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Forum Juridicum: Louisiana Trusts for the Louisiana Lawyer - Some Comments on the New Statute

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LOUISIANA TRUSTS FOR THE LOUISIANA LAWYER

Some Comments on the New Statute

FRANK P. STUBBS*

With the enactment of Act 81 of 1938[1]—better known as the Trust Estates Act—the Legislature placed in the hands of every Louisiana lawyer a tool which has always been a respectable and useful part of the kit of his fellow craftsmen in the forty-seven other states but which, for fairly well known historical reasons, was prohibited in Louisiana for an aggregate of one hundred and fourteen years. That tool is the private trust device.

The long absence of the trust from Louisiana proved to be a great benefit in at least one respect—it made possible the adoption of a modern, comprehensive statute which is almost a code in itself and is, by the way, the first enactment of its kind.

The special advantage to the Louisiana lawyer in having at hand a rather broad and detailed statute is quickly apparent. For generations past the great majority of law students destined to practice in this state have given the subject of trusts but scant attention because they have known that it was of little practical importance to them. It has been so, likewise, and for the same reason, among lawyers in general practice and among judges. Consequently, it is not sufficient that the statute which at last brings the trust device to Louisiana be merely a vehicle for its legalization. If it is to be of full value to our bench and bar the statute must also present Louisiana's trust law to them in its prime essentials, in some detail, and in terms they know and understand. The Trust Estates Act does so.

It has deficiencies, naturally, but in the light of its total achievement they will seem minor indeed. As the statute matures from year to year, as its pattern and philosophy become thoroughly understood, as practice under it grows from novelty into commonplace, its gaps will be narrowed and closed.

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1. Dart's Stats. (Supp. 1938) § 9850.1-9850.101.

This article is not a critique of the statute. It simply points out the landmarks in the new field of opportunity which the Act has opened up for the practicing lawyer and pauses to inspect a few of the features which command his first attention.

New Solutions for Old Problems

Obviously the greatest usefulness of the trust device lies in the vast field of testamentary dispositions for the protection of widows and immature and inexperienced heirs. A mere glance by the practicing lawyer at some of his clients' testamentary problems reveals the trust as the classic solution.

A different but often closely related need for the trust device is found in the family situation where there are two or more heirs and the testator desires that his estate be managed as a unit for their benefit under his parting directions. The availability of the trust device as a means of assuring centralized control in hands of the testator's own selection, working in accordance with his own general or specific plan, is of considerable value to the lawyer who has this familiar problem before him in one of its myriad forms.

The rapid and widespread development of oil and gas production in this state has brought along its new and special complexities to the testators—and their lawyers—who are affected by it. In many such cases the trust device has a great deal to offer and should reward a close study of its possibilities.

No less vast, but much less obvious, than the field for testamentary trusts is the opportunity for inter vivos trusts. Here is the trust in its infinite variety. That settlors can create trusts for themselves as well as for others, that the ten-year limitation measures from the settlor's death and not from the date of creation, and that virtually any degree of revocability is possible—these facts suggest the extremely wide range of usefulness for the living trust in the hands of the Louisiana practitioner.

Voluntary living trusts for the management of estates owned by several persons in indivision, trusts for the conduct of joint enterprises, trusts to secure and pay creditors, and business insurance trusts are a few examples of the employment of the inter vivos trust for business purposes.

On the more personal side are the voluntary living trust created primarily for the benefit of the settlor himself, the inter vivos donation in trust for the benefit of others, and the personal life insurance trust.

The life insurance trust deserves a special word. Whether for business purposes (e.g., stock purchase and partnership liquidation trusts) or for essentially personal ends (e.g., family protection trusts), the insurance trust is an exceedingly useful arrangement. The *sui generis* nature of the life insurance contract itself, the debt exemptions accorded life insurance proceeds, the tax advantages enjoyed by life insurance, and the unparalleled convenience of gathering a number of policies and their proceeds together under a single trust instrument—these features show how useful the life insurance trust can be to the lawyer.

One is often tempted, when faced with a problem in which he discerns a probable need for a trust, to superimpose a conventional type and form of trust on the situation. Thus the problem is sometimes forced into a rigid mold which may or may not fit it, with results which may tend to discourage both lawyer and client from using the trust device. The approach should be from the other direction. The desired results should be set down quite frankly and an arrangement—regardless of name or form—which obtains these results should then be worked out. The emphasis is then on substance and utility, which are the important things, and the type and form of the trust will largely develop themselves.

In Louisiana there remain traces of a tendency, which is quite understandable from the historical viewpoint, to associate the word "trust" exclusively with the tieing up of property for a long period. Often the word has carried with it connotations of passivity, of economic enervation, of the fixation and sterilization of wealth. Where these impressions still persist they tend to obscure not only the broad significance of the Trust Estates Act but also its enormous usefulness to the Louisiana lawyer of this day and time. The Act makes possible a ten-day trust for a business transaction or a ten-month trust for the liquidation of a man's debts as well as a ten-year trust for the protection of a young heir's inheritance.

The practical application of the Trust Estates Act and indeed its very existence are of course better known to lawyers than to most of their clients. It naturally follows that the suggestion for the employment of a trust arrangement must emanate in many cases from the lawyer rather than from the client. Sometimes not only the responsibility for the idea itself but the duty of decision actually rests with the lawyer. Often the client and his lawyer are in the position of the patient and his doctor: the pa-

tient describes his case as best he can; the doctor listens, observes, examines, prescribes, and treats. So it must be with trusts in Louisiana.

THE UTILITY OF THE RESTATEMENT AND THE UNIFORM ACTS

In his *Trust Estates Act Handbook,* Mr. George M. Wallace says of the sources of the statute:

". . . the Trust Estates Act is derived mainly from the general common law of express, private trusts in the United States as announced in the American Law Institute's Restatement of the Law of Trusts and as modified and supplemented by the Uinform Trusts Act, the Uniform Principal and Income Act, and the proposed Uniform Spendthrift Trusts Act."

"In being carried over into the Trust Estates Act some of the rules of the Restatement are modified and others radically changed so as to bring them into harmony with certain legal concepts and principles which are well understood and settled in Louisiana, and in order to meet other special needs of this state."

"The very nature of the statute made it necessary to have some of the sections constructed from the ground up out of a variety of materials and according to designs which were more or less original."[2]

He also points to the great utilitarian advantage, from the standpoint of the practicing lawyer, of having the Restatement and the Uniform Acts as principal sources:

"The reasons behind the Uniform Trusts Act and the Uniform Principal and Income Act appear in the prefactory notes which are included in the pamphlet copies of these acts published by the National Conference of Commissioners on Uniform State Laws. Both of these acts were prepared under the auspices of the National Conference and have been approved by it.

"The reasons behind the Uniform Spendthrift Trusts Act are given in Griswold's 'Spendthrift Trusts' which also contains a copy of the act, of which Mr. Griswold is likewise the author."

"In the Restatement full explanations and illustrations are given under every statement of a rule. These comments and

2. Wallace, The Trust Estates Act Handbook (1938) ix, x.

examples make the Restatement extremely valuable as source material for the Trust Estates Act in that they supply lawyers and judges with a reliable guide to understanding and interpretation of the greater part of the Act. Where the wording of a provision in the Trust Estates Act is copied from or is substantially the same as the corresponding rule in the Restatement one has only to refer to the Restatement itself for an authoritative explanation. Moreover, where a provision in the Trust Estates Act differs from the rule on the same point in the Restatement and interpretation is desired, the very fact of difference may be a helpful clue."[3]

The Beginning and the End

There is of course only one way to create a testamentary trust and that is by will in any of the prescribed forms, and the time of creation is the time of the testator's death.

An inter vivos trust, on the other hand, is created when the trustee accepts it, and it can be established in a variety of ways ranging from a strictly formal act of donation inter vivos to a highly informal agreement between the settlor and the trustee. The statute's requirements as to form lend themselves to local usage anywhere in the state and to the needs of any given case. The words "or other appropriate transaction" in Section 8 constitute a catch-all phrase making it clear that the nomenclature of the instrument is not the governing factor. Let it be an *indenture* if you will, or a *contract,* or a *deed,* or a *declaration of trust,* or an *act of sale,* or a *memorandum,* or what not. Of course, all these things are *agreements* in the last analysis since the trust instrument must be a two-sided affair; and the phrase "or other appropriate transaction" may therefore be an unnecessary one from a purely technical standpoint.

The Act upholds the doctrine that a valid trust, once it is created, should run the precise course and the full course which its settlor has charted in its terms. Deviations can be ordered only by the court and then only the better to carry out the purposes of the trust. The order to turn back or to abandon the trust can be given only by the court and then only for the most compelling reasons. Specifically, the parties at interest are forbidden to break up the trust in violation of its terms by consent between or among themselves. This salutary rule against premature de-

3. Ibid.

struction of the trust is deeply grounded in doctrine and in reasons of public policy which have no place in this discussion. It should be remembered that the settlor "writes his own ticket" with respect to revocation and modification; that he himself sets the date of termination; that if he wishes to give the beneficiary or the trustee, or both of them acting together, the right to bring the trust to an earlier end he is free to do so; that the *court* can order a deviation from the terms of the trust if necessary to carry out the purposes of the trust; and, finally, that:

> "If owing to circumstances not known to the settlor and not anticipated by him, the continuance of the trust would defeat or substantially impair the accomplishment of the purposes of the trust, the proper court shall direct or permit the termination of the trust, in whole or in part."[4]

Fifty-Six Sections on Administration

Well over half of the Act is devoted to the subject of administration. Here is the core and substance of trusteeship. These sections are intensely and severely practical, and are of immeasurable benefit to the lawyer not only in matters connected with a trust which is a going concern but also in planning trusts and preparing trust instruments.

A Boon to Draftsmen

The very extensiveness of the chapters on administration makes the lawyer's work in preparing trust instruments much easier, and generally more effective, than it would have been had these rules been given in less detail. The duties and powers of the trustee are carefully spelled out in plain language, making it quite unnecessary for the draftsman of a trust instrument to spend precious time digging them up here and there (and never being quite sure about them all) and then more time making certain—perhaps in a torrent of words—that his trust instrument has set them out in the exact way required to produce the desired results.

The statutory duties and powers are not forced on the settlor (save only the trustee's duty of loyalty to the beneficiary) and he can vary them at his pleasure in the trust instrument. They merely establish the base line for the draftsman to go by.

Nowhere is the incalculable advantage of this crystallization more plainly apparent than in the domain of testamentary trusts

4. La. Act 81 of 1938, § 91 [Dart's Stats. (Supp. 1938) § 9850.91].

where the olographic will is king. It makes possible the creation of a good, sound, workable trust in a short will. By way of illustration, in a will setting up a simple trust for the testator's child, where the only reference to the trustee's duty is to say that he is to pay the income to the beneficiary, and no reference is made whatever to his powers, at least eighteen affirmative and negative duties and one general and eight specific powers are automatically given the trustee by the statute. To quote again from Mr. Wallace's *Handbook*:

> "The reader who is accustomed to the somewhat lengthy trust instruments which are generally used in other states will probably notice the brevity of the trust provisions in the forms—especially the wills—in these pages. It should be remembered that the Louisiana draftsman's problem under the Trust Estates Act is different from that of his fellows in every other state in one very important respect. The Louisiana lawyer has his trust law at hand in one compact, cohesive, comprehensive statute which covers thoroughly the normal duties and powers of the trustee and the relationship between him and the beneficiary—in short, the essence of trusteeship. In no other state is this true. It follows that nearly any trust situation can be covered adequately in a Louisiana trust instrument with less wordage than would normally be used for the same arrangement in another state. The widespread use of the olographic will in Louisiana makes this a very great advantage here."[5]

The Trustee and his Lawyer

The instant the trust is created, Title 7 becomes the trustee's manual—one is almost tempted to say his Bible. No trustee should undertake the administration of a trust without familiarizing himself with his statutory duties, powers, and liabilities *at the very outset.* For him to fail to do so is to invite serious consequences. In the writer's opinion a grave responsibility rests on the trustee's lawyer in this regard. He must see to it that the trustee knows these things in the very beginning, and it is not over-stressing the point to say that the lawyer should sit down with the trustee and coach him seriously on the legal aspects and implications of his job. This may require but a few minutes in some instances; in others it may take hours and several sittings. The trustee's duty to record the trust instrument if it transfers

5. Wallace, op. cit. supra note 2, at 47.

real estate and his duty to render an accounting once a year are only two of the urgent items which will generally have to be brought to the trustee's attention by his lawyer, especially where an individual, non-professional trustee is involved.

The rules on administration are clearly put and for the most part easily understood; nevertheless the need for interpretation and explanation is bound to arise from time to time. In this connection it is helpful to know that the great majority of these sections were taken bodily from the Restatement of the Law of Trusts and two uniform acts, the Uniform Trusts Act and the Uniform Principal and Income Act. The extensive comments and illustrations given in the Restatement, the prefatory notes to the uniform acts, and the recent writings thereon will prove to be invaluable aids to the lawyer seeking further light on the provisions which were drawn from these sources. From the lawyer's standpoint it is also encouraging to remember that the court, if called on, can give him a helping hand in the form of authoritative interpretation of the trust instrument and instructions regarding administration.

It is the writer's belief that a very substantial proportion of the cases of maladministration and alleged maladministration which have come before the courts throughout the United States in past years are traceable directly to a lack of realization or a faulty understanding on the part of the trustees involved as to just what duties, powers, and liabilities the law really gave them. In a great many instances the unsettled condition of the law itself was fundamentally to blame. In some other situations the times had outrun the law. This will not be so in Louisiana. In no other state are the duties, powers, and liabilities of the trustee so completely set forth, in no other state is the unique relationship between beneficiary and trustee so clearly defined.

With an absolutely clean slate and with a full set of modern, wholesome, forthright rules for the trustee and his lawyer to be guided by, there is good reason to hope that the standard of trust administration in Louisiana will become the model for the entire country.

The Beneficiary's Network of Protection

An outstanding feature of the Trust Estates Act is the protection which it throws around the beneficiary. His principal safeguards are these:

1. The accounting requirements given in Section 34 and the

procedural requirements given in Section 95, coupled with Section 85 on prescription.

2. The definition of a breach of trust in Section 32 coupled with the clear statement of the trustee's liability and the beneficiary's remedies in Sections 54, 56, 57, 61, and 80.
3. The listing of the trustee's duties in Sections 33 and 35.
4. The prohibition of all forms of self-dealing in Sections 37, 38, and 39.
5. The carefully restricted legal list in Section 62.
6. The limitations in Sections 58 and 59 on the power of the settlor and the beneficiary in the matter of exculpatory provisions.
7. The supervising and regulating powers of the court as referred to throughout the Act, and the procedure authorized in Sections 93 to 96.

The mere enumeration of these seven points gives only a bird's-eye view of a deep, broad, and well organized defensive position. It would take too long to explore it at this time on foot, so to speak. But if the lawyer will examine the sections mentioned and if he will ponder a little on their significance and their crossfire, he will perceive the strength of the protective forces operating in the beneficiary's behalf.

A word should be said about the accounting requirements of Section 34, the first item in the foregoing list. This section is one of the gems of the Act, and in conjunction with Sections 85 and 95 it brings a tremendous amount of protection to the beneficiary. By forcing the trustee to account to the beneficiary once a year (failure to do so being a breach of trust), by encouraging the trustee to have his accounts approved and settled by the court, by postponing the beginning of prescription in favor of the trustee until he has rendered his final account, by requiring the trustee of a testamentary trust to file copies of his accounts with the court, and by requiring the trustee to account to the undertutor or under-curator where the trustee acts in the dual capacity of trustee and tutor or curator, these sections lay down the beneficiary's foremost line of security, *which is to know what the trustee is doing with the trust.*

Without weakening any of the remedies of the beneficiary, and without diminishing the drastic penalties for the trustee's sins of omission and commission, the Act stresses *prevention* of breaches of trust and, by simple and unequivocal statements of

what the trustee should and should not do, and what the beneficiary has a right to expect, it seeks to produce, in so far as it is possible for a statute to do so, administrations of such good and honest quality that breaches of trust will not occur.

Protection for the Trustee

With so many provisions for the protection of the beneficiary one wonders how the trustee has fared. It is important to remember, in thinking of the trustee, that the Act's coverage is very wide and that individual trustees will far outnumber corporate trustees for many years to come. The great majority of trustees throughout the sixty-four parishes of the state will be nonprofessional fiduciaries, usually relatives, business associates, and close friends.

What, then, is the trustee's protection under the Act? It rests mainly on these features:

1. His settlor can go as far as he likes in the trust instrument (subject to the loyalty restriction in Section 58) in relieving the trustee of duties and liabilities.
2. He does not have to accept the trust at all.
3. His position is clarified by the Act's detailed statement of his duties, powers, and liabilities. His lawyer can tell him exactly where he stands.
4. He can have his accounts approved and conclusively settled by the court.
5. When in doubt he can obtain interpretations and instructions from the court.
6. His beneficiary (if of age, etc.) can go as far as he likes (subject to the loyalty restriction in Section 59) in relieving the trustee of duties and liabilities.
7. The court (for cause and after hearing, etc.) can relieve him of duties; and can wholly or partly excuse him from liability for past violations if he acted honestly and reasonably.
8. He can resign whenever he wants to.
9. Actions by the beneficiary against him prescribe in one year from the rendering of his final account or from a minor beneficiary's twenty-first birthday.

The Act holds no terrors for the honest, competent, active trustee who is willing and able to give his trust the attention

necessary to carry out its terms. It does not pamper him but it does not pillory him either. It definitely discourages appointment of and acceptance by the incompetent and the slothful trustee, and the trustee who, for reasons of health or for other considerations, can not give the trust the requisite attention. It offers no hope whatsoever to the dishonest or scheming trustee.

The Duty of Loyalty

Because of its special importance to the lawyer in connection with the selection of a trustee, in the drafting of the trust instrument, and in the ensuing administration of the trust, the trustee's *duty of loyalty* is deserving of comment.

This duty is not an abstraction. It means certain definite things. The Restatement sums up the duty of loyalty in two paragraphs which were carried over into the Trust Estates Act as sub-sections (2) and (3) of Section 33, making it the trustee's duty

> "To administer the trust solely in the interest of the beneficiary; and
>
> "In dealing with the beneficiary on the trustee's own account, to deal fairly with him and to communicate to him all material facts in connection with the transaction which the trustee knows or should know . . ."

The Restatement in its comments lists a number of things which the trustee can not do without violating his duty of loyalty. The trustee violates this duty, for example, if he enters into competition with the beneficiary, if he leases trust property to himself, if he buys a mortgage on the trust property, if he uses trust monies in his own business, if he sells trust property and takes a commission from the purchaser on the sale, if he discloses trust information to a third person where he should know that the effect of such disclosure would be detrimental to the beneficiary. These examples are by no means all those given in the Restatement.

One of the main purposes of the Uniform Trusts Act was to tighten and clarify the loyalty rules with regard to self-dealing. Hence Sections 37, 38, and 39 and sub-section (5) of Section 35 of the Trust Estates Act. So intimately related are these sections to the general loyalty rules given in sub-sections (2) and (3) of Section 33 that the trustee's duty of loyalty can be said to be stated in these two sub-sections *and* Sections 37, 38, 39, and sub-section (5) of Section 35.

The interrelation of these sections under the heading *Duty of Loyalty* should be borne in mind for its effect on the power of the settlor and the beneficiary to vary the statutory duties, powers, and liabilities of the trustee. Sections 58 and 59 give them the utmost freedom in this regard *except* where the duty of loyalty is concerned.

Section 58, on the power of the settlor, says that no provision in the trust instrument "shall be effective to limit the trustee's duty of loyalty to the beneficiary or his liability for breach of such duty." The statute relaxes this prohibition at only two isolated points: Section 35 (5) allows the settlor by specific words in the trust instrument to relieve a corporate trustee from putting up the security required by that sub-section for the funds of that particular trust deposited with itself; and Section 38 (2) allows the settlor or settlors of two or more trusts having the same trustee to permit, by express provisions in the trust instruments, sales between or among the trusts concerned.

Section 59, on the power of the beneficiary, says that no writing of the beneficiary "shall be effective to the extent that it purports to limit prospectively the trustee's duty of loyalty to the beneficiary or his liability for breach of such duty." To this sweeping prohibition there is no exception.

All this can mean but one thing: That under the Trust Estates Act there is nothing a settlor can effectively do to waive any of the statute's loyalty rules, including the rules against all forms of self-dealing except the two narrow species above mentioned, and there is nothing a beneficiary as such can effectively do to authorize a violation of any of the loyalty rules.

Situations will undoubtedly arise where self-dealing transactions which can not be authorized even by the settlor may actually be desirable in the interest of the beneficiary. It is not difficult to imagine such a case in certain kinds of family trusts, in a trust where the beneficiary is one of the trustees, in a community where the trustee has a family or business relationship with everybody normally expected to deal with the trust, and so on. Naturally, the best way to avoid such dilemmas is to forestall them in the selection of the trustee. It is not always possible and feasible to do this, however.

Although the statute expressly withholds from the settlor and the beneficiary the power to waive a loyalty rule it does not withhold this power from the court. If an occasion arises in which it appears to the court that under the special, compelling

circumstances the trustee should be permitted to enter into a self-dealing transaction the court, in the exercise of the power granted in Section 60, can lift the restrictions to such extent as may be necessary. No doubt this power will be used very sparingly.

Said Cardozo in a famous opinion of the New York Court of Appeals:

> "Many forms of conduct permissible in a workaday world for those acting at arm's length, are forbidden to those bound by fiduciary ties. A trustee is held to something stricter than the morals of the market place. Not honesty alone, but the punctilio of an honor the most sensitive, is then the standard of behavior. As to this there has developed a tradition that is unbending and inveterate. Uncompromising rigidity has been the attitude of courts of equity when petitioned to undermine the rule of undivided loyalty by the 'disintegrating erosion' of particular exceptions. . . . Only thus has the level of conduct for fiduciaries been kept at a level higher than that trodden by the crowd. It will not consciously be lowered by any judgment of this court."[6]

What better guide than these words in Louisiana, where the Trust Estates Act spells out the duty of loyalty in even stricter terms than does the common law?

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6. Meinhard v. Salmon, 249 N.Y. 458, 164 N.E. 545, 546 (1928).