Business Relationships
Under the Michigan Trust Code

By George F. Bearup

The Michigan Trust Code (MTC) codifies many common law rules and creates a few new rules that will be of interest to businesses and other third parties who regularly deal with trusts. Much of the MTC is intended to facilitate business transactions with trustees. Some of the more basic MTC provisions that will affect transactions and relationships with trustees are briefly summarized in the following paragraphs.

Certificates

One helpful change is the codification of the use of a certificate of trust.[1] Instead of providing a copy of the entire trust document to a non-trust beneficiary, a trustee may provide the third party with a certificate of trust. Paraphrasing slightly, the MTC specifies that the certificate of trust must include (1) the name of the trust, (2) the date of the trust instrument and any amendments to the trust, (3) the name and address of the currently acting trustees, (4) the powers of the trustee that relate to the purpose for which the certificate is offered, (5) the revocability or irrevocability of the trust and the identity of any person who holds a power to revoke the trust, and (6) the authority of co-trustees to sign or otherwise authenticate a summary of the trust and whether fewer than all of the co-trustees are required to exercise the trustee's authority. A certificate is required to be in affidavit form. The statute expressly provides that the certificate need not contain the trust's dispositive terms. Anyone acting in reliance upon the certificate "without knowledge that the representations contained in the certificate are incorrect is not liable to any person for so acting," and third persons "may assume without inquiry the existence of the facts contained in the certificate."[2] A third person "who in good faith enters into a transaction in reliance upon a certificate of trust may enforce the transaction against the trust property as if" the certificate's representations were true.[3] Paraphrasing slightly, if a third person requests a copy of the entire trust instrument, that party *will be* liable for damages, costs, expenses, and legal fees if a court determines that the third person did not act pursuant to a legal requirement when it demanded a copy of the entire trust instrument.[4]

Reliance

In order for a business to deal with trustees, generally a third party can rely on a trustee's representations. Paraphrasing only slightly, MCL 700.7912(1) provides that a person who in good faith assists the trustee, or who in good faith and for value deals with a trustee, without knowledge that the trustee's action exceeds the trustee's authority, or that there exists an improper exercise of the trustee's powers under the trust, will be protected from liability as if the trustee had properly exercised those powers. A third party dealing in good faith with a trustee will not be required "to inquire into the extent of the trustee's powers or the propriety" of the trustee's exercise of any authority with regard to the trust.[5]

Fast Facts:

Under the Michigan Trust Code (MTC), a trustee may provide a non-trust beneficiary with a certificate of trust instead of providing a copy of the entire trust document.

The MTC treats a trust's spendthrift provision to be material; it presumes that the spendthrift protection was intended by the settlor to be an essential reason for establishing the trust.

One of the major changes codified by the MTC is the authorized use of trust protectors.

A similar protection exists if the third party does not know that the trusteeship has terminated; a person dealing with the former trustee "in good faith and for value," without knowledge, is protected from liability as if the former trustee legally acted on behalf of the trust.[6] Other laws that exonerate those who deal with trustees in commercial transactions or in the transfer of securities by fiduciaries will prevail over this statutory protection.[7]

Creditors

Part 5 of the MTC addresses creditors of trust beneficiaries and the enforceability of a trust's spendthrift provision. The most important principle is that Michigan's common law with regard to creditors' rights is sufficiently established to not warrant substantial modification. The MTC follows the Restatement (Second) of Trusts with regard to the rights of creditors. While the MTC is generally modeled after the Uniform Trust Code (UTC), this is one area of significant departure between the two statutory schemes. The UTC reflects the Restatement (Third) of Trusts description of creditor rights, which generally provides a beneficiary's creditors more access to trust assets. The MTC deliberately did not adopt the UTC's section. The interest of a beneficiary in a *support* trust is not subject to the claims of the beneficiary's creditors under the MTC until the assets are distributed directly to the beneficiary from the trust.[8] Trust assets in excess of what is needed for the support of that beneficiary cannot be attached by a beneficiary's creditors. In the case of a *discretionary* trust under the MTC, a beneficiary's creditor only possesses the right to attach payments when and as they are made by the trustee directly to the trust beneficiary.[9] Consequently, Michigan's favorable common law with regard to special-needs trusts will not be jeopardized by the MTC.[10] Note that if a trust beneficiary possesses the right to receive a trust distribution, that beneficiary's creditor cannot be evaded by the trustee's unreasonably delaying the required distribution from the time that the distribution is actually due under the terms of the trust.[11]

Generally, a *spendthrift* provision in a trust will be respected and enforced when it restrains the voluntary and involuntary transfer of a beneficiary's interest in that trust. An interest in a spendthrift trust cannot be transferred by the beneficiary, and the trust's assets are not subject to a beneficiary's creditors' claims unless and until the property is actually distributed from the trust to the beneficiary.[12] Unlike the UTC, the MTC treats a trust's spendthrift provision as material; it presumes that the spendthrift protection was intended by the settlor to be an essential reason to establish the trust. Consequently, the MTC did not adopt the UTC § 411(c), which provides that the presence of a spendthrift clause is not to be treated as a material purpose of the trust, which facilitates the modification or termination of trusts.

One of the few statutory exceptions in the MTC to the protection of spendthrift and support trusts are child support claims and judgment creditors who provided services that enhanced, preserved, or protected the beneficiary's interest in the trust.[13] Again, however, trust assets cannot be reached by creditors until they become due and are actually paid by the trustee to the beneficiary.[14]

But creditors can continue to reach the assets of a debtor-settlor's revocable trust. After the settlor's death, the claims of the creditors may be pursued against the revocable trust in the same manner as now permitted under the Estates and Protected Individuals Code (EPIC).[15] The MTC incorporates Part 5 of Article VII of EPIC without modification, which establishes a means for a decedent's creditors to bring their claims against the decedent's formerly revocable trust if there is no probate proceeding or the assets of the probate estate are insufficient to satisfy all of the decedent's creditors' claims. Moreover, to dispel any confusion, Michigan's MTC does *not* authorize self-settled asset protection trusts.

Business Interests

Paraphrasing only slightly, the MTC provides that a trustee who holds an interest as a general partner in a general or limited partnership will not be personally liable for a contract that is entered into with the partnership after the trust's acquisition of the partnership interest, but only as long as that fiduciary capacity was disclosed in the contract or in a statement that was previously filed pursuant to the Michigan Uniform Limited Partnership Act or which was actually known by the other party to the contract.[16] Similarly, a trustee holding a partnership interest as a general partner will not be "personally liable for torts committed by the partnership or for obligations arising from ownership or control of the interest unless the trustee is personally at fault."[17] The MTC further provides: "If the trustee of a revocable trust holds an interest as a general partner, the settlor is personally liable for contracts and other obligations of the partnership as if the settlor were a general partner."[18]

When a trustee votes shares of stock in a corporation or exercises any power of control over similar interests in other forms of business enterprises, e.g., LLC units, the trustee must always act "in the best interests of the trust beneficiaries."[19] If the trust owns 100 percent of an enterprise, "the trustee shall elect or appoint directors or other managers to manage the corporation or enterprise in the best interests of the trust beneficiaries."[20]

Often a closely held business is the settlor's principal asset held in trust. A common question is whether a trustee must orderly divest the trust of the business that comprises most or all of the trust estate to fulfill the trustee's fiduciary duties to prudently invest in assets, which usually requires some diversification of those assets. Under the MTC, a trustee can be directed by the trust instrument to hold specific assets even though the trust's corpus is not diversified in its investments. The MTC expressly relieves a trustee of liability for "breach of trust for the acquisition or retention of a particular asset or asset class or failure to diversify investments" away from a single closely held business if that authorization is expressly contained in the trust instrument.[21]

Voidable Transactions

The MTC contains a comprehensive list of powers granted by statute to a trustee that directly address business interests. Specific provisions deal with a trustee who may have a conflict of interest in a transaction with the trust. Paraphrasing only slightly, the MTC provides that, subject to the rights of persons who deal with or who assist the trustee with a sale, encumbrance, or any other transaction that involves the investment or management of trust property entered into by the trustee for the trustee's own personal account or which is otherwise affected by a conflict between the trustee's fiduciary and personal interest, that transaction is voidable by a trust beneficiary who is affected by the transaction unless it is authorized by the terms of the trust or it is approved by a court after notice to interested persons.[22]

Trust Protectors

One of the major changes codified by the MTC is the authorized use of trust protectors. While historically trusts have been drafted with the use of designated advisors as trustees, e.g., investment advisors, a trust protector has never been formally codified or recognized by statute or caselaw. Under the MTC, a "trust protector" is formally defined as:

> [a] person or committee of persons appointed pursuant to the terms of the trust who has the power to direct certain actions with respect to the trust. Trust protector does not include either of the following: (i) The settlor of a trust[; or] (ii) the holder of a power of appointment.[23]

A distinction should be drawn between a trust protector and a trust advisor. Generally, a trust advisor can have input into the administration of the trust or the investment of trust assets, but as a practical matter the advisor does not have any power to direct or veto a trustee's proposed action. In contrast, a trust protector can override or control the actions of a trustee. Paraphrasing slightly, a trust protector, other than when a trust protector is also a beneficiary of the trust, is a fiduciary to the extent that the powers, duties, and discretion are granted to the protector under the terms of the trust instrument.[24] With a couple of exceptions, the MTC requires a trust protector to act as a fiduciary, in good faith, and in accordance with the terms of the trust instrument, and to be liable for actions that are taken pursuant to the trust protector's directions. Noted exceptions are when a trust protector is a beneficiary of the trust and a trust protector whose powers of administration are within the meaning of IRC § 675(4).[25] The role of a trust protector as a fiduciary is one of the few areas under the MTC that cannot be altered by the settlor in the provisions of the trust instrument.[26]

To conclude, while the MTC does not drastically alter the common law of trusts in Michigan with regard to business and creditor transactions with trustees, many nuances will arise in the future from its provisions that will warrant a working familiarity of the MTC by attorneys. ■

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FOOTNOTES

1. MCL 700.7913.
2. MCL 700.7913(6).
3. MCL 700.7913(7).
4. MCL 700.7913(8).
5. MCL 700.7912(2).
6. MCL 700.7912(4).
7. The MTC codifies the Restatement (Second) of the Law of Trusts, which has been incorporated into Michigan's common law. See *Miller v Dep't of Mental Health*, 432 Mich 426; 442 NW2d 617 (1989).
8. MCL 700.7505.
9. MCL 700.7505.
10. MCL 700.7505.
11. MCL 700.7507(1).
12. MCL 700.7502.
13. MCL 700.7504(1)(a) through (c).
14. *Id.*
15. See generally MCL 700.7506(1)(a) through (c).
16. MCL 499.1101 through 499.2108.
17. MCL 700.7911(1).
18. MCL 700.7911(4).
19. MCL 700.7802(6).
20. MCL 700.7802(6).
21. MCL 700.7908(2).
22. MCL 700.7802(1) and (2).
23. MCL 700.7103.
24. MCL 700.7809(1)(a).
25. MCL 7809(2).
26. MCL 700.7105(2)(h).