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# Secret Trusts: (Some) Questions and (Fewer) Answers About Florida's New Designated Representative Statute

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*Representation by a designated representative is a new and unique provision of the Florida Trust Code which attempts to strike a balance between the settlor's right to privacy and the beneficiaries' right to trust information, but with it comes some interesting issues.*

This article discusses representation by a settlor designated representative, a new and unique provision of the Florida Trust Code allowing a settlor to appoint a person to receive trust information on behalf of and bind a trust beneficiary, even in the presence of a conflict of interest. The article explains the designated representative provision, including the rationale for its enactment and how it differs from the Uniform Trust Code. Included is a discussion of why a trust settlor may want to use a designated representative, limitations on the designated representative's authority, liability implications for Trustees who make disclosures only to the designated representative, and more.

Every trust beneficiary deserves "adequate" representation. Historically, this was imbedded in the fiduciary duty imposed on trustees, leading on occasion to an impractical, if not awkward, dynamic. Florida law often serves to rescue such situations via a mechanism of representation. Part III of the Florida Trust Code (the "Code") contains the representation provisions applicable to Florida trusts.<sup>1</sup> **Representation in this context refers to the authority of one person to act on behalf of a trust beneficiary.** Under the Code, notice, information, accountings, and reports given to a representative serve as a substitute for and have the same effect as sending such information to the beneficiary directly.<sup>2</sup> Further, actions taken by a representative bind the beneficiary to the same extent as if such actions were taken by the beneficiary.<sup>3</sup> As many practitioners know, Florida's Trust Code was substantially rewritten in 2007 and now includes five types of representation:

- Representation by the holder of a power of appointment,<sup>4</sup>
- Representation by fiduciaries and parents,<sup>5</sup>
- Representation by a person having a substantially identical interest,<sup>6</sup>
- Court-appointed representation,<sup>7</sup> and

- Representation by a settlor designated representative.<sup>8</sup>

This article will discuss the fifth form, representation by a settlor designated representative, particularly as it is a new and unique provision of the Code adopted for the first time in 2007 and amended in 2009.

## Framework

Representation by a designated representative is new to Florida law and was included in the Code to strike a balance between the settlor's right to privacy and the beneficiaries' right to trust information. There is no counterpart provision in the Florida Probate Code, Florida's prior trust laws under Chapter 737 of the Florida Statutes, or the Uniform Trust Code from which about half of Florida's Code was adopted. A few other states have also adopted similar provisions allowing settlors to limit disclosures of trust information as competition increases among the states for trust business.<sup>9</sup>

Under the Code, the term "qualified beneficiaries" includes then living beneficiaries who are currently eligible to receive trust distributions and those beneficiaries who would become eligible to receive trust distributions if either the current beneficiary's interest terminated or the trust terminated.<sup>10</sup> Contrast this with the Code's definition of "beneficiaries" which includes all beneficiaries, including all future and contingent beneficiaries.<sup>11</sup> The Code requires the trustee to provide qualified beneficiaries with information concerning the trust and its administration including, upon request, a copy of the trust instrument, information concerning the trust's assets and liabilities and the particulars concerning the administration of the trust (this includes distributions to beneficiaries).<sup>12</sup> In addition, the trustee is required to send detailed accountings to the qualified beneficiaries at least annually and upon termination of a trust or on change of the trustee.<sup>13</sup> There are also a number of other areas under the Code where information should be given to certain beneficiaries, such as in trust modification

and termination proceedings,<sup>14</sup> exercise of the trustee's authority to "decant" a trust<sup>15</sup> or combine or divide a trust,<sup>16</sup> the appointment and removal of trustees,<sup>17</sup> and approval of certain transactions by the trustee.<sup>18</sup>

While a settlor cannot waive a trustee's duty to notify, account to, and respond to the requests for information by qualified beneficiaries,<sup>19</sup> the provisions of the Code governing the trustee's duty to inform and account clearly provide that the representation provisions of the Code apply with respect to all rights of a qualified beneficiary to trust information.<sup>20</sup> Thus, through effective use of Florida's designated representative statute, a settlor is now permitted under the Code to limit disclosures of some or all trust information to some or all trust beneficiaries. This is done by the settlor designating a representative in the trust instrument to receive information on behalf of, and to represent and bind, the beneficiaries of the trust. In making the appointment, the settlor can limit the representative's authority or the beneficiaries the representative represents.

### **Uses of a Designated Representative**

Many settlors are surprised and taken aback to learn about the qualified beneficiaries' right to trust information and other rights under the Code. Often, settlors view these rights as overreaching or "crossing a line." In fact, there may be any number of reasons for these reactions, including what the settlor sees as a right to keep "his" finances private, a desire for efficient trust administration, protection of a beneficiary whose relationship with other beneficiaries may be strained, or protection of a beneficiary whose knowledge of the trust or access to its assets may cause the beneficiary to become complacent with their goals or increase their substance abuse or financial problems.

Take, for example, the elderly settlor who creates a credit shelter trust solely for the benefit of his spouse for her lifetime, and upon her death, distributes to his descendants from his prior marriage. The qualified beneficiaries of such trust include his spouse and *all* of his then living descendants (this could include several generations of descendants, many of whom may be minors). Under the Code, all of these qualified beneficiaries are entitled to trust information, such as account statements, and to be notified of certain trust matters, including distributions to the current beneficiary (recall she is their step-mother). Many settlors would find this objectionable – if not an invitation for disharmony and litigation. This is a definitive situation for the use of a designated representative, who could represent the descendants in perhaps a less meddlesome way.

In addition to limiting disclosures of trust information, effective use of the designated representative provision can also make trust administration more efficient and provide protection to the trustee. Florida allows non-charitable trusts to last for 360 years.<sup>21</sup> As a trust gets older, the number of trust beneficiaries typically increases and

consequently so does the amount of trust administration work and expense. Use of a designated representative can certainly promote efficiency and reduce administration expenses because it can be used to minimize otherwise required disclosures, and it can also reduce the burden of getting approval (or lack of objection) from a large class of people (say to decant or adopt the power to adjust). In addition, many provisions of the Code only require the trustee to give trust information to qualified beneficiaries. A trustee who then only accounts or provides notice to qualified beneficiaries may be subject to liability to all other beneficiaries unless such other beneficiaries are otherwise adequately represented. Effective use of the designated representative allows the trustee to notify and account only to the designated representative who represents and binds *all* beneficiaries, not just qualified beneficiaries. This is particularly useful to a settlor whose objectives include providing protection to a Trustee who acts in good faith.

### **Statutory Limitations**

Importantly, there are limitations on a designated representative's ability to represent and bind beneficiaries that may not be overridden by the trust terms.<sup>22</sup> The first is a limitation on who can be appointed as designated representative. A second is how a designated representative may be appointed. Under the Code, a representative may be designated in the trust expressly by name or the trust may provide a mechanism by which a designated representative may be appointed. However, the designated representative may not be the trustee nor may the trustee appoint the designated representative.<sup>23</sup> This limitation was included to insure that the trustee is not in a position to approve its own actions. Lastly, a beneficiary may only serve as the designated representative if he or she is either expressly appointed in the trust or is a "close relative" of the represented beneficiary or the represented beneficiary's spouse (i.e., is their spouse, grandparent, or descendant of their grandparent).<sup>24</sup> This requirement was included to minimize the risk of bad faith by the designated representative.

### **A Designated Representative is Not a Fiduciary**

The Code also imposes upon the designated representative a duty to act in "good faith". A designated representative is not, however, a fiduciary and is not liable for acts or omissions so long as the designated representative has not acted in bad faith.<sup>25</sup> It is important to note that there is no conflict of interest limitation to the designated representative's authority as there is for most other forms of representation under the Code. Thus, a designated representative may represent and bind beneficiaries even in the presence of a conflict of interest so long as the designated representative's actions or omissions do not constitute bad

faith. The Code, however, provides no guidance on determining what actions may constitute bad faith on the part of the designated representative, and there are no Florida cases (yet) on the subject. Florida cases have, however, generally defined “bad faith” as follows:

“...generally implying or involving actual or constructive fraud, or a design to mislead or deceive another, ...not simply bad judgment or negligence, but rather implies the conscious doing of a wrong because of dishonest purpose or moral obliquity;”<sup>26</sup>

As the designated representative provision becomes more widely used, the authors expect Florida case law will further define the duties of the designated representative and the limitations on their authority to act.

### **Too New to Have All the Questions Answered**

There are several areas of concern among practitioners concerning use of a designated representative. The first relates to the application of the designated representative concept outside of the Code. If a beneficiary is adequately represented under the Code, is that beneficiary represented for all legal purposes such as for purposes of the Probate Code? What about for purposes of litigation? Under the Probate Code, the term “beneficiary” of an estate that is devised to a trust includes each qualified beneficiary of the trust if each trustee of the trust is also a personal representative of the estate.<sup>27</sup> If the trust appoints a designated representative and each trustee of the trust is also a personal representative, is it sufficient for probate administration purposes to include only the trustee and the designated representative as beneficiaries of the estate?

More concerning is the question of whether a designated representative may receive notice and bind a trust beneficiary in a trust litigation proceeding (as opposed to routine trust administration disclosures). Representation has long been recognized by Florida courts as a permissible means to bind interested parties who are not before the court. In addition, both the Code and the Probate Code reference its provisions having application in *all* judicial proceedings involving estates and trusts.<sup>28</sup> Further, nothing in Part III of the Code governing representation indicates that otherwise effective representation does not apply in the context of trust litigation. In fact, the Code’s express language provides that the designated representative may represent and bind a beneficiary with respect to *any* notice.<sup>29</sup> When Florida enacted the Code from the Uniform Trust Code, it made significant variations in its representation provisions. First, as mentioned above, the concept of a settlor designated representative is unique to Florida and was not derived from the Uniform Trust Code. Second, while the Comments to the representation provisions of the Uniform Trust Code state that the representation principles

apply for purposes of settlement of disputes, whether by a court or nonjudicially, the Uniform Trust Code expressly grants the represented beneficiary the power to object to the representation.<sup>30</sup> Because this right to object to the representation was not adopted by Florida as it was by most other states adopting the Uniform Trust Code, the inference is that the designated representative has the legal authority to bind a beneficiary even over the objection of such beneficiary. It should be noted, however, that under the Code the court always has the power to take any action necessary in the interests of justice.<sup>31</sup> It would seem then that a beneficiary who objects to being represented or to a representative’s action may have standing at least to ask the court to intervene. But in the absence of such court involvement, presumably the beneficiary will be bound by the representative’s actions, including if the beneficiary is unaware of the representative’s actions. To reach a contrary result essentially would render the designated representative provision meaningless. It is conceivable, however, that there will be Florida cases which find that refusal to notify an adult competent beneficiary of an action relating to his interest in a trust constitutes a violation of his constitutional due process rights.<sup>32</sup>

A troubling aspect of the designated representative provision is that it does not clearly describe the authority of the representative, it merely refers to the authority to “bind” the beneficiary. Does this mean the representative has sufficient standing to enforce the trust on behalf of the represented beneficiary? If the representative’s authority is merely to receive trust information and to bind the beneficiary with respect to disclosed transactions, then who has standing to enforce the beneficiary’s rights for other matters? If trust information provided only to the representative discloses a potential claim against the trustee, does the representative have standing to file suit against the trustee or does the representative need to notify the beneficiary, and can the beneficiary then file suit? Further, what if the representative consents to a proposed trustee action and the beneficiary in contrast seeks to object – on whose response can the trustee rely? The Code also is silent on the rights of a represented beneficiary. Does such beneficiary have standing to demand trust information from either the trustee or the representative in the absence of bad faith? As discussed above, the court always has the power to take any action necessary in the interests of justice and therefore a beneficiary will likely always have the right to be heard. But in such action, does the designated representative have standing to enforce his representative authority?

Trustees, especially corporate trustees, may be reluctant to rely upon the authority of the designated representative even though the Code protects the trustee for acting in reasonable reliance on the trust terms.<sup>33</sup> Such reluctance might result, at least in part, from an express provision

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of the Code allowing the trustee to give trust information directly to a represented beneficiary and protecting the trustee for so doing.<sup>34</sup> There is no similar express protection for a trustee who gives trust information only to the designated representative.

Finally, use of the designated representative raises tax issues. A beneficiary often is granted an interest in, or rights under, an irrevocable trust to achieve certain tax objectives. Examples include withdrawal rights over contributions intended to qualify for the annual exclusion from federal gift tax under Section 2503(b) of the Internal Revenue Code,<sup>35</sup> and the right of a spouse to make trust property productive of income so such property qualifies for the federal estate tax marital deduction.<sup>36</sup> The Internal Revenue Service has routinely ruled that a fiduciary, such as a legal guardian, having the legal authority to exercise certain rights on behalf of a beneficiary is sufficient to continue the tax benefits that were dependent upon the beneficiary having such rights.<sup>37</sup> However, since the designated representative is not a fiduciary and is held only to a standard of good faith, uncertainty results. Until there is some clarity, cautious drafters may conclude it not prudent to have a designated representative representing a beneficiary granted rights required for tax reasons. On the other hand, use of a designated representative to provide beneficiary consents made in good faith and without the knowledge of the beneficiary may be useful to minimize the beneficiary's gift tax exposure if the beneficiary's direct consent could be deemed a gift (e.g., during a decanting of a trust).

There are certainly some issues with the designated representative provision of the Code that remain to be resolved. But for now, settlors creating trusts in Florida can appoint a designated representative, create administrative efficiency and potentially even keep their trust business private. ■

#### Endnotes:

- 1 Fla. Stat. §§736.0301 to 736.0306
- 2 Fla. Stat. §736.0301(1)
- 3 Fla. Stat. §736.0301(2)
- 4 Fla. Stat. §736.0302
- 5 Fla. Stat. §736.0303
- 6 Fla. Stat. §736.0304
- 7 Fla. Stat. §736.0305
- 8 Fla. Stat. §736.0306
- 9 D.C. Code §19-1301.05(c)(3) allows the settlor to appoint a person to receive trust information on behalf of a trust beneficiary but note D.C. Code §19-1303.01(b) allows a represented beneficiary to object thus preventing his representative from binding him; 12 Del. C. §3303(a)
- 10 Fla. Stat. §736.0103(14)
- 11 Fla. Stat. §736.0103(4)
- 12 Fla. Stat. §736.0813(1)
- 13 Fla. Stat. §736.0813(1)(d)
- 14 Fla. Stat. §§736.04113, 736.04115, 736.0412, 736.0413, 736.0414,

- 736.0415 and 736.0416
- 15 Fla. Stat. §736.04117
- 16 Fla. Stat. §736.0417
- 17 Fla. Stat. §§736.0704 and 736.0706
- 18 Fla. Stat. §736.0802
- 19 Fla. Stat. §736.0105(2)(r), (s) and (t)
- 20 Fla. Stat. §736.0813(3)
- 21 Fla. Stat. §689.225(2)(f)
- 22 Fla. Stat. §736.0105(2)(h)
- 23 Fla. Stat. §736.0306(1) and (2)
- 24 Fla. Stat. §736.0306(3)
- 25 Fla. Stat. §736.0306(4)
- 26 *Bosso v. Neuner*, 426 So.2d 1209 (Fla. 4th DCA), *pet. for rev. denied*, 436 So.2d 100 (Fla. 1983); *Parker v. State of Florida Board of Regents*, 724 So.2d 163 (Fla. 1st DCA 1998); *Ford v. Rowland*, 562 So.2d 731 (Fla. 5th DCA 1990); Black's Law Dictionary 139 (6th ed. 1990)
- 27 Fla. Stat. §731.201(2)
- 28 Fla. Stat. §§731.303, 736.0305(2) and 736.1303(1)(b)
- 29 Fla. Stat. §736.0306(1)
- 30 Unif. Trust Code §301(b) (amended 2010)
- 31 Fla. Stat. §§736.0105(2)(e) and 736.0201
- 32 *Barber v. Barber*, 837 P.2d 714 (Alaska 1992) which held that the refusal to allow an objection by an adult competent beneficiary violated due process; but note that the subject beneficiary was not properly represented under Alaska law
- 33 Fla. Stat. §736.1009
- 34 Fla. Stat. §736.0301(4) which was not part of the counterpart Uniform Trust Code provision
- 35 Rev. Rul. 80-261, 1980-2 C.B. 279
- 36 Treas. Reg. §20.2056(b)-5(f)(5)
- 37 Priv. Ltr. Rul. 9232013 (May 4, 1992); Priv. Ltr. Rul. 8712014 (Dec. 18, 1986); Priv. Ltr. Rul. 8022048 (Mar. 4, 1980)



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