

## EXCERPT FROM PRIMER ON AMERICAN TRUST LAW

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### Termination and Modification of Trusts

**What are the circumstances under which a trust terminates?** Traditionally, a trust terminates when:

- the term of the trust expires;
- the trust purpose is fulfilled, including the completion of all active duties of the trustee;
- the trust purpose becomes unlawful or impossible to fulfill;
- the trust is revoked.

The trust purpose has not been fulfilled if there is a spendthrift provision, contingent interests, a mandated age for distribution, discretionary provisions, or support provisions. Despite the extreme unlikelihood of all trust purposes being fulfilled, trusts are occasionally terminated because the risk of liability is small or non-existent.

Under certain circumstances, specified parties may take action to terminate the trust, as described below. If a trust may be terminated, it may also be modified; but the reverse is not true.

**What are the trustee's obligations upon termination?** The trustee must exercise the powers necessary to wind up the affairs of the trust and distribute the property.

**May a trust be terminated upon consent?** Yes, an irrevocable trust may be terminated (or modified) with the consent of the settlor and all beneficiaries. A court order is not required. And, because of the settlor's participation in the decision, consensual termination is effective even when there is a spendthrift provision or when the purpose of the trust has not been achieved. Upon termination, the trustee must distribute the trust property in the manner agreed to by the settlor and beneficiaries.

**How can an irrevocable trust be terminated without settlor's consent?** If all beneficiaries of an irrevocable trust agree, they may terminate (or modify) the trust. Under what is known as the Claflin rule, the beneficiaries can only agree to terminate the trust if the trust no longer serves a material purpose. Like the spendthrift trust, the Claflin rule is an American invention. Under British law, the beneficiaries may terminate an irrevocable trust regardless of whether there is a purpose not yet fulfilled.

**How can consent to terminate a trust be obtained from unborn or unascertained beneficiaries?** Virtual representation is used to protect the interests of unborn beneficiaries and unascertained class beneficiaries. Even though the unborn or unascertained beneficiary is not officially made a party to the lawsuit, their interests are deemed to be sufficiently represented by a

living class member or other beneficiary with whom there is an "identity of interests". That allows for a binding judgment to be entered.

**Can a trust be terminated as a result of adverse circumstances unforeseen by the settlor?** Yes, it is settled that administrative provisions of a trust may be equitably modified or terminated by court order if continuation would defeat or substantially impair the accomplishment of the trust purpose due to unanticipated circumstances. The Uniform Trust Code also allows the court to modify the dispositive provisions of the trust.

**Can a trust be modified to correct a mistake of law or fact?** The answer to this often depends on whether the question refers to a testamentary trust or inter vivos trust. Many states hold wills to a higher evidentiary standard and make the correction of mistakes embodied in a will very difficult. Thus, if the settlor left something out of a testamentary trust it is unlikely it will be allowed to be changed, whereas an inter vivos trust can be reformed to reflect settlor's intent. Extrinsic evidence is liberally allowed to reform an inter vivos trust whereas for wills, and thus testamentary trusts, extrinsic evidence is not allowed for the purpose of interpreting a patent mistake. The Uniform Trust Code eliminates this distinction, allowing a testamentary trust to be modified on the same basis as an inter vivos trust.

**How can the modification of trusts make administration more efficient?** Consolidation or division of trusts is often beneficial. While not recognized at common law, those options are recognized under many state statutes and under the Uniform Trust Code. Many state statutes allow two or more trusts to be combined into a single trust, which may reduce administrative costs. Likewise, many state statutes and the UTC permit division of a single trust into two or more trusts with substantially similar terms. Division may be advantageous for tax avoidance or to minimize conflicts between beneficiaries.