SSHHH! Should Trustees Speak Up About Quiet Trusts?

By Jennifer F. Hillman and Joseph T. La Ferlita

While some clients flaunt their wealth, others like to keep things quiet. Sometimes, such "financial modesty" is motivated by a concern that knowledge of family wealth could result in disincentivized children or grandchildren. Although some may question whether such financial modesty is a virtue, there is no requirement that parents disclose their net worth to their children.

However, the analysis changes when wealth is transferred to a so-called "Quiet Trust"—an irrevocable trust that purports to limit or prohibit the trustee from disclosing the assets of the trust, or even the trust's very existence, to some of the beneficiaries. New York trusts and estates practitioners will undoubtedly encounter a Quiet Trust at some point, either because a client would like to create one, or needs guidance as a beneficiary or trustee of one, and they must understand the challenges posed by Quiet Trusts in New York.

Challenges Faced by Trustees of New York Quiet Trusts

The crux of the challenge is reconciling trustees' fiduciary duty, which generally leans in favor of disclosure of trust information to beneficiaries, with explicit provisions of a trust that limits or prohibit disclosure. Depending on how stringent the trust's limitations on disclosure are, trustees might find it challenging to carry out the trust's terms while also fulfilling their fiduciary duty and limiting their potential liability.

Under the common law, trustees have had a long-recognized duty to inform the beneficiaries in certain situations and focus on a trustee's duty to timely and appropriately respond to a beneficiary's inquiry into the trust's terms, its assets, and the trustee's actions. The underlying principle is that such disclosure keeps trustees honest. Absent this policing ability of the beneficiaries, trustees may neglect their fiduciary duties.

While to date, New York statutory law does not deal explicitly with the concept of Quiet Trusts, the basic principle of disclosure nevertheless is enshrined in various New York trust statutes. For example, SCPA 2205 provides an extensive list of individuals and entities, including income and remainder beneficiaries, that have standing to petition the court to compel judicial settlement of a trustee's account including income and remainder beneficiaries of the trust. Another example is found in the commissions statute for individual trustees which require a trustee to provide annual statements to beneficiaries pursuant to SCPA 2308 and 2309. Even a trustee who has not retained annual commissions is still required under SCPA 2306 to furnish the annual statements to a beneficiary who requests annual statements.

Perhaps the most significant issue for trustees of a New York Quiet Trust concerns whether they can be released from liability through the settlement of their account as trustee either formally or informally. A judicial settlement is very detailed and predicated on the Surrogate's Court first having obtained personal jurisdiction over all necessary parties, perhaps including the very beneficiaries from whom the trustees are prohibited to disclose trust information. A non-judicial, informal settlement, while not requiring any particular level of asset disclosure, at a minimum requires disclosing the existence of the trust. However, if the information provided to the beneficiary is limited, the beneficiary may be able to later set aside such release on the basis of fraud or misrepresentation. Moreover, the statute of limitations on compelling trustees to account and seeking to hold them liable for breach of fiduciary duty may not begin to run until after the trustee accounts and/or discloses their actions. Thus, from a liability perspective, a New York Quiet Trust may be viewed as somewhat unfriendly to trustees.

The Proposed New York Trust Code

While New York law is not currently hospitable to Quiet Trusts, there may be changes pursuant to the proposed New York Trust Code (NYTC) which borrows concepts from the Uniform Trust Code (UTC), while still retaining and codifying New York-specific common law concepts. (The NYTC is an Office of Court Administration program bill which does not currently have a sponsor in the New York State Senate or Assembly.)

Both the UTC and the NYTC include laws authorizing settlors to direct the nondisclosure of the existence of a trust at least for some time period, unless a trust document states otherwise, to solely the "qualified beneficiaries" of the trust (*see* NYTC 7-A-1.3(18); 7-A-1.5(15)) (Proposed New York Trust Code: Surrogate's Court Advisory Committee to the Chief Administrative Judge of the Courts of the State of New York dated Sept. 4, 2019), which is a class of beneficiaries who are current beneficiaries or presumptive remainder beneficiaries of the trust. These are beneficiaries who, under current New York law, would be entitled to notice of proceedings involving the trust, but not beneficiaries whose rights would be deemed represented under the concept of virtual representation in SCPA 315.

The NYTC requires the trustee to inform and furnish requested information about an irrevocable trust to these qualified beneficiaries who are over the age of 25 after the death of the survivor of the settlor and the settlor's spouse (or 21 years if the settlor was an entity and not an individual).

Thus, it appears that if the settlor and the settlor's spouse are alive, there is no age at which a beneficiary must receive information. In many cases, this delayed disclosure may be enough to accomplish a client's goal.

However, pursuant to NYTC § 7-A-8.13, a trustee must send annual statements to any beneficiary who requests them—regardless of whether they are a qualified beneficiary or not. If the beneficiary becomes aware of the Quiet Trust and makes a request, the trustee must comply.

While the NYTC remains a proposal, practitioners should be aware that it exists.

What To Do When Confronted With a Quiet Trust?

If a client requests that you draft a Quiet Trust, it is prudent to discuss with the client whether disclosure through annual statements or other trustee communication might promote a more open and trusting relationship between trustee and beneficiary. Discuss with the client whether an open discourse about family wealth would instill fiscal responsibility.

If the client still decides that a Quiet Trust is appropriate, careful consideration should be given to the practicality and enforceability of the particular desired restrictions on disclosure. For example, a provision that forbids a trustee from ever disclosing a trust's existence even when asked is contrary to New York public policy and unenforceable even under the more permissive proposal of the NYTC. *See* NYTC § 7-A-8.13. But *see Friedrich v. Klaristenfel*, 195 A.D.3d 597 (2d Dept. 2021); *In re Kassover*, 124 Misc.2d 630 (Surr. Ct. Nassau Co. 1984).

Virtual representation pursuant to SCPA 315 can help limit disclosure to some beneficiaries (and arguably mirrors the limitation of disclosure to solely "qualified beneficiaries" under the proposed NYTC). Practitioners should consider including provisions in trust documents that authorize "horizontal" virtual representation of beneficiaries under a disability (SCPA 315(5)). "Vertical" virtual representation already exists under New York law. Virtual representation can be especially helpful if there is an infant beneficiary because it might allow the trustee to avoid the appointment of a guardian ad litem in a court proceeding (although there may be an advantage to having a guardian ad litem recommend approval of an account on behalf of their ward).

Practitioners can also consider setting forth in the trust document a specific commission schedule which is not linked to the default statutory rules under SCPA 2309 which require furnishing annual statements. *See* SCPA 2309(10). However, SCPA 2306 would still require the trustee to furnish the annual statements to a beneficiary upon request.

Another consideration is a trust protector, which may indirectly protect a beneficiary during a delayed notification period by allowing someone other than such beneficiaries to perform certain designated actions such as removing and replacing the trustee. There is no statutory authority for a trust protector under New York law, but it is a generally accepted concept particularly concerning inter vivos trusts which are largely governed by contract law.

Notwithstanding these aspects of existing New York law, the state (at least until the NYTC is adopted) is not among the Quiet Trust-friendliest jurisdictions. To serve the client's best interests, you should consider creating the Quiet Trust in another jurisdiction (with local counsel) that has adopted Quiet Trust legislation. Some states have enacted versions of the UTC or their own statutes which may allow settlors to waive or modify all notice and disclosure requirements by not mandating disclosure. These include Arkansas (A.C.A. 28-73-105), North Carolina (N.C. Gen. Stat. § 36C-1-105) and North Dakota (N.D. Cent. Code, § 59-09-05) to name a few.

Some states have adopted the concept of the "designated representative," who is authorized to bind a beneficiary in any judicial proceedings or for non-judicial matters including consents, releases and ratification of a trustee's acts. *See* e.g., Delaware (12 Del. C. § 3339); Florida (Fla. Stat. § 736.0306) and Illinois (760 ILCS 3/307). In Delaware, for example, the designated representative is deemed to be a fiduciary and owes a fiduciary duty to the beneficiary and may be accountable for their actions taken on a beneficiary's behalf.

If the New York practitioner confronts a New York Quiet Trust after it has been created, either during its administration or litigation, the practitioner should undertake a fact-specific analysis of the particular Quiet Trust provision under current law to determine the provision's enforceability and practicality.

In sum, New York trusts and estates practitioners should be cognizant of the challenges presented by New York Quiet Trusts.

Jennifer F. Hillman is a partner at Rivkin Radler LLP where she concentrates her practice on trusts and estate-related litigation. She is a former Chair of the Trusts and Estates Law Section, a Fellow of the American College of Trust and Estate Counsel and frequent lecturer and author.

Joseph T. La Ferlita is a partner at Rivkin Radler LLP who concentrates his practice on estate and trust planning and administration. He helps individuals develop appropriate business succession, gift, estate and GST tax plans, taking into account their particular family and business circumstances. He also counsels individual and corporate fiduciaries, as well as beneficiaries, in all aspects of estates and trusts, including tax and breach of fiduciary duty issues. La Ferlita is a frequent lecturer and author. He serves on the Board of Directors of the Nassau County Estate Planning Counsel, and is a long-time active member of NYSBA's Trusts and Estates Law Section.