid under the doctrine of acts of independent significance: N may also argue that the name(s) B put on the memo may be used to determine who gets the stamp collection because they are facts of independent significance. However, there is no indication that the memo had any other meaning or importance apart from determining who would get the stamp collection; therefore, this argument should be rejected.

(4) The memo was a codicil to Bill's will: A codicil is a valid testamentary instrument that adds to, subtracts from, or alters the terms of a pre-existing will.

The memo is not valid as a codicil because it does not comply with the requirements for either a formal testamentary instrument or a holograph. It was not witnessed, a requirement for a formal will, and it was not signed by B, a requirement for both a formal will and a holograph.

(5) Conclusion: Because N has no viable argument that the memo should be given testamentary effect, she has no rights under B's will, and the stamp collection becomes part of the residue of B's estate, governed by paragraph 2 of the will.

B. Rita

Rita's claim depends first on whether paragraph 2 is a valid pour-over provision. There are three theories which validate the pour-over from the will into the trust.

(1) Incorporation by reference: The trust instrument was in existence at the time B executed his will, and apparently it created a valid *inter vivos* trust. (The facts do not indicate that there was a trust *res* when the trust document was created.) Further, there is no indication that B attempted to alter the terms of the trust after the execution of his will. The fact that the trust was revocable does not invalidate it. Thus, the requirements for an incorporation by reference, as discussed earlier, are fulfilled.

(2) Acts of independent significance: Alternatively, Rita (R) can argue that the existence of the valid trust is an act of independent significance, as described earlier, which validates the pour-over provision.

(3) Statutory validity: Finally, in most jurisdictions, a provision in a will pouring property into a valid pre-existing trust is valid by statute. There is a split of authority as to whether this is true where the testator/settlor later alters the terms of the trust.

(4) Conclusion: Because the pour-over provision is probably valid, R is entitled to one-half of the residue of B's estate, since the trust instrument divides the remainder between Tilly and Rita in equal shares. (The disposition of the other half will be discussed below.) Since the stamp collection also fell into the residue, R is entitled to one-half of it, and one-half of the \$350,000 worth of stocks and bonds.

C. Allan

Allan (A) will be asserting a claim to his mother, Tilly's, ("T") one-half interest in B's estate. There are two possible grounds for this claim.

(1) Taking under an anti-lapse statute: If T's interest in B's estate is only vested upon B's death, then ordinarily her gift would lapse because she predeceased B. However, because most jurisdictions have anti-lapse statutes, A would probably take T's share because he is her sole surviving issue.

(2) Taking under T's will: Alternatively, A can argue that T had a remainder interest in the *res* of the trust that vested when the trust was executed, while T was still alive. Such a remainder interest is marketable and devisable, and thus would become

part of T's estate upon her death. A's will be discussed below. A has a strong argument that he is entitled to a share of T's estate as a pretermitted heir.

ANSWER B

Paragraph One of Bill's Will

The first issue is whether or not Nellie can take a valuable stamp collection under this provision of Bill's will. There are several theories she may argue.

Incorporation by Reference

Nellie may argue that the memo found in Bill's home should be incorporated into his will by reference in order to identify her as the taker of the stamp collection. In order for a document to be incorporated, it must be: (1) in existence at the time the will was executed, (2) clearly referred to in the will, and (3) intended to be incorporated by the testator.

Because the memo here was undated, she will have to prove by extrinsic evidence that it was in existence prior to February 1, 1987. Nellie may also have a problem with the second element because the reference in the will is not very specific and we don't know exactly where the memo submitted was found. Her case would be strengthened if it was in Bill's nightstand. If Nellie can successfully satisfy the first two elements, Bill's intent will be presumed, and Nellie can take the stamp collection. However, her chances based on the minimal facts here look weak.

Acts of Independent Significance

Alternatively, Nellie may argue that this theory applies. Under this theory, documents and/or acts executed by the testator during his lifetime can be used to "fill in the blanks" in a will if the acts or documents have primarily non-testamentary significance. The reasoning is that these documents or acts reliably indicate the testator's intent. Here, unfortunately for Nellie, it is unlikely that she will be able to articulate a non-testamentary purpose for Bill to place a memo in his nightstand indicating who gets the stamp collection. Consequently, she will probably lose on this theory too.

Holographic Codicil

Nellie may finally try to argue that the memo is a codicil to Bill's will. However, the critical problem here is that it is unsigned. For a codicil to be valid, it must comply with all the requirements of a formally executed will or a holograph (depending on whether holographic wills are valid in the jurisdiction). A signature of the testator is required for both.

Power of Appointment

Nellie might finally argue that this provision creates a special power of appointment in Bill's executor. However, it will probably be found to be not specific enough to enforce, and there is too much potential for fraud.

Paragraph Two of Bill's Will

This provision looks like an attempt by Bill to create a pour-over trust. Such a provision can be found valid under one of several theories.

Incorporation by Reference

Applying the same elements as those discussed above, the trust instrument was in existence prior to the execution of the will, January 31, 1987, so element (1) is easily satisfied. There would only be a potential problem if that instrument had been subsequently modified. The trust instrument is also clearly identified and thus there seems to be no uncertainty as to Bill's intent. The terms of the trust can probably be incorporated by reference into Bill's will.

Acts of Independent Significance

Alternatively, the pour-over provision can be validated on this theory. As discussed above, the lifetime act/document must have non-testamentary significance. Here, since Bill was to receive the income from the trust for life, his motive in creating it was not purely testamentary. There is, therefore, little chance of fraud. Consequently, the trust, together with modifications, if any, could be used in the probate of Bill's will.

Uniform Testamentary Addition to Trust Act

Finally, pour-over provisions are valid under this provision of the probate code where it applies. A trust executed prior to, or contemporaneous with, a will may be used for this purpose so long as it is clearly identified in the will and sufficiently clear and definite in its terms to be enforced. These conditions, as discussed above, appear to be satisfied. The trust instrument can be brought into probate court in order to execute Bill's will.

What Is In the Residue?

If Nellie is unsuccessful in her arguments to obtain the stamp collection, it will go into the residue, together with the stocks and bonds valued at \$350,000.

Remainder to Bill's Children

Rita is entitled to one-half of the residue valued at either \$500,000 or \$350,000. The real fight will be over Tilly's share since she predeceased Bill. The conflict will be between Allan and Calvin.

Lapsed Gift

Because Tilly did not survive Bill, her gift appears to have lapsed. Allan will argue that there was a survival requirement and therefore any anti-lapse provision of the probate code should apply. An anti-lapse statute applies where a gift under a will lapses because the devisee fails to survive the testator. If that devisee is kindred of the testator, then, absent a contrary provision in the will, the issue of the predeceased devisee takes the gift. Here, that would be Allan.

Calvin will argue, on the other hand, that there was no survival requirement and Tilly's remainder was fully vested, and therefore she could leave it to him in her will.

Rita can also have a claim to the entire residue if the gift is a class gift. But then Allan will point out that anti-lapse applies to class gifts too. It probably isn't a class gift anyway because the children are named individually. In the end, Calvin is likely to prevail in arguing that Tilly could dispose of her remainder interest by will. And to determine who ultimately gets that, we turn to Tilly's will.

2. What rights, if any, does each of the survivors have in Tilly's estate?

ANSWER A

A. Pretermitted Heir

Whether Calvin (C) or Allan (A) has a right to T's estate depends on whether A can assert a successful claim as a pretermitted heir. A pretermitted heir is a child who is born after the parents' will is executed and is not provided for in his parents' will. Such a child is entitled to take his intestate share of the parents' estate.

There are several exceptions to the pretermitted heir rule:

(1) Intention to disinherit the child appears on the face of the will: There is no indication in the facts that this exception applies.

(2) At time the will was executed, the testator had other living children and left all of the estate to the parent of the pretermitted heir. This exception is apparently inapplicable.

(3) The testator made an alternative disposition to the child which was intended to replace his testamentary share: C may argue that T's gift of \$10,000 to A was intended to replace any testamentary gift. However, this is a weak argument. There is absolutely no evidence of what T's intent was. Further, the size of the gift, \$10,000, versus the size of her estate, \$150,000, plus her share of B's estate, indicates the gift was probably not intended to replace a testamentary disposition.

Therefore, as a pretermitted heir, A is entitled to claim his intestate share as T's sole issue, and he will get her \$150,000 estate plus her one-half share of B's estate.

ANSWER B

Tilly's Will

Calvin will argue that all of Tilly's property goes to him, assuming her will has been validly executed.

Pretermitted Child

Allan can claim to be a pretermitted child because the will offered into probate by Calvin was executed prior to Allan's birth, and he was not provided for in that will. An omitted child is entitled to take what he or she would have taken intestate unless (1) the intent to omit the child appears on the face of the will, (2) the child is provided for outside the will in lieu of a testamentary disposition, or (3) at the time the will was executed, the testator had one or more children already and he or she left substantially all of his estate to the other parent of the child.

Situations (1) and (3) do not appear on these facts. However, exception (2) could arguably apply given the \$10,000 gift Tilly made to Allan on his first birthday. This will be Calvin's argument. It is not likely to convince a court, however, given the size of the gift relative to Tilly's entire estate. Allan will probably be entitled to his intestate share of Tilly's estate. The size of that share depends on whether Tilly has a husband or other kids. Conceivably, Allan could take it all.

3. Describe an *inter vivos* trust and give a detailed example.

Definition

An *inter vivos* trust is one created during the trustor's lifetime. For an *inter vivos* trust, a trustor must declare that legal title to the subject property is now held by a trustee for the beneficiary. Furthermore, a trustor must, in the case of real property, execute a deed conveying title to the trustee and deliver that document to the trustee or his agent. Where the trustor has personal property, transfer may be made by physical delivery, symbolic delivery or constructive delivery.

Specific Examples

Parents might set up an *inter vivos* trust to provide for their children's education, to support an elderly relative, or to fund medical research. Grandparents might establish an *inter vivos* trust to give grandchildren a piece of the family business, to help grandchildren pay for college expenses, or to support a charitable cause. A stranger could establish an *inter vivos* trust to care for a child who is the victim of domestic violence. There are many types of *inter vivos* trusts, as the requirements outlined above leave room for many variations.

4. Describe a testamentary trust and give a detailed example.

Definition

A testamentary trust is created by a testator's will. Its essential terms are described in, or incorporated by reference into, a valid will. Such a trust speaks as of the testator's death and takes effect at that time. Various kinds of trusts may be created in the will of a trustor.

Specific Examples

A parent could establish a testamentary trust to care for minor or grown children upon the parent's death. A grandparent could establish a testamentary trust to leave grandchildren an interest in a family business. A man could establish a testamentary trust to support his aging parents in the event of his death. A woman could establish a testamentary trust in favor of a children's orphanage. As long as the trust meets the requirements set out above, a testamentary trust could take almost any form.

5. Describe a secret trust and give a detailed example.

Definition

A secret trust situation arises where property is devised to another without reference in the will to the fact that the devisee promised the trustor to hold the property received in trust for another. A secret trust may also arise where a decedent refrains from making a will based upon promises by intestate heirs to, at his death, hold the estate in trust for specific beneficiaries.

Specific Examples

A parent could establish a secret trust in favor of his illegitimate child, about whom his wife knows nothing. In doing so, he might ask the child's mother to serve as the secret trustee. Then he would make a devise to the child's mother, who would hold the property in trust for the child. Similarly, a businessman could create a secret trust in favor of his estranged children by leaving his portion of the business to his business partner, who has promised to hold the property in trust for the children. An infinite number of other variations are certainly possible.

Along other lines, a secret trust would arise where a husband promises a wife that he will hold her family inheritance in trust for their children should she pass away. A secret trust would be formed in this situation under two sets of circumstances: where the wife made a will in favor of her husband, or where she refrained from making a will at all in reliance on his promise. As stated above, an infinite number of variations on this theme exist.

6. What should the result be in each of these actions? Discuss.

1. Action for reimbursement of \$1,500

By accepting the position of trustee of A's trust, T, in effect, steps into "A's shoes" by operation of law. A landlord has the obligation to make repairs resulting from the natural deterioration of commercial premises if (1) he has covenanted to do so, or (2) the repair pertains to the common areas (which ordinarily remain under the landlord's control). The facts are silent as to what part of the premises B sought to have remedied. However, since there is an express clause requiring repair by A, T was obliged to cure the defects.

B might also contend that A's covenant to make repairs ran with the land. The requisites of this doctrine appear to be satisfied, since (1) A and B probably intended that it run (as evidenced by the fact that the promise affects B's use of his land), (2) T is in vertical privity with A, and (3) the promise arguably touches and concerns T's land (i.e., T's is required to keep his property in good repair).

T might possibly assert that B waived this promise by making the repairs himself (rather than commencing a lawsuit). However, since B (1) made demand upon both the executor of A's estate and T, and (2) sued T promptly after making the repairs, this contention should fail.

Thus, B could probably obtain reimbursement from T.

2. *C's lawsuit.*

A trustee is ordinarily liable in tort to third parties to the same extent as an ordinary owner. Since the parking lot was under T's (as A's successor-in-interest) control, C appears to have an action for negligence against T. Since T was aware that the parking lot area had become dangerous, he arguably failed to act reasonably by allowing this condition to continue. T had an obligation toward C (a business invitee) to either warn of the danger or make the area safe.

It is unclear as to whether C had previously visited the premises. If so, T might argue that C had assumed the risk (i.e., voluntarily assumed a known risk) of the cracked pavement. In this event, C might contend that, while she was generally aware of the hazard, (1) her use of the parking lot was not voluntary (i.e., it was difficult to find parking spaces in that vicinity), and (2) she had no knowledge of the particular crack which caused her injuries.

C might also assert an action for battery against T (i.e., that injury to a customer was substantially certain to occur as a consequence of the cracks). T would have to prove that C consented to the harm she incurred to avoid liability if this assertion was successfully made by C. However, while there was a strong possibility that customers might be injured by the hazardous parking lot, the probability of injury to members of this group probably does not satisfy the "substantial certainty" standard.

In summary, unless C was specifically aware that cracks existed in the area of the lot in which she had parked, an action for negligence against T should be successful.

7. **Is T entitled to indemnification from the trust estate for any damages recovered against him individually? Discuss.**

Indemnification.

A trustee is personally liable for breach of contract and tort actions. However, he has a right of indemnification from the trust estate, if he was not personally at fault.

With respect to the contractual claim, T can probably obtain indemnity. Since he succeeded to A's interest in the land, he was (as discussed above under B's action for

reimbursement) probably obliged to make the repairs in question. Where a trustee expends funds to satisfy a contractual obligation of the trust estate, he is entitled to reimbursement from that source. Therefore, since B's judgment merely reflects payment for the accomplishment of an act (repair of the premises) for which T could have been reimbursed, T should be able to obtain indemnity when he satisfies B's judgment. Otherwise, the trust estate would obtain a windfall. However, since T should have recognized the validity of B's action, he probably cannot recover for any attorney's fees incurred in defending against B's suit.

T probably could not, however, obtain indemnity for C's personal injury judgment. A trustee has a duty to take whatever action is necessary to preserve and protect the trust assets. A reasonably prudent businessperson would recognize that potential liability could arise from a severely cracked parking lot, and (1) immediately repair the defective areas, and (2) obtain liability insurance covering any accidents which might occur. Since T failed to do these things, he was probably personally at fault. Therefore he cannot obtain indemnity.

8. Describe a semi-secret trust and give a detailed example.

Definition

A semi-secret trust is similar to a secret trust. A trustor devises property to a devisee who will hold it in trust for other, unnamed beneficiaries. However, unlike in a secret trust, the trustor's will specifically states that the bequest is being given to the devisee for the purpose of establishing a trust. In a majority of jurisdictions, semi-secret trusts are void.

Specific Examples

John asks his friend, Sam, to hold money in trust for John's children upon John's death. Sam promises to do so. John then makes out a will which states, "To Sam, to hold in trust upon my death." Other variations upon this theme abound. Remember, however, that semi-secret trusts are usually void.

9. Describe a Totten trust and give a detailed example.

Definition

A Totten trust arises where a person opens a bank account in his own name and intends to create a trust, but does not intend that the trust take effect until the trustor's death. Totten trusts are created like trusts and do not have to comply with the formalities of a will. However, they are similar to wills in that they are revocable by the depositor at any time, the beneficiary has no account until the depositor dies, the beneficiary must survive the depositor to receive the account, the depositor owes no fiduciary duties to the beneficiary, and the deposit is subject to the claims of the depositor's creditors.

Specific Examples

Mork and Mindy establish a bank account at Planetary Bank. They intend that the bank account will serve as a trust to support their three grandchildren upon the grandparents' death. However, during their lifetimes, Mork and Mindy continue to deposit and withdraw funds from the account for their own use. For another example, consider that Elmo wants to establish a trust in favor of his friend, Big Bird. Elmo opens a bank account at the Sesame Street branch of Wells Fargo Bank in his own name, but tells everyone that he wants Big Bird to have the money if he dies. Endless other examples are possible.

10. Describe a charitable trust and its purposes and give a detailed example.

Definition

A charitable trust is a trust established for a charitable purpose, such as the relief of poverty, the advancement of education, the advancement of religion, the promotion of health, or the performance of governmental and municipal purposes. Other types of charitable purposes that are beneficial to the community may be considered appropriate purposes for a charitable trust, as well. Charitable trusts are perpetual, and the Rule Against Perpetuities therefore does not apply. Furthermore, unlike with a private trust, the beneficiaries of a charitable trust must be indefinite.

Specific examples

There are many examples of charitable trusts. A benefactor could establish a trust for a scholarship to Harvard University or to his alma mater. A woman could establish a charitable trust to contribute money to cancer research. A man could establish a charitable trust to help famine victims in Ethiopia. As many charities and causes as exist, there are an equal number of types and reasons for charitable trusts.

11. Who is entitled to the assets and why? Discuss.

The Insurance Policy

The proceeds of an insurance policy are not deemed to be part of the insured's estate, so June would have no interest in this asset.

Joe ("J") might contend that no trust was created by the letter to him; and therefore he is entitled to all of the proceeds from the policy. Joe could contend that (1) Bill ("B") had no immediate trust intent as evidenced by the fact that at the time of the initial letter, 2/3's of the beneficiaries were neither named nor ascertainable, and (2) there was no delivery of the trust *res* (the insurance proceeds) to J at that time. J could also contend that even if the trust were created by the letter to him from B, the policy proceeds became his sole property, since a merger occurs when trustee and the sole beneficiary are the same party (which was the case until B attempted to name two additional beneficiaries later).

However, Tom Allen and his wife (the "Other Beneficiaries") could argue in rebuttal that while B is probably correct in asserting that no trust arose by reason of the initial letter to B, all of the elements of a trust relationship were concurrently satisfied when B wrote out the piece of paper the day before his death. At that time, (1) the requisite intent to create a trust was renewed by reason of the piece of paper containing the names of the "Other Beneficiaries," since that memo was obviously written with reference to the earlier letter to J, (2) all of the beneficiaries were known (and it is only necessary that the beneficiaries be ascertainable at the time their enjoyment is to vest), and (3) there was a sufficient constructive delivery of the trust *res* to J (as trustee) by naming him as the beneficiary of the policy since this is all that could be done, i.e., the insurance company was not legally obliged to deliver the proceeds to the designated beneficiary prior to the time of B's death). Additionally, no merger could have occurred since (1) no trust probably arose by reason of B's initial note to J for the reasons described above, and (2) even assuming such a trust had arisen, there was not a complete merger of legal and equitable interests because while the identities of the "Other Beneficiaries" were unknown, their prospective existence was communicated to J.

Finally, it should be mentioned that even if no valid trust were found to exist, the "Other Beneficiaries" could probably successfully seek the imposition of a constructive trust upon 2/3's of the insurance proceeds. Under this doctrine, one is under an equitable duty to convey property to another where the former would be unjustly enriched at the latter's expense by the retention of such property. Because J had advised B that he would do whatever the latter requested (upon which statement B presumably relied), J would be unjustly enriched if he were permitted to retain more than 1/3 of the insurance proceeds.

Blackacre (the "Farm")

If a valid trust were not created in favor of Pete ("P") as trustee, as well as June and the church as beneficiaries, the Farm would still be a part of B's estate; and therefore passed to June under B's will. However, if a valid trust were created, the Farm would not have been a part of P's estate.

We'll assume that B's church is capable of identification (i.e., the entity with which he was affiliated could be shown by extrinsic evidence).

June could conceivably contend that no valid trust arose because (1) there was no conveyance of Blackacre to P in accordance with real property law, since P did not physically receive the deed prior to his departure, (2) there was no delivery of the trust *res* to P, since he had embarked on a trip prior to the time the deed arrived, (3) P never explicitly agreed to act as trustee (in fact, leaving on an extended trip despite receipt of the letter indicates his refusal to serve as trustee), and (4) P never signed a writing indicating his acceptance of the Farm, and therefore the Statute of Frauds (applicable to transfers of real property) is not satisfied.

However, P (who presumably would like to observe the trust) and the church could probably successfully contend in rebuttal that (1) for a conveyance of real property to occur there need only be completion of a valid deed with the intent that it be

immediately operative (the deed does not have to be manually delivered to the grantee), and these requisites appear to be satisfied in light of B's letter and physical delivery of the deed to the housekeeper (acceptance of the deed by the grantee is ordinarily presumed, unless he/she immediately objects to the conveyance when informed of it - which P did not do), (2) although there was no physical delivery of the trust *res* to P, there was constructive delivery of the deed to P's housekeeper, (3) it is not necessary that the trustee specifically acknowledge acceptance of his/her capacity as trustee (as B's old friend, P presumably would have objected immediately to the appointment of trustee if he did not desire to act in that capacity), and (4) only parties to the alleged trust can assert the Statute of Frauds, and so June cannot complain about the lack of a writing signed by the trustee if P is willing to observe a trust relationship. Thus, the Farm was not part of B's estate.

Did the reference to Aunt Selma ("AS") create a testamentary trust?

AS might contend that the language in B's will created a trust, whereby June was to support her for life from B's estate (with the remainder then going to June). However, June could probably successfully argue in rebuttal that B's language was merely precatory in nature (it was a mere request, rather than a clear directive, as evidenced by utilization of the word "I recommend"). While AS' argument would be strengthened if B had supported her during his lifetime, the language in the will is still probably too weak to constitute a finding that a trust was intended. Additionally, "such gifts and provisions" as June thinks "best" is probably too vague of a standard to attempt to apply against a trustee's actions. Thus, no testamentary trust arose by reason of B's will, and June is not obliged to provide any type of support to AS.

12. Describe a support trust and give a detailed example.

Definition

A support trust is one which contains a provision allowing the trustee to distribute trust assets only for education, maintenance and support of the beneficiary. Such a provision limits the beneficiary's interest to amounts necessary for her support. If more trust property exists than that necessary for the beneficiary's support, it is distributed as otherwise provided for in the trust instrument. Note that a beneficiary cannot transfer her interest in a support trust and creditors cannot ordinarily attach a beneficiary's interest in a support trust.

Specific Examples

A parent could establish a support trust to pay for a child's college education. A grandparent could establish a support trust to help support a child who needs special health care. A friend could establish a support trust to help a friend who has lost her home due to fire. Of course, there are endless other possibilities.

13. Describe a discretionary trust and give a detailed example.

Definition

A discretionary trust is one that contains a provision allowing the trustee to distribute assets for any purpose within the trustee's discretion. Should the trustee so desire, he may distribute all of the assets of the trust; should he also deem it proper, he could refrain from distributing anything under the trust. The key factor in a discretionary trust is that the trustee has all of the control. Note that, while creditors may attach a beneficiary's interest in a discretionary trust, the interest has no marketable value until the trustee determines when a contribution to the beneficiary should be made. Furthermore, a beneficiary may assign his interest in the trust but, similarly, this assignment has no value until a disbursement is actually made by the trustee.

Specific Examples

A parent could establish a trust "for whatever the trustee deems my child needs or wants." A friend could establish a trust to be distributed "as the trustee sees fit." A philanthropist could establish a trust "for whatever charitable causes are in need of the money." In all of these cases, the trustee would have the discretion to decide when distribution was appropriate, if at all.

14. Describe a spendthrift trust and give a detailed example.

Definition

A spendthrift trust is one that contains a provision that precludes the beneficiary from voluntarily transferring his interest in the trust and creditors from reaching that interest. It is important to note that a trust need not have specific language stating the trustor's intent to create a spendthrift trust. However, the existence of a spendthrift trust may be determined from all of the circumstances. Because a spendthrift provision generally prevents alienation by the beneficiary and attachment by creditors, creditors cannot ordinarily reach the beneficiary's interest.

Specific Examples

A parent could establish a trust stating that "the trust is to be used for the benefit of my child only, and my child's interest is non-transferrable." A benefactor could establish a trust "in favor of the drama department at Dartmouth College, and no other college or department may benefit." Finally, a parent whose child died of leukemia could establish a trust "for the Center for Leukemia research, who took such good care of Danny before he died." In the final example, the existence of a spendthrift trust would be inferred from the circumstances, as it is clear that the parent wants only to benefit a particular entity.

15. What are the rights and liabilities of John, Agatha, and Larry? Discuss.

Beneficiaries of Trust E2 ("Beneficiaries") v. Agatha ("A") and Larry ("L")

A trustee owes a duty of loyalty to beneficiaries of his trust; which duty precludes making any personal profit from trust transactions. Where this duty is breached, the beneficiaries can recover the value of the gain derived by the trustee, or, when possible, rescind the transaction and recover back the original trust property. There appears to be little doubt that A breached her duty of loyalty by, in effect, utilizing trust property to satisfy her personal obligation, and is therefore liable to the Beneficiaries for at least the stock's reasonable value (\$10,000) at the time of the transfer. In most states, however, the Beneficiaries would probably be entitled to recover the value of the stock at the time of the trial. Therefore, if T stock increases in value, the Beneficiaries could probably recover its enhanced worth.

If the Beneficiaries believed that the stock would continue to increase in value after trial, they might seek to recover the shares directly from L. Under the constructive trust doctrine, when the retention of identifiable property would result in unjust enrichment (i.e., the holder of the item is not a bona fide purchaser), the court may deem the item to be held in trust for the benefit of the party from whom such property has been wrongfully obtained. The Beneficiaries might contend that since L received the stock as a gift, the constructive trust doctrine should be applied to cause him to return the stock to them. L might contend in rebuttal that he received the stock from a bona fide purchaser (John released A from her obligation to him), and therefore he should stand in John's shoes. However, the Beneficiaries could probably successfully argue in rebuttal that (1) J really was not acting in good faith, since he should have realized that A had no right to transfer trust assets for an amount below their value for the purpose of satisfying a personal obligation, and (2) if L were to return the stock to the trust, J would probably be entitled to recover the original \$10,000 back from A, since there would have been a material failure of consideration to J in that he relieved A of a \$10,000 obligation and, in effect, received nothing in return.

Assuming the stock was recovered back by the Beneficiaries, could J invade Trust E1 for the purpose of satisfying A's obligation to him (or, if the Beneficiaries obtained a judgment against A, could they invade Trust E1)?

A spendthrift trust is one that prohibits (1) a beneficiary from voluntarily alienating his/her interest in the trust *res*, and (2) creditors from reaching the interest of the beneficiaries for the purpose of satisfying claims against such person. Where only the latter provision exists, most courts hold that no spendthrift trust exists (i.e., that the beneficiary's interests can be reached by creditors). The facts indicate only that the trusts in the will "contained a spendthrift provision stating that creditors could not reach income in the trustee's hands." Thus, there does not appear to have been any provision specifically stating that the beneficiaries could not alienate their interests. In states which make such a clause a requisite to the enforceability of spendthrift provisions, the absence of such a clause would permit A's creditors to invade the trust (at least up to the extent of her income interest).

Even if the spendthrift clause were valid, in virtually all states, where a beneficiary has furnished (directly or indirectly) the trust *res* (as A did in this instance by releasing her \$300,000 claim against George's estate), a spendthrift clause will not prevent persons who were creditors of the such beneficiary at the time of the creation of the trust to reach the latter's interest in the trust. A, in effect, did this by agreeing to release George's estate from the \$300,000 obligation which George owed to her. Thus, J (who was a creditor of A when the trust in her favor was created) should be able to invade the trust to the extent of A's life interest therein.

16. During his lifetime, Ted establishes a trust to provide for the education of his children. What type of trust is being established? What are the characteristics of this type of trust?

Type of Trust

Ted's trust would be a *inter vivos* trust and possibly a support trust if he intends and specifically states that the trust is to be used for the support, maintenance and education of his children.

Characteristics

An *inter vivos* trust is one created during the trustor's lifetime. For an *inter vivos* trust, a trustor must declare that legal title to the subject property is now held by a trustee for the beneficiary. Furthermore, a trustor must, in the case of real property, execute a deed conveying title to the trustee and deliver that document to the trustee or his agent. Where the trustor has personal property, transfer may be made by physical delivery, symbolic delivery or constructive delivery.

17. In his will, Joe establishes a trust for his daughter, Margo, and any other surviving children. What type of trust is being established? What are the characteristics of this type of trust?

Type of Trust

Joe's trust will be a testamentary trust. If the trustee is given absolute discretion over the trust, this may also be a discretionary trust. Furthermore, if Joe's trust contains a provision providing that the trust is to be used only for his children's education, maintenance and support, it will be classified as a support trust.

Characteristics

A testamentary trust is created by a testator's will. Its essential terms are described in, or incorporated by reference into, a valid will. Such a trust speaks as of the testator's death and takes effect at that time. Various kinds of trusts may be created in the will of a trustor.

- 18. Courtney devises her bank account at Wells Fargo Bank to her sister, Susan. Although it is not so stated in Courtney's will, Susan has promised to use this money for the benefit of Courtney's niece and nephew, Susan's children, Andrea and Charles. What type of trust is being established? What are the characteristics of this type of trust?**

Type of Trust

If Courtney's will does not make reference to Susan's promise, this will be a secret trust.

Characteristics

A secret trust arises where property is devised to another without reference in the will to the fact that the devisee promised the trustor-decedent or agreed to hold the property received under the will in trust for another. A secret trust may also arise where a decedent refrains from making a will based upon promises by intestate heirs to, at his death, hold the estate in trust for specific beneficiaries.

- 19. A client comes to you and asks you to draft a trust for her. What kinds of questions would you want to ask her to insure that her trust adequately serves her needs?**

Names and contact information for her beneficiaries

You will want to include contact information for the people she names as beneficiaries. This information will be useful to the trustee upon your client's death.

Name and contact information for the trustee she appoints

You will want to obtain the name and contact information of the person she wishes to have serve as the trustee. This person will be responsible for making sure your client's wishes are carried out.

Identification and location of the trust res

What does your client wish to place in the trust? Where is it currently located? You will need to know this information in order to properly draft her trust.

Time frame for drafting the trust

Your client may have a reason, such as a terminal illness, for wanting the will to be executed within a short time frame. You should keep this in mind as you schedule your obligations to her and to your other clients.

Intent behind trust clauses

You will need to know whether the client intends to benefit a charity, whether she intends for the trust to be only for maintenance and support, and so on. Her intent will dictate the clauses you include.

When the trust should terminate

You will need to know under what circumstances your client wishes for the trust to terminate. Will it be perpetual (charitable trust)? Will it end e.g., when her children graduate from college? You will want to be clear in the trust about the circumstances under which it should terminate.

What duties she intends for the trustee to carry out

You will want to know what duties the trustor wishes to delegate to the trustee, as well as what powers she wishes to grant him.

When the trust should take effect

Will this trust take effect immediately or upon the trustor's death? This information will help you determine whether you need to draft a will, as well, in order to form a testamentary trust.

Is there an alternate trustee she would like to name?

Be sure to advise your client that she may want to appoint an alternate trustee, so that if her first choice cannot serve, the trust will remain in effect with a trustee she has designated.

20. Your client has answered your questions. What clauses should you be sure to include in her trust?

Trustee

You will want to include a clause that names and identifies the person your client has chosen as the trustee of her trust. In addition, you will want to list the trustee's duties, his rights, and any compensation due the trustee. Finally, you will probably want to include a provision for an alternate trustee if the one your client has designated cannot or will not serve.

Beneficiaries

You will want to include a clause that identifies the beneficiaries clearly, or, if it is a charitable trust, identifies the class of beneficiaries. You should include contact information for these individuals.

Trust res

You will need to identify the trust *res* as specifically as possible, then specify its current location. This information will aid the trustee in carrying out the trust.

Type of trust

If your client intends that this will be a spendthrift or support trust, you will need to include clauses so specifying. You will want to make the purposes of the trust very clear.

Termination clause

You will want to specify when and under what circumstances the trust should terminate.

- 21. Courtney devises all of the money in her bank account at Wells Fargo Bank to her sister, Susan, "in trust". What type of trust is being established? What are the characteristics of this type of trust?**

Type of Trust

Courtney's trust would be a semi-secret trust.

Characteristics

In a majority of jurisdictions, semi-secret trusts are void. A semi-secret trust is similar to a secret trust. A trustor devises property to a devisee who will hold it in trust for other, unnamed beneficiaries. However, unlike in a secret trust, the trustor's will specifically states that the bequest is being given to the devisee for the purpose of establishing a trust. In a majority of jurisdictions, semi-secret trusts are void.

- 22. Jonathan creates a trust for the benefit of his daughter, Miranda, and includes a provision which states that Miranda may not transfer her interest in the trust and that creditors may attach her interest in the trust. What type of trust is being established? What are the characteristics of this type of trust?**

Type of Trust

Jonathan's trust would be a spendthrift trust. Note that Jonathan would not have had to use the specific language he used in order to establish a spendthrift trust. Indeed, whether the trustor intended to create a spendthrift trust is generally a factual issue, determined from all of the circumstances.

Characteristics

A spendthrift trust is one that contains a provision that precludes the beneficiary from voluntarily transferring his interest in the trust and creditors from reaching that interest. It is important to note that a trust need not have specific language stating the trustor's intent to create a spendthrift trust. However, the existence of a spendthrift trust may be determined from all of the circumstances. Because a spendthrift provision generally prevents alienation by the beneficiary and attachment by creditors, creditors cannot ordinarily reach the beneficiary's interest.

23. What advice would you give to your new client about revisions?

I, Willy Wonka, give the value of 25,000 chocolate bricks to my friend, the Wicked Witch. I hope that the Wicked Witch will use the trust to benefit chocolate lovers everywhere. Furthermore, I promise my friend, Stuart Little, that I will create a similar trust in his favor at some point in the future, but no later than the year 2002. I intend that that trust will be in effect for all perpetuity.

Precatory language

In granting the value of the chocolate bricks to the Wicked Witch, Willy Wonka has only used precatory language. In other words, he has not used language of intent. Unless he has a history of supporting chocolate lovers everywhere, this language will probably be considered to be insufficient to demonstrate intent, and the trust will probably fail. You should suggest that he change the language so that his intent is clear.

Indefinite beneficiaries

"Chocolate lovers everywhere" is not sufficiently definite to satisfy the requirements of a trust. In order to establish a trust, the beneficiaries must be able to be identified with particularity (unless it is a charitable trust, which this is not, as it does not promote a charitable cause). It will be very difficult to identify these beneficiaries. What constitutes a chocolate lover? How will the Wicked Witch go about finding chocolate lovers everywhere? For the trust to be valid, the beneficiaries must be limited severely.

Intent to create a trust in the future

We see no evidence whatsoever that Stuart Little has given Willy Wonka any consideration for Wonka's promise to create a trust in Little's favor. If such consideration exists, it should be spelled out. If it does not, the promise to create the trust will be considered gratuitous, and the trust will probably fail.

All perpetuity

A non-charitable trust may not extend for all perpetuity, as this would violate the Rule Against Perpetuities. Your client will need to limit the time frame for the trust.

Conclusion

The former attorney has done a pretty incompetent job of drafting the trust, and you may have yourself a new client!

- 24. Cynthia creates a trust for “the promotion of health and the elimination of AIDS in sub-Saharan Africa”. What type of trust is being established? What are the characteristics of this type of trust?**

Type of Trust

Cynthia has created a charitable trust. The beneficiaries are indefinite, the trust has a charitable purpose, and this charitable trust may have a perpetual existence (even if AIDS is cured, the proceeds may be used in a more general way under the cy pres doctrine).

Characteristics

A charitable trust is a trust established for a charitable purpose, such as the relief of poverty, the advancement of education, the advancement of religion, the promotion of health, or the performance of governmental and municipal purposes. Other types of charitable purposes that are beneficial to the community may be considered appropriate purposes for a charitable trust, as well. Charitable trusts are perpetual and therefore the rule against perpetuities does not apply. Furthermore, unlike with a private trust, the beneficiaries of a charitable trust must be indefinite.

- 25. Andrea creates a trust “for all of the people who like Alfred Hitchcock movies”. The assets of the trust are to be used to provide money for weekly screenings of Alfred Hitchcock movies. What type of trust is being established? What are the characteristics of this type of trust?**

Type of Trust

Unless Andrea can somehow convince a court that the screening of Alfred Hitchcock films qualifies as the promotion or advancement of education or some other charitable purpose, this trust will probably fail. The beneficiaries are too indefinite, as it will be difficult to identify all of the fans of Alfred Hitchcock movies. The class of beneficiaries would have to be considerably limited in order to make this a valid private trust.