The Florida Senate

PROFESSIONAL STAFF ANALYSIS AND ECONOMIC IMPACT STATEMENT

(This document is based on the provisions contained in the legislation as of the latest date listed below.)

Prepared By: Banking and Insurance Committee

BILL: CS/SB 2218

INTRODUCER: Banking and Insurance Committee and Senator Posey

SUBJECT: Trustees Duties/Powers/Liabilities

DATE: April 16, 2007 REVISED:

	ANALYST	STAFF DIRECTOR	REFERENCE	ACTION
1.	Knudson	Deffenbaugh	BI	**Fav/CS**
2.			JU	
3.				
4.				
5.				
6.				

I. Summary:

The bill amends various sections of the Florida Trust Code to:

- Expand the power of a bank or trust company that is acting as a trustee to invest in investment instruments that the bank or trust company owns or controls.
- Limit the power of a trustee to distribute the principal of a trust when the trustee has absolute power under the trust's terms to invade the principal of the trust.
- State that exculpatory terms caused to be drafted by a trustee are invalid unless the trustee proves that the exculpatory term is fair under the circumstances, and (if the trust is created after July 1, 2007) if the term's existence and contents were adequately communicated to the settlor or the independent attorney of the settlor.

This bill substantially amends the following sections of the Florida Statutes: 660.417, 736.0802, 736.0816, 736.1008, and 736.1011.
The bill creates the following section of the Florida Statutes: 736.04117

II. Present Situation:

The Florida Trust Code

The Florida Trust Code contains Florida laws regarding the creation, administration, interpretation, and termination of trusts. The code provides the default rules for trust administration which can be limited or altered by the trust's creator. The 2006 Legislature in chapter 2006-217, L.O.F. (CS/SB 1170) adopted a comprehensive New Florida Trust Code that will be effective on July 1, 2007. The new Trust Code is primarily based on the National Conference of Commissioners on Uniform State Laws Uniform Trust Code of 2000, with revisions made to account for distinctions contained in Florida statutory and case law.

A trust is generally defined as:

> a fiduciary relationship with respect to property, subjecting the person by whom the title to the property is held to equitable duties to deal with the property for the benefit of another person, which arises as a result of a manifestation of an intention to create it. . . . [A] "beneficiary of a trust" [is] one who has an equitable interest in property subject to a trust and who enjoys the benefit of the administration of the trust by a trustee. The trustee is the person who holds the legal title to the property held in trust, for the benefit of the beneficiary. The settlor, or trustor, is the person who creates the trust.[1]

A settlor of a trust is a person who creates or contributes property to a trust. A trustee is a person who holds property in a trust and administers it for the benefit or use of another. A beneficiary of the trust is a person who has a present or future beneficial interest in the trust, whether it is vested or contingent; or who holds a power of appointment (ability to select who will benefit from trust property) other than that of a trustee.

Trustee's Duty of Loyalty

The Florida Trust Code requires a trustee to "administer the trust in good faith, in accordance with its terms and purposes and the interests of the beneficiaries," and in accordance with the Florida Trust Code. There is a duty of loyalty placed upon a trustee in s. 736.0802, F.S., to administer the trust solely in the interests of the beneficiaries. The requirements regarding the trustee's duty of loyalty specify various instances where a conflict of interest is presumed to exist. Generally, any sale, encumbrance or other transaction involving trust property that is entered into by the trustee for the trustee's own personal account, or where the trustee has a conflict of interest between its fiduciary interests and personal interests is voidable by a beneficiary that is affected by the transaction. However, there are 6 exceptions if:

- The transaction was authorized by the trust terms;
- The transaction was court-approved;
- The beneficiary did not commence a judicial proceeding within the time allowed by s. 736.1008, F.S.;
- The beneficiary consented, ratified, or released the transaction per s. 736.1012, F.S.;
- The transaction involves a contract or claim entered into by the trustee before the trustee had contemplated becoming trustee; or
- The settlor consented in writing to the transaction while the trust was revocable.

Subsection (5) of s. 736.0802, F.S., contains requirements regarding investments by a trustee for an irrevocable trust in investment instruments that are owned or controlled by the trustee or its affiliate, or from which the trustee receives compensation other than for acting in the capacity of a trustee. Generally, a conflict of interest is not presumed to exist if the trustee complies with disclosure requirements and the investment instrument complies with the requirements of chapter 518, F.S. (investment of fiduciary funds) and chapter 660, F.S. (regulation of banks or associations conducting trust business). Disclosures must be made to beneficiaries regarding the potential conflict of interest itself, and the amount of compensation the trustee receives from investment instruments in which the trustee invests trust funds. Disclosure must be made at least annually by the trustee unless the trustee's method or rate of compensation has not changed since

[1] 55A Fla. Jur. 2d Trusts s.1.

the prior disclosure. The aforementioned requirements of subsection (5) apply to investment instruments other than qualified investment instruments that expressly authorize the trustee by specific reference to s. 736.0802, F.S., to invest in investment instruments owned or controlled by the trustee or its affiliate. If there is not specific authorization in the trust instrument, then beneficiaries are given additional time to object before the investment can be made. However, only if two-thirds of the beneficiaries object is the objection considered to have been made.

Breach of Trust

The violation by a trustee of a duty owed to a beneficiary is a breach of trust.[2] When a breach of trust occurs, a court may remedy the breach in a number of ways, including compelling the trustee to perform the trustee's duties, compelling the trustee to pay money or restore property, suspending or removing the trustee, and other specified measures.[3] The trustee's liability for a breach of trust is the greater of the amount required to restore the value of the trust property (including lost income, capital gain or appreciation) that would have occurred from proper trust administration, or the profit made by the trustee from the breach.[4]

Section 736.1011, F.S., states that a term of a trust relieving a trustee of liability for breach of trust is unenforceable to the extent that it:

- Relieves the trustee of liability for breach of trust committed in bad faith or with reckless indifference to the trust's purposes or beneficiaries' interests; or
- Was inserted into the trust instrument due to an abuse by the trustee of a fiduciary or confidential relationship with the settlor.

In order for an exculpatory term that relieves a trustee of liability for breach to be valid, the trustee must prove that the term is fair under the circumstances and that it was adequately communicated directly to the settlor of the trust.

Section 736.1008, F.S., specifies that the statutes of limitations provided in chapter 95, F.S., apply to breach of trust claims for all matters adequately disclosed in a trust disclosure document, with the limitations period beginning once adequate disclosure has been received. Such limitations also apply to a matter where the trustee has issued a final trust accounting and provided written notice to the beneficiary that trust records are available to be examined and that claims may be barred unless the action is commenced timely, with the limitations period beginning upon receipt of the final trust accounting and notice. However, a beneficiary must bring an action for breach of trust within 6 months of receiving notice pursuant to a trust disclosure document (a written report of the trustee that discloses a matter and provides notice of the existence of a claim) unless the action is barred even sooner by adjudication, consent, or limitations.

[2] Section 736.1001(1), F.S.
[3] Section 736.1001(2), F.S.
[4] Section 736.1002, F.S.

Power to Direct a Trust
Section 736.0808, F.S., states that a trustee may follow a direction of the settlor that is contrary to the terms of the trust while the trust is revocable. The settlor may also give fiduciary powers to a third party other than the trustee, but regardless of such an act, the trustee cannot obey the direction of the third party if the attempted exercise is manifestly contrary to the terms of the trust or would constitute a serious breach of fiduciary duty on the part of the third party. Trustees have an affirmative duty to exercise reasonable care to prevent a co-trustee from committing a breach of trust.[5] The terms of the trust may also confer power on a trustee or third party to direct the modification or termination of the trust.

The power to direct also places requirements and potential liability on its holder. Any person, other than a beneficiary, that has a power to direct is presumed to be a fiduciary and must act in good faith and in the interests of the beneficiary. The holder of a power to direct is liable for any loss that results from a breach of a fiduciary duty.

Trust Business
Chapter 660, F.S., permits a state bank or association to establish a trust department for the purpose of conducting trust business, if the Office of Financial Regulation (OFR) determines that the bank or association has the requisite management ability, will provide quality supervision to fiduciary activities, can financially support handling such business, and other relevant matters.[6] A trust company or department has the power to act in every fiduciary capacity with regard to its fiduciary accounts and has all the rights, privileges, and immunities as well as the duties and obligations that apply to any fiduciary capacity it undertakes.[7] However, effective July 1, 2007, a bank or trust company or its affiliates that own or control investment instruments may only invest or reinvest such instruments when acting in its fiduciary capacity if the investment instrument:

- Is held for sale by the bank, trust company, or an affiliate in the ordinary course of its business of providing investment services to customers and does not include interests held for an investment rather than for sale to its customers.
- Is sold primarily to accounts for which the bank or trust company is not a fiduciary at terms that are not more favorable than at which the instrument is sold to an account for which it is acting as a fiduciary.[8]

III. Effect of Proposed Changes:

Section 1. Amends s. 660.417, F.S., as amended by s. 18 of ch. 2006-217, L.O.F., regarding the investment of investment instruments that are owned or controlled by a bank or trust company that is also acting as a fiduciary. The bill amends paragraph (3)(b) to permit a trust company or bank that is acting as a trustee of a trust to invest in an investment instrument it owns or controls if the investment instrument is:

- Available for sale to accounts of other customers (rather than “primarily” sold to other customers; and

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[5] Section 736.0703, F.S.
[6] Section 660.26, F.S.
[7] Section 660.34, F.S.
[8] Section 660.417, F.S., as amended by chapter 2006-217, L.O.F.

- Not sold to the trust account upon less favorable terms than the terms upon which they are "normally" sold to other customers.

Section 2. Creates s. 736.04117, F.S., to create limitations on the power of a trustee to distribute the principal of a trust when the trustee has absolute power under the trust's terms to invade the principal of the trust. Subsection (1) states that a trustee with absolute power to invade principal may take all or part of the principal of a trust (first trust) and place the property in a second trust if:

- The beneficiaries of the second trust include only beneficiaries of the first trust.
- The second trust does not reduce any fixed income, annuity, or unitrust interest in the assets of the first trust.
- If the first trust qualified for a marital or charitable federal income tax deduction, the second trust may not contain any provision that would have prevented the first trust from qualifying for the deduction or that would have reduced the deduction.

The bill also specifies that an absolute power to invade principal is not limited to specific purposes. A power to invade principle for purposes such as best interests, welfare, comfort, or happiness is an absolute power. When principle is invaded under this power, it must be done in writing, signed and acknowledged by the trustee, and filed with the records of the first trust. The exercise of this power may not be used to appoint in favor of the trustee or the trustee's creditors and cannot be used in a manner that would postpone the vesting of the trust estate beyond the rule against perpetuities. Sixty days advance notice must be given to all qualified beneficiaries of the first trust prior to the exercise of the power to invade principal. The exercise of the power to invade principle is not prohibited by a spendthrift clause or prohibition against amending or revoking the trust. The trustee has no duty to invade principal, nor does the section abridge the right of a trustee who has power of invasion to appoint property in further trust as specified under the terms of the first trust or under other laws.

Section 3. Amends s. 736.0802, F.S., regarding the duty of loyalty that a trustee owes to beneficiaries. Subsection (2) contains exceptions to the requirement that a transaction is voidable by a beneficiary if it involves an instrument of trust property affected by a conflict of the trustee's fiduciary and personal interests. The bill adds an additional exception for a transaction made by a corporate trustee that involves a money market fund, mutual fund, or common trust fund described in s. 736.0816(3), F.S.

Subsection (5) is amended to clarify that the affiliated investment rules contained in the Florida Trust Code:

- Do not apply to qualified investment instruments.
- Apply to revocable trusts created after July 1, 2007, if they do not expressly authorize the trustee by specific reference to the subsection, to invest in investment instruments owned or controlled by the trustee or its affiliate.
- Apply to revocable trust created before July 1, 2007, and those created on or after that date that do not have a specific authorization, after compliance with a notice and objection procedure.

The bill specifies that subsection (5) is not the exclusive authority for a trustee investing in investment instruments owned or controlled by a trustee or its affiliate, or from which the trustee or affiliate receives compensation for services.

Section 4. Amends s. 736.0816, F.S., regarding the powers of a trustee. The bill classifies derivatives and hedge funds as “mutual funds” for purposes of this section. It would include such instruments in the trustee’s ability under current law to acquire an undivided interest in a trust asset such as a mutual fund in which the trustee holds an undivided interest, including a mutual fund from which the trustee or any affiliate or associate of the trustee is entitled to receive reasonable compensation for providing investment advice, portfolio management, or servicing agent duties.

Section 5. Amends s. 736.1008, F.S. to provide a corrected effective date of July 1, 2007 regarding limitations on proceedings against trustees that corresponds with the effective date for the new Florida Trust Code. Current law makes the provisions effective January 1, 2008.

Section 6. Amends s. 736.1011, F.S., regarding exculpatory terms caused to be drafted by a trustee. The exculpatory term is invalid unless:

- The trustee proves that the exculpatory term is fair under the circumstances; and
- If the trust is created after July 1, 2007, if the term’s existence and contents were adequately communicated directly to the settlor or the independent attorney of the settlor. Permitting disclosure to the attorney of the settlor would prevent a trustee from having to verify that the attorney communicated the fact of the term’s existence to the settlor, or informing the settlor directly in every such situation.

Section 7. The act is effective July 1, 2007.

IV. Constitutional Issues:

A. Municipality/County Mandates Restrictions:

None.

B. Public Records/Open Meetings Issues:

None.

C. Trust Funds Restrictions:

None.

V. Economic Impact and Fiscal Note:

A. Tax/Fee Issues:

None.

B. Private Sector Impact:

The Florida Bankers Association supports the legislation, stating that it will provide greater flexibility regarding the management of trust assets and clarify the newly enacted Florida Trust Code. The Real Property and Probate Trust Law section of the Florida Bar has not expressed concerns with the CS.

C. Government Sector Impact:

None.

VI. Technical Deficiencies:

None.

VII. Related Issues:

None.

This Senate Professional Staff Analysis does not reflect the intent or official position of the bill's introducer or the Florida Senate.

VIII. Summary of Amendments:

None.

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