

Resolving Trust Administration Issues Outside of Court

A look at nonjudicial settlement agreements under the New Jersey Uniform Trust Code

By Christopher P. Massaro, Jenny R. Flom and Michael J. Kearney | April 30, 2018 at 11:27 AM



The New Jersey Uniform Trust Code (UTC or “the Act”) was enacted on Jan. 19, 2016, and became effective on July 17, 2016. The UTC provides a sweeping set of directives regarding the administration of trusts in this state and is largely based on model legislation prepared by the Uniform Law Commission in 2000. Not only do the provisions of the UTC control newly created trusts, but they also generally apply retroactively to trusts created before its effective date. N.J.S.A. 3B:31-84(a)(1).

Despite passage of such comprehensive legislation, the UTC does not repeal existing New Jersey case law governing trusts. Rather, the UTC confirms that accepted principles of common law and equity continue to apply unless specifically modified by the Act or another New Jersey statute. N.J.S.A.

3B:31-6. While the UTC contains many useful provisions, the ability for parties to enter into nonjudicial settlement agreements is one of the most significant.

‘Interested Persons’ May Enter into Nonjudicial Settlement Agreements

Before the UTC, parties were often forced to commence costly and time-consuming litigation proceedings to address trust administration issues, even in situations where all of the parties were in agreement as to the appropriate outcome. For example, if a testamentary trustee died and no successor was named in the instrument governing the trust, the parties were required to commence proceedings in the Superior Court seeking the appointment of a new trustee. The UTC now provides an avenue for all interested persons to appoint a new trustee by way of an out-of-court agreement. Under the Act, “interested persons” includes those parties “whose consent would be required in order to achieve a binding settlement were the settlement to be approved by the court.” N.J.S.A. 3B:31-11(a). As a practical matter, creating enforceable nonjudicial settlement agreements requires the consent of all trustees and trust beneficiaries, either directly or through authorized representatives.

Material Purpose of the Trust

The UTC imposes limits on the permissible scope of nonjudicial settlement agreements. Interested persons are not simply allowed to disregard the material purpose of a trust or enter into an agreement that a court would not have the authority to approve. N.J.S.A. 3B:31-11(c). Nevertheless, so long as a nonjudicial settlement agreement does not violate a material purpose of the trust and the terms of the agreement could be properly approved by the court, interested persons may enter into an agreement with respect to virtually any matter involving a trust. N.J.S.A. 3B:31-11(b). By way of example, the Act includes the following non-exclusive list of matters that may be resolved using a nonjudicial settlement agreement (N.J.S.A. 3B:31-11(d).):

- the interpretation or construction of the terms of the trust;

- the approval of a trustee's report or accounting;
- direction to a trustee to refrain from performing a particular act or the grant to a trustee of any necessary or desirable power;
- the resignation or appointment of a trustee and the determination of a trustee's compensation;
- the transfer of a trust's principal place of administration; and
- liability of a trustee for an action relating to the trust.

While not specifically mentioned, additional issues that could potentially be addressed by a nonjudicial settlement agreement include:

- the appointment of a trust protector with the ability to remove and replace trustees;
- the correction of a scrivener's error;
- the addition of certain provisions to incorporate tax planning;
- the addition of provisions to address a beneficiary with special needs to better ensure that any assets passing to such beneficiary would not cause the loss of means-based government assistance; and
- trust modifications that are consistent with the material purpose of the trust.

Determining whether a proposed agreement contravenes a "material purpose" requires a consideration of the trust's governing instrument as a whole and any other available information reflecting the intent of the trust's creator (a/k/a the settlor or grantor). If the settlor is alive, he or she may be able to provide clarity with respect to issues of intent, and even bolster the validity of the nonjudicial settlement agreement by certifying that it is consistent with the trust's purposes. If the grantor is deceased, however, ascertaining intent may prove to be difficult depending on the situation. Accordingly, estate planning practitioners should carefully document the settlor's intent either in the trust document itself or in a memorandum to the file (or both). Also, a practitioner could request the settlor to express his or her intent in separate correspondence that could be kept with the trust document for future reference. Not only will taking these additional steps make disputes over intent less likely, they will also offer a solid foundation for analyzing whether a proposed settlement agreement is appropriate.

A few concrete examples illustrate the point. Settlers often include provisions in trusts that instruct trustees to refrain from providing distributions to beneficiaries who are gambling or abusing drugs or alcohol. Any agreement with a trustee that would circumvent that provision and allow the beneficiary to have unfettered access to distributions would certainly violate a material purpose of the trust. In contrast, an agreement between that same trustee and beneficiary merely approving an accounting of the trustee's expenditures for a given period would be acceptable. Additionally, since anticipated tax savings is often a trust's predominant purpose, it is important to remember that certain trust modifications could produce unintended tax consequences. While the proposed modification itself may appear innocuous and consistent with the settlor's intent on its face, it could nevertheless work substantial damage to a settlor's tax plan. For instance, a modification allowing distributions from a trust to a grandchild might trigger an unexpected generation-skipping transfer tax.

Ability to Seek Court Approval

Although nonjudicial settlement agreements can eliminate the cost and delay associated with seeking court approval, the UTC regards their use as an optional alternative to judicial proceedings. Interested persons still possess the right to have any proposed agreement reviewed and approved by the court. More specifically, the Act allows any interested person to request the court to approve the agreement, to determine the adequacy of representation (an issue discussed below), and to determine whether the agreement contains lawful and appropriate terms. N.J.S.A. 3B:31-11(e). If court approval is desired, it is necessary to file an order to show cause and verified complaint with the New Jersey Superior Court setting forth the reasons why the proposed agreement should be approved and provide notice to all interested persons. The court will then evaluate the matter and enter a final judgment either granting or denying the request.

Representation

Individuals who lack the ability to consent because they are minors or incapacitated, or potential beneficiaries who are not yet born, can still be bound to a nonjudicial settlement agreement using the doctrine of virtual representation. Using that doctrine, so long as there is no apparent conflict of interest, the Act authorizes guardians, agents, trustees, personal representatives and parents to act as representatives for their respective wards, principals, beneficiaries and minor or unborn children. N.J.S.A. 3B:31-15. A minor, incapacitated or unborn person may also be represented and bound by another having a substantially identical interest with respect to the matter. N.J.S.A. 3B:31-16. These provisions are helpful in that they eliminate the need for the court to appoint a guardian ad litem or attorney to review the proposed agreement on behalf of those beneficiaries who lack the ability to consent.

Nevertheless, the UTC recognizes that situations may arise when there is no qualified representative available, and the Act empowers the court to take action under those circumstances. If the court determines that an interest is not represented or that available representation might not be adequate, the court may appoint a guardian ad litem or other representative for a minor, incapacitated person or unborn individual. N.J.S.A. 3B:31-17. The critical factor to remember is that all interested parties must consent, either directly or through an appropriate representative, or they will not be bound to any agreement reached.

Conclusion

Nonjudicial settlement agreements can be an effective tool for avoiding the expense and delays associated with court proceedings, so long as the desired objectives are aligned with the material purposes of the trust, and the terms of the agreement could have been properly approved by the court. They are

especially useful for addressing routine, noncontroversial trust administration issues. When a proposed agreement involves more complex issues or the settlor's intent is ambiguous, the parties and counsel have the option of exercising their own judgment as to the appropriateness of the agreement (which may remain subject to challenge in the future) or seeking court approval to achieve immediate certainty as to its validity.

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