

Choice of Law in a Trust

Take-Away: A trust instrument may include a ‘choice of law’ provision that may not ultimately control certain questions when it comes up against another state’s *strong public policy* or the other state is found to have the *most significant relationship* with the trust question.

Background: With Greenleaf Trust now having obtained a national charter, it may more frequently find itself asked to administer a trust subject to another state’s laws. Most trust instruments contain a choice of law provision. A choice of law provision in a trust usually covers three legal concerns: (i) the validity of the trust; (ii) the meaning of the trust terms; and (iii) the trust’s administration. However, implementing a choice of law provision in a trust is not as easy as it sounds.

MTC: The choice of law authorization is found in the Michigan Trust Code (MTC) at MCL 700.7107. That short statute provides:

The meaning and effect of the terms of a trust are determined by the following: (a) The law of the jurisdiction designated in the terms of the trust unless the designation of that jurisdiction’s law is contrary to a strong public policy of the jurisdiction having the most significant relationship to the matter at issue. (b) In the absence of controlling designation in the terms of the trust, the law of the jurisdiction having the most significant relationship to the matter at issue.

Strong Public Policy: MCL 700.7107 is based on UTC Section 107. Unfortunately, the comments to this UTC section do not provide much guidance for how to determine a state’s “*strong public policy*” in contrast to a state’s *normal* or customary public policy when this limitation is reviewed. The UTC comment only provides: “*This section does not attempt to specify the strong public policies sufficient to invalidate a settlor’s choice of governing law. These public policies will vary depending upon the locale and may change over time.*”

In essence this means that a state's *strong public policy* can override a trust instrument's choice of law provision. Examples of some topics for which a state may have a strong public policy against, include: (i) a broad trustee exoneration provision; (ii) a trustee's power to fix valuations for distribution purposes; (iii) a provision that allows a trustee to self-deal; or (iv) a trust that relieves the trustee duty to report to trust beneficiaries, a/k/a a *silent trust*.

Most Significant Relationship: Nor do the comments to the UTC 's section 107 provide any guidance on how to determine which state has '*the most significant relationship to the matter at issue*' if the trust instrument is silent on its choice of law. Nor do the UTC provisions that deal with a trust's governing law address the statutory governing law with respect to issues of trust administration, like the trustee's affirmative duty to disclose information to trust beneficiaries.

Governing Law Missing Provision: If a trust instrument is silent, or there is no clear designation of a governing law in that instrument, the determination of the state with the '*most significant relationship*' usually will take into account the following factors: (i) the place of the trust's creation; (ii) the location of the trust property; (iii) the settlor's domicile; (iv) the trustee's domicile; and (v) the beneficiary's domicile. *Restatement (2nd) of Conflict of Laws, Sections 270, 272*. This *Restatement* also goes on to describe other 'general factors that could be pertinent to the choice of law that governs a trust, to include: (i) the relevant policies of the forum; (ii) the relevant policies of other interested jurisdictions and the degree of their interest; (iii) the protection of justified expectations; and (iv) the certainty and predictability and uniformity of result. *Restatement (2nd) Conflict of Laws, Section 6*.

All of which means that a trustee and settlor will be required to consider all these factors that bear on the settlor's intent and the reasonable expectation of the trust beneficiaries and courts, as well as the different policies of the various states involved. The determination of the state with the '*most significant relationship*' when a trust instrument is silent on the choice of law does not, obviously, permit a straightforward analysis.

Restatement (2nd) Conflict of Laws: This *Restatement* permits a settlor to specify a governing law for matters of trust administration involving *movables*, even when the settlor

and the trustee have no connection with the law of that state. The *Restatement*, Section 272(a), comment c, notes: “[H]e may designate a state which has no connection with the trust.” Even without an express choice of law provision, choice of law is governed by ‘local’ law and does not include the chosen jurisdiction’s conflict of law rules. However, this same *Restatement* also notes that “if a testator fixes the administration of a trust in a state other than his domicile, it is not certain whether the courts will apply the rule of the domicile or the rule of the place of administration,” which apparently then supports the conclusion that a trust instrument’s choice of law provision that opts to apply another state’s law will not necessarily withstand scrutiny by another state.

Rule-of-Thumb: What the UTC 107 tells us is that usually the law of the trust’s principal place of administration will govern administrative questions and the law of the state that has the *most significant relationship* to the trust’s creation will govern the trust’s dispositive provisions.

Yet it is unclear whether the limitations on the settlor’s freedom to choose governing law found in MCL 700.7107(a) apply as well in the context of a governing law clause in a trust instrument that relates to matters of trust administration. To the extent the UTC comments pertain to MCL 700.7107(b), and it applies as well to governing law clauses bearing on matters of trust administration, there will be a need for the trustee to formally establish the principal place of trust administration. The *Restatement (2nd) Conflict of Laws* thus limits the freedom to choose a governing law for trust administration when the matter is one that ‘cannot be controlled by the terms of the trust’ which brings us back to the potential public policy impediment of another state.

Comment: The lack of specificity of MCL 700.7107 with respect to an express choice of law that involves administrative matters, like the settlor’s intent to create a *silent* trust, works to the advantage of a state that is committed to the traditional concept of a trust, like California, that has an express statute that provides that the reporting by a trustee to its beneficiaries cannot be waived by the settlor because it is against California public policy, and any attempt to do so makes that waiver void. [California law, Section 16061.7(i).]

Yet the *Restatement (2nd) of Conflict of Laws*, citing Section 169-85 of the *Restatement (2nd) of Trusts*, notes that “Matters of administration include those relating to the duties owed by

the trustee to the beneficiaries...They are matters relating to the business of administering the trust....The trustee is under a duty to the beneficiary to give him upon his request at reasonable times complete and accurate information as to the nature and amount of trust property.” Which comment seems to beg the question whether an individual settlor can choose to create a Michigan *silent* trust when the settlor resides in a state with a strong public policy that is against *silent* trusts.

The Future?: It is a gross understatement to claim that a choice of governing law trust provision is easily implemented when it confronts strong public policy positions of other states that may have *some significant relationship* or bearing on the trust. This may be why the Uniform Law Commission is currently looking at adopting a uniform conflict of laws statute that is related solely to Wills and Trusts, to provide more guidance and consistency when it comes to a settlor selecting another state’s laws to govern his/her trust, which seems to be an acknowledgement that there is plenty of forum-shopping these days when it comes to ‘purchasing’ a trust’s situs and its governing laws.

Conclusion: Usually not a lot of thought goes into a choice of law provision in a trust. However, as more and more states update their trust laws with the goal to attract trust ‘business,’ the temptation to ‘shop’ for a more favorable state to govern the trust’s interpretation and administration will occur. It is in these situations where the choice of law provision of a trust will run up against another state’s contrary *strong public policy* which will override the settlor’s choice of law provision.

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