

Chapman Client Alert

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Current Issues Relevant to Our Clients

The New Illinois Trust Code: What It Means for Trustees and Trustmakers, Part III

This Alert is the third installment in a six-part series on the new Illinois Trust Code (“ITC”), a version of the Uniform Trust Code (“UTC”), which goes into effect on January 1, 2020. This series highlights the significant changes to Illinois law and also notes where the Illinois statute varies from the UTC. Trustees, both individual and corporate, should be aware of these expanded powers, and trustmakers (the creators or settlors of a trust) and their advisors should also be aware of these changes and consider the impact they may have on how trust property is managed.

This Alert covers the new rules that apply to the modification or termination of irrevocable trusts. The ITC follows the UTC’s approach for the modification and early termination of irrevocable trusts. The UTC approach is more expansive than the standard applied in prior Illinois caselaw. Previously, Illinois courts applied a narrower standard to requests to modify or terminate an irrevocable trust. Essentially, a court could modify or terminate a trust if: (1) there was a scrivener’s error, (2) the trust property was in serious danger of depletion or waste, in circumstances not contemplated by the settlor, and modification or termination would better effectuate the intent of the settlor, or (3) the beneficiary was in dire or severe financial straits, in circumstances not contemplated by the settlor, and modification would better effectuate the intent of the settlor. These facts had to be established by clear and convincing evidence. While the ITC follows the UTC’s broader standards, certain modifications and early terminations will require the approval of a court.

Modification – By Agreement Only

Illinois has long recognized the use of nonjudicial settlement agreements (“NJSAs”), by statute, to address a variety of matters regarding trusts. The ITC maintains many of the same statutory rules regarding the matters that can be addressed by an NJSA: (1) interpretation or construction of a trust, (2) modification of the administrative terms of a trust, (3) a change in the governing law or place of administration of a trust, and (4) resolution of disputes, etc.

However, the ITC omits one category that the prior Illinois statute contained. Previously, the Illinois statute on NJSAs included a catchall provision—an NJSA could address “any other matter involving a trust to extent the terms and conditions of the [NJSA] could be properly approved under applicable law by a court.” The ITC does *not* have this catchall.

The deletion of this catchall was deliberate. As discussed in this Alert, courts will have a broader standard to modify or terminate a trust. Had the catchall provision remained in the ITC, an NJSA could have been used to modify an irrevocable trust under the new, broader standards, so long as the trustees and beneficiaries were in agreement. By omitting the catchall, a modification that is unrelated to the resolution of an issue listed in the NJSA statute will require court approval.

The impact of this change to the NJSA statute is significant in one respect for modifications. An agreement that involves a

modification of a *beneficial interest*, which is unrelated to an interpretation or construction (e.g., resolution of an ambiguity) or resolution of a bona fide dispute or a dispute where the resolution does not conflict with a clear material purpose of the trust, must be done with court approval and finding as discussed below.

The lack of the catchall provision in the ITC does not diminish the usefulness of NJSAs—the ITC still has a laundry list of issues that can be addressed by an NJSA, as noted above. A future installment of this series will cover in more detail the new rules on representation, what parties are required for a valid NJSA and the uses of NJSA.

Modification – By Court with Beneficiary Consent

Under the ITC, a court has much broader authority to modify an irrevocable, noncharitable trust if *all* of the beneficiaries consent. Notably, a trustee’s consent is not required by the statute. However, nothing in the statute prevents a trustee from objecting. If all beneficiaries consent, a court may modify any noncharitable, irrevocable trust so long as the modification is not inconsistent with the material purposes of the trust. To satisfy the requirement of beneficiary consent, all beneficiaries (current and future) must provide consent or be represented by a person who is providing consent. The statute does permit modification, even if not all beneficiaries consent, so long as the court also finds that the nonconsenting beneficiary is being treated equitably.

Modification – By Court upon Request of Any Interested Party

Upon petition by any beneficiary, any trustee, any settlor or the attorney general (in the case of a charitable trust), a court may modify any irrevocable trust, whether charitable or not, if the current terms are impracticable or cause waste or impair administration and if the modification is of the administrative terms only. In addition, if there has been a change in circumstances not anticipated by the settlor and modification would further the purposes of the trust, the court may modify any terms of the trust.

Termination – By the Trustee

Under the ITC, as with prior Illinois law, a trustee may terminate any trust under \$100,000 if it determines that it is uneconomical to continue the trust. (Note that a trust agreement may provide a different threshold value for a small trust termination. Because the ITC is the default rule, the terms of the trust agreement will control.) Under the ITC, a trust will also terminate if no purpose of the trust remains to be achieved, or if the purposes of the trust have become unlawful, contrary to public policy, or impossible to achieve.

Termination – By Court

A court may approve the early termination of a trust if (1) the trust is noncharitable, all of the beneficiaries consent, and the court finds that continuation of the trust is not necessary to achieve any material purpose of the trust, (2) there is a change in circumstances not anticipated by the settlor and termination would further the purposes of the trust, or (3) the court determines that the value of the trust property is insufficient to justify the costs of administration.

Conclusion

For trustees and beneficiaries, the new provisions of the ITC provide some flexibility to address irrevocable trusts whose circumstances have changed significantly.

For trustmakers and their advisers, careful thought should be given to the purposes of a trust. If continuation of a trust for a certain term or for life is material to the trustmaker, the trust instrument should reflect that purpose. In addition, if creditor protection is a material purpose in the creation of a trust for a beneficiary, the trust agreement should also reflect this purpose.

For More Information

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