



Uniform Laws Update

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Uniform Laws Update provides information on uniform and model state laws in development as they apply to property, trust, and estate matters. The editors of *Probate & Property* welcome information and suggestions from readers.

Uniform Trust Decanting Act

This past July, the Uniform Law Commission (ULC) approved the Uniform Trust Decanting Act (UTDA), which proposes comprehensive legislation dealing with the exercise of a trustee's discretionary power in the increasingly popular action known as "decanting." Generally, decanting refers to a trustee's power to make distributions of trust property in further trust, subject to the terms and conditions of a new governing instrument. Less commonly, decanting can refer to a trustee's power to modify a trust instrument. In all cases, decanting is a flexible tool in the modern practitioner's toolbox to optimize existing trusts for ongoing administration.

Decanting has become a widely used technique because of its potential benefits. One such benefit is the ability to modernize trust provisions by, for example, incorporating directed trust provisions, allowing for a protector or designated representative, and updating provisions for investments and trustee succession. In addition, decanting can preserve certain tax benefits and creditor protections afforded by trusts that might otherwise terminate earlier than necessitated by applicable law. Decanting also can change the governing law or situs of a trust or consolidate trusts for a common class of beneficiaries.

Perhaps the most attractive feature of decanting is that it does not require court approval, which can be a time-consuming and costly process; nor does it require the consent of the grantor or beneficiaries, which may carry with it certain risks, including negative gift, estate, and generation-skipping transfer (GST) tax consequences.

Currently 23 states have some form of decanting statute. The

statutes vary greatly from state to state, with significant differences in application and procedural requirements. The ULC drafted the UTDA to facilitate uniformity among the states. This is especially important for trusts that have connections with multiple states where the applicable law is not clear.

The act includes standard provisions typically found in the existing statutes, as well as a few innovative provisions. Existing decanting statutes allow a trustee who has broad discretion to make distributions of principal for the benefit of one or more beneficiaries to make those distributions into a second trust. When the fiduciary has broad discretion, few restrictions limit the exercise of the decanting power. Some of these statutes also allow a trustee with limited discretion to decant, although the application and restrictions on the power vary widely state to state.

The UTDA permits decanting when the trustee's discretion is limited by an ascertainable standard, but only for administrative purposes; the interests of the beneficiaries in the first and second trusts are required to be substantially similar. These restrictions are relaxed for distributions to a special-needs trust for a beneficiary who becomes disabled. The act also specifically addresses decanting of pet trusts.

For trusts that contain charitable interests, the UTDA is more restrictive. The decanting power does not apply to wholly charitable trusts. For all other trusts with "determinable charitable interests" (as defined in the act), the state's attorney general must be notified before a decanting, and a decanting cannot change the governing law of such a trust without court approval if the attorney general objects. Further, determinable charitable interests cannot be diminished in the second trust, and decanting cannot be used to change an identified charity or stated charitable purpose. These provisions are intended to protect the settlor's charitable intent without unduly limiting the ability to decant.

The power to decant under the

UTDA does not require creation of a separate trust. Rather, the term “decanting” is defined to include the power to *modify* the trust. Similar to an amendment, modification does not require retitling the assets and may avoid needing to obtain a new taxpayer identification number for the “second” trust. The power to modify the trust adds an element of administrative convenience.

Before a decanting, the trustees are required to give 60-days’ notice of their intention to decant a trust to the settlor, if living, the “qualified beneficiaries” (defined in the act to include current beneficiaries and the first generation of presumptive remainder beneficiaries), any holders of then-exercisable powers of appointment, any person with the power to remove the trustee, each other fiduciary, and (if there is a charitable interest in the first trust) the attorney general. Beneficiary consent is required, however, only to the extent that the decanting would benefit the decanting fiduciary—for example, by decanting to a trust that permits self-dealing, raises the trustee’s compensation, or increases the trustee’s liability protection.

Generally, decanting can be accomplished without court approval. But the UTDA specifically allows interested parties to petition a court to approve (or disapprove) an anticipated decanting or to appoint a special fiduciary who may exercise the decanting power.

Because decanting is a flexible tool, it could be used to frustrate the settlor’s intent. To address that concern, the UTDA requires that the trustee act in accordance with its fiduciary duties, including the duty to act in accordance with the purposes of the first trust. This reflects the view that decanting is primarily a vehicle to enable the fiduciary to adapt the trust in response to a change in circumstance or law not anticipated by the settlor.

The UTDA also attempts to reduce ambiguity over whether the decanting statute applies. As drafted, it applies to any trust that has a principal place of administration in the

enacting state, as well as trusts with a choice-of-law provision designating the enacting state’s law, except to the extent explicitly prohibited by the trust instrument.

Various protections are contained in the UTDA. As with many existing statutes, the UTDA includes savings language that prohibits decanting a trust in a manner that would cause the trust no longer to qualify for a tax benefit afforded by the first trust—for example, the benefits afforded to marital deduction trusts, IRC § 2503(c) trusts, or trusts with retirement accounts. In addition, decanting cannot extend the term of the trust beyond the period permitted by the applicable rule against perpetuities. The UTDA also provides a cure for a flawed decanting by reading into the second trust any missing language or reading out of it any invalid language. By providing a cure, the UTDA avoids any question over which trust is operative and avoids the logistical problems associated with trying to undo a decanting. Further, the act permits a trustee to rely reasonably on a prior decanting. These protections facilitate a fiduciary’s exercise of the decanting power and acceptance of a trusteeship for previously decanted assets.

Notably, the IRS issued Notice 2011-101 to advise that it was considering the tax consequences of decanting and to request public comment. The IRS has not yet issued guidance. Although the UTDA includes provisions to account for areas that implicate tax issues, one hope identified by the drafters of the uniform act is that its existence may provide common ground for the promulgation of tax guidance.

The UTDA provides a statutory basis for a trustee to exercise the power to decant, but it does not preempt or replace other permitted methods. A trustee can decant or modify a trust in accordance with the trust instrument, common law, any other state law, court order, or a nonjudicial settlement agreement. The UTDA, however, may provide greater opportunities for decanting than available using other methods.

And using the statute to decant carries with it the protections it provides against potential negative tax consequences, fiduciary liability, and conflict among states’ laws.

The UTDA has been recommended for enactment in all states. In March, New Mexico became the first state to enact a UTDA statute. At press time UTDA legislation was pending in California, Colorado, and Illinois. ■

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