

# The Use and Abuse of Governing-Law Clauses in Trusts: What Should the New Restatement Say?

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*ABSTRACT: This Essay offers a novel solution to a thorny problem at the intersection of trust law and the conflict of laws: When should the settlor be able to choose a governing law other than the law of the jurisdiction with the most significant relationship to the trust? The law of the conflict of laws gives effect to a governing-law clause in a trust instrument except when contrary to the “strong public policy” of the jurisdiction with the most significant relationship to the matter at issue. But what is “strong public policy”? The answer should not depend on the size of the Chancellor’s foot. This Essay proposes, instead, that the answer should incorporate the well-established distinction between the default rules of trust law, which aim to effectuate the intention of the typical settlor but yield to a particular settlor’s contrary intention, and the mandatory rules of trust law, which apply without regard to intention for reasons of overriding public policy. This Essay proposes that a governing-law clause in a trust instrument should be effective unless contrary to the mandatory law of the jurisdiction with the most significant relationship to the matter at issue. The Essay urges the adoption of this approach by the Restatement (Third) of the Conflict of Laws, which is currently in the process of being drafted.*

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Disclosure: I served as an associate reporter for the Restatement (Third) of Trusts and currently serve as executive director of the Uniform Law Commission’s Joint Editorial Board on Uniform Trust and Estate Acts. However, I emphasize that the views in this Essay are mine alone. I am not speaking for the American Law Institute or the Uniform Law Commission.

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## I. INTRODUCTION

Donald Huber, a real estate developer from the state of Washington, created a trust to protect his assets from creditors.<sup>1</sup> The trust instrument contained a provision designating the law of Alaska as the governing law.<sup>2</sup> Alaska authorizes the asset protection trust,<sup>3</sup> whereas Washington does not.<sup>4</sup> Three years later, Huber filed for bankruptcy.<sup>5</sup> In the bankruptcy proceeding, the question arose whether the trust should be invalidated.<sup>6</sup> The court determined that the state with the most significant relationship to the trust, and therefore the state with the relevant substantive law, was Washington: Huber—who was the trust’s creator (“settlor”) and also one of the trustees—was domiciled in Washington and so were the beneficiaries.<sup>7</sup> Moreover, the trust assets, before they were transferred into the asset protection trust, were located there.<sup>8</sup> The connection to Alaska was that it was the location of a corporate co-trustee, and it was the state where the trust was to be administered; the court determined that these factors gave Alaska “only a minimal relation” to the trust.<sup>9</sup> The question then was: What should be the effect of the governing-law clause? The court held that the governing-law clause should be disregarded because it was an attempt to circumvent the law and the public policy of the state with the most significant relationship to the

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1. *In re Huber*, 493 B.R. 798, 804–05 (Bankr. W.D. Wash. 2013).

2. *See id.* at 807.

3. *See* ALASKA STAT. § 34.40.110 (2016).

4. *See* WASH. REV. CODE § 19.36.020 (2016).

5. *In re Huber*, 493 B.R. at 806.

6. *Id.* at 807.

7. *Id.* at 808–09.

8. *Id.*

9. *Id.* at 809.

trust—namely Washington.<sup>10</sup> The court therefore applied Washington law and held that Huber’s transfers of assets into the asset protection trust were void.<sup>11</sup>

Donald Huber is not alone. In modern trust practice, many settlors attempt to have their trusts governed by favorable substantive law. They do this by specifying the governing law in the trust instrument—through a governing-law clause—and/or by locating the trust’s administration in the favorable jurisdiction by selecting a corporate trustee or corporate co-trustee domiciled there.<sup>12</sup>

To what extent should trust settlors be permitted to select favorable substantive law? The question is important because of burgeoning trust practice; an empirical study published in 2005 concluded that “roughly \$100 billion in trust assets” had been moved between 1985 and 2003 into states perceived to have favorable substantive law.<sup>13</sup> The question is timely because the American Law Institute (“ALI”) is in the process of drafting a new Restatement—the Restatement Third of the Conflict of Laws.

This Essay is the first of two connected articles addressing the important conflict of laws questions raised by modern trust practice and illustrated by the *Huber* case: (1) when should the settlor’s designation of governing law in a governing-law clause be given effect; and (2) what weight should a court give to the location of the trust’s administration when the court is determining the jurisdiction with the most significant relationship to the trust? This Essay addresses the first question. A subsequent article will address the second question. The aim of these two articles is to guide the drafters of the Restatement Third of the Conflict of Laws.

## II. THE RESTATEMENTS OF THE CONFLICT OF LAWS

As defined by the ALI, the “[c]onflict of [l]aws is that part of the law of each state which determines what effect is given to the fact that the case may have a significant relationship to more than one state.”<sup>14</sup>

The ALI has been restating the law of the conflict of laws since the 1920s.<sup>15</sup> The first Restatement of the Conflict of Laws was started in 1923 and

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10. *Id.*

11. *See id.*

12. Robert H. Sitkoff & Max M. Schanzenbach, *Jurisdictional Competition for Trust Funds: An Empirical Analysis of Perpetuities and Taxes*, 115 YALE L.J. 356, 374 (2005).

13. *Id.* at 359.

14. RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 2 (AM. LAW INST. 1971). A leading hornbook offers a different, but compatible, definition: The conflict of laws is “the body of law that aspires to provide solutions to international or interstate legal disputes between persons or entities other than countries or states *as such*.” PETER HAY, PATRICK J. BORCHERS & SYMEON C. SYMEONIDES, CONFLICT OF LAWS 1 (5th ed. 2010).

15. Work on the first Restatement began in June 1923. *See* RESTATEMENT (FIRST) OF CONFLICT OF LAWS, at ix (AM. LAW INST. 1934).

was finished in 1934.<sup>16</sup> Its principal author (“reporter”) was Professor Joseph Beale of the Harvard Law School. Beale’s approach to the conflict of laws was territorial.<sup>17</sup> For him, the aim of the law of the conflict of laws was to determine which one territory had power to govern the particular dispute. As Beale wrote:

Law operates by extending its power over acts done throughout the territory within its jurisdiction and creating out of those acts new rights and obligations. . . . It follows . . . that not only must the law extend over the whole territory subject to it . . . , but only one law can so apply.<sup>18</sup>

The task of the law of the conflict of laws was to identify that one applicable law. For example, with respect to the law of tort, the first Restatement of the Conflict of Laws provided that “[t]he law of the place of wrong determines whether a person has sustained a legal injury,”<sup>19</sup> and the Restatement defined the place of wrong as “the state where the last event necessary to make an actor liable for an alleged tort takes place.”<sup>20</sup> Similarly, with respect to the law of contract, the first Restatement provided that “[t]he law of the place of contracting determines the validity” of a contract,<sup>21</sup> and the law of the “place of performance” governs questions of performance or non-performance,<sup>22</sup> including whether the contract has been breached.<sup>23</sup>

Beale’s territorial approach had many critics, perhaps the most influential of whom was Professor Brainerd Currie, who taught at many U.S. law schools including the University of Chicago and Duke. Currie’s approach to the conflict of laws has become known as governmental interest analysis.<sup>24</sup> In the words of Professor Larry Kramer,

Currie’s basic insight . . . was that choosing the applicable law is a process of interpreting the relevant laws. Adopting a conventional “purposive” approach to interpretation, Currie reasoned that laws have objectives and that a court should therefore apply a law in a particular case only if this advances its underlying objective. . . . If only one state’s policy would be advanced by the application of its laws . . . the court should apply the interested state’s law. If more

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16. See *id.* at intro.

17. See Ernest G. Lorenzen & Raymond J. Heilman, *The Restatement of the Conflict of Laws*, 83 U. PA. L. REV. 555, 555–59 (1935).

18. 1 JOSEPH H. BEALE, A TREATISE ON THE CONFLICT OF LAWS 45–46 (1935).

19. RESTATEMENT (FIRST) OF CONFLICT OF LAWS § 378 (AM. LAW INST. 1934).

20. *Id.* § 377.

21. *Id.* § 332.

22. *Id.* § 358.

23. *Id.* § 370.

24. HERMA H. KAY, LARRY KRAMER & KERMIT ROOSEVELT, CONFLICT OF LAWS: CASES—COMMENTS—QUESTIONS 147–50 (9th ed. 2013).

than one state has an interest, . . . the court should apply forum law.<sup>25</sup>

Currie's approach influenced the Restatement (Second) of the Conflict of Laws, published in 1971,<sup>26</sup> though the Second Restatement differed from Currie's approach in important respects.

The essence of the Second Restatement's approach can be found in Section 6 of that Restatement, which articulates a list of factors or policies that should guide a court in making a choice of law. These are:

- (a) the needs of the interstate and international systems,
- (b) the relevant policies of the forum,
- (c) the relevant policies of other interested states and the relative interests of those states in the determination of the particular issue,
- (d) the protection of justified expectations,
- (e) the basic policies underlying the particular field of law,
- (f) certainty, predictability and uniformity of result, and
- (g) ease in the determination and application of the law to be applied.<sup>27</sup>

The objective of this multi-factor approach was "to apply the law of the state that, with regard to the particular issue, has the most significant relationship with the parties and the dispute."<sup>28</sup> With respect to the law of tort, for example, the Second Restatement provided that "[t]he rights and liabilities of the parties with respect to an issue in tort are determined by the local law of the state which, with respect to that issue, has the most significant relationship to the occurrence and the parties under the principles stated in § 6."<sup>29</sup> Similarly, with respect to the law of contract, unless the parties made an effective choice of the governing law, the Second Restatement provided that "[t]he rights and duties of the parties with respect to an issue in contract are determined by the local law of the state which, with respect to that issue, has the most significant relationship to the transaction and the parties under the principles stated in § 6."<sup>30</sup>

The ALI is in the process of writing the Restatement Third of the Conflict of Laws. The reporter is Professor Kermit Roosevelt of the University of

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25. Larry Kramer, *Return of the Renvoi*, 66 N.Y.U. L. REV. 979, 998–99 (1991) (footnotes omitted).

26. RESTATEMENT (SECOND) OF CONFLICT OF LAWS (AM. LAW INST. 1971).

27. *Id.* § 6.

28. HAY, BORCHERS & SYMEONIDES, *supra* note 14, at 65; see RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 6 cmt. c (AM. LAW INST. 1971).

29. RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 145(1) (AM. LAW INST. 1971).

30. *Id.* § 188(1). On the ability of contracting parties to select the law governing their contract, see *id.* § 187. On the distinctions between trusts and contracts, see RESTATEMENT (THIRD) OF TRUSTS § 5(i) cmt. i (AM. LAW INST. 2003).

Pennsylvania Law School.<sup>31</sup> Although only part of this new Restatement has been drafted, and none of it yet has been approved by the ALI membership, the approach of the draft Third Restatement is similar to that of the Second Restatement.<sup>32</sup> The choice of law is a two-step process: “The first step is to identify the state laws that are relevant to a particular issue; the second is to select one such law to govern the issue.”<sup>33</sup> In that second step, the draft of the Third Restatement directs the court to apply “the most appropriate law” for each “particular [legal] issue.”<sup>34</sup> As did the Second Restatement, the Third Restatement expects the appropriate law to depend on the nature of the particular legal issue. For example, after a car accident occurs, the appropriate law to determine whether the driver of a car was negligent may be different from the appropriate law to determine whether the driver may be sued by his own passenger.<sup>35</sup> Each legal issue has its own appropriate law.<sup>36</sup>

The Third Restatement’s provisions determine the appropriate law with respect to various categories of legal issues—including tort, property, and contract.<sup>37</sup> A preliminary draft has been produced of the chapters on tort and property.<sup>38</sup> Significantly, for present purposes, the projected chapter on trusts has not yet been drafted. Thus, the time is ripe to ask: About trusts, what should the new Restatement say?

### III. TRUSTS AND THE EFFECT OF A GOVERNING-LAW CLAUSE: A NEW APPROACH

This Essay focuses on one aspect of that question: What should be the effect of a governing-law clause in a trust instrument? A governing-law clause expresses the settlor’s intention about what law should govern the trust. For example, the trust instrument might provide that the trust shall be governed by the law of New York or the law of Iowa or the law of the Cayman Islands.

If a dispute arises with respect to a trust that touches more than one jurisdiction, a court will have to determine the jurisdiction with the most significant relationship to the matter at issue.<sup>39</sup>

The question explored in this Essay is: When should the trust be governed by the substantive law of the jurisdiction named in a governing-law

31. AM. LAW. INST., *Restatement of the Law Third, Conflict of Laws*, [https://www.ali.org/projects/show/conflict-laws/#\\_participants](https://www.ali.org/projects/show/conflict-laws/#_participants) (last visited Mar. 9, 2018).

32. RESTATEMENT (THIRD) OF CONFLICT OF LAWS xix–xx (AM. LAW INST., Council Draft No. 2, 2017).

33. *Id.* at ch. 5, intro.

34. *Id.* § 5.02(2).

35. *See id.* § 5.02 illus. 5.

36. *Id.* § 5.02 cmt. d (authorizing the technique known as *dépeçage*). *But see id.* at § 5.02 cmt. e (describing limits on *dépeçage*).

37. *See id.* at chs. 6–8.

38. *See id.*

39. *See supra* notes 27–30 and accompanying text.

clause rather than the substantive law of the jurisdiction that has the most significant relationship to the matter at issue?

The Second Restatement has a complex set of answers. The answers are complex because they differ depending on whether the trust is a trust of “movables”<sup>40</sup> or a trust of “an interest in land,”<sup>41</sup> and also on whether the trust is inter vivos or created by will. To find an answer to the simple question of what is the effect of a governing-law clause, one must consult Sections 268, 269, 270, 271, 272, 273, 277, 278, 279, and 280 of the Second Restatement.<sup>42</sup> The pertinent parts of these sections are reproduced in Appendix A.

A more concise and helpful starting point for the new Third Restatement is contained in the Uniform Trust Code (“UTC”), promulgated by the Uniform Law Commission in 2000.<sup>43</sup> With respect to the effect of a governing-law clause, Section 107(1) of the UTC provides in pertinent part: “The meaning and effect of the terms of a trust are determined by . . . the law of the jurisdiction designated in the terms 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 . . . .”<sup>44</sup> The Official Comment explains that this provision

allows a settlor [within appropriate limits] to select the law that will govern the meaning and effect of the terms of the trust. . . . The settlor is free to select the governing law regardless of where the trust property may be physically located, whether it consists of real or personal property, and whether the trust was created by will or during the settlor’s lifetime.<sup>45</sup>

Thirty-two U.S. jurisdictions have enacted all or most of the UTC.<sup>46</sup> Of these 32 jurisdictions, 30 have enacted some form of Section 107(1). Put

40. RESTATEMENT (SECOND) OF CONFLICT OF LAWS §§ 267–75 (AM. LAW INST. 1971).

41. *Id.* §§ 276–82.

42. *See id.* §§ 268–73, 277–80.

43. The current text of the Uniform Trust Code is available on the Uniform Law Commission’s website, [www.uniformlaws.org](http://www.uniformlaws.org).

44. UNIF. TR. CODE § 107. For a discussion of this UTC section, see generally Eugene F. Scoles, *Choice of Law in Trusts: Uniform Trust Code, Sections 107 and 403*, 67 MO. L. REV. 213 (2002) (discussing the effect of choice-of-law provisions within UTC Sections 107 and 403).

45. UNIF. TR. CODE § 107 cmt., para. 1.

46. *See* UNIF. LAW COMM’N, *Legislative Fact Sheet – Trust Code*, <http://www.uniformlaws.org/LegislativeFactSheet.aspx?title=Trust%20Code> (last visited Mar. 9, 2018) (listing the following enacting jurisdictions: Alabama, Arizona, Arkansas, District of Columbia, Florida, Kansas, Kentucky, Maine, Maryland, Massachusetts, Michigan, Minnesota, Mississippi, Missouri, Montana, Nebraska, New Hampshire, New Jersey, New Mexico, North Carolina, North Dakota, Ohio, Oregon, Pennsylvania, South Carolina, Tennessee, Utah, Vermont, Virginia, West Virginia, Wisconsin, and Wyoming).

differently: Only in two of the 32 UTC jurisdictions was Section 107(1) not enacted in any form.<sup>47</sup>

Of the 30 UTC jurisdictions that enacted some form of Section 107(1), 16 enacted Section 107(1) verbatim<sup>48</sup> or essentially verbatim.<sup>49</sup> The remaining 14 made substantive changes. The laws of these 14 jurisdictions are detailed in Appendix B. The most common substantive change, made by six states, was to delete the “unless . . . contrary to a strong public policy” exception. In these six states, the governing law designated in the terms of the trust *always* determines the trust’s meaning and effect. However, this is a minority position.

The official version of Section 107(1) is the plurality position among UTC states, and it is consistent with the modern case law such as *Huber*. Thus, this Essay recommends it as the starting point for the Third Restatement.

There is a problem, however. Neither the UTC black-letter nor the Comment does much to help a court determine when there is a “strong public policy” that should override the settlor’s choice of governing law. Indeed, the Comment admits as such. It says: “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.”<sup>50</sup> The Comment does refer to Article 15 of The Hague Convention on the Law Applicable to Trusts and on Their Recognition, which lists policies such as “the protection of minors and incapable parties,” “the personal and proprietary effects of marriage,” and “the protection . . . of third parties acting in good faith.”<sup>51</sup> But the UTC Comment does not explain why these policies rise to the level of a “strong public policy,” nor does it give guidance about what policies there are, if any, that are not listed in the Hague Convention but that should be given similar protection against a governing-law clause.

Can the Third Restatement do better? Yes, it can.

47. See MASS. GEN. LAWS ch. 203E, § 107 (2016) (Section 107 reserved); MD. CODE ANN., EST. & TRUSTS § 14.5-107 (West 2017) (same).

48. See ALA. CODE § 19-3B-107 (LexisNexis 2015); ARK. CODE ANN. § 28-73-107 (2012); D.C. CODE § 19-1301.07 (2001); KAN. STAT. ANN. § 58a-107 (2005); KY. REV. STAT. ANN. § 386B.1-050 (West 2017); ME. REV. STAT. ANN. tit. 18-B, § 107 (2012); MICH. COMP. LAWS ANN. § 700.7107 (West 2012); MO. REV. STAT. § 456.1-107 (2016); MONT. CODE ANN. § 72-38-107 (2015); N.J. STAT. ANN. § 3B:31-7 (West Supp. 2017); N.M. STAT. ANN. § 46A-1-107 (West 2003); OHIO REV. CODE ANN. § 5801.06 (West 2007); VT. STAT. ANN. tit. 14A, § 107 (2010); VA. CODE ANN. § 64.2-705 (2017).

49. See OR. REV. STAT. § 130.030 (2015) (replacing “jurisdiction” with “state, country or other jurisdiction”); W. VA. CODE ANN. § 44D-1-107(1) (LexisNexis 2014) (changing “terms of the trust” to “terms of the trust instrument, including terms which may provide for change of jurisdiction from time to time”).

50. UNIF. TR. CODE § 107 cmt.

51. Hague Convention on the Law Applicable to Trusts and on Their Recognition, art. 15, July 1, 1985, 23 I.L.M. 1389.



An important and relevant insight is that the rules of trust law are either default rules or mandatory rules.<sup>52</sup>

Default rules apply unless the settlor has expressed a contrary intention in the terms of the trust.<sup>53</sup> In the field of trust law, default rules are intent-effectuating. They attempt to replicate the intention of the typical settlor but yield in the face of a particular settlor's contrary intention. An example of a default rule of trust law is the trustee's duty to avoid self-dealing.<sup>54</sup> The typical settlor will want the trustee to refrain from entering into a self-dealing transaction. However, a particular settlor may wish to authorize the trustee's self-dealing, at least in some circumstances, through express terms in the trust instrument. For example, a settlor might wish to provide in the trust instrument that a corporate trustee may invest in the corporation's own stock.<sup>55</sup>

Mandatory rules, in contrast, apply irrespective of the settlor's expressed intention. In the field of trust law, mandatory rules are intent-defeating. They apply without regard to the settlor's intention because there is, instead, an overriding public policy at issue. An example of a mandatory rule of trust law is the trustee's duty to act in good faith.<sup>56</sup> An exculpatory clause in a trust instrument cannot insulate a trustee from liability to the extent the trustee has failed to act in good faith.<sup>57</sup>

The Third Restatement can make good use of this well-accepted distinction between the default rules of trust law that are intent-effectuating and the mandatory rules of trust law that are intent-defeating due to overriding public policy. This is the same distinction that should be used to determine when a governing-law clause should alter the ordinary conflict-of-laws analysis and when it should not.

The rule that this Essay proposes for the Third Restatement is as follows: The meaning and effect of the terms of a trust are determined by the trust law of the jurisdiction designated in the terms *unless* that jurisdiction's law is contrary to a mandatory rule of the law of the jurisdiction having the most appropriate relationship to the matter at issue. In other words, the instrument may establish the applicable law unless the jurisdiction with the most appropriate relationship to the matter at issue has a contrary mandatory rule.

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52. For discussion of the distinction between mandatory and default rules in U.S. trust law, see Thomas P. Gallanis, *The Trustee's Duty to Inform*, 85 N.C. L. REV. 1595, 1617–19 (2007). See generally John H. Langbein, *Mandatory Rules in the Law of Trusts*, 98 NW. U. L. REV. 1105 (2004) (discussing mandatory rules and the rationale behind them, as well as their development in the United States).

53. For the definition of “terms of the trust,” see UNIF. TR. CODE § 103(18); RESTATEMENT (THIRD) OF TRUSTS § 4 (AM. LAW INST. 2003).

54. See RESTATEMENT (THIRD) OF TRUSTS § 78 (AM. LAW INST. 2007).

55. See *id.* § 78 cmt. c(2).

56. See UNIF. TR. CODE § 105(b)(2).

57. See *id.* § 1008(a)(1); RESTATEMENT (THIRD) OF TRUSTS § 96(1)(a) (AM. LAW INST. 2012).

The central insight of this Essay is that, with respect to the effect of a governing-law clause in a trust instrument, the choice-of-law rule does not need to rely on the vague and uncertain concept of “strong public policy”<sup>58</sup>—which is the phrase used in the UTC<sup>59</sup> and in the Second Restatement.<sup>60</sup> Rather, the choice-of-law rule can use the well-settled and predictable distinction between the mandatory and default rules of trust law. This distinction already explains when the law will honor a settlor’s intention as expressed in the terms of the trust and when the law will disregard the settlor’s expressed intention for reasons of overriding public policy. In other words, a mandatory rule of trust law already incorporates the public policy concern.

An example will demonstrate the proposed approach. The example concerns the trustee’s duty to provide information about the existence and administration of the trust to at least some of the trust’s beneficiaries.<sup>61</sup> Within the United States, at least one state has made this a mandatory duty;<sup>62</sup> some other states have made it a default duty that can be modified or eliminated by the settlor in the terms of the trust.<sup>63</sup> Suppose that a trust has contact with more than one jurisdiction and that a dispute arises about whether the trustee must provide information about the trust to at least some of the trust’s beneficiaries. Suppose further that the jurisdiction with the most significant relationship to the matter at issue—in the language of the draft Third Restatement, the jurisdiction with the most appropriate law—is a jurisdiction in which the duty to inform is a mandatory rule. What should change, if anything, if the trust has a governing-law clause specifying the law of a different jurisdiction in which the duty to inform is a default rule? Under the approach of the UTC, the court would have to determine whether the duty to inform is “strong public policy.”<sup>64</sup> How the court would make this determination is beguilingly unclear. Under the approach proposed in this Essay, there is a clear and appropriate answer. The meaning and effect of the terms of the trust are determined by the law of the jurisdiction designated in the terms unless that jurisdiction’s law is contrary to a mandatory rule of the law of the jurisdiction having the most appropriate relationship to the matter

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58. Recall the words of John Selden (1584–1654): “Equity is according to the conscience of him that is Chancellor, and as that is larger or narrower soe is equity. . . . One Chancellor has a long foot another A short foot a third an indifferent foot; tis the same thing in the Chancellors Conscience.” *TABLE TALK OF JOHN SELDEN* 43 (Frederick Pollock ed., 1927).

59. UNIF. TR. CODE § 107(1).

60. See, e.g., RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 270(a) (AM. LAW INST. 1971).

61. For discussion, see generally Gallanis, *supra* note 52.

62. See N.M. STAT. ANN. § 46A-1-105(B)(8) (2007).

63. See, e.g., W. VA. CODE ANN. § 44D-1-105 (Lexis Nexis 2014) in which UTC § 105(b)(8) and (b)(9) have been deleted.

64. UNIF. TR. CODE § 107(1). How the Second Restatement would resolve this question is difficult to discern because the question concerns a matter of trust administration that, at least in one state, “cannot be controlled by the terms of the trust.” See RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 272 cmt. f (AM. LAW INST. 1971).

at issue. On these facts, the settlor cannot eliminate the trustee's duty to inform, because the duty to inform is a mandatory rule of the jurisdiction having the most appropriate relationship to the issue.

A second example will drive home the point. This example concerns the Rule Against Perpetuities. The Rule Against Perpetuities limits the length of time that a trust (other than a purely charitable trust) can exist.<sup>65</sup> The common-law Rule Against Perpetuities is a mandatory rule.<sup>66</sup> So is the Uniform Statutory Rule Against Perpetuities, promulgated by the Uniform Law Commission in 1986 and modified in 1990.<sup>67</sup> Some U.S. jurisdictions, however, have modified the Rule Against Perpetuities into a default rule and/or have greatly lengthened the perpetuity period, and some other jurisdictions have abolished the Rule Against Perpetuities entirely.<sup>68</sup> Suppose that a settlor executes a trust instrument containing a governing-law clause stating that the trust is to be governed by the law of a jurisdiction that (1) has abolished the Rule Against Perpetuities; (2) has made it a default rule; or (3) has greatly extended the perpetuity period. Suppose further that the jurisdiction with the most significant relationship to the trust—in the parlance of the draft Third Restatement, the jurisdiction with the most appropriate law—is a jurisdiction with the Uniform Statutory Rule Against Perpetuities. When litigation arises about the trust's duration, what should a court do? Under the approach of the current UTC, the court would have to determine

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65. For discussion, see THOMAS P. GALLANIS & LAWRENCE W. WAGGONER, *ESTATES, FUTURE INTERESTS, AND POWERS OF APPOINTMENT IN A NUTSHELL* 114–54 (5th ed. 2014).

Technically, the Rule Against Perpetuities places a limit on the remote vesting of contingent future interests. *Id.* at 115. However, future interests in favor of unborn or unascertained persons are contingent. *Id.* at 135–36. Thus, with respect to interests in trust, the practical effect of the Rule is to place a limit on the trust's duration. *Id.* at 145–47. For proposals to reformulate the Rule Against Perpetuities into a direct limit on duration, see Thomas P. Gallanis, *The Future of Future Interests*, 60 WASH. & LEE L. REV. 513, 549–60 (2003); Daniel M. Schuyler, *Should the Rule Against Perpetuities Discard Its Vest?*, 56 MICH. L. REV. 683 (1958) (Part I), 56 MICH. L. REV. 887 (1958) (Part II). The proposal was adopted by the Third Restatement of Property. See RESTATEMENT (THIRD) OF PROP.: WILLS AND OTHER DONATIVE TRANSFERS § 27.1(a) (AM. LAW. INST. 2011) (“A trust or other donative disposition of property is subject to judicial modification under § 27.2 to the extent that the trust or other disposition does not terminate on or before the expiration of the perpetuity period . . .”).

66. JOHN CHIPMAN GRAY, *THE RULE AGAINST PERPETUITIES* 166 (2d ed. 1906) (“No interest is good unless it must vest, if at all, not later than twenty-one years after some life in being at the creation of the interest.”).

67. UNIF. STATUTORY RULE AGAINST PERPETUITIES § 1(a) (“A nonvested property interest is invalid unless: (1) when the interest is created, it is certain to vest or terminate no later than 21 years after the death of an individual then alive; or (2) the interest either vests or terminates within 90 years after its creation.”).

68. For discussion and criticism, see RESTATEMENT (THIRD) OF PROP.: WILLS & OTHER DONATIVE TRANSFERS ch. 27, intro. note (AM. LAW INST. 2011). The ALI's official position is that “the recent statutory movement allowing the creation of perpetual or near-perpetual trusts is ill advised.” *Id.*

whether the Rule Against Perpetuities is “strong public policy.”<sup>69</sup> Under the approach proposed in this Essay, the meaning and effect of the terms of the trust are determined by the law of the jurisdiction designated in the terms unless that jurisdiction’s law is contrary to a mandatory rule of the law of the jurisdiction having the most appropriate relationship to the matter at issue. On these facts, the court should conclude the settlor cannot extend the trust’s duration beyond what is permitted by the Uniform Statutory Rule Against Perpetuities because it is a mandatory rule of the jurisdiction having the most appropriate relationship to the matter at issue.

The approach proposed by this Essay also explains the three examples within the Hague Convention, discussed above<sup>70</sup>: the legal rules governing “the protection of minors and incapable parties,” “the personal and proprietary effects of marriage,” and the protection of “third parties acting in good faith” are all matters of mandatory law.<sup>71</sup> Therefore, they cannot be avoided by a settlor’s use of a governing-law clause.

When, then, will a governing-law clause be given effect? The answer is that a settlor may specify the governing law when doing so does not contravene a mandatory rule of the jurisdiction with the most appropriate law. Here is an example. This example concerns rules of interpretation, also known as rules of construction. Suppose a settlor creates a trust in favor of the settlor’s “descendants and their spouses.” Does this beneficial interest include same-sex spouses or only opposite-sex spouses? Does it include descendants by adoption as well as descendants by blood? Does it include descendants conceived out of wedlock? Does it include descendants conceived through the use of assisted reproductive technologies? Does it include descendants conceived posthumously? These are all questions of default law;<sup>72</sup> the settlor is free to include or exclude these categories of beneficiaries. The settlor might spell out answers to all of these questions in the trust instrument, or the settlor instead might use a governing-law clause to specify a jurisdiction that has default rules of interpretation reflecting the settlor’s views. This governing-law clause will be given effect even if the interpretive rules are different in the jurisdiction with the most appropriate relationship to the trust, because the latter are default law.

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69. UNIF. TR. CODE § 107(1).

70. See *supra* note 51 and accompanying text.

71. See *supra* note 51.

72. For the default rules promulgated by the Uniform Law Commission on how to interpret a class gift to “descendants,” see UNIF. PROB. CODE § 2-705. The Uniform Law Commission has not yet promulgated a default rule on whether same-sex spouses are included in a reference to “spouse” or “spouses” in a donative instrument. This is an important question of interpretation, especially with respect to the many family trusts that are still in existence but that were created before the recent legalization of same-sex marriage.

## IV. CONCLUSION

The approach proposed in this Essay places a clear, practicable, and appropriate limit on a settlor's ability to alter the conflict-of-laws analysis through the use of a governing-law clause. The approach relies on the well-established, meaningful, and predictable distinction between the default rules of trust law that yield to the intention of the particular settlor and the mandatory rules of trust law that apply irrespective of the settlor's intention for reasons of overriding public policy. This Essay encourages the adoption of this approach by the drafters of the Third Restatement.

APPENDIX A:  
THE SECOND RESTATEMENT ON THE EFFECT OF A GOVERNING-LAW CLAUSE

This Appendix contains the provisions of the Restatement Second of Conflict of Laws<sup>73</sup> that pertain to the effect of a governing-law clause in a trust instrument.

Chapter 10. Trusts  
Topic 1. Movables

§ 268 Construction of Trust Instrument

(1) A will or other instrument creating a trust of interests in movables is construed in accordance with the rules of construction of the state designated for this purpose in the instrument. . . .

§ 269 Validity of Trust of Movables Created by Will

The validity of a trust of interests in movables created by will is determined

(a) as to matters that affect the validity of the will as a testamentary disposition, by the law that would be applied by the courts of the state of the testator's domicil at death, and

(b) as to matters that affect only the validity of the trust provisions, except when the provision is invalid under the strong public policy of the state of the testator's domicil at death,

(i) by the local law of the state designated by the testator to govern the validity of the trust, provided that this state has a substantial relation to the trust, . . . .

§ 270 Validity of Trust of Movables Created Inter Vivos

An inter vivos trust of interests in movables is valid if valid

(a) under the local law of the state designated by the settlor to govern the validity of the trust, provided that this state has a substantial relation to the trust and that the application of its law does not violate a strong public policy of the state with which, as to the matter at issue, the trust has its most significant relationship under the principles stated in § 6, . . . .

§ 271 Administration of Trust of Movables Created by Will

The administration of a trust of interests in movables created by will is governed as to matters which can be controlled by the terms of the trust

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73. RESTATEMENT (SECOND) OF CONFLICT OF LAWS (AM. LAW INST. 1971).

(a) by the local law of the state designated by the testator to govern the administration of the trust, . . . .

#### § 272 Administration of Trust of Movables Created Inter Vivos

The administration of an inter vivos trust of interests in movables is governed as to matters which can be controlled by the terms of the trust

(a) by the local law of the state designated by the settlor to govern the administration of the trust, . . . .

#### § 273 Restraints on Alienation of Beneficiaries' Interests

Whether the interest of a beneficiary of a trust of movables is assignable by him and can be reached by his creditors is determined

(a) in the case of a testamentary trust, by the local law of the testator's domicile at death, unless the testator has manifested an intention that the trust is to be administered in another state, in which case it is governed by the local law of that state, and

(b) in the case of an inter vivos trust, by the local law of the state, if any, in which the settlor has manifested an intention that the trust is to be administered, . . . .

### Topic 2. Land

#### § 277 Construction of Trust Instrument

(1) A will or other instrument creating a trust of an interest in land is construed in accordance with the rules of construction of the state designated for this purpose in the instrument. . . .

#### § 278 Validity of Trust of Land

The validity of a trust of an interest in land is determined by the law that would be applied by the courts of the situs.

#### § 279 Administration of Trust of Land

The administration of a trust of an interest in land is determined by the law that would be applied by the courts of the situs as long as the land remains subject to the trust.

#### § 280 Restraints on Alienation of Beneficiaries' Interests

Whether the interest of a beneficiary of a trust of an interest in land is assignable by him and can be reached by his creditors, is determined by the law that would be applied by the courts of the situs as long as the land remains subject to the trust.

APPENDIX B:  
UNIFORM TRUST CODE SECTION 107(1) AND ITS VARIATIONS

Uniform Trust Code Section 107 provides in pertinent part: “The meaning and effect of the terms of a trust are determined by: (1) the law of the jurisdiction designated in the terms 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; . . . .”<sup>74</sup>

Thirty of the thirty-two Uniform Trust Code jurisdictions have enacted some form of Section 107(1).<sup>75</sup>

Of the thirty Uniform Trust Code jurisdictions that enacted some form of Section 107(1), sixteen enacted Section 107(1) verbatim or essentially verbatim.<sup>76</sup>

The remaining fourteen jurisdictions made substantive changes.

Six jurisdictions—Arizona, Mississippi, North Dakota, South Carolina, Wisconsin, and Wyoming—enacted Section 107(1) but without the “unless . . . contrary to a strong public policy” exception.<sup>77</sup> In other words, these six jurisdictions provide that the governing law designated in the terms of a trust always determines the trust’s meaning and effect.

One jurisdiction—Minnesota—enacted Section 107(1) but added a sentence stating: “The mere fact that a jurisdiction having the most significant relationship to the matter at issue has a law contrary to the law of the designated jurisdiction does not, standing alone, indicate a strong public policy contrary to that of the designated jurisdiction . . . .”<sup>78</sup>

One jurisdiction—Utah—provides that the designation of Utah law governs “if any administration of the trust is done in this state.”<sup>79</sup>

The remaining six jurisdictions changed Section 107(1) to favor their own substantive law.

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74. UNIF. TR. CODE § 107.

75. See *supra* notes 45–46 and accompanying text.

76. See *supra* notes 48–49 and accompanying text.

77. See ARIZ. REV. STAT. ANN. § 14-10107 (2012); MISS. CODE. ANN. § 91-8-107 (Supp. 2017); N.D. CENT. CODE § 59-09-07; S.C. CODE ANN. § 62-7-107 (2017); WIS. STAT. § 701.0107 (2015–16); WYO. STAT. ANN. § 4-10-107 (2015).

78. MINN. STAT. § 501C.0107(a)(1) (2016).

79. UTAH CODE ANN. § 75-7-107(2) (LexisNexis Supp. 2017).



Florida provides that the law of the jurisdiction designated in the terms of the trust controls “provided there is a sufficient nexus to the designated jurisdiction at the time of the creation of the trust or during the trust administration”<sup>80</sup> but emphasizes that “a designation in the terms of a trust is not controlling as to any matter for which the designation would be contrary to a strong public policy of this state.”<sup>81</sup>

Nebraska added language to provide that “[t]he meaning and effect of the terms of a trust that pertain to title to Nebraska real estate are determined by the law of Nebraska.”<sup>82</sup>

New Hampshire added language to provide that New Hampshire “has the most significant relationship to a matter involving a trust’s validity, construction, or administration if: (1) under the terms of the trust, this state’s laws govern that matter; and (2) the trust has its principal place of administration in this state.”<sup>83</sup>

North Carolina provides that, notwithstanding a designation of governing law, “the rights of a person other than a trustee or beneficiary are governed by” sections 1010 through 1013 of the North Carolina Uniform Trust Code.<sup>84</sup>

Pennsylvania removed the “unless . . . contrary to a strong public policy” exception<sup>85</sup> and provided that the mandatory rules in Pennsylvania Uniform Trust Code Section 105 “govern if different from the law of the jurisdiction designated in the trust instrument.”<sup>86</sup>

Tennessee enacted a detailed statute explaining the effect of a settlor’s designation of Tennessee law, including that Tennessee law “shall apply to all realty or other forms of immovable property physically in this state, as well as to all personal or movable property wherever situated.”<sup>87</sup>

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80. FLA. STAT. § 736.0107(1) (2017).

81. *Id.* § 736.0107.

82. NEB. REV. STAT. § 30-3807(b) (2016).

83. N.H. REV. STAT. ANN. § 564-B:1-107(b) (Supp. 2016).

84. N.C. GEN. STAT. § 36C-1-107(b) (2015).

85. *See* UNIF. TR. CODE § 107(1).

86. 20 PA. CONS. STAT. § 7707(1) (Supp. 2016).

87. TENN. CODE ANN. § 35-15-107(b)(3)(C) (2015).