Modification and Termination of Trusts Under the Ohio Trust Code: A Drafter's Guide

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Categories:

Publications

Chapter 4 of Ohio Trust Code, and specifically, Ohio Revised Code Sections 5804.10 through 5804.17 provide a series of interrelated rules governing when a trust may be terminated or modified other than by its express terms.[1] In most cases, these terminations or modifications must be made by a court, but in two instances, a trustee may have that authority.2 Some of these rules represent a departure from prior Ohio law, and the provisions relating to the modification and termination of trusts are some of the more controversial provisions of the Ohio Trust Code. Although the comments to the Uniform Trust Code state that the overall objective of these sections is to enhance flexibility consistent with the principle that preserving the settlor's intent is paramount, some may argue that the ability to carry out the settlor's intent is jeopardized by these provisions. Just as the probate and trust law practitioner needs to be familiar with the flexibility that some of these statutes provide for revising trust arrangements once thought to be truly irrevocable, the estate plan drafter needs to be aware of how these provisions operate so as to draft for, or around, these provisions. This article will address both sides of that "drafting coin".

Modification or Termination of Non-Charitable Irrevocable Trusts By Consent of the Settlor and the Beneficiaries

Ohio Revised Code § 5804.11 provides that if the settlor and all the beneficiaries consent, the court must enter an order approving modification or termination of the trust, even if the modification or termination is inconsistent with a material purpose of the trust. The court must distribute the trust property as agreed by the beneficiaries. The Code addresses how a settlor's consent can be obtained if he is incapacitated. An agent under a power of attorney may exercise the settlor's power to consent to a trust's

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modification or termination, but only to the extent expressly authorized by both the power of attorney and the terms of the trust.

Drafting point: Consider whether to include such authorization in the power of attorney and the trust.

The provisions relating to the termination or modification of a trust by the settlor's and the beneficiaries' consent apply only to:

- Irrevocable trusts created on or after January 1, 2007;
- Revocable trusts that become irrevocable on or after January 1, 2007; and
- Do not apply to non-charitable irrevocable trusts described in 42 USC 1396p(d)(4) [Medicaid Pay Back Trusts; Federal Special Needs Trusts].

Modification or Termination of Non-Charitable Irrevocable Trust Upon Consent of the Beneficiaries

If the settlor is not involved in an action to modify or terminate a trust due to death or incapacity, or if the settlor does not consent, Ohio Revised Code § 5804.11 still allows a trust to be modified or terminated under certain circumstances. Specifically, a trust can be terminated if all the beneficiaries consent and the court concludes that the continuance of the trust is not necessary to achieve any material purpose of the trust.[4] Upon ordering such a termination, the court must distribute the property as agreed by the beneficiaries.[5] Further, the court may modify an irrevocable trust without settlor involvement if all the beneficiaries consent and the court finds that modification is not inconsistent with a material purpose of the trust. Note, however, that trusts cannot be modified to remove or replace the trustee through the consent of all the beneficiaries. Also note that the statute specifically states that a spendthrift provision may, but is not presumed to, constitute a material purpose of the trust.[6]

Drafting point: Ohio Revised Code § 5801.04, the provision of the Ohio Trust Code that sets forth the mandatory rules which cannot

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be waived in the trust instrument, provides that the terms of the trust cannot override the power of the court to modify or terminate the trust under Sections 5804.10 through 5804.16 of the Ohio Revised Code. Therefore, estate planners need to consider drafting to protect a trust from a modification or premature termination that would not conform to the settlor's intent. For instance, the trust instrument should make clear the material purposes of the trust. Such a recitation of the material purposes may make it more difficult for beneficiaries to obtain court approval of a trust modification or termination. If creditor protection is one of the objectives of the trust, the drafter will want to include a spendthrift provision (being careful to follow the requirements of Ohio Revised Code § 5805.01 governing spendthrift provisions) and specifically state in the trust instrument that the spendthrift provision is a "material purpose" of the trust so that the trust cannot be terminated if the beneficiary has creditor problems.

Finally, from a drafting standpoint, consider the Ohio Trust Code's treatment of uneconomic trusts. Ohio Revised Code § 5804.14 provides two ways to modify or terminate an uneconomic trust: by trustee action or court action. A trustee of a trust with a corpus having a total value of less than $100,000 may terminate the trust after notice to qualified beneficiaries if the trustee concludes that the value of the trust property is insufficient to justify the cost of administration. Further, if a trust consists of trust property having a total value of less than $100,000, the court may modify or terminate the trust, or remove the trustee and appoint a different trustee, if it determines that the value of the trust property is insufficient to justify the cost of administration.

Drafting point: The power of a trustee (but not the court) to terminate an uneconomic trust can be waived or modified. Generally, this power should not be waived in the trust instrument unless the trust is established for a beneficiary with special needs or creditor issues. The statute specifically states that a spendthrift clause does not preclude the termination of an uneconomic trust.

In practice, an action to terminate or modify an irrevocable trust where the settlor has died often will be brought by the trustee. In such cases, all the current and potential trust beneficiaries would

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be named defendants. The provisions of Article 3 of the Ohio Trust Code on representation, virtual representation, and the appointment and approval of representatives appointed by the court are used to determine whether all beneficiaries have consented to the action.7 Although these actions for trust modification or termination often are brought by the trustee, note that a trust may be modified or terminated over a trustee's objection. Ohio Revised Code § 5804.10 provides the trustee standing to object to a proposed termination or modification. Although a private settlement agreement may be used to modify a trust, Ohio Revised Code § 5801.10(C) specifically states that a private settlement agreement may not be used if it effects "a termination of the trust before the date specified for the trust's termination in the trust instrument." Therefore, to effect an "early termination" of a trust, Ohio Revised Code § 5804.11 must be used. The following is a sample complaint drawn under that section for the termination of a trust where all the beneficiaries consent and it is asserted that continuance of the trust is not necessary to achieve any material purpose of the trust. Also included are sample consents to be executed by the adult current and remainder beneficiaries. As in many cases involving early termination of a trust, virtual representation is not available for the representation of minor and unborn beneficiaries due to an inherent conflict between those beneficiaries' interests and the interests of the adult remainder beneficiaries. Therefore, a sample application for the appointment of a guardian ad litem and trustee for unborn is included.

ENDNOTES:

* For additional suggestions on court action on trusts, see the preceding article by Robert M. Brucken on filing PSAs in court.

1. English, David, General Comment – Article 4, Comments on the Uniform Trust Code as included in OSBA CLE Reference Manual Ohio Trust Code, NCCUSL Comments, p. 3.27.

2. Upon appropriate findings, a court may:

- modify or terminate a noncharitable irrevocable trust if certain parties have consented (R.C. § 5804.11);

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- modify the administrative or dispositive terms of a trust or terminate a trust because of unanticipated circumstances, impracticality or impairment (R.C. § 5804.12);
- modify or terminate a charitable trust using cy pres (R.C. § 5804.13);
- reform the terms of a trust to conform to the settlor's intention if the settlor's intent and the terms of the trust were affected by a mistake of fact or law (R.C. § 5804.15);
- modify the terms of a trust to achieve the settlor's tax objectives (R.C. § 5804.16);

With respect to "uneconomic trusts," as defined in R.C. § 5804.14, a court has the power to modify or terminate a trust or change trustees of trusts having a value of less than $100,000. In addition, after notice to qualified beneficiaries, a trustee may terminate a trust having assets of less than $100,000 if the trustee concludes that the value of the trust property is insufficient to justify the cost of administration. See R.C. § 5804.14. Finally, after notice to qualified beneficiaries, a trustee may combine two or more trusts or divide a trust into separate trusts. See R.C. § 5804.17.

3. R.C. § 5804.11(A)
4. R.C. § 5804.11(B)
5. R.C. § 5804.11(C)
6. R.C. § 5804.11(B)
7. See R.C. § 5803.01-.05

APPENDIX A
IN THE COURT OF COMMON PLEAS
PROBATE DIVISION
[_____] COUNTY, OHIO

GEORGE WHITE, TRUSTEE
OF THE ELIZABETH BLACK TRUST
AGREEMENT dated December 22, 1986
Case No.:
Plaintiff,
v.
RICHARD A. BLACK
COMPLAINT FOR

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TERMINATION OF TRUST
and
SALLY BLACK SMITH
and
DANIEL C. SMITH
and
MICHAEL F. SMITH
and
GARETH L. BLACK
and
DEBORAH S. BLACK
and
DAVID J. BLACK
and
ALLISON E. SMITH
and
BENJAMIN C. SMITH
and
MARY K. BLACK
and
LINDA R. BLACK
and
EMMA S. BLACK
and
SAMUEL W. BLACK
and
Jane Does and John Does
unborn issue of Sally Black Smith and
unborn issue of Richard A. Black,
Defendants.

This is an action pursuant to Ohio Revised Code §5804.11(B) for the termination of the trust held under Article V of the Elizabeth Black Trust Agreement dated December 22, 1986 (the "Trust"). A true copy of the Elizabeth Black Trust Agreement is attached hereto as Exhibit A.

1. Elizabeth Black created the Elizabeth Black Trust Agreement (the "Trust Agreement"),
as Grantor, on December 22, 1986, and named George White

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Trustee of the Trust
Agreement. George White has served as Trustee of the Trust Agreement since the
creation of the Trust Agreement on December 22, 1986.
2. Elizabeth Black died on February 6, 1990 and upon her death, the Elizabeth Black
Trust Agreement became irrevocable.
3. Plaintiff, George White, brings this action at the request of Elizabeth Black's children
and grandchildren.
4. Defendants Sally Black Smith and Richard A. Black are the only children of Elizabeth
Black and her husband, Harvey Black, and both are adults.
5. Harvey Black died on November 6, 2005.
6. Defendants Daniel C. Smith and Michael F. Smith are the only living children of Sally
Black Smith and are adults.
7. Gareth L. Black, Deborah S. Black, and David J. Black are the only children of Richard
A. Black, and are all adults.
8. The Trust Agreement requires that upon the death of Elizabeth Black (the "Grantor"),
the trust assets be held as one trust for the benefit of the Grantor's husband and the
Grantor's children under Article V of the Trust Agreement. Specifically, the Trust
Agreement provides:
[Insert pertinent portion of Trust Agreement]
9. The Trust Agreement contains inconsistent provisions, such that a dispute has arisen as to the intended disposition of the trust assets at the death of the Grantor's husband. Defendants Richard A. Black and his children contend that the Trust must be maintained as one trust for the benefit of the Grantor's two children, until the death of the later to die of the Grantor's two children, at which time the trust assets are to be distributed to the Grantor's then living lineal descendants, per stirpes. Such an interpretation would require an equal division among the five grandchildren of the Grantor, with the issue of a deceased grandchild succeeding to such grandchild's share on a per stirpital basis. Defendants Sally Black Smith and her

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two children contend that upon the death of Harvey Black, the Trust was intended to be split into equal separate shares for the Grantor's children, which shares were to be held for each child's benefit during his or her lifetime. Upon a child's death, the assets held in the separate share trust would pass to such child's issue, per stirpes. As shown herein, all the adult potential beneficiaries of the Trust agree with the resolution of this inconsistency by the termination of the Trust and distribution of the Trust assets according to the percentages set forth herein.

10. Defendants are all the living persons who are or may be beneficiaries of the Trust and the unborn issue of Elizabeth Black.

11. Currently there are six (6) great-grandchildren of Elizabeth Black, all of whom are minors. All living great-grandchildren will be represented in this action by a Guardian ad Litem, to be appointed by this Court. All unborn issue of Elizabeth Black who may become beneficiaries of the Trust will be represented in this action by a Trustee for Unborn, to be appointed by this Court.

12. Thus, all possible beneficiaries of the Trust are or will be before this Court.

13. As evidenced by the Waivers of Service of Process and Consents filed herewith, all the adult potential beneficiaries of the Trust have consented to the termination of the Trust and the distribution of its assets among the living grandchildren of Elizabeth Black in the following manner:

Daniel C. Smith 20%
Michael F. Smith 20%
Gareth L. Black 20%
Deborah S. Black 20%
David J. Black 20%
100%

Respectfully submitted,

_____
Attorney for Plaintiff

APPENDIX B
IN THE COURT OF COMMON PLEAS
PROBATE DIVISION
[ ] COUNTY, OHIO
GEORGE WHITE, TRUSTEE OF THE

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ELIZABETH BLACK TRUST AGREEMENT
dated December 22, 1986,
Plaintiff,
Case No.:
v.
RICHARD A. BLACK, ET AL.,
WAIVER OF SERVICE OF
Defendants.
PROCESS OF COMPLAINT
FOR TERMINATION OF
TRUST AND CONSENT TO
TERMINATION OF TRUST

I, Deborah S. Black, do hereby waive service of process in the above-captioned matter and direct that all further process be served upon my counsel, Robert Martin, Attorney at Law, [Law Firm Name].

Further, as a daughter of Richard A. Black and a granddaughter of Elizabeth Black, I am a potential remainder beneficiary of the assets currently held in trust under Article V of the Elizabeth Black Trust Agreement dated December 22, 1986. I hereby consent to the termination of the Trust and, after payment of proper expenses, distribution of the Trust assets in the following manner:

Daniel C. Smith 20%
Michael F. Smith 20%
Gareth L. Black 20%
Deborah S. Black 20%
David J. Black 20%
100%

_____
Deborah S. Black

APPENDIX C
IN THE COURT OF COMMON PLEAS
PROBATE DIVISION
[ ] COUNTY, OHIO
GEORGE WHITE, TRUSTEE OF THE
ELIZABETH BLACK TRUST AGREEMENT
dated December 22, 1986,
Plaintiff,

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Case No.:
v.
RICHARD A. BLACK, ET AL.,
WAIVER OF SERVICE OF
Defendants.
PROCESS OF COMPLAINT
FOR TERMINATION OF
TRUST AND CONSENT TO
TERMINATION OF TRUST

I, Sally Black Smith, do hereby waive service of process in the above-captioned matter and direct that all further process be served upon my counsel, Katherine Brown, Attorney at Law, [Law Firm Name].
Further, as a current beneficiary of the Trust held under Article V of the Elizabeth Black Trust Agreement, I hereby consent to the termination of the Trust and, after payment of proper expenses, distribution of the Trust assets to the grandchildren of Elizabeth Black in the following manner:
Daniel C. Smith 20%
Michael F. Smith 20%
Gareth L. Black 20%
Deborah S. Black 20%
David J. Black 20%
100%

_____
Sally Black Smith

APPENDIX D
IN THE COURT OF COMMON PLEAS
PROBATE DIVISION
[ ] COUNTY, OHIO

GEORGE WHITE, TRUSTEE
OF THE ELIZABETH BLACK TRUST
AGREEMENT dated December 22, 1986,
Plaintiff,
Case No.:
v.
RICHARD A. BLACK, ET AL.,

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Defendants.
APPLICATION FOR
APPOINTMENT OF GUARDIAN
AD LITEM
TRUSTEE FOR UNBORN

Applicant is Plaintiff in the above-referenced action brought under Ohio Revised Code § 5804.11(B) for the termination of the Trust held under Article V of the Elizabeth Black Trust Agreement dated December 22, 1986. Ohio Revised Code § 5804.11(B) provides that a noncharitable irrevocable trust may be terminated upon consent of all the beneficiaries if the Court concludes that continuance of the Trust is not necessary to
achieve any material purpose of the Trust. In this case, the current Trust beneficiaries are Elizabeth Black's children, Sally Black Smith and Richard A. Black. The remainder beneficiaries are the grandchildren of Elizabeth Black, who are Defendants herein. However, should a grandchild die before the Trust is terminated, his or her share will be distributed to his or her issue, per stirpes. Currently, there are six (6) great-grandchildren
of Elizabeth Black in being, all of whom are minors. The great-grandchildren of Elizabeth Black who are in being, as well as any unborn issue of Elizabeth Black have interests which are adverse to those of Elizabeth Black's children and grandchildren. As such, the class of potential remainder beneficiaries consisting of the great-grandchildren in being and future lineal descendants of Elizabeth Black cannot be represented in this action by either of the current beneficiaries or by the adult remainder beneficiaries of the Trust under the doctrine of virtual representation.

THEREFORE, Plaintiff respectfully requests this Court for an order appointing the same individual Guardian ad Litem to represent the interests of the living great-grandchildren of Elizabeth Black and Trustee for Unborn to represent the interests of the unborn future lineal descendants of Elizabeth Black, all of whom are potential remainder beneficiaries under the Trust.

_____
Plaintiff's Attorney

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