Directed Trusts

Navigating Directed Trusts: Roles, Responsibilities & Risks

Patti S. Spencer, Esq. – Spencer Law Firm LLC

Historical Background

Common law: trustee duties were non-delegable

Restatement (Third) introduced delegation under Prudent Investor Rule

UPIA §9: standards for prudent delegation

What Is a Directed Trust?

- Trustee powers vested in another person (trust director/advisor)
- Applies to investments, management, or distributions
- Shifts control from trustees to advisors/clients

Uniform Directed Trust Act (UDTA)

- Defines “power of direction” and “trust director”
- Directed trustee = subject to power of direction
- Fiduciary duties clarified for directors and trustees

Reasons for Directed Trusts

- Family control and flexibility
- Avoid diversification requirements
- Keep long-term advisors involved
- Handle family businesses
- Reduce trustee fees

Delaware Example

- 12 Del. C. §3313: liability standard = “willful misconduct”
- Fiduciary has no duty to monitor or correct the advisor or to alert beneficiaries as to advisor actions unless the governing instrument states otherwise.
- High threshold beyond negligence or recklessness
- Other states vary (some full exculpation)

Pennsylvania Directed Trust Act (2024)

- Subchapter H.1, 20 Pa.C.S.A. §§ 7780.11–7780.27
- Effective October 14, 2024
- Trust director: trustee-like fiduciary duty for assigned power (§ 7780.19)
- Directed trustee: reasonable action to comply; willful-misconduct limit (§ 7780.20)

Types of Directors

- Investment director — marketable assets and investment decisions
- Special holdings director — family business and unique assets
- Distribution advisor — beneficiary-specific distribution decisions
- Trust protector — may modify trust terms and exercise extraordinary powers under § 7780.17

A Directed Trust ≠ Delegation

- Direction ≠ delegation: authority comes from the trust instrument
- Directed trustee generally has no duty to monitor the director
- Directed trustee must take “reasonable action to comply” (§ 7780.20)
- Trust director bears fiduciary responsibility for the assigned power

Trustee Services in Directed Trusts

- Administrative: custody, records, continuity
- Tax: returns, beneficiary reporting
- Accounting: distributions, expenses, valuations

Drafting Considerations

- Written, specific directions; avoid unintended trustee discretion
- Define powers, implementation duties, information flow and valuation
- Plan for succession, vacancy and incapacity
- Identify who handles deadlines and tax consequences
- State responsibility for special holdings expressly

Fiduciary Status of Directors

- Trust director: same fiduciary duty/liability as a similarly situated trustee (§ 7780.19)
- Directed trustee: special protection when acting at direction (§ 7780.20)
- Willful misconduct = malicious, fraudulent or unconscionable intentional conduct
- Negligence, gross negligence and recklessness are not willful misconduct

Corporate Trustee Concerns

- Poor drafting remains the central practical risk
- No general duty to monitor does not mean blind compliance
- Open question: what is “reasonable action to comply”?
- Example: director orders $4M business sold to a relative for $500K — may trustee simply sign?

Trust Protector: Extraordinary Authority

- § 7780.17 permits expressly granted powers to modify beneficial distributions and administrative terms
- May terminate the trust, alter powers of appointment, change situs/governing law, and appoint or remove fiduciaries
- Notice to trustees and qualified beneficiaries ordinarily required — but instrument may expressly dispense with notice
- Drafting question: who should hold these powers, under what standard, and with what succession mechanism?

Information ≠ Supervision

- § 7780.21 requires information reasonably related to each fiduciary's powers and duties
- § 7780.22 generally imposes no duty to monitor another fiduciary outside the recipient's assigned authority
- Receiving information ordinarily does not create a duty to advise, warn or second-guess
- Draft the information flow without accidentally recreating supervisory responsibility

New Nonjudicial Settlements in PA

- § 7785.1 permits nonjudicial account settlement with statutory preclusive effect
- Pa. Orphans' Court Procedural Rules Committee proposed Rule 5.8 amendments in Aug. 2025
- Collateral development: useful, but separate from directed-trust liability rules

Methods to Correct Drafting Issues

- Savings clauses
- Reformation
- Modification/amendment
- Disclaimers
- Decanting

Key Takeaways

- Power → Duty → Liability
- Trust director and directed trustee have different liability standards
- Information sharing ≠ duty to supervise
- Trust protectors may hold extraordinary powers
- State-law authority does not eliminate federal tax concerns
- Drafting precision is the principal risk-control mechanism

Questions?

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