

TIPS OF THE TRADE: DIRECTED TRUSTS: A FURTHER EXAMINATION

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I. SYNOPSIS

In a prior issue of the *Trusts & Estates Quarterly* (Vol. 30, Issue 4), the article "A Planner's Guide to the Long Awaited California Uniform Directed Trust Act," by David Khanjyan, Esq., and Michael Rosen-Prinz, Esq.,⁰¹ discussed California's new Uniform Directed Trust Act ("CUDTA") and made comparisons between California's legislation and that in Delaware and Nevada. In a nutshell, under the CUDTA a settlor can now, in a practical way, allocate fiduciary authority, duty, and liabilities amongst directed Trustees, trust directors, and co-trustees.

Building upon that discussion, let us now explore: (1) specific scenarios when a settlor may want to use a directed trust arrangement; (2) how the CUDTA enables estate planning with co-trustees with allocated duties who are not responsible for overseeing each other's performance of such duties; (3) how the relationship between the directed trustee and trust director, and the relationship between co-trustees, may possibly benefit from a trust protector; (4) a "how to" drafting approach for an estate planner using the CUDTA to achieve tailored fiduciary arrangements; and (5) how the Probate Code still needs to catch up to the CUDTA.

II. TRUST DIRECTOR SCENARIOS

The Uniform Directed Trust Act's ("UDTA") potential is to solve problems or limitations arising with one trustee having all trustee duties, powers, and liabilities. Drafting directed trusts entails understanding the trustee's duties and powers found in the Probate Code,⁰² common law,⁰³ and the trust itself.

A. Discretionary Distributions

A possible use of the CUDTA might be to appoint a trust director in a special needs trust with sole authority for all

discretionary distributions for the special needs beneficiary. Such a trust director might possess special expertise in government benefits law and so would better know when, how, and what distributions to make and what not to make. The administrative directed trustee might be a family member who is willing to be responsible for all other aspects of the trust administration and to work under the trust director's control.

Other discretionary distribution scenarios include: (1) the bypass and marital trusts, where the surviving spouse might be trustee and someone else can be the trust director; and (2) the support trust where a private fiduciary serving as trustee may control everything, but have distribution decisions made by a trusted family member.

B. Investment Decisions

A primary reason (driving force) the UDTA was enacted in California and elsewhere, is to allow large trust companies to act as directed trustees without the trust company becoming liable for imprudent investment decisions made by the client's trusted financial advisors acting as trust director (for investments).

These trust directors are selected by settlors because of the desire to achieve investment objectives that might violate the duty to diversify and/or not to invest in speculative and/or high-risk assets.

For example, a settlor may want to invest heavily in cryptocurrency, and a corporate trustee might well refuse. Naturally, the trust instrument itself would need to waive California's statutory diversification and risky asset rules that prohibit the trust director from making such trust investments.⁰⁴

C. Managing Special Assets

A trust may contain special assets which the settlor may want managed, in one or more ways, by a trusted advisor, such as the following.

1. Artwork

Art consultant elevated to trust director to control marketing and sale of artwork. For example, a settlor may want to involve special art consultants to decide the *price*, *where* (i.e., at what studios) and *how* (i.e., the setting and display) the artwork is sold. The settlor may feel that their objectives are best achieved if such decisions are made by a special consultant of the settlor's own choosing. Otherwise, a trustee without the necessary expertise would have a fiduciary duty to hire relevant art experts. Now, the settlor can proactively address this issue.

2. Rental Property

Property manager appointed as trust director to decide all management issues related to trust owned real property (including property held in an LLC). The directed trustee would implement such decisions either personally or through trustee supervised agents.

3. Control over Business Interests

Business consultant(s) appointed as trust director(s) or co-trust directors to make some or all decisions related to owning, managing, and selling the trust's interest in a business entity. The settlor may want trusted advisors (even family) to act collectively as a team of co-trust directors with authority over the trust's ownership of a business interest. These directors could act like a board of directors with the directed trustee acting like the chief executive officer in charge of implementing trust director resolutions and handling day to day administration.

4. House Trusts

A family home held in trust for multiple family members must allocate the trust benefits (shared use of the house) and burdens (expenses associated with the house and trust administration) amongst various beneficiaries. A trust director, perhaps a property management company, could make such allocations and direct the trustee to enforce the same.

5. Education Trusts

Consider an education trust that includes an academic evaluation standard to evaluate whether the student beneficiary should continue to receive trust benefits. The settlor may wish to entrust a particular person with

discretion to evaluate the student's progress and with the personal connection.

D. Trustee with Conflict of Interests

Particular and important administration issues may arise for which the settlor wants specific person(s), or a specific type of person, in control, for one reason or another. For example, the settlor may want a trusted family member or close friend to control the division of valuable personal property amongst family members, to avoid any intra-family disagreements. If the trustee is also a beneficiary, then having a non-beneficiary in control removes the self-interested trustee from a conflict of interest. Also, the settlor may need an independent fiduciary as trust director to authorize distributions from an asset protection trust that would otherwise be inappropriate for the trustee to make as a related party.

E. Ad Hoc Trust Director

A creative application of the CUDTA, perhaps pushing the envelope, is a trust that appoints a trust protector with the power to appoint an ad hoc trust director whose duties and powers are fashioned by the trust protector to meet the occasion. This would arise if the trust protector needs to direct the trustee but wants to avoid having to file a petition for instructions with the court. Such a trust would say that the trustee has full duty and powers unless and until such time when the trust protector appoints a trust director, at which time the trustee becomes a directed trustee pursuant to the trust protector's appointment of a trust director.

III. THE TRUST PROTECTOR AS A HELPFUL ADJUNCT TO THE CUDTA

A. Managing Disagreements Between Directed Trustees and Trust Directors

The administrative directed trustee may only be directed by the trust director regarding those aspects of the trust administration within the trust director's authority. That begs the question, what if the trust director and directed trustee disagree over who has authority?

1. Authority

The Probate Code does not mention "trust protectors" anywhere. Talking about a "trust protector" may, therefore, sound like discussing a *chimera*. Nonetheless, for years, California irrevocable trusts, including special needs trusts, have incorporated trust protectors, generally, with the following types of authority: (1) to hire, fire, and replace

trustees; (2) to modify the terms of the trust without going to court; and (3) to correct ambiguities in the trust.

Whether a trust protector is or is not a fiduciary has been the subject of much contention. However, if a trust protector is utilized in a directed trust, they would need to be fiduciary, the same as the directed trustee and the trust director, to resolve disagreements between fiduciaries.

2. Resolving Disagreements

Presently, the Probate Code allows only a trustee or trust beneficiary to petition the court for instructions.⁰⁵ That does not help a trust director should a directed trustee refuse to follow a direction.

Accordingly, a trust protector who has both the fiduciary duty and authority to resolve such conflicts would mean that the directed trustee and the trust director can each rely on the trust protector's resolution. However, if the directed trustee does not follow the trust protector's decision, then the trust protector also does not necessarily have standing under Probate Code section 17200 to file a petition for instructions.⁰⁶ While the Court of Appeal in *Hamlin v. Jendayi* (2024) 105 Cal.App.5th 1064 ("*Hamlin*")⁰⁷ held that filing a petition under Probate Code section 17200 is not limited to trustees and trust beneficiaries, in the context of a trust contest, the question of whether or not that decision supports standing for a trust protector is not yet established.⁰⁸

In *Hamlin* the court opined,

We begin with the general observation that "standing for purposes of the Probate Code is a fluid concept dependent on the nature of the proceeding before the trial court and the parties' relationship to the proceeding, as well as to the trust (or estate). "(*Arman v. Bank of America* (1999) 74 Cal.App.4th 697, 702-703 [88 Cal.Rptr.2d 410].)⁰⁹

Moreover, in *Hamlin*, the party asserting standing under Probate Code section 17200 was a disinherited heir entitled to notice of the trust's administration and with statutory standing to object to the terms of the trust.¹⁰ Without standing, a disinherited heir would not be able to petition the court under Probate Code section 17200 to contest the trust.

On the other hand, if the trust protector's relationship to the trust and its assets is that of a fiduciary, who is not personally entitled to receive any trust distributions, then that trust protector has no personal interest in the trust and its administration. Moreover, trust protectors are nowhere mentioned or described in the Probate Code. Thus, it appears unlikely that a trust protector acting as a fiduciary would have standing under Probate Code section 17200,

notwithstanding the *Hamlin* decision. A trust beneficiary, however, does have standing to petition the court.¹¹

IV. EXTENDING THE DIRECTED TRUST PARADIGM TO CO-TRUSTEES

The CUDTA expressly allows the directed trust rules regarding duty and liability (discussed above) to apply to the duties and relationships between co-trustees.¹² That is, the CUDTA allows co-trustees to divide (compartmentalize) whole areas of the trust administration between themselves such that co-trustees are no longer responsible for each other's own fiduciary duties under the trust's arrangement.

The CUDTA also may more narrowly be utilized to allow co-trustees to segment out responsibility between themselves for one or more aspects of the trust administration to allow co-trustees different involvements and responsibilities. For example, a co-trustee with a conflict of interest may be removed from certain aspects of the trust administration under the terms of the trust and relieved of any duties under sections 16012 and 16013 for the other co-trustee's exercise or non-exercise of the power that the trustee with the duty has regarding this particular aspect of the trust administration.

Otherwise, generally speaking:

[t]he trustee [still] has a duty not to delegate to others the performance of acts that the trustee can reasonably be required personally to perform and may not transfer the office of trustee to another person nor delegate the entire administration of the trust to a co-trustee or other person [emphasis added].¹³

Under the CUDTA, co-trustees may now each be responsible for different areas of the trust administration, the same way as trust directors and directed trustees each have their own segmented areas of control without having to monitor each other. Again, a trust director is a fiduciary the same as a trustee, so it is logical to allow co-trustees a very similar bifurcated fiduciary arrangement between each other.

A. Compartmentalized and Segmented Co-Trustee Scenarios

1. Spousal Joint Trust

Spouses often establish joint trusts that they fund with both community property and separate property assets. Typically, the spouses are co-trustees. The trust could compartmentalize the settlors' separate property assets as being separately managed by the co-trustee spouse who contributed such assets. Unless substantial separate property assets are involved the compartmentalized co-trustee approach could be appropriate.

2. *Special Co-Trustee with Professional License*

A special co-trustee with a relevant professional license may have exclusive authority to control and to manage the settlor's professional (licensed) practice (e.g., a dentistry), if the professional settlor were to become incapacitated or die. The settlor's spouse, however, might be the other co-trustee with general control over all other trust assets and affairs. The settlor's spouse still has authority to receive assets from the special co-trustee managing the settlor's professional practice (such as money). The spouse as general co-trustee would administer the trust for the benefit of the settlor's family while the special co-trustee winds up the settlor's professional practice.

3. *Special Co-Trustee Administering Out of State Assets*

A co-trustee may be appointed with exclusive authority to manage trust owned real property assets located outside of California. The other California co-trustees would be relieved of responsibility for such assets. Essentially, the result would be parallel trust administrations occurring in California and elsewhere under the same trust provisions. This compartmentalization protects the California trustees from both responsibilities and liabilities associated with ownership and management of such out-of-state assets.

4. *Co-Trustees of a Blended Family Trust*

Later in life second marriages where the spouses' prior children do not really know one another can result in the spouses naming co-trustees from each side of the marriage. While many aspects of the trust administration may be jointly handled by the co-trustees, perhaps the control and distribution of each spouse's separate property heirlooms to their own children may be a segmented aspect of the trust administration. That is, the co-trustee who represents the spouse owning the separate property would control and distribute the property. Also, as mentioned above, given that such trustee is also likely a beneficiary, to the extent that there is any discretion involved in the distribution of these heirlooms, a trust director could be involved to direct how the trustee distributes the heirlooms. This approach would see CUDTA applied both to create a directed trust and to create a special co-trustee arrangement.

5. *Co-Trustees with Conflicts of Interest*

If one or the other of a co-trustee has a conflict of interest with respect to any one or more aspects of the trust administration, then the trust could provide that with respect to such conflict that the non-conflicted co-trustee have full sole decision-making authority. This segmentation of a specific aspect within the overall trust administration could

prove helpful with respect to tax sensitive decisions and discretionary distributions.

V. AREAS IN PROBATE CODE THAT NEED TO BE UPDATED

The discrete addition of the CUDTA as its own standalone Chapter 6 within Part 4 [Trust Administration] of Division 9 [Trust Law] of the Probate Code left other related sections within Division 9 unamended. With the CUDTA's segmentation of fiduciary duties, the following sections of the Probate Code appear to lag behind the times and need to be updated to reflect the CUDTA.

A. Probate Code Section 16012

Section 16012, subdivision (b), requires a trustee who has properly delegated a duty to a co-trustee to exercise general supervision over the co-trustee performing the delegated function.¹⁴ This supervision requirement may appear to conflict with section 16622 of the Probate Code that relieves a co-trustee of duty and liability with respect to another co-trustee's exercise or non-exercise of a power of the other co-trustee that such trustee is given under the trust instrument.¹⁵ However, the important difference here is that section 16012 speaks to delegated functions and section 16622 speaks to duties allocated under the trust instrument without co-trustee delegation between themselves.

B. Probate Code Section 16612

Section 16612 of the Probate Code expressly considers the possibility of a power of direction that is jointly held by a trustee and a trust director.¹⁶ However, section 16602, subdivision (d), which defines a power of direction, expressly prohibits a power of direction being held by a person acting as trustee.¹⁷ Thus, section 16612 appears to be directly at odds with the very definition of power of direction in section 16602, subdivision (d).

C. Probate Code Section 17200

Section 17200, subdivision (a), of the Probate Code allows a trustee or a trust beneficiary to petition the court concerning the internal affairs or the existence of a trust.¹⁸ Section 17200, subdivision (a), does not allow a trust director to petition the court for instructions or to instruct a trustee to follow a trust director's direction. What recourse does a trust director have to remedy the situation where the directed trustee does not comply with a direction given within the trust director's given power or extended power? Also, if a trust protector is employed to resolve such conflicts, what recourse does a trust protector have to remedy a situation created by a recalcitrant directed trustee?

D. Probate Code Section 18100.5 - Certification of Trust

The statutory certification of trust is an instrument signed by a trustee to certify the existence of a trust and certain pertinent information, including the powers of the trustee and the identity of the trustees.¹⁹ Such certificate is for the benefit of third parties with whom the trustee wants to transact business.²⁰ Given the CUDTA, the foregoing is now insufficient with respect to directed trusts.

First, the trust director and the scope of their powers of direction need to be discussed. Second, if co-trustees are segmenting their duties and responsibilities over trust matters between themselves, then the scope of each co-trustee's duties and responsibilities need to be discussed. Otherwise, the certificate of authority is misleading and inadequate to its intended purpose of enabling third parties to know relevant information as to what each signatory fiduciary can and cannot do with respect to managing the trust's affairs.

VI. DRAFTING TRUSTS USING THE CUDTA

The CUDTA allows estate planning attorneys to redefine how any and all aspects of trust administration are managed by directed trustees and co-trustees. Seeing the drafting opportunities offered by the CUDTA requires awareness of those trust administration scenarios that might benefit from utilizing either a trust advisor or a compartmentalized or segmented co-trustee approach. Here is a possible systematic approach to applying the CUDTA in estate planning.

1. Decide whether you need an additional fiduciary, beyond the trustee, with independent authority involved in the trust administration.
2. Decide whether to use (a) the directed trustee and trust director approach, or (b) the compartmentalized co-trustees (general and special co-trustees) approach.
 - a. If only a narrow part of the trust administration requires an additional fiduciary then the trust director approach is more appropriate; but
 - b. If certain assets require broad or exclusive administration by an additional fiduciary acting alone then the co-trustee approach is needed.
3. Delineate (carve-out) the responsibilities of either trust director or special co-trustee, as relevant, that are removed from the directed trustee or the general co-trustee, as relevant. Define the power of direction or the scope of the special co-trustee's authority and duties, as relevant, using the following

considerations, as appropriate, to allocate certain aspects of trust administration to such fiduciaries.

- a. Duties – Allocating certain statutory and/or common law trustee duties to the trust director or the special co-trustee can be used as part of (or as the whole) delineation.
Example: The trust director has the exclusive fiduciary duty to make investment decisions, as defined in section __ of the Probate Code, involving all trust assets and direct the trustee to implement such decisions.
 - b. Powers – Allocating the authority to use a trustee power to the trust director or the special co-trustee can be used as part of (or as the whole) delineation.
Example: The special co-trustee alone shall have the authority to exercise the trustee power to sell the trust's ownership interest in the ABC.
 - c. Assets – Allocating some or all trustee authority, duties, and powers over certain assets to the trust director or special co-trustee can be used as part of (or as the whole) delineation.
Example: The special co-trustee has exclusive authority, duties, and powers over the trust's interest in a medical practice.
 - d. Actions – Allocating certain actions in the trust administration over some or all of the trust assets can be used as part of (or as the whole) delineation.
Example: The trustee shall only exercise the trust's voting rights related to its ownership interests in the ABC corporation upon receiving direction from the trust director as to how to vote.
 - e. Distributions – Allocating the authority to make discretionary distributions of income and principal to some or to all beneficiaries can be used as part of (or as the whole) delineation.
4. Define the fiduciary authority of the directed trustee or the general co-trustee, as relevant, to include all duties and powers not allocated to the trust director or special co-trustee in step #3.
 5. Consider whether the administration would benefit from adding any additional duties or powers to the trust director or special co-trustee, as relevant, just like you would do with respect to a trustee.
 6. Expressly require the trust director or special co-trustee to provide information as needed by the

directed trustee or general co-trustee in order for the directed trustee or general co-trustee to perform their duties with respect to the trust generally.

7. Consider whether adding a trust protector to resolve any disagreements between the directed trustee and the trust director or between the general co-trustee and the special co-trustee, as relevant, would facilitate the administration and avoid court proceedings.
8. If using a trust protector, consider giving the trust protector authority to redefine the delineated scope of authority granted to the trust director or special trustee, as relevant.

VII. CONCLUSION

With the CUDTA, a settlor now has a choice: either place full responsibility for the trust administration on one or more chosen trustees (who thereafter may hire additional expertise, as needed), or select a team of fiduciaries, each with specific tasks, and reduce the overall trustee to being a directed trustee, perhaps one with only ministerial (administrative) type back-office duties. The latter approach is for a settlor who wants to involve specific experts, with powers over the trustee; this may be because the settlor cannot find a trustee willing to administer the assets as the settlor wants. The assembled team of fiduciaries will encompass all fiduciary duties and collectively manage the trust.²¹

Besides the trust director/directed trustee relationship, the CUDTA also allows autonomous co-trustees whose duties are compartmentalized between themselves, parallel to how the duties of a trust director and directed trustee are bifurcated.²² Thus, co-trustees including, for example, a special trustee in charge of a special asset acting alongside a general trustee, may separately administer different assets, almost as if they were administering different sub-trusts. They would still cooperate, as necessary, in the administration of the single trust arrangement, but without such co-trustees overseeing each other.²³

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- 01 Khanjyan & Rosen-Prinz, *A Planner's Guide to the Long Awaited California Uniform Directed Trust Act (2025)* 30 Cal. Tr. & Est. Q., Issue 4.
- 02 Duties in Prob. Code, section 16000 et. seq., and Powers in section 16200 et. seq.
- 03 Prob. Code, section 15002.
- 04 Prob. Code, sections 16047, 16048.

- 05 Prob. Code, section 17200, subs. (a), (b)(6).
- 06 Prob. Code, section 17200, subd. (a).
- 07 *Hamlin v. Jendayi* (2024) 105 Cal.App.5th 1064.
- 08 *Id.* at pp. 1074–1078.
- 09 *Hamlin v. Jendayi, supra*, 105 Cal.App.5th at p. 1074.
- 10 *Id.* at p. 1067.
- 11 Prob. Code, section 17200, subd. (a).
- 12 Prob. Code, section 16622.
- 13 Prob. Code, section 16012.
- 14 Prob. Code, section 16012, subd. (b).
- 15 Prob. Code, section 16622.
- 16 Prob. Code, section 16612.
- 17 Prob. Code, section 16602, subd. (d).
- 18 Prob. Code, section 17200, subd. (a).
- 19 Prob. Code, section 18100.5, subs. (b)(2), (b)(3).
- 20 Prob. Code, section 18100.5, subd. (a).
- 21 Prob. Code, section 16600, subd. (b).
- 22 Prob. Code, section 16620.
- 23 *Ibid.*

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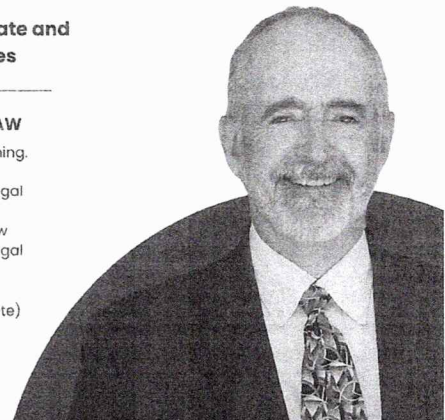
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