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Estates, Gifts and Trusts Portfolios
Trusts
Portfolio 867-2nd: Choosing a Domestic Jurisdiction for a Long-Term Trust
Portfolio Description

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## PORTFOLIO DESCRIPTION

Tax Management Portfolio, *Choosing a Domestic Jurisdiction for a Long-Term Trust*, No. 867-2nd, explores two important developments in trust law that emerged late in the 20th century. The first was the recognition of the tax and nontax benefits of creating long-term or "dynasty" trusts. The second was the recognition of the benefits that clients may achieve in many situations by creating trusts in states other than the state of residence.

After covering some preliminary matters, this Portfolio summarizes the federal income and transfer-tax attributes of long-term trusts. It next discusses a client's freedom to choose a jurisdiction for a new trust, the ability of courts to disregard that selection, and factors for clients to consider in making such a choice. The Portfolio then addresses ethical and practical concerns, relocating existing trusts, and the use of dynasty trusts by nonresident aliens. The Worksheets contain illustrations, state law charts, and a sample trust form.

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Estates, Gifts and Trusts Portfolios
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Detailed Analysis
I. Initial Considerations

## A. Background

This Portfolio explores two important developments in trust law that emerged in the waning years of the 20th century. [1] The first was the recognition of the tax and nontax benefits of creating long-term, or "dynasty," trusts. The second was the recognition of the benefits that clients may achieve in many situations by creating trusts in states other than the state of residence. [2]

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[1] The author would like to thank his Wilmington Trust Company colleagues Eileen M. Allen, Tammis M. Dowling, Peter M. Hyde, and Glenda S. Lewis for their assistance in the preparation of this Portfolio.

[2] In this Portfolio, a reference to a "jurisdiction" or a "state" means the District of Columbia or one of the 50 states of the United States.

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Specifically, this Portfolio, after covering some preliminaries in this section, will summarize the federal transfer- and federal income-tax attributes of these trusts in section II. Then it will discuss a client's freedom to choose a jurisdiction for a new trust, the ability of courts to disregard that selection, and factors for clients to consider in making such a choice in Section III. through Section V. Sections VI., VII., and VIII., respectively, will address ethical and practical concerns, relocating existing trusts, and the use of dynasty trusts by nonresident aliens ("NRAs"). The Worksheets contain illustrations, state law charts, and a sample trust form.

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## B. Advisability of Creating Trusts

Trusts generally may be designed to give trustees discretion to distribute assets to beneficiaries to enable them to utilize the advantages of outright ownership, but the benefits of holding assets in trust cannot be restored entirely once an individual owns the assets. The default setting for practitioners, therefore, should be to advise clients to create trusts rather than to leave assets outright. Several of the oft-cited reasons clients are hesitant to create trusts and some of the benefits associated with creating trusts are set forth below.

### 1. Reasons Not to Create Trusts

Individuals might not create trusts because they:
• Do not have enough money to create them;

• Do not obtain estate planning advice and do not otherwise learn about trusts;

• Want to take advantage of portability of a deceased spousal unused exclusion amount; [3]

• Want to take advantage of lower federal income tax rates that are available to individuals over trusts; [4]

• Want to make sure that assets receive a stepped-up income-tax basis at death; [5]

• Obtain estate planning advice but are not informed of this option or are counseled not to use it;

• Don't care what happens to assets after their deaths and the deaths of any spouses;

• Believe that children will need to spend their inheritances;

• Want children to be able to decide what to do with assets regardless of the tax consequences;

• Do not want to “tie up” assets in trust;

• Find the subject to be too complicated or incomprehensible;

• Do not choose this vehicle from the wide array of available legal and financial choices;

• Do not devote sufficient time to the subject because of demands on time by occupational, recreational, religious, or other concerns;

• Find the documentation to be too long and too complicated; and/or

• Feel that the costs of developing and implementing plans are too high.

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[3] *See* § 2010(c)(4). All section references herein are to the Internal Revenue Code of 1986, as amended,

and the Treasury regulations thereunder, unless otherwise stated.

[4] *See* II.E., below.

[5] *See* § 1014.

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## 2. Reasons to Create Trusts

Individuals might create trusts:
• To ensure that estate planning wishes are carried out;

• To provide professional asset management;

• To protect assets from beneficiaries' creditors;

• To protect assets in divorce proceedings involving beneficiaries; [6]

• To protect beneficiaries from improvidence or designing persons;

• To manage assets for minor or handicapped children or for individuals who have become disabled due to illness or old age;

• To encourage beneficiaries to act in desired ways (e.g., by providing funds only if beneficiaries earn a certain amount of income, marry, or have children); [7]

• To discourage beneficiaries from acting in undesirable ways (e.g., by providing funds only if beneficiaries are not addicted to drugs or alcohol);

• To preserve the character of separate or community property;

• To prevent assets (e.g., stock in a close corporation) from being encumbered or sold;

• To save federal income and transfer taxes;

• To save state income and death taxes; and/or

• To use the federal GST exemption of the first spouse to die.

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[6] *See* Nelson, *Protecting Trusts From Claims of Alimony or Child Support*, 153 Tr. & Est. 25 (Mar. 2014); Roman, *Protecting Your Clients' Assets From Their Future Ex-Sons and Daughters-in-Law: The Impact of Evolving Trust Laws on Alimony Awards*, 39 ACTEC L.J. 157 (Spr./Fall 2013).

[7] *See* Redd, *The Ultimate in Dead Hand Control — Incentive Trusts Part II*, 154 Tr. & Est. 9 (July 2015); Redd, *The Ultimate in Dead Hand Control — Incentive Trusts Part I*, 154 Tr. & Est. 12 (May 2015).

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## C. Advisability of Creating Perpetual Trusts

Having determined in I.B., above, that the proper default position should be to advise clients to create trusts rather than to leave assets outright, the next line of inquiry relates to selecting an appropriate duration for clients' trusts. If individuals had to choose a termination date for their trusts, it certainly would not be at the expiration of the common-law rule against perpetuities (i.e., 21 years after the death of an individual living when the trust became irrevocable) and it probably would not be at the end of the 90-year period of the Uniform Statutory Rule Against Perpetuities ("USRAP"). [8] In any event, as discussed in V.D., below, the desire of clients to create perpetual trusts to use their exemptions from the federal generation-skipping transfer tax ("GST tax") and their wish to exert control far into the future have led well over half the states to allow perpetual or very long trusts. [9]

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[8] The text of the USRAP is available at, www.uniformlaws.org/shared/docs/statutory%20rule%20against%20perpetuities/usrap_final_90.pdf. To determine which jurisdictions have enacted the USRAP, go to www.uniformlaws.org/LegislativeFactSheet.aspx?title=Statutory Rule Against Perpetuities.

[9] Sitkoff & Schanzenbach, *Perpetuities, Taxes, and Asset Protection: An Empirical Assessment of the Jurisdictional Competition for Trust Funds*, 42 U. Miami Inst. on Est. Plan. ¶ ¶ 1402.4–1402.5 at 14-10–14-11 (2008).

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### 1. Reasons Not to Create Perpetual Trusts

Individuals might not create perpetual trusts because:
• Their objectives will be accomplished within the period of the applicable rule against perpetuities;

• They are not interested in planning for people whom they do not know; [10]

• The rule against perpetuities has been around a long time and "the prevailing academic view is that the Rule does, by and large, effectively prevent tying up property for an inordinate length of time"; [11]

• It is impossible to predict the future so that the creation of perpetual trusts constitutes hubris by individuals and their attorneys; and/or

• Even though a trust is practicable now, it won't be in the future because of the birth of beneficiaries, inadequate investment results, and the unwillingness of trustees to relinquish miniscule trusts for fear of losing fees.

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[10] Waggoner, *The Creeping Federalism of Wealth-Transfer Law*, 67 Vand. L. Rev. 1635, 1657 n.126 (Nov. 2014).

[11] Sitkoff & Schanzenbach, *Perpetuities, Taxes, and Asset Protection: An Empirical Assessment of the Jurisdictional Competition for Trust Funds*, 42 U. Miami Inst. on Est. Plan ¶ 1402 at 14-6 (2008).

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## 2. Reasons to Create Perpetual Trusts

Individuals might create perpetual trusts because:
• If trusts are desirable now, they probably will be in the future;

• The principal alternative to creating perpetual trusts — leaving everything outright at some point — presents difficulties of its own (e.g., forcing beneficiaries to cope with sudden influxes of funds; denying them protection from claims by creditors, spouses, designing persons, or themselves; preventing them from saving taxes);

• Creating trusts will equip people whom the individual does know with tools to plan for their beneficiaries;

• Attorneys should not be reluctant to take on the challenge of attempting to help their clients meet family needs;

• Trustees are just as eager to terminate small trusts as are the beneficiaries because such trusts require trustees to provide full service for inadequate compensation; and/or

• Trusts may adapt to changing circumstances through powers of appointment, decanting and distribution powers, and judicial and nonjudicial modification procedures.

Based on the history of charitable trusts, long-term trusts can be viable. Hence, a trust established by President John Adams in 1822 continues today, [12] and a trust created by an inhabitant of the Massachusetts Bay Colony in 1652 was terminated 360 years later in 2012, even though the trust could have continued. [13]

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[12] *See The Woodward Sch. for Girls, Inc. v. City of Quincy*, 469 Mass. 151, 13 N.E.3d 579 (2014).

[13] *See* Chester, *The Life and Death of the Ipswich Grammar School Trust: Is Enduring Dead Hand Control Possible?*, 39 ACTEC L.J. 49 (Spring 2013/Fall 2013).

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In discussing oft-cited practical barriers to the creation of perpetual trusts, a 2003 UCLA Law Review article concludes: [14]

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[14] Dukeminier & Krier, *The Rise of the Perpetual Trust*, 50 UCLA L. Rev. 1303, 1339–1340 (Aug. 2003).

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If there is a case against perpetual trusts, it must in our judgment be found in the argument that their costs and burdens at some point become too great. As we have seen, most of the difficulties of duration can be eliminated by skillful drafting of the trust instrument: creating special powers of appointment in beneficiaries; discretionary powers in trustees; enabling beneficiaries to remove trustees and, when a

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trustee's office is vacant, to appoint a successor trustee; providing that trustees account to adult beneficiaries, so as to avoid judicial accountings; and so on.

## D. Advisability of Minimizing Federal Income Tax

The federal income tax brackets for trusts are more compressed than those for individuals. Hence, as a result of the regular income tax and the net investment income tax, trusts reach the top 40.8% bracket for short-term capital gains and ordinary income in 2019 at only $12,750 of taxable income, whereas single and joint filers don't do so until over $510,300 and over $612,350 of such income, respectively. [15] Similarly, in 2019, trusts reach the top 23.8% bracket for long-term capital gains and qualified dividends (the sources of income on which many trusts largely will be taxed) at just $12,950 of taxable income, but single and joint filers don't do so until over $434,550 and over $488,850 of such income, respectively. [16]

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[15] Rev. Proc. 2018-57, § 3.01. For inflation-adjusted estate and trust tax brackets in prior years, see Worksheet 13 in 852 T.M., *Income Taxation of Trusts and Estates*.

[16] Rev. Proc. 2018-57, § 3.03. For inflation-adjusted estate and trust tax brackets in prior years, see Worksheet 13 in 852 T.M., *Income Taxation of Trusts and Estates*. *See also* § 1(j)(5)(B), added by the 2017 tax act, Pub. L. No. 115-97, effective for tax years beginning after 2017 and before 2026.

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In light of this disparity between the federal income taxation of trusts and individuals, attorneys and trustees are considering increasing distributions to beneficiaries and including capital gains in distributable net income ("DNI") to take advantage of the beneficiaries' lower tax burden. Federal income taxation is only part of the picture, however, so that practitioners must analyze nontax and other tax factors as well. From a nontax standpoint, advisers should evaluate the trusts' purposes, loss of protection from creditor claims, and fairness among beneficiaries. From a tax standpoint, they should factor in potential federal transfer-tax and state death-tax costs as well as the state income-tax impact on the beneficiaries.

And, the savings from structuring trusts to minimize state income taxes often can offset much — if not all — of the added federal tax costs. For example, if a nongrantor trust, which was created by a California resident but was not subject to California income tax because it had no California fiduciary or noncontingent beneficiary, incurred as $1 million long-term capital gain in 2017 and had no other income, the trustee would have owed $0 of California income tax on December 29, 2017, and $236,514 of federal income tax on April 17, 2018. However, if the trustee distributed $1 million to a California resident beneficiary (who had no other income) in 2017, the trustee caused the $1 million of long-term capital gain to be included in DNI, and the beneficiary paid the California income tax on the distribution by year-end, the beneficiary would have owed $108,255 of California income tax on December 29, 2017, and $203,788 of federal income tax on April 17, 2018. Thus, $108,255 of California income tax was incurred to achieve a $32,726 federal tax reduction, a $75,529 added tax cost.

## E. Advisability of Creating Trusts in Other Jurisdictions

### 1. Reasons Not to Create Trusts in Other Jurisdictions

Individuals might not create trusts in jurisdictions where they don't live because:
• In many instances, the trust laws of the home state might be perfectly adequate for clients' purposes;

• Individuals might be unaware that their objectives might be better served by creating trusts elsewhere. This might result from attorney ignorance of the laws of other states or attorney failure to acquaint clients with the possible superiority of other jurisdictions' laws; and/or

• Even though attorneys know that clients might be better served by creating trusts in other states (e.g., because trusts will escape state income taxes), attorneys might not share that information with clients for fear of losing legal business or for fear of losing fees for serving as trustee of clients' trusts.

Perhaps the most significant reason why individuals don't take advantage of the better trust laws of other states is that it's simply easier to stay home. Even though individuals and attorneys might recognize the advantages of going elsewhere, clients might decide that, by staying home, they will have ready access to counsel, trust officers, and other advisers.

### 2. Reasons to Create Trusts in Other Jurisdictions

Although numerous factors that clients and their attorneys should consider in choosing a jurisdiction are discussed in detail in V., below, it is worth noting here that attorneys should approach this subject with an open mind because it will often redound to their clients' benefit. Even if individual clients ultimately decide to stay at home for trusts, the subject at least should be brought to their attention.

## F. Market Trends and Observations

### 1. Market Trends

Regardless of what one thinks about creating long-term trusts in other states, it is important to note that publicly available market data clearly indicate growing trends in the flow of trust funds to perpetual trust-friendly states. In 2005, the authors of an empirical study found that: [17]

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[17] Sitkoff & Schanzenbach, *Jurisdictional Competition for Trust Funds: An Empirical Analysis of Perpetuities and Taxes*, 115 Yale L.J. 356, 412 (Nov. 2005) (footnote omitted).

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The jurisdictional competition for trust funds is both real and intense. Since 1986 a host of states have altered their perpetuities laws to give their local banks and lawyers a competitive advantage in what our results show is a national market for trust fund services. Our estimates imply that, [from 1987] through 2003, the movement to abolish the Rule Against Perpetuities has affected the situs of $100 billion in [federally] reported trust assets — roughly 10% of the 2003 total. Not surprisingly, the trend toward abolition has accelerated in recent years.

In 2008, the same authors observed: [18]

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[18] Sitkoff & Schanzenbach, *Perpetuities, Taxes, and Asset Protection: An Empirical Assessment of the Jurisdictional Competition for Trust Funds*, 42 U. Miami Inst. on Est. Plan. ¶ 1412.2 at 14-28 (2008).

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Our analysis demonstrates that choice of law and trust situs are important considerations in trust practice. Trust funds flow to states with more favorable laws and lower taxes. States that do not provide such benefits will lose trust business.

### 2. Observations

It is troubling that otherwise well-informed attorneys refuse to recognize that their clients would fare better by creating trusts in other states. Given the benefits discussed above, the resistance encountered by practitioners to trust-friendly states is unwarranted. The decision as to the type of trusts to employ rests with clients, and some commentators have even suggested that attorneys might face liability if they do not discuss the perpetual dynasty trust option with their clients. [19] Two examples of typical contentions and responses thereto are discussed below.

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[19] *See* Myers & Samp, *South Dakota Trust Amendments and Economic Development: The Tort of*

*'Negligent Trust Situs' at Its Incipient Stage?,* 44 S.D. L. Rev. 662 (Fall 1999).

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First, at the March 2008 Annual Meeting of the American College of Trust and Estate Counsel ("ACTEC"), a prominent Pennsylvania practitioner described the advantages of Delaware trust law as the "Delaware Myth," and contended that Pennsylvania trust law might be superior. In the author's opinion, her views are baseless. Thus, whereas Delaware updates trust laws regularly, recognizes self-settled and directed trusts, and has the 11th-ranked liability system, Pennsylvania updates trust laws at a glacial pace, does not allow self-settled and effective directed trusts, and has the 38th-ranked liability system. [20] Moreover, Delaware's power to adjust and unitrust statutes precisely fit within the safe harbors provided by the regulations under § 643, but Pennsylvania's do not and thereby might require trustees to obtain private letter rulings before modernizing trusts. [21]

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[20] *See* V.B. and V.K., below.

[21] *See* V.J., below.

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Similarly, in commenting on differences between Massachusetts and Delaware trust laws, a partner in a major Boston law firm conceded in an April 2008 e-mail that Massachusetts law on the division of trustee duties, decanting powers, and the ability of a trustee to convert an income trust to a total return unitrust is somewhat unclear because it was developed by common law rather than by statute as in Delaware. He acknowledged that Delaware permits perpetual and self-settled trusts and offers a better income-tax climate. He then concluded that "[o]therwise I don't see that DE has a very big advantage." As discussed below, the advantages presented by states, like Delaware, providing for perpetual and self-settled trusts and better income-tax climates are quite significant.

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II. Federal Tax Implications of Perpetual Dynasty Trusts

## A. Introduction

## 1. Scope

For purposes of the GST tax, most dynasty trusts created by U.S. citizens and residents fall into one of the following three categories: [22]
(1) Grandfathered Dynasty Trust — a trust that is not subject to the GST tax because it was irrevocable on September 25, 1985;

(2) Exempt Dynasty Trust — a trust that uses an individual's GST exemption from the GST tax; and

(3) Nonexempt Dynasty Trust — a long-term trust that is not exempt or grandfathered for GST tax purposes. [23]

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[22] A fourth kind of dynasty trust — the NRA Dynasty Trust — is discussed in VIII., below.

[23] *See* Brown & Ross, *Diagnosing the GST Tax Status of a Trust*, 31 Prob. & Prop. 32 (July 2017); Handler & Higgins, *Tricky GST Issues*, 42 Tax Mgmt. Est., Gifts & Tr. J. 99 (Mar. 9, 2017). For a detailed discussion of generation-skipping transfer-tax planning, see 850 T.M., *Generation-Skipping Transfer Tax.*

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## 2. Initial Observations and Planning Considerations

Since 1987 (when the current GST tax system took effect), use of the three types of dynasty trusts has shifted in-step with the growing sophistication of estate planners and the changing needs of clients and their beneficiaries, with the trend favoring the use of long-term trusts.
• Grandfathered Dynasty Trust: Because a Grandfathered Dynasty Trust had to be established before September 26, 1985, no new ones are being created. As a result, a beneficiary of such a trust who holds a nongeneral power of appointment (not the creator of the trust) has the ability to extract the greatest tax benefit from the trust. Most beneficiaries choose to exercise the power to maximize the benefit of the trust's grandfathered status, probably because they already are familiar with trusts and because doing so does not involve a loss of income during life.

• Exempt Dynasty Trust: Almost immediately following the implementation of the GST tax, the wealthy began revising their revocable estate planning documents to provide for the use of their GST exemptions. Many created irrevocable inter vivos trusts to use part or all of their exemptions. But, experience has shown that the use of the GST exemption during life or at death has not gained general acceptance among those of moderate wealth.

• Nonexempt Dynasty Trust: With few exceptions, the almost universal reaction following the enactment of the Tax Reform Act of 1986 was to revise estate planning documents to leave all assets in excess of

the GST exemption outright to beneficiaries. However, many individuals whose assets have grown through success in business, savvy investing, or the receipt of inheritances have begun to recognize the tax and nontax benefits of leaving assets over the GST exemption in long-term trusts.

Planning with a dynasty trust, particularly a Grandfathered Dynasty Trust or an Exempt Dynasty Trust, requires a knowledge of arcane principles of tax, property, and fiduciary law and should be undertaken only by those with a thorough grounding in these principles.

The drafting of a dynasty trust should be undertaken with care. Far too often, such trusts contain ambiguous language. For example, unless the governing instrument provides a definition, the phrase “in equal shares to trustor's then living issue, per stirpes” is ambiguous because “in equal shares” indicates a per capita or equal division among issue whereas “per stirpes” indicates division by representation. Similarly, dynasty trust instruments sometimes do not reflect an understanding of the nature of these trusts by omitting entire generations of beneficiaries. [24]

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[24] For suggested language, see Section 1.C.(2) of the sample form in Worksheet 16, below.

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The job of creating a dynasty trust is not complete with the signing of the document. In particular, it is imperative that all members of the estate planning team make sure that all requisite GST exemption allocations (or elections out of automatic allocations) are made in a timely fashion.

As discussed in I.C., above, the planner's bias should be in favor of creating perpetual dynasty trusts.

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## B. The Grandfathered Dynasty Trust

### 1. Introduction

The GST tax does not apply to transfers from a trust that was irrevocable on September 25, 1985, [25] unless one of the following exceptions applies:
• property was added after September 25, 1985; [26]

• the client held a power to alter, amend, revoke, or terminate the trust that would have been taxable under § 2038 if the client had died on that date; [27]

• the client possessed an incident of ownership over a policy of life insurance treated as a trust that would have been taxable under § 2042 if the insured had died on that date; [28] or

• the client made a constructive addition. [29]

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[25] Reg. § 26.2601-1(b)(1)(i).

[26] Reg. § 26.2601-1(b)(1)(i), § 26.2601-1(b)(1)(iv).

[27] Reg. § 26.2601-1(b)(1)(ii)(B).

[28] Reg. § 26.2601-1(b)(1)(ii)(C).

[29] Reg. § 26.2601-1(b)(1)(v).

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The GST tax does not apply to:
• a trust that was irrevocable on September 25, 1985, for which a qualified terminable interest property ("QTIP") election was made before, on, or after that date; [30] or

• post-September 25, 1985, principal growth and income accumulations in a trust that was irrevocable on that date. [31]

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[30] Reg. § 26.2601-1(b)(1)(iii).

[31] Reg. § 26.2601-1(b)(1)(vi).

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A constructive addition is made to a Grandfathered Dynasty Trust if:
• a liability of the trust is paid from another source; [32] or

• property remains in the trust after the possessor of a taxable power of appointment over the trust exercises or releases the power or permits it to lapse after September 25, 1985. [33]

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[32] Reg. § 26.2601-1(b)(1)(v)(C).

[33] Reg. § 26.2601-1(b)(1)(v)(A), § 26.2601-1(b)(1)(v)(D) *Exs.* 1, 3.

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A constructive addition is not made to a Grandfathered Dynasty Trust if federal estate tax attributable to a QTIP trust is paid from another source. [34] A constructive addition should not be made if the client pays income tax attributable to a grantor trust because the client is satisfying his or her own liability. [35] If an addition or a constructive addition is made to a Grandfathered Dynasty Trust after September 25, 1985, a pro rata portion of subsequent distributions from, and terminations of property held in, the trust is subject to GST tax. [36]

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[34] Reg. § 26.2601-1(b)(1)(v)(C), § 26.2652-1(a)(3).

[35] *See* PLR 201735005 (reimbursement of beneficiary for income taxes that should have been paid by trustee), PLR 201735009 (amendments to trust and judicial construction of trust did not cause trust to lose grandfathered status), PLR 200822008 (reformation of exempt trust to give trustee discretion to reimburse grantor for income taxes on grantor trust did not cause trust to cease to be exempt, subject to certain conditions, because modification would have been acceptable for grandfathered trust), PLR 200816008 (reimbursement of beneficiary for income taxes that should have been paid by trustee).

[36] Reg. § 26.2601-1(b)(1)(iv).

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Preserving the assets of a Grandfathered Dynasty Trust is desirable because they will not be subject to federal transfer tax as long as they remain in the trust. Although no tax law or regulation requires a Grandfathered Dynasty Trust to terminate at the end of the USRAP period (or any other statutory period) or the common-law rule against perpetuities period, it is doubtful that many perpetual Grandfathered Dynasty Trusts exist because, for the most part, the movement to extend or abolish the rule against perpetuities began after September 25, 1985.

## 2. Exercising a Nongeneral Power of Appointment

Many Grandfathered Dynasty Trusts provide for their continuation as long as is permitted by the applicable rule against perpetuities and thereby defer the imposition of federal transfer tax as long as possible, but many do not. For example, a trust might provide for the payment of income to the client's child for life with remainder to the child's issue, per stirpes, living at the child's death. Although the principal of the trust would not be subject to federal transfer tax at the child's death, it would again be subject to the federal transfer tax system once it is distributed to the child's issue.

Often, a trust, like the one described above, gives the child a nongeneral power to appoint the principal at death (e.g., to or in trust for the child's issue). In such a situation, the child should consider exercising the

power to extend the grandfathered status of the trust. [37] Nevertheless, now that the federal estate tax exemption is so high, the child might have available GST exemption and therefore might want to exercise the power to trigger the Delaware Tax Trap (discussed in II.F.3., below) in order to include trust assets in the gross estate and to get a stepped-up income-tax basis.

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[37] *See* II.F., below, for tax dangers in exercising a nongeneral power of appointment over a Grandfathered Dynasty Trust.

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## C. The Exempt Dynasty Trust

### 1. Introduction

Section 2631(a) gives every individual — U.S. citizen, resident alien, or NRA — a GST exemption from the GST tax that the individual or the individual's executor may allocate to any property of which the individual is the transferor. As a result of the 2012 tax act, [38] the GST exemption is equal to the basic exclusion amount under § 2010(c) for the calendar year. [39] On December 22, 2017, President Trump signed An Act to Provide for Reconciliation Pursuant to Titles II and V of the Concurrent Resolution on the Budget for Fiscal Year 2018, formerly known as the Tax Cuts and Jobs Act ("2017 Tax Act"). [40] Among other things, the 2017 Tax Act increased the federal gift-tax, estate-tax, and GST exemptions to $10 million adjusted for inflation. [41]

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[38] American Taxpayer Relief Act of 2012, Pub. L. No. 112-240.

[39] § 2631(c).

[40] Pub. L. No. 115-97 (Dec. 22, 2017).

[41] § 2010(c)(3)(C), added by Pub. L. No. 115-97, § 11061. This exemption amount will revert to $5 million (plus an inflation adjustment) in 2026. For the inflation-adjusted gift tax, estate tax, and GST tax exclusion amounts for recent years, see 800 T.M., *Estate Planning*, Worksheet 1.

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No tax law or regulation prevents an Exempt Dynasty Trust from being perpetual, so a client may create a perpetual dynasty trust simply by establishing such a trust in one of the many jurisdictions that permit trusts to last forever. [42] The legislative history to the enactment of the GST tax and § 2631 makes clear that Congress fully intended to allow exempt property to remain free of GST tax indefinitely. The Joint Committee on Taxation's General Explanation of the Tax Reform Act of 1986 provides in pertinent part as follows: [43]

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[42] *See* V.D., below.

[43] Staff of the Joint Comm. on Tax'n, General Explanation of the Tax Reform Act of 1986 (H.R. 3838; Pub. L. No. 99-514), 99th Cong. 1265 (1987) (emphasis added).

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If the grantor allocates $1 million of exemption to the trust, no part of the trust will *ever* be subject to generation-skipping transfer tax — even if the value of the trust property appreciates in subsequent years to $10 million or more.

At the time of the enactment of the GST tax and the GST exemption in 1986, Wisconsin, Idaho, and South Dakota permitted perpetual trusts.

As mentioned previously, some practitioners say that the 90-year USRAP period or the common-law rule against perpetuities period (i.e., lives in being when the trust became irrevocable plus 21 years) is "long enough." Nevertheless, long-term trusts have proven useful, and new trusts have flocked in recent years to states where trusts may be perpetual. [44]

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[44] *See* Sitkoff & Schanzenbach, *Perpetuities, Taxes, and Asset Protection: An Empirical Assessment of the Jurisdictional Competition for Trust Funds*, 42 U. Miami Inst. on Est. Plan. ¶ 1407.1 at 14-19, ¶ 1407.2 at 14-19–14-20, ¶ 1407.5 at 14-22–14-23 (2008); Schanzenbach & Sitkoff, *Perpetuities or Taxes? Explaining the Rise of the Perpetual Trust*, 27 Cardozo L. Rev. 2465, 2479, 2495–96 (Apr. 2006); Sitkoff & Schanzenbach, *Jurisdictional Competition for Trust Funds: An Empirical Analysis of Perpetuities and Taxes*, 115 Yale L.J. 356, 375 n.62, 393–94 (Nov. 2005).

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## 2. Illustrations

Many individuals fund Exempt Dynasty Trusts with assets equal in value to part or all of their gift tax exemptions. The Worksheets, below, contain illustrations assuming a $1 million gift and a 40% transfer tax rate, the current gift tax rate. [45] Worksheet 1, below, contains simplified illustrations comparing the amount that would be in a $1 million Exempt Dynasty Trust at the end of 100 years with the amount that would remain if assets were left from generation to generation and taxed at 40% using various rates of return and assuming that each generation would last 25 years. Assuming a 3% return, the Exempt Dynasty Trust would be worth $19,218,632 whereas the no-trust arrangement would be worth only about $2,500,000 at the end of the 100-year period. Assuming a 10% return, the Exempt Dynasty Trust would be worth in excess of $13,780,000,000 whereas the no-trust arrangement would be worth only about $1,780,000,000. The illustrations assume that either no distributions would be made or that an after-tax return of the indicated rate could be earned despite distributions.

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[45] § 2001(c), § 2502(a).

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Other individuals fund a charitable-lead unitrust ("CLUT") with assets equal in value to part or all of their gift tax exemption plus the federal gift tax deduction for the charitable interest. Worksheet 2, below, shows the amount that can be placed in a CLUT to produce a taxable gift of $1 million using various payout rates and charitable terms and assuming that the CLUT will achieve 6% annual growth. Using a 3% payout and a 1.8% § 7520 rate, a 20-year CLUT can be funded with $1,833,916 whereas an 80-year CLUT can be funded with $11,304,033. Using an 8% payout and the same § 7520 rate, a 20-year CLUT can be funded with $5,257,595 whereas an 80-year CLUT can be funded with $762,776,506.

Given the availability of the $10 million gift tax exemption (indexed for inflation), [46] some clients might want to consider creating lifetime QTIP trusts, lifetime credit-shelter trusts, [47] and Supercharged Credit-Shelter Trusts, [48] while others might want to structure self-settled trusts as completed gifts. [49]

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[46] § 2010(c)(3)(C), added by Pub. L. No. 115-97, § 11061. The gift tax exemption amount will revert to $5 million (plus an inflation adjustment) in 2026. For the inflation-adjusted gift tax, estate tax, and GST tax exclusion amounts for recent years, see 800 T.M., *Estate Planning,* Worksheet 1.

[47] *See* V.I.7., below.

[48] *See* Blattmachr, Gans & Zeydel, *Supercharged Credit Shelter Trust*[sm] Versus Portability, 28 Prob. & Prop. 11 (Mar./Apr. 2014).

[49] *See* V.I., below.

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## D. The Nonexempt Dynasty Trust

### 1. Introduction

Interest in keeping assets that are not exempt from the GST tax in trust has grown for both nontax and tax reasons. Unlike the creator of an Exempt Dynasty Trust and the holder of a nongeneral power of appointment over a Grandfathered Dynasty Trust or an Exempt Dynasty Trust, individuals planning the disposition of nonexempt assets often are faced with the unpalatable but unavoidable choice between subjecting assets either to federal estate tax or to GST tax at the deaths of their children. Nevertheless, planning can produce significant savings.

No tax law or regulation limits the duration of a Nonexempt Dynasty Trust. In fact, the Internal Revenue Service ("IRS") withdrew former Reg. § 26.2652-1(a)(4) because the regulation would have enabled the possessor of a nongeneral power of appointment over a Nonexempt Dynasty Trust to move assets down a generation free of federal transfer tax. [50]

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[50] T.D. 8720, 62 Fed. Reg. 27,498 (May 20, 1997).

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A typical Nonexempt Dynasty Trust might provide for the payment of income to the client's child for life, then to the child's child for life, then to that child's child for life, and so on. Assuming that no GST exemption is allocated to the trust, GST tax will be payable at each generation. Each time GST tax is paid, however, the transferor will be moved down a generation so that distributions to the income beneficiary will not be taxable distributions. [51]

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[51] § 2653(a).

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Section I.B., above, identifies some reasons to place (and not to place) nonexempt assets in trust. The rest of this section II.D. discusses some federal-transfer tax advantages of leaving nonexempt assets outright, a few federal transfer-tax advantages of keeping nonexempt assets in trust, and a few ways of choosing between paying federal estate tax or GST tax.

Given that the GST exemption and the federal estate-tax exemption are the same amount and that the GST-tax rate and the estate-tax rate are equal at 40% in 2018, the long-standing bias in favor of subjecting assets to estate tax to use the graduated estate-tax rates no longer applies. Indeed, in states where there is no state GST tax (or in which the state GST tax rate is relatively low) but there is a state death tax, it might be preferable (depending upon the client's goals) to subject nonexempt assets to GST tax rather than to estate tax.

## 2. Federal Transfer-Tax Advantages of Leaving Nonexempt Assets Outright

### a. Make Annual Exclusion Gifts

Individuals may reduce their gross estates by making annual exclusion gifts each year during life. [52] There are no equivalent exclusions for taxable distributions or taxable terminations. An individual [53] and the trustee of a Nonexempt Dynasty Trust both may make tax-free medical and tuition payments by direct payment to the service provider. [54]

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[52] § 2503(b) (for the inflation-adjusted gift tax annual exclusion amounts for recent years, see 800 T.M., *Estate Planning*, Worksheet 1). To be exempt from GST tax, a gift in trust to a skip person must comply with § 2642(c). For a detailed discussion of gift planning techniques, see 845 T.M., *Gifts*, and 846 T.M., *Gifts to Minors.*

[53] § 2503(e), § 2611(b)(1).

[54] § 2611(b)(1), § 2642(c)(3)(B). *See* Karibjanian, *Income Tax Caveat for Medical/Educational GST Exception*, 44 Est. Plan. 37 (May 2017).

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### b. Make Gifts to Enable Spouses to Use Tax Exemptions

An individual might want to make outright gifts to his or her spouse to enable the spouse to use the federal gift-tax, estate-tax, and/or GST exemptions and/or to take advantage of portability of the deceased spousal unused exemption amount. [55]

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[55] *See* § 2010(c)(4).

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### c. Take Advantage of Individuals' Larger Income Tax Brackets

For many years, the federal income tax brackets for trusts have been more compressed than those for individuals, and recent changes in the tax law have accentuated this difference. Hence, as a result of the regular income tax and the net investment income tax, as of 2019, trusts reach the top 40.8% bracket for short-term capital gains and ordinary income at only $12,750 of taxable income, whereas single and joint filers do not do so until over $510,300 and over $612,350 of such income, respectively. [56] Similarly, as of 2019, trusts reach the top 23.8% bracket for long-term capital gains and qualified dividends (the sources of income on which many trusts will largely be taxed) at just $12,950 of taxable income, but single and joint filers do not do so until over $434,550 and over $488,850 of such income, respectively. [57] In light of this increased disparity between the federal income taxation of trusts and individuals, an individual might want to consider making outright gifts to beneficiaries in order to take advantage of the beneficiaries' lower tax burden.

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[56] Rev. Proc. 2018-57, § 3.01. For inflation-adjusted estate and trust tax brackets in prior years, see Worksheet 13 in 852 T.M., *Income Taxation of Trusts and Estates*.

[57] Rev. Proc. 2018-57, § 3.03. For inflation-adjusted estate and trust tax brackets in prior years, see Worksheet 13 in 852 T.M., *Income Taxation of Trusts and Estates*. *See also* § 1(j)(5)(B), added by the

2017 tax act, Pub. L. No. 115-97, § 11001, effective for tax years beginning after 2017 and before 2026.

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## d. Get Increased Income Tax Basis at Death

The increasing federal transfer tax exemptions makes obtaining a stepped-up income-tax basis at death all the more important as income tax concerns may be more relevant to many taxpayers than estate tax concerns. [58] Leaving assets outright to beneficiaries makes this possible, although this is not the only way to get a step-up in basis. [59]

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[58] *See* § 1014.

[59] *See, e.g.*, Zaritsky, *Getting Irrevocable Trust Assets Back in the Grantor's Gross Estate*, 45 Est. Plan. 46 (Sept. 2018); Bridgers, *Basis Step-Up Planning: A Double-Edged Sword—A Review of Common State Law Nuances*, 32 Prob. & Prop. 24 (Jul./Aug. 2018); Lee, *Putting It On & Taking It Off: Managing Tax Basis Today for Tomorrow*, 52 Heckerling Inst. on Est. Plan. (2018).

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## e. Take Advantage of Marital Deduction

If a decedent makes a gift that qualifies for the federal estate tax marital deduction, then payment of federal estate tax on the property may be deferred until the surviving spouse's death, and the property will receive a stepped-up income tax basis both at the first spouse's death and at the surviving spouse's death. [60] No such basis increase is available under the GST tax if, following a beneficiary's death, the trust continues for a beneficiary in the same or a higher generation. [61]

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[60] § 1014(a).

[61] § 2654(a)(2).

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## f. Use GST Exemption

Individuals may allocate their GST exemptions to assets that are includible in their gross estates, [62] but beneficiaries of Nonexempt Dynasty Trusts may not allocate their GST exemption to trust assets because these beneficiaries are not the transferors of the trust assets.

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[62] *See* Zaritsky, *Using the Newly Increased GST Exemption*, 45 Est. Plan. 46 (May 2018).

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## g. Use Previously Taxed Property Credit

A decedent's estate is entitled to a credit for property includible in the gross estate that was subject to federal estate tax within ten years before and two years after death. [63] There is no equivalent GST tax

credit.

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[63] § 2013(a). For a detailed discussion of the § 2013 credit for prior transfers, see 844 T.M., *Estate Tax Credits and Computations.*

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### h. Employ Qualified Disclaimers

A beneficiary may disclaim an interest (other than in a QTIP trust) that is includible in a decedent's gross estate within nine months of death. [64] A taxable termination does not begin a new qualified disclaimer period.

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[64] § 2518(b)(2). For a detailed discussion of qualified disclaimers, see 848 T.M., *Disclaimers — Federal Estate, Gift and Generation-Skipping Tax Considerations*.

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## 3. Federal Transfer-Tax Advantages of Keeping Nonexempt Assets in Trust

### a. Tax-Free Gifts Are Possible

If a trust is structured as a grantor trust for federal income tax purposes, then the grantor may, in effect, make tax-free gifts to the trust by paying income taxes that are attributable to it. The IRS initially attempted to treat such income-tax payments as additional transfers to the trust but has since confirmed that it will not pursue this issue (subject to a few caveats). [65]

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[65] Rev. Rul. 2004-64. *See* PLR 200822008 (modification of exempt trust to give trustee discretion to reimburse grantor for income taxes on grantor trust didn't cause trust to cease to be exempt, subject to certain conditions, because modification would have been acceptable for grandfathered trust).

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### b. Tax May Be Saved

An interest in a Nonexempt Dynasty Trust may pass to a beneficiary in the same or a higher generation without payment of GST tax (e.g., if a child dies without issue and the trust continues for his or her siblings). If a decedent leaves assets outright to beneficiaries in any generation, then federal estate tax might have to be paid upon a beneficiary's death.

### c. Utilize Longer Tax Deferral

Payment of the GST tax may be deferred without meeting the requirements of the federal estate-tax marital deduction until no person in the same or a higher generation has an interest in a Nonexempt Dynasty Trust. No complete basis increase will be received, however, until a taxable termination occurs. [66]

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[66] § 2654(a)(2).

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### d. Take Advantage of Lower Tax on Double Skip

If the trustee of a Nonexempt Dynasty Trust distributes assets to the current income beneficiary's great-grandchild, then only one GST tax is payable. [67] If assets are left outright, estate tax must be paid in each generation.

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[67] § 2653(a).

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### e. Total Tax Might Be Lower

Given that the federal estate tax credit for state death taxes was repealed [68] and replaced with a deduction [69] at the end of 2004, many states "decoupled" from the federal system by enacting separate estate or inheritance taxes, while other states already had such taxes. [70] Consequently, many estates will pay state death tax as well as federal estate tax. Although the federal state GST tax credit was also eliminated, [71] only three states — Hawaii, Massachusetts, and Vermont — have a separate GST tax. [72] For example, Vermont imposes its own estate tax at a rate of up to 16% [73] and its own GST tax at a rate of only 2%. [74] Thus, the state and federal transfer-tax burden on Nonexempt Dynasty Trusts will often be lower than on assets that are owned outright.

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[68] § 2011(f).

[69] § 2058.

[70] *See* Fox, 2018 *State Death Tax Chart* (Nov. 2, 2018), www.actec.org/resources/state-death-tax-chart/.

[71] § 2604(c).

[72] Haw. Rev. Stat. § 236E-17; Mass. Gen. L. ch. 65C, § 4A; Vt. Stat. Ann. tit. 32, § 7460. New York repealed its generation-skipping transfer tax effective April 1, 2014. As a result, the New York State generation-skipping transfer tax no longer applies to any distributions or terminations made after March 31, 2014. Chapter 59 of the Laws of 2014, Part X.

[73] Vt. Stat. Ann. tit. 32, § 7442a.

[74] Vt. Stat. Ann. tit. 32, § 7460(b).

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## 4. Choosing Between the Federal Estate Tax and the GST Tax

If a family has enough wealth to warrant GST-tax planning, it is impossible to predict whether the family will be better off by paying federal estate tax or GST tax at a decedent's death. Consequently, an individual's estate plan should be flexible enough to permit the payment of either form of federal transfer tax. Although trustees of Nonexempt Dynasty Trusts might be able to distribute enough assets to income

beneficiaries to allow the beneficiaries to use the options described in II.D.2., above, such trusts must already be in place for beneficiaries to avail themselves of the benefits described in II.D.3., above. Thus, the best planning course would seem to involve creating a Nonexempt Dynasty Trust and then giving the trustee or the beneficiary enough discretion to minimize the federal transfer tax that is payable at the beneficiary's death.

A frequently suggested method for choosing between the payment of federal estate tax and GST tax is to give a trustee the power to grant and to take back a general power of appointment. This approach is an imperfect solution, however, because the trustee may not have complete financial information for the beneficiary. Individual trustees must also satisfy themselves that the exercise of such a power will not be a taxable gift. [75]

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[75] *See Matter of Goldman*, 764 N.Y.S.2d 175 (N.Y. Sur. Ct. N.Y. Cty. 2003).

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Because clients might move or state death-tax laws might change after the preparation of an estate plan, the attorney might consider two other alternatives. First, instead of forcing the payment of estate tax or GST tax, the trust instrument might include a formula that will produce the more advantageous outcome. Second, the governing instrument might confer nongeneral powers of appointment as discussed in II.F.3., below.

## E. Federal Income-Tax Implications

From an estate-planning standpoint, it might be desirable for a dynasty trust to be a grantor trust for federal income-tax purposes. [76] The client might want grantor-trust treatment because the trust will not be depleted to pay taxes on accumulated ordinary income and capital gains or because trust income may be taxed at a lower rate if it is taxed to the grantor. Clients might not want grantor-trust treatment, however, because they may not be willing and able to pay income taxes on income (capital gains in particular) that they do not actually receive [77] and/or because creating the trust as a grantor trust might subject the trust to state income tax that could have been escaped if it had been structured as a separate taxpayer.

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[76] *See* Redd, *Unexpected Consequences of Irrevocable Grantor Trusts*, 157 Tr. & Est. 10 (Nov. 2018); Kornstein, et. al., *The Intersection of Subchapter J and the Qualified Business Income Deduction*, 129 J. Tax'n 18 (Aug. 2018); Breitstone & Jacobson, *Estate Planning With Grantor Trusts*, 155 Tr. & Est. 15 (Mar. 2016); Jones & Horne, *Grantor Trust Income Tax Reporting Requirements — A Primer*, 30 Prob. & Prop. 40 (Jan./Feb. 2016); LaPiana & Bekerman, *Estate Planning in an Income Tax World*, 40 Tax Mgmt. Est., Gifts & Tr. J. 111 (Mar. 12, 2015); Yuhas & Radom, *The New Estate Planning Frontier: Increasing Basis*, 122 J. Tax'n 4 (Jan. 2015); Waxenberg & Brown, *The Narrowing 'Tax Efficiency Gap': Part II*, 153 Tr. & Est. 24 (Sept. 2014); Waxenberg & Brown, *The Narrowing 'Tax Efficiency Gap*', 153 Tr. & Est. 22 (July 2014).

[77] *See Millstein v. Millstein*, 2018-Ohio-2295, 2018 WL 3005347, at *3 (Ohio Ct.App. June 14, 2018) (court *dismissed* grantor's petition for reimbursement of income taxes). For a summary of *Millstein* see Redd, *Unexpected Consequences of Irrevocable Grantor Trusts* at 12–13. *See also* PLR 201647001 (addition of tax-reimbursement clause approved). But see Harrison, Kamin & Shenkman, *The Gumby Trust: Creating Flexibility*, 157 Tr. & Est. 18, 22 (Oct. 2018) ("If a grantor trust is decanted into a non-grantor trust, might the beneficiaries sue the trustee effectuating the decanting for creating a cost to the trust or beneficiaries that had theretofore been borne by the settlor?")

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A dynasty trust may be structured in various ways so that it will be a grantor trust but not includible in the client's gross estate; [78] the trust instrument might contain more than one of them to ensure that grantor-trust treatment is achieved. In the author's experience, the most common ways to do so are to give the client [79] or a third party [80] the power (exercisable in a nonfiduciary capacity) to reacquire trust assets by substituting property of an equivalent value [81] and to give an independent trustee the power to add spouses or charitable beneficiaries. [82]

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[78] *See* 819 T.M., *Grantor Trusts (Sections 671-679).*

[79] *See* Rev. Rul. 2011-28; Rev. Rul. 2008-22, *modified by* , Announcement 2008-46; PLR 201349001, PLR 200848006, PLR 200845015 – PLR 200845017. *See also* Shenkman & Steiner, *Swap Powers*, 154 Tr. & Est. 45 (Dec. 2015).

[80] *See* Rev. Proc. 2008-45, § 8.09(1); Rev. Proc. 2007-45, § 8.09(1) (charitable-lead trust might be grantor trust if person other than donor, trustee, or disqualified person has power to substitute trust assets in

nonfiduciary capacity); PLR 201730018.

[81] § 675(4)(C). *See* Redd, *Unexpected Consequences of Irrevocable Grantor Trusts*, 157 Tr. & Est. 10, 11–12 (Nov. 2018) ("Almost certainly, the most widely used method for generating grantor trust status is to include in the governing instrument a power, exercisable in a nonfiduciary capacity by the grantor or any person without the approval or consent of any person in a fiduciary capacity, to reacquire the trust corpus by substituting property of an equivalent value (a substitution power)"). For potential difficulties in administering the substitution power, see *id.* at 12. *See also Manatt v. Manatt*, No. 4:17-cv-00378, 2018 BL 235689, 2018 WL 3154461, at *7 (S.D. Iowa May 2, 2018) ("Brad had the unilateral right of substitution of assets held in the BJM Trust unencumbered by Erik's fiduciary duties to determine whether the substitution was of equivalent value"); *Benson v. Rosenthal*, 2016 BL 155561, 2016 WL 2855456, at *6 (E.D. LA May 16, 2016) ("Plaintiff complied with all of the requirements of the Substitution Provisions of the trusts to effect a substitution on January 24, 2015. Defendants must now comply with their obligations under the trusts in confirming the equivalence of value as of that date."); *In re Dino Rigoni Intentional Grantor Trust for Benefit of Rajzer*, No. 321589, 2015 BL 225550, 2015 WL 4255417, at *6 (Mich. App. July 14, 2015) ("Rigoni may reacquire trust assets *by* substituting property of an equivalent value.") (internal quotation marks omitted and emphasis in original).

[82] § 674(c). *See* PLR 200747001.

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In Revenue Ruling 2008-22, [83] the IRS ruled, inter alia, that: [84]

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[83] *See also* PLR 201349001.

[84] Rev. Rul. 2008-22 (emphasis added).

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A grantor's retained power, exercisable in a nonfiduciary capacity, to acquire property held in trust by substituting property of equivalent value will not, by itself, cause the value of the trust corpus to be includible in the grantor's gross estate under § 2036 or 2038, *provided the trustee has a fiduciary obligation (under local law or the trust instrument) to ensure the grantor's compliance with the terms of this power by satisfying itself that the properties acquired and substituted by the grantor are in fact of equivalent value.*

To facilitate the use of this "swap" power, states have begun to pass legislation to memorialize the above requirement. For example, Delaware enacted a statute that now reads as follows: [85]

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[85] Del. Code Ann. tit. 12, § 3316.

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Except as otherwise expressly provided by the terms of a governing instrument, if a trustor has a power to substitute property of equivalent value, the fiduciary responsible for investment decisions has a fiduciary duty to determine that the substituted property is of equivalent value prior to allowing the substitution.

In Revenue Ruling 2011-28, the IRS authorized the substitution of life insurance policies under § 2042; the relevant part of the ruling holds as follows: [86]

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[86] Rev. Rul. 2011-28.

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A grantor's retention of the power, exercisable in a nonfiduciary capacity, to acquire an insurance policy held in trust by substituting other assets of equivalent value will not, by itself, cause the value of the insurance policy to be includible in the grantor's gross estate under § 2042, provided the trustee has a fiduciary obligation (under local law or the trust instrument) to ensure the grantor's compliance with the terms of this power by satisfying itself that the properties acquired and substituted by the grantor are in fact of equivalent value, and further provided that the substitution power cannot be exercised in a manner that can shift benefits among the trust beneficiaries.

A 2009 IRS Chief Counsel Advice Memorandum concluded that the conversion of a nongrantor trust into a grantor trust was not a transfer for federal income tax purposes. [87]

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[87] CCA 200923024. *See* PLR 201730018.

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Trustors sometimes create new trusts as nongrantor trusts; in addition, many existing trusts are nongrantor trusts, and most, if not all, grantor trusts become nongrantor trusts when the grantor dies. For many years, the federal income tax brackets for trusts have been more compressed than those for individuals. Hence, as noted in I.D., above, trusts reach the top 40.8% bracket for short-term capital gains and ordinary income in 2019 at only $12,750 of taxable income, whereas single and joint filers do not do so until over $510,300 and over $612,350 of such income, respectively. [88] Similarly, as of 2019, trusts reach the top 23.8% bracket for long-term capital gains and qualified dividends (the sources of income on which many trusts will largely be taxed) at only $12,950 of taxable income, but single and joint filers do not do so until over $434,550 and over $488,850 of such income, respectively. [89]

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[88] Rev. Proc. 2018-57, § 3.01. For inflation-adjusted estate and trust tax brackets in prior years, see Worksheet 13 in 852 T.M., *Income Taxation of Trusts and Estates*.

[89] Rev. Proc. 2018-57, § 3.03. For inflation-adjusted estate and trust tax brackets in prior years, see Worksheet 13 in 852 T.M., *Income Taxation of Trusts and Estates*. *See also* § 1(j)(5)(B), added by the 2017 tax act, Pub. L. No. 115-97, § 11001, effective for tax years beginning after 2017 and before 2026.

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In light of this increased disparity between the federal income taxation of trusts and individuals, attorneys and trustees are currently considering increasing distributions to beneficiaries and including capital gains in distributable net income in order to take advantage of the beneficiaries' lower tax burden. Federal income taxation is only part of the picture, however; practitioners must also analyze nontax and other tax factors. From a nontax standpoint, advisers should evaluate the trusts' purposes, the loss of protection from creditor claims, and fairness among beneficiaries; from a tax standpoint, advisers should factor in potential federal transfer-tax and state death-tax costs as well as the state income tax impact on the beneficiaries.

As also shown in I.D., above, the savings from structuring a trust to minimize state income tax as described below [90] can often offset much if not all of the added federal tax costs.

[90] *See* V.E., below.

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## F. Tax Dangers when Exercising Powers over Trusts

### 1. Introduction

When a beneficiary is considering exercising a nongeneral power of appointment over a Grandfathered Dynasty Trust, an Exempt Dynasty Trust, or a Nonexempt Dynasty Trust, or when a trustee [91] is considering taking action that will affect such a trust, the attorney advising the beneficiary or trustee must be wary of the following two federal transfer-tax hazards:

• Any restrictions that regulations under the GST tax impose on such action; and

• Section 2041(a)(3) and § 2514(d), commonly known as the “Delaware tax trap.”

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[91] For convenience, these actions are discussed as being taken by a trustee but the reader should understand that beneficiaries, advisers, protectors, and committees might also be involved.

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Both hazards are described below.

### 2. The GST Regulations

### a. Grandfathered Dynasty Trusts

### (1) Exercise of Nongeneral Power of Appointment by Beneficiary

A beneficiary's exercise of a nongeneral power of appointment over a Grandfathered Dynasty Trust will not produce adverse federal transfer-tax consequences if it does not: [92]

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[92] Reg. § 26.2601-1(b)(1)(v)(B)(2).

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[P]ostpone or suspend the vesting, absolute ownership or power of alienation of an interest in property for a period, measured from the date of creation of the trust, extending beyond any life in being at the date of creation of the trust plus a period of 21 years plus, if necessary, a reasonable period of gestation (the perpetuities period). For purposes of this paragraph (b)(1)(v)(B)(2), the exercise of a power of appointment that validly postpones or suspends the vesting, absolute ownership or power of alienation of an interest in property for a term of years that will not exceed 90 years (measured from the date of creation of the trust) will not be considered an exercise that postpones or suspends vesting, absolute ownership or the power of alienation beyond the perpetuities period. If a power is exercised by creating another power, it is deemed to be exercised to whatever extent the second power may be exercised.

Note that (i) the regulation applies even if the donee does not create another nongeneral power of appointment and (ii) the donee may expand the class of measuring lives in the original trust, provided that all members of the new class were living at the date of creation of the original trust. [93] In addition, the regulation says that the donee may exercise the power to extend the trust until the expiration of the common law rule against perpetuities, 90 years from the trust's creation, or the shorter (not the longer) of such periods. [94] The IRS has approved exercises of powers of appointment that comply with the regulation. [95] The validity of the regulation is questionable, however, because one can argue that the IRS may not limit actions involving Grandfathered Dynasty Trusts — trusts to which the GST tax does not apply. [96] Nevertheless, only a foolhardy practitioner would counsel a client to exercise a nongeneral power of appointment over a Grandfathered Dynasty Trust to extend the trust beyond what is permitted by the regulation without first obtaining a favorable private letter ruling (which the IRS certainly would not be willing to issue). Hence, practitioners should make sure that exercises of nongeneral powers of appointment do not violate the regulation's restriction.

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[93] Reg. § 26.2601-1(b)(1)(v)(B)(2), § 26.2601-1(b)(1)(v)(D) *Exs.* 4 and 5.

[94] Reg. § 26.2601-1(b)(1)(v)(B)(2), § 26.2601-1(b)(1)(v)(D) *Exs.* 6 and 7.

[95] *See, e.g.*, PLR 201425007, PLR 201418005, PLR 201246004.

[96] *See* 850 T.M., *Generation-Skipping Transfer Tax*.

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## (2) Other Modifications

A beneficiary may change the terms of a Grandfathered Dynasty Trust by exercising a nongeneral power of appointment. The GST regulations also govern when other methods for modifying the terms of trusts will cause such trusts to lose their tax-favored status. [97] They include four safe harbors — for trustee discretionary powers (i.e., decanting powers [98]), court-approved settlements, [99] judicial constructions, [100] and other changes (including decanting powers [101] and other modifications that do not meet the three previous safe harbors [102]) — as well as 12 examples. [103] The safe harbors provide the following: [104]

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[97] Reg. § 26.2601-1(b)(4)(i). *See* 850 T.M., *Generation-Skipping Transfer Tax*.

[98] Reg. § 26.2601-1(b)(4)(i)(A). *See, e.g.*, PLR 201718014, PLR 201025026

[99] Reg. § 26.2601-1(b)(4)(i)(B). *See, e.g.*, PLR 201628008, PLR 201606002, PLR 201532008 – PLR 201532013, PLR 201531003 – PLR 201531007, PLR 201530008 – PLR 201530013, PLR 201528024, PLR 201527011, PLR 201519012.

[100] Reg. § 26.2601-1(b)(4)(i)(C). *See, e.g.*, PLR 201814002, PLR 201814001, PLR 201803003, PLR 201735009, PLR 201732029, PLR 201712003 – PLR 201712005, PLR 201707003 – PLR 201707005, PLR 201532008 – PLR 201532013, PLR 201531003 – PLR 201531007, PLR 201530008 – PLR 201530013, PLR 201521002 – PLR 201521004

[101] *See, e.g.*, PLR 201718014, PLR 201025026.

[102] Reg. § 26.2601-1(b)(4)(i)(D). *See, e.g.*, PLR 201833015, PLR 201825007, PLR 201818005, PLR 201817012 – PLR 201817014, PLR 201817016, PLR 201817002 – PLR 201817003, PLR 201719008, PLR 201718014, PLR 201711002, PLR 201706002, PLR 201702016 – PLR 201702018, PLR 201702005–006, PLR 201642028 – PLR 201642030, PLR 201642027, PLR 201641020, PLR 201634016

– PLR 201634017, PLR 201633022–023, PLR 201626016, PLR 201543006, PLR 201532008 – PLR 201532013, PLR 201531003 – PLR 201531007, PLR 201530008 – PLR 20153013, PLR 201528029, PLR 201527032, PLR 201521002 – PLR 201521004.

[103] Reg. § 26.2601-1(b)(4)(i)(E).

[104] Reg. § 26.2601-1(b)(4)(i)(A)–(D).

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**(A)** ***Discretionary powers***. The distribution of trust principal from an exempt trust to a new trust or retention of trust principal in a continuing trust will not cause the new or continuing trust to be subject to the provisions of chapter 13, if —

(1) Either —

(i) The terms of the governing instrument of the exempt trust authorize distributions to the new trust or the retention of trust principal in a continuing trust, without the consent or approval of any beneficiary or court; or

(ii) At the time the exempt trust became irrevocable, state law authorized distributions to the new trust or retention of principal in the continuing trust, without the consent or approval of any beneficiary or court; and

(2) The terms of the governing instrument of the new or continuing trust do not extend the time for vesting of any beneficial interest in the trust in a manner that may postpone or suspend the vesting, absolute ownership, or power of alienation of an interest in property for a period, measured from the date the original trust became irrevocable, extending beyond any life in being at the date the original trust became irrevocable plus a period of 21 years, plus if necessary, a reasonable period of gestation. For purposes of this paragraph (b)(4)(i)(A), the exercise of a trustee's distributive power that validly postpones or suspends the vesting, absolute ownership, or power of alienation of an interest in property for a term of years that will not exceed 90 years (measured from the date the original trust became irrevocable) will not be considered an exercise that postpones or suspends vesting, absolute ownership, or the power of alienation beyond the perpetuities period. If a distributive power is exercised by creating another power, it is deemed to be exercised to whatever extent the second power may be exercised.

**(B)** ***Settlement***. A court-approved settlement of a bona fide issue regarding the administration of the trust or the construction of terms of the governing instrument will not cause an exempt trust to be subject to the provisions of chapter 13, if —

(1) The settlement is the product of arm's length negotiations; and

(2) The settlement is within the range of reasonable outcomes under the governing instrument and applicable state law addressing the issues resolved by the settlement. A settlement that results in a compromise between the positions of the litigating parties and reflects the parties' assessments of the relative strengths of their positions is a settlement that is within the range of reasonable outcomes.

**(C)** ***Judicial construction.*** A judicial construction of a governing instrument to resolve an ambiguity in the terms of the instrument or to correct a scrivener's error will not cause an exempt trust to be subject to the provisions of chapter 13, if —

(1) The judicial action involves a bona fide issue; and

(2) The construction is consistent with applicable state law that would be applied by the highest court of

the state.

***(D) Other changes.***

(1) A modification of the governing instrument of an exempt trust (including a trustee distribution, settlement, or construction that does not satisfy paragraph (b)(4)(i)(A), (B), or (C) of this section) by judicial reformation, or nonjudicial reformation that is valid under applicable state law, will not cause an exempt trust to be subject to the provisions of chapter 13, if the modification does not shift a beneficial interest in the trust to any beneficiary who occupies a lower generation (as defined in section 2651) than the person or persons who held the beneficial interest prior to the modification, and the modification does not extend the time for vesting of any beneficial interest in the trust beyond the period provided for in the original trust.

(2) For purposes of this section, a modification of an exempt trust will result in a shift in beneficial interest to a lower generation beneficiary if the modification can result in either an increase in the amount of a GST transfer or the creation of a new GST transfer. To determine whether a modification of an irrevocable trust will shift a beneficial interest in a trust to a beneficiary who occupies a lower generation, the effect of the instrument on the date of the modification is measured against the effect of the instrument in existence immediately before the modification. If the effect of the modification cannot be immediately determined, it is deemed to shift a beneficial interest in the trust to a beneficiary who occupies a lower generation (as defined in section 2651) than the person or persons who held the beneficial interest prior to the modification. A modification that is administrative in nature that only indirectly increases the amount transferred (e.g., by lowering administrative costs or income taxes) will not be considered to shift a beneficial interest in the trust. In addition, administration of a trust in conformance with applicable local law that defines the term income as a unitrust amount (or permits a right to income to be satisfied by such an amount) or that permits the trustee to adjust between principal and income to fulfill the trustee's duty of impartiality between income and principal beneficiaries will not be considered to shift a beneficial interest in the trust, if applicable local law provides for a reasonable apportionment between the income and remainder beneficiaries of the total return of the trust and meets the requirements of § 1.643(b)-1 of this chapter.

Because the regulations provide four “safe harbors,” other permitted modifications theoretically are possible. However, research in this area has failed to produce a private letter ruling that does not fall within a safe harbor.

Two examples cover the safe harbor for a trustee's exercise of a decanting power [105] as follows: [106]

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[105] Reg. § 26.2601-1(b)(4)(i)(A).

[106] Reg. § 26.2601-1(b)(4)(i)(E) *Exs.* 1 and 2.

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*Example 1. Trustee's power to distribute principal authorized under trust instrument.* In 1980, Grantor established an irrevocable trust (Trust) for the benefit of Grantor's child, A, A's spouse, and A's issue. At the time Trust was established, A had two children, B and C. A corporate fiduciary was designated as trustee. Under the terms of Trust, the trustee has the discretion to distribute all or part of the trust income to one or more of the group consisting of A, A's spouse or A's issue. The trustee is also authorized to distribute all or part of the trust principal to one or more trusts for the benefit of A, A's spouse, or A's issue under terms specified by the trustee in the trustee's discretion. Any trust established under Trust, however, must terminate 21 years after the death of the last child of A to die who was alive at the time Trust was executed. Trust will terminate on the death of A, at which time the remaining principal will be

distributed to A's issue, per stirpes. In 2002, the trustee distributes part of Trust's principal to a new trust for the benefit of B and C and their issue. The new trust will terminate 21 years after the death of the survivor of B and C, at which time the trust principal will be distributed to the issue of B and C, per stirpes. The terms of the governing instrument of Trust authorize the trustee to make the distribution to a new trust without the consent or approval of any beneficiary or court. In addition, the terms of the governing instrument of the new trust do not extend the time for vesting of any beneficial interest in a manner that may postpone or suspend the vesting, absolute ownership or power of alienation of an interest in property for a period, measured from the date of creation of Trust, extending beyond any life in being at the date of creation of Trust plus a period of 21 years, plus, if necessary, a reasonable period of gestation. Therefore, neither Trust nor the new trust will be subject to the provisions of chapter 13 of the Internal Revenue Code.

*Example 2. Trustee's power to distribute principal pursuant to state statute*. In 1980, Grantor established an irrevocable trust (Trust) for the benefit of Grantor's child, A, A's spouse, and A's issue. At the time Trust was established, A had two children, B and C. A corporate fiduciary was designated as trustee. Under the terms of Trust, the trustee has the discretion to distribute all or part of the trust income or principal to one or more of the group consisting of A, A's spouse or A's issue. Trust will terminate on the death of A, at which time, the trust principal will be distributed to A's issue, per stirpes. Under a state statute enacted after 1980 that is applicable to Trust, a trustee who has the absolute discretion under the terms of a testamentary instrument or irrevocable inter vivos trust agreement to invade the principal of a trust for the benefit of the income beneficiaries of the trust, may exercise the discretion by appointing so much or all of the principal of the trust in favor of a trustee of a trust under an instrument other than that under which the power to invade is created, or under the same instrument. The trustee may take the action either with consent of all the persons interested in the trust but without prior court approval, or with court approval, upon notice to all of the parties. The exercise of the discretion, however, must not reduce any fixed income interest of any income beneficiary of the trust and must be in favor of the beneficiaries of the trust. Under state law prior to the enactment of the state statute, the trustee did not have the authority to make distributions in trust. In 2002, the trustee distributes one-half of Trust's principal to a new trust that provides for the payment of trust income to A for life and further provides that, at A's death, one-half of the trust remainder will pass to B or B's issue and one-half of the trust will pass to C or C's issue. Because the state statute was enacted after Trust was created and requires the consent of all of the parties, the transaction constitutes a modification of Trust. However, the modification does not shift any beneficial interest in Trust to a beneficiary or beneficiaries who occupy a lower generation than the person or persons who held the beneficial interest prior to the modification. In addition, the modification does not extend the time for vesting of any beneficial interest in Trust beyond the period provided for in the original trust. The new trust will terminate at the same date provided under Trust. Therefore, neither Trust nor the new trust will be subject to the provisions of chapter 13 of the Internal Revenue Code.

Like a beneficiary exercising a nongeneral power of appointment over a Grandfathered Dynasty Trust, [107] a trustee exercising a decanting power over such a trust that satisfies the first safe harbor [108] may extend the trust until the end of the common-law rule against perpetuities, 90 years, or the shorter of such periods. But, a trustee exercising a decanting power under the fourth safe harbor (because the first safe harbor is not satisfied) may not lengthen the trust beyond the “period provided for in the original trust.” [109] Very few Grandfathered Dynasty Trusts probably will qualify under the first safe harbor for two reasons. First, it appears that relatively few pre-September 26, 1985, trusts conferred a decanting power upon the trustee. Second, although caselaw in Iowa, New Jersey, and Florida might have empowered a trustee to decant, [110] New York did not enact the first decanting statute until 1992. [111]

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[107] Reg. § 26.2601-1(b)(1)(v)(B)(2).

[108] Reg. § 26.2601-1(b)(4)(i)(A).

[109] Reg. § 26.2601-1(b)(4)(i)(D).

[110] *See In re Estate of Spencer*, 232 N.W.2d 491 (Iowa 1975); *Wiedenmayer v. Johnson*, 254 A.2d 534 (N.J. Super. Ct. App. Div. 1969); *Phipps v. Palm Beach Tr. Co.*, 196 So. 299 (Fla. 1940).

[111] N.Y. Est. Powers & Trusts Law § 10-6.6.

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The regulations also include an example that demonstrates the application of the safe harbor for judicial constructions [112] as follows: [113]

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[112] Reg. § 26.2601-1(b)(4)(i)(C). *See, e.g.*, PLR 201814002 (judicial construction of ambiguous term), PLR 201814001 (judicial construction of ambiguous term), PLR 201803003 (court construction), PLR 201735009 (construction), PLR 201732029 (reformation to correct scrivener error), PLR 201712003–005 (reformation to correct scrivener error and resolve ambiguity), PLR 201707003 – PLR 201707005 (construction).

[113] Reg. § 26.2601-1(b)(4)(i)(E) *Ex.* 3.

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*Example 3. Construction of an ambiguous term in the instrument.* In 1980, Grantor established an irrevocable trust for the benefit of Grantor's children, A and B, and their issue. The trust is to terminate on the death of the last to die of A and B, at which time the principal is to be distributed to their issue. However, the provision governing the termination of the trust is ambiguous regarding whether the trust principal is to be distributed per stirpes, only to the children of A and B, or per capita among the children, grandchildren, and more remote issue of A and B. In 2002, the trustee files a construction suit with the appropriate local court to resolve the ambiguity. The court issues an order construing the instrument to provide for per capita distributions to the children, grandchildren, and more remote issue of A and B living at the time the trust terminates. The court's construction resolves a bona fide issue regarding the proper interpretation of the instrument and is consistent with applicable state law as it would be interpreted by the highest court of the state. Therefore, the trust will not be subject to the provisions of chapter 13 of the Internal Revenue Code.

*Example 2* and *Examples 4–12* involve the application of the fourth safe harbor. [114] *Examples 4–12* cover:

• Change in trust situs; [115]

• Division of a trust; [116]

• Merger of a trust; [117]

• Modification that does not shift an interest to a lower generation; [118]

• Conversion of an income interest into unitrust interest; [119]

• Allocation of capital gain to income; [120]

• Administrative change to terms of a trust; [121]

• Conversion of income interest to unitrust interest under state statute; [122] and

• Equitable adjustments under state statute. [123]

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[114] Reg. § 26.2601-1(b)(4)(i)(D).

[115] Reg. § 26.2601-1(b)(4)(i)(E) *Ex.* 4.

[116] Reg. § 26.2601-1(b)(4)(i)(E) *Ex.* 5.

[117] Reg. § 26.2601-1(b)(4)(i)(E) *Ex.* 6.

[118] Reg. § 26.2601-1(b)(4)(i)(E) *Ex.* 7.

[119] Reg. § 26.2601-1(b)(4)(i)(E) *Ex.* 8.

[120] Reg. § 26.2601-1(b)(4)(i)(E) *Ex.* 9.

[121] Reg. § 26.2601-1(b)(4)(i)(E) *Ex.* 10.

[122] Reg. § 26.2601-1(b)(4)(i)(E) *Ex.* 11.

[123] Reg. § 26.2601-1(b)(4)(i)(E) *Ex.* 12.

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Reflecting that it is issued under the fourth safe harbor, the example regarding the change of a trust's situs provides as follows: [124]

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[124] Reg. § 26.2601-1(b)(4)(i)(E) *Ex.* 4.

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*Example 4. Change in trust situs.* In 1980, Grantor, who was domiciled in State X, executed an irrevocable trust for the benefit of Grantor's issue, naming a State X bank as trustee. Under the terms of the trust, the trust is to terminate, in all events, no later than 21 years after the death of the last to die of certain designated individuals living at the time the trust was executed. The provisions of the trust do not specify that any particular state law is to govern the administration and construction of the trust. In State X, the common law rule against perpetuities applies to trusts. In 2002, a State Y bank is named as sole trustee. The effect of changing trustees is that the situs of the trust changes to State Y, and the laws of State Y govern the administration and construction of the trust. State Y law contains no rule against perpetuities. In this case, however, in view of the terms of the trust instrument, the trust will terminate at the same time before and after the change in situs. Accordingly, the change in situs does not shift any beneficial interest in the trust to a beneficiary who occupies a lower generation (as defined in section 2651) than the person or persons who held the beneficial interest prior to the transfer. Furthermore, the change in situs does not extend the time for vesting of any beneficial interest in the trust beyond that provided for in the original trust. Therefore, the trust will not be subject to the provisions of chapter 13 of the Internal Revenue Code. If, in this example, as a result of the change in situs, State Y law governed such that the time for vesting was extended beyond the period prescribed under the terms of the original trust instrument, the trust would not retain exempt status.

A trust would fail this test if it provides that the duration of the trust will be governed by the law of the state where the trust is administered from time to time and if the trust is moved from a state that follows the

common-law rule against perpetuities to a state that does not. Conversely, a trustee might not "degrandfather" a trust if the trust expresses the intent that the trust be perpetual and if the trustee moves the trust as described in the preceding sentence, but it probably is impossible to get assurance on this point from the IRS. A Delaware statute provides that the duration of a trust does not change merely because it is moved to Delaware. [125]

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[125] Del. Code Ann. tit. 12, § 3332(a).

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Accordingly, attorneys should consider carefully any action (e.g., the modification of a trust's administrative terms, the exercise of a decanting power, the change of a trust's situs, the division or merger of a trust, a conversion to a unitrust, the exercise of a power to adjust, or the partial termination of a trust) that might affect a Grandfathered Dynasty Trust. In this regard, the IRS takes the position that moving a Grandfathered Dynasty Trust to save state income tax [126] or to utilize (or to avoid) another state's total return unitrust conversion law [127] or statutory power to adjust [128] will not cost the trust its grandfathered status.

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[126] Reg. § 26.2601-1(b)(4)(i)(D)(2).

[127] Reg. § 26.2601-1(b)(4)(i)(E) *Ex.* 11.

[128] Reg. § 26.2601-1(b)(4)(i)(E) *Ex.* 12.

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The IRS no longer will issue rulings on: [129]

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[129] Rev. Proc. 2019-3, § 3.01(108).

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Whether a trust exempt from generation-skipping transfer (GST) tax under § 26.2601-1(b)(1), (2), or (3) of the Generation-Skipping Transfer Tax Regulations will retain its GST exempt status when there is a modification of a trust, change in the administration of a trust, or a distribution from a trust in a factual scenario that is similar to a factual scenario set forth in one or more of the examples contained in § 26.2601-1(b)(4)(i)(E).

A trustee therefore may, without risk, modify a trust that is covered by a safe harbor without first obtaining a favorable private letter ruling. Nevertheless, it's not clear whether a trustee will cause a Grandfathered Dynasty Trust to lose its GST-exempt status if a proposed action meets the requirements of one safe harbor but fails the requirements of another. This might arise, for example, if the exercise of a decanting power complies with the first safe harbor but violates the fourth safe harbor because a change of trust situs is involved. The situation is further complicated by the fact that, after over 30 years under the current version of the GST tax, the tax effects of the forfeiture of grandfathered status remain uncertain. [130]

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[130] *See* 850 T.M., *Generation-Skipping Transfer Tax*.

It should also be noted that the IRS has indicated that it is studying and, thus, will not rule on (until it publishes guidance) whether a trustee's distribution of property from an irrevocable GST tax-exempt trust to another irrevocable trust (sometimes referred to as a decanting) resulting in a change in beneficial interests is a loss of such exempt status or constitutes a § 2612 taxable termination or taxable distribution for GST tax purposes. [131]

[131] Rev. Proc. 2019-3, § 5.01(13). The same ruling limitation applies to whether a trustee's distribution of property from an irrevocable trust to another irrevocable trust resulting in a change in beneficial interests is: (1) a distribution for which a § 661 deduction is allowable or § 662 gross income inclusion is required; and (2) a gift under § 2501. Rev. Proc. 2019-3, § 5.01(7), § 5.01(12).

### b. Exempt Dynasty Trusts

### (1) Exercise of Nongeneral Power of Appointment by Beneficiary

Given that Exempt Dynasty Trusts have been around since 1987, beneficiaries have begun to consider exercising nongeneral powers of appointment over them. By statute, such trusts are “exempt” from the reach of the GST tax, which means that the IRS has no clear authority to limit them. In recognition of this situation, the IRS has not issued any pertinent regulations concerning the exercise of nongeneral powers over Exempt Dynasty Trusts.

In a few instances, the IRS considered whether a beneficiary's exercise of a nongeneral power of appointment over an Exempt Dynasty Trust would change its inclusion ratio. [132] Each time, the IRS ruled that the trust would not lose its zero inclusion ratio because the donee did not exercise the power in a manner that would subject the trust assets to gift or estate tax and thereby cause him or her to become the transferor for GST tax purposes.

[132] *See* PLR 201013002, PLR 200928013, PLR 200236030, PLR 200219034. *See also O'Connell v. Houser*, 18 N.E.3d 344, 347–348 (Mass. 2014) (reformation of trust created by exercise of nongeneral power of appointment allowed to prevent loss of exempt status).

### (2) Other Modifications

There is also a dearth of guidance on the GST-tax consequences of other modifications to Exempt Dynasty Trusts. In numerous private letter rulings, the IRS approved modifications because they would have been permissible for Grandfathered Dynasty Trusts. [133] In a 2016 ruling, [134] for example, the IRS approved the modification of an Exempt Dynasty Trust to give the trustee discretion to reimburse the grantor for income taxes attributable to a grantor trust and included the following typical language: [135]

[133] *See, e.g.*, PLR 201829005, PLR 201820007 – PLR 201820008, PLR 201814005, PLR 201647001, PLR 201604001, PLR 201525001, PLR 201518002 – PLR 201518005, PLR 201418001, PLR 201417001 – PLR 201417002.

[134] PLR 201647001. *Accord* PLR 200822008. A trustee, who has a fiduciary duty to protect and preserve trust assets, should probably not initiate or consent to this modification because the trust will be diminished by taxes that otherwise would be paid by the grantor. But a trustee may join in a proceeding like that addressed in PLR 200848017, in which the IRS, without discussing GST tax issues, approved the conversion by the trustor and all beneficiaries of a nongrantor trust into a grantor trust.

[135] PLR 201647001.

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No guidance has been issued concerning changes that may affect the status of trusts that are exempt from GST tax because sufficient GST exemption was allocated to the trust to result in an inclusion ratio of zero. At a minimum, a change that would not affect the GST status of a trust that was irrevocable on September 25, 1985, should similarly not affect the exempt status of such a trust.

In other private letter rulings, the IRS approved modifications of Exempt Dynasty Trusts that would have been acceptable for Grandfathered Dynasty Trusts without justifying the application of these rules to Exempt Dynasty Trusts. [136] As a result, an Exempt Dynasty Trust may be modified, terminated, or divided and modified; a trustee may exercise a decanting power over or make a unitrust conversion for an Exempt Dynasty Trust; and the situs of an Exempt Dynasty Trust may be changed; and a scrivener error corrected, provided that the modification would have been allowed for a grandfathered trust. Interestingly, on several occasions, the IRS approved changes of trust situs between jurisdictions that allowed perpetual trusts. [137]

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[136] *See, e.g.*, PLR 200910003, PLR 200908003, PLR 200714016, PLR 200708001.

[137] *See* PLR 200841027, PLR 200840024, PLR 200839025 – PLR 200839027, PLR 200817009.

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As noted above, the IRS will no longer issue private letter rulings regarding modifications of Grandfathered Dynasty Trusts that satisfy the safe harbors in the GST regulations. It probably is safe for a beneficiary who exercises a nongeneral power of appointment over an Exempt Dynasty Trust and for a trustee who initiates a modification of such a trust to proceed without first getting a private letter ruling if the exercise or modification meets the conditions of one of those safe harbors, but the cautious attorney advising the beneficiary or trustee might conclude otherwise. In addition, a beneficiary or trustee of an Exempt Dynasty Trust might be able to go beyond the Grandfathered Dynasty Trust safe harbors, but the IRS has not conceded this, and the author is not aware of a private letter ruling that considers such an action. As also noted above, the IRS has indicated that it is studying and, thus, will not rule on certain GST and other tax issues concerning the decanting of irrevocable trusts. [138]

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[138] Rev. Proc. 2019-3, § 5.01(7), § 5.01(12), § 5.01(13).

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The author is often asked whether a Grandfathered Dynasty Trust or an Exempt Dynasty Trust may be moved to a perpetual-trust jurisdiction from a state that does not permit perpetual trusts if the governing instrument expresses the intent that the trust be perpetual. This move should be possible under the language quoted above.

### c. Nonexempt Dynasty Trusts

Given that a Nonexempt Dynasty Trust has an inclusion ratio of one, a beneficiary's exercise of a nongeneral power of appointment over such a trust and a modification of its provisions usually will not affect its GST tax status. But, as shown in several 2010 private letter rulings, [139] the modification of trusts that are not grandfathered or exempt for GST tax purposes may raise various GST tax concerns. In the rulings in question, the initial transfers were direct skips into trust so that GST tax was payable at the outset. The parties were concerned that merger of the trusts might cause distributions that otherwise would be tax-free to be subject to tax. The IRS issued reassuring rulings as follows: No guidance has been issued concerning modifications that may affect the status of GST exempt distributions to the highest generation individual having an interest in a direct skip trust. At a minimum, a modification that would not affect the GST status of a grandfathered trust should similarly not affect the exempt status of distributions to the highest generation individual having an interest in a direct skip trust.

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[139] PLR 201025026, PLR 201024014 – PLR 201024016.

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## 3. Section 2041(a)(3) and § 2514(d) — The Delaware Tax Trap (Opportunity)

### a. Introduction

Estate planning attorneys throughout the United States have long fretted about the poorly understood aspect of the federal tax laws known as the Delaware Tax Trap, which is codified in § 2041(a)(3) and § 2514(d). Although practitioners have had a vague notion that triggering the Delaware Tax Trap might be beneficial in certain situations, they have been scared to death that a client's exercise of a power of appointment might inadvertently subject a trust to federal estate or gift tax. [140] As a result, the goal has been to escape the Delaware Tax Trap at all costs.

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[140] *See* Kolaso, *Problems in Springing the Delaware Tax Trap*, 157 Tr. & Est. 12 (Apr. 2018); Raatz, *USRAP Surprise Trigger of Delaware Tax Trap*, 43 Est. Plan. 22 (May 2016); Nenno, *Getting A Stepped-Up Income-Tax Basis and More by Springing — or Not Springing — The Delaware Tax Trap the Old-Fashioned Way*, 40 Tax Mgmt. Est., Gifts & Tr. J. 215 (Sept. 10, 2015); Raatz, *Delaware Tax Trap Opens Door to Higher Basis for Trust Assets*, 41 Est. Plan. 3 (Feb. 2014); 825 T.M., *Powers of Appointment — Estate, Gift, and Income Tax Considerations*; 850-2d T.M., *Generation Skipping Transfer Tax* at A-62. *See also* Zaritsky, *The Rule Against Perpetuities: A Survey of State (and D.C.) Law* (Mar. 2012), www.actec.org/assets/1/6/Zaritsky_RAP_Survey.pdf .

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Times change. Hence, more than ever, the Delaware Tax “Trap” might be the Delaware Tax “Opportunity.”

It is true that planners must still avoid stumbling into the Delaware Tax Trap for many trusts. For example, it would be disastrous for a client to spring the Delaware Tax Trap in a Grandfathered Dynasty Trust or an Exempt Dynasty Trust if the client already had enough assets to exhaust his or her federal estate tax exemption, which is a lofty $10 million (indexed for inflation). [141] This is because springing the Delaware Tax Trap would subject assets to a 40% federal transfer tax that otherwise would pass free of tax for one or more additional generations.

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[141] § 2010(c)(3)(C), added by Pub. L. No. 115-97, § 11061. This exemption amount will revert to $5 million (plus an inflation adjustment) in 2026. For the inflation-adjusted gift-tax, estate-tax, and GST exclusion amounts for recent years, see 800 T.M., *Estate Planning*, Worksheet 1.

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Similarly, given that (1) the federal estate tax exemption and the GST exemption are equal, (2) the federal estate tax rate and the GST tax rate are equal at 40%, and (3) a stepped-up income-tax basis is available under § 1014 for assets owned at death and under § 2654(a)(2) for assets that are subject to a taxable termination, the decision to spring or not to spring the Delaware Tax Trap for a Nonexempt Dynasty Trust will often be tax-neutral. It would be disadvantageous, however, to trigger the Delaware Tax Trap if doing so would subject trust assets to state death tax. [142]

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[142] *See* Fox, 2018 *State Death Tax Chart* (Nov. 2, 2018), www.actec.org/resources/state-death-tax-chart/.

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Nevertheless, given the increasing exemption amount, clients might sometimes benefit more by forgoing continued immunity from GST tax in order to obtain a stepped-up income tax basis. Thus, a client might want to spring the Delaware Tax Trap for a Grandfathered Dynasty Trust or an Exempt Dynasty Trust in order to obtain a stepped-up income tax basis under § 1014 to the extent the client has available federal estate tax exemption. Unused GST exemption might then be allocated to those trust assets.

Although various commentators have developed ways to trigger the Delaware Tax Trap by exercising nongeneral powers of appointment to confer presently exercisable general powers of appointment, these commentators recognize that there is a crucial risk with this technique: the donee of the presently exercisable general power might exercise that power and take the money. [143] Instead, the author will focus on the original approach, viz., the successive exercise of nongeneral powers of appointment.

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[143] *See* 825 T.M., *Powers of Appointment — Estate, Gift, and Income Tax Considerations*; Blattmachr & Pennell, *Adventures in Generation-Skipping, or How We Learned to Love the 'Delaware Tax Trap'*, 24 Real Prop., Prob. & Tr. J. 75 (Spring 1989); Blattmachr & Pennell, *Using the 'Delaware Tax Trap' to Avoid Generation-Skipping Taxes*, 68 J. Tax'n 242 (Apr. 1988).

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Accordingly, the author will use the following definitions:
• First Power — a nongeneral lifetime or testamentary power of appointment granted by a Will or an inter vivos trust instrument.

• Second Power — a second or further nongeneral lifetime or testamentary power of appointment conferred by a First Power.

The rest of this II.F.3. will:
• Review the Delaware Tax Trap's history.

• Describe how to spring and not to spring the Delaware Tax Trap.

• Discuss when to spring and not to spring the Delaware Tax Trap.

• Summarize how the Delaware Tax Trap works under current Delaware law.

• Note how the Delaware Tax Trap works under the laws of some other states.

• Identify related issues.

## b. History

Under Delaware statutory law, the exercise of a power of appointment usually begins a new perpetuities period. [144] The predecessor to this provision, which was enacted in 1933, provided: [145]

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[144] Del. Code Ann. tit. 25, § 501(a).

[145] 38 Del. Laws 198, § 1 (1933) (emphasis added).

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Every estate or interest in property, real or personal, created through the exercise, by will, deed or other instrument, of a power of appointment, irrespective of whether such power is limited or unlimited as to appointees, irrespective of the manner in which such power was created or may be exercised, and irrespective of whether such power was created before or after the passage of this Act, shall for the purpose of any rule of law against perpetuities, remoteness in vesting, restraint upon the power of alienation or accumulations now in effect or hereafter enacted be deemed to have been created at the *time of the exercise and not at the time of the creation* of such power of appointment; and no such estate or interest shall be void on account of any such rule unless such estate or interest would have been void had it been created at the *date of the exercise* of such power of appointment otherwise than through the exercise of a power of appointment.

The above provision offered the possibility, through the exercise of nongeneral powers of appointment in successive generations, of having a perpetual trust without the imposition of federal transfer tax.

Illustration: Fred died in 1934. In his Will, he created a trust for his daughter Alice for her life, giving her a First Power. At Alice's death in 1959, the trust was not subject to federal estate tax because she held only a nongeneral power of appointment. By her Will, she exercised her First Power to create a trust for her son George, giving him a Second Power. Under the Delaware statute, the determination of whether Delaware's traditional rule against perpetuities was violated was measured from the date of Alice's death, not from the date of Fred's death. Under this regime, assets could remain in trust perpetually, and no federal estate tax would be due other than at Fred's death.

To prevent taxpayers from availing themselves of this opportunity, the predecessor to § 2041(a)(3) was enacted in 1951. [146] Under this provision, a trust is subject to federal estate tax at the death of the donee of a First Power who "exercises a power of appointment created after October 21, 1942, by creating another power of appointment which under the applicable local law can be validly exercised so as to postpone the vesting of any estate or interest in such property, or suspend the absolute ownership or power of alienation of such property, *for a period ascertainable without regard to the date of the creation of the First Power*." [147]

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[146] The corresponding federal gift tax provision is § 2514(d).

[147] § 2041(a)(3) (emphasis added). *See* Reg. § 20.2041-3(e)(1).

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The legislative history to § 2041(a)(3) makes clear that the Delaware statute was Congress's target: [148]

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[148] S. Rep. No. 82-382 (1951).

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In at least one state [i.e., Delaware] a succession of powers of appointment, general or limited may be created and exercised over an indefinite period without violating the rule against perpetuities. In the absence of some special provision in the statute, property could be handed down from generation to generation without ever being subject to estate tax.

The determination as to whether the donee springs the Delaware Tax Trap is based on (1) the instrument that created the First Power, (2) the instrument that exercises the First Power to create a Second Power, and (3) applicable local law. [149]

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[149] Reg. § 20.2041-3(e)(1)(ii).

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Consequently, even if state law provides that the exercise of a First Power to create a Second Power starts a new perpetuities period, and even if the instrument granting the First Power does not limit the First Power's exercise, the donee may avoid invoking § 2041(a)(3) by including appropriate limitations in the instrument exercising the First Power to create the Second Power. To prevent triggering the Delaware Tax Trap, instruments exercising First Powers over Grandfathered Dynasty Trusts in Delaware typically include language such as the following:

I further direct that any power of appointment conferred upon any person under the provisions of this instrument may not be exercised in any manner which would vest an interest in trust beyond the expiration of twenty-one (21) years after the death of the last survivor of my spouse and my issue living on [date original trust became irrevocable]. If any such power is so exercised, I direct that it be declared void ab initio.

The regulations illustrate the application of the Delaware Tax Trap as follows: [150]

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[150] Reg. § 20.2041-3(e)(2) (citation omitted).

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If...the decedent appoints the income from the entire [$100,000] fund to a beneficiary for life with power in the beneficiary to appoint the remainder by will, the entire $100,000 will be includable in the decedent's gross estate under section 2041(a)(3) if the exercise of the Second Power can validly postpone the vesting of any estate or interest in the property or can suspend the absolute ownership or power of alienation of the property for a period ascertainable without regard to the date of the creation of the First Power.

## c. Case law

The only reported case that has considered § 2041(a)(3) is *Estate of Murphy v. Commissioner* (1979), [151] in which the Tax Court held that the exercise of a First Power to create a Second Power had not sprung the Delaware Tax Trap because, under applicable Wisconsin law, the exercise of a nongeneral power of appointment had not commenced a new perpetuities period. The IRS acquiesced in the result. [152] The Action on Decision explained that: [153]

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[151] *Estate of Murphy v. Commissioner*, 71 T.C. 671 (1979).

[152] 1979-2 C.B. 1 (May 1979).

[153] AOD 1979-87, 1979 WL 53162, at *1.

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Section 2041(a)(3) refers to the creation of a power which under state law can be validly exercised so as to postpone vesting or suspend ownership "for a period ascertainable without regard to the date of the creation of the [F]irst [P]ower." Since the Wisconsin rule measures the period from the creation of the first nongeneral power, the statute by its very words cannot apply. This conclusion is supported by Treas. Reg. § 20.2041-3(e)(1)(ii). While an argument can be made that Congress intended to tax all creations of successive powers where vesting or ownership/power of alienation are affected, without regard to state law, such an argument ignores the very language of the Code and regulation. The regulation itself indicates that postponing of vesting and suspension of ownership/alienation power are mutually exclusive conditions of includibility which are governed by the particular applicable state law. Finally, under Wisconsin law, ownership has not been suspended because the trustee was given the power to sell trust assets. The regulation, as it is written, appears to say that because local law is phrased in terms of the suspension of ownership/power of alienation, and if there is no such suspension under that local law, then section 2041(a)(3) cannot apply.

## d. How and When to Spring the Delaware Tax Trap

As noted above, § 2041(a)(3) provides for estate taxation if a trust beneficiary:

Exercises a power of appointment created after October 21, 1942, by creating another power of appointment which under the applicable local law can be validly exercised so as to postpone the vesting of any estate or interest in such property, or suspend the absolute ownership or power of alienation of such property, for a period ascertainable without regard to the date of the creation of the [F]irst [P]ower.

Hence, for a trust to be includible in the gross estate of the donee of a First Power created after October 21, 1942, the donee must:
• Exercise the First Power.

• Exercise the First Power to create a Second Power.

• Exercise the First Power to create a Second Power that, under applicable local law, can be validly exercised to do one of the following for a period ascertainable without regard to the date of the creation of the First Power.

• Postpone the vesting of any estate or interest in such property.

• Suspend the absolute ownership or power of alienation of such property.

Conversely, the donee of a First Power will not fall into the Delaware Tax Trap if the donee
• Does not exercise the First Power.

• Exercises the First Power but does not create a Second Power.

• Exercises the First Power to create a Second Power that is tied to the date of creation of the First Power.

From the foregoing, it is apparent that the key to whether the exercise of a First Power to create a Second Power springs the Delaware Tax Trap is whether the duration of trusts created by the Second Power will be based on the date of creation of the First Power or on the date of the First Power's exercise. If tied to the date of creation, then the Delaware Tax Trap should not be sprung; if tied to the date of exercise, then the Delaware Tax Trap should be sprung. The author summarizes where various states stand on this issue below.

Some commentators have suggested that the Delaware Tax Trap makes it impossible for donees to exercise First Powers to create Second Powers over trusts created in states that allow perpetual trusts without adverse tax consequences. This concern was articulated in a 2009 article in the following way: "To avoid the Trap, it is necessary to specify a period during which vesting may be postponed, or absolute ownership or the power of alienation suspended, that begins on the date of the Second Power's exercise and ends on a date that cannot be ascertained without regard to the date of creation of the First Power. *Such a period must be finite*." [154]

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[154] Spica, *A Trap for the Wary: Delaware's Anti-Delaware-Tax-Trap Statute Is Too Clever by Half (of Infinity)*, 43 Real Prop., Tr. & Est. J. 673, 682 (Winter 2009) (emphasis added).

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As a result, several states have set a maximum period (ranging from 360 years to 1,000 years) for the duration of trusts created by the exercise of nongeneral powers of appointment. [155]Several comments are in order in this regard.
• The fixed-period requirement appears nowhere in the authorities summarized above. This isn't surprising because perpetual trusts were not generally available when the authorities were developed, but the fact remains that a fixed period is not required by the tax laws or regulations. The primary authority cited by the author of the above article is an earlier article that also cites meager sources. [156]

• The argument assumes that § 2041(a)(3) requires the existence of a "fixed period" to escape the Delaware Tax Trap's application. In fact, by its terms, § 2041(a)(3) only applies to a Second Power that can be exercised to suspend vesting for one type of period — a "period ascertainable without regard to the date of the creation of the first power." [157] If the Second Power can be exercised to suspend vesting indefinitely and if this is not a "period," then the statute literally does not apply.

• Even if avoidance of § 2041(a)(3) does require a "period" to demonstrate that such a period was ascertainable with regard to the date of the creation of the First Power, Delaware and other perpetual-trust states do have such a period — an indefinite one. The notion that a period may be indefinite is consistent with dictionary meanings of the word. For example, the *Oxford English Dictionary* [158]defines "period" as both "an indefinite portion of time" and as "any specified portion or division of time."

• It is difficult to distinguish in any practical sense among states that permit perpetual trusts and states with definite periods of such inordinate length (such as 360 years or 1,000 years) that they might as well be indefinite. Note that the foregoing fixed periods greatly exceed the IRS's "safe harbor" period (the common-law rule against perpetuities, 90 years, or the shorter of such periods) in the regulations for the exercise of nongeneral powers of appointment over Grandfathered Dynasty Trusts. [159]These regulations apply to any exercise of a power and not just to an exercise of a First Power that creates a Second Power. [160] The regulations suggest that if an ending period is essential to escape the application of § 2041(a)(3), then the IRS will require such an ending period to be no longer than the traditional period or 90 years. During informal discussions in 2003, IRS representatives confirmed this view with the author. At that time, the IRS declined to issue a revenue ruling or private letter ruling on the Delaware Tax Trap.

• Given that the determination of whether the Delaware Tax Trap will be triggered is based, in part, on the instrument exercising the First Power, [161] such instruments should place a maximum fixed period on trusts that are created by the exercise of Second Powers if the drafting attorney shares this concern.

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[155] *See* Worksheet 4, below.

[156] Greer, *The Alaska Dynasty Trust*, 18 Alaska L. Rev. 253, 276 (Dec. 2001).

[157] § 2041(a)(3).

[158] Oxford English Dictionary (24th ed. 1985).

[159] Reg. § 26.2601-1(b)(1)(v)(B)(2).

[160] *See* Reg. § 26.2601-1(b)(1)(v)(B)(2).

[161] Reg. § 20.2041-3(e)(1).

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The Delaware Tax Trap will be of particular concern for a donee who is exercising a First Power over a Grandfathered Dynasty Trust because, if the power is exercised improperly, he or she might subject an otherwise tax-free trust to estate or gift tax. Nonetheless, the Delaware Tax Trap will rarely be of concern for Grandfathered Dynasty Trusts for at least two reasons. First, very few states allowed perpetual trusts before September 26, 1985. Therefore, most Grandfathered Dynasty Trusts expressly require all trusts (including those established through the exercise of powers of appointment) to terminate at the end of the common-law period. Second, the GST regulations allow a donee who is exercising a nongeneral power of appointment over a Grandfathered Dynasty Trust (whether or not he or she creates a Second Power) to extend the trust until the expiration of the common-law rule against perpetuities, the passage of 90 years, or the end of the shorter of those periods. [162] If a donee complies with these regulations, then he or she will probably not have a Delaware-Tax-Trap concern.

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[162] Reg. § 26.2601-1(b)(1)(v)(B)(2).

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On several occasions, the IRS has ruled that exercises of First Powers over Grandfathered Dynasty Trusts to create Second Powers would not cause the trusts to lose their tax-favored status. [163]

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[163] *See* PLR 201029011, PLR 200535009, PLR 200243048, PLR 200206045, PLR 200124006, PLR 199912021, PLR 9351016.

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The Delaware Tax Trap can pose a significant problem for Exempt Dynasty Trusts. As shown in Worksheet 4, below, over half the states currently authorize perpetual or very long trusts, and many Exempt Dynasty Trusts take advantage of these statutes. Exempt Dynasty Trusts typically also confer First Powers that enable donees to modify trust terms over time to adapt to changing circumstances. Assessing the potential impact of the Delaware Tax Trap is crucial to this planning.

As discussed above, the donee of a First Power over an Exempt Dynasty Trust should not create federal gift or estate tax liability if he or she does not exercise the First Power to create a Second Power or includes appropriate limiting language in the Will or instrument by which the power is exercised.

In a 2002 private letter ruling, [164] the IRS concluded that a donee's exercise of a First Power to create a Second Power had not caused an Exempt Trust to lose its zero inclusion ratio because all resulting trusts had had to terminate within the common-law perpetuities period determined from the date of creation of the original trust.

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[164] PLR 200219034.

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Placing a fixed limitation on the duration of trusts created by the exercise of First Powers over Exempt Dynasty Trusts puts a state that is trying to attract trust business at a serious competitive disadvantage. The problem is that once an Exempt Dynasty Trust is established in one of these states, the trust cannot be moved to a state with a longer perpetuities period without adverse transfer-tax consequences; this situation will discourage wealthy families who want to preserve flexibility from creating trusts in that state in the first place. [165] This is particularly true for states that set relatively short fixed periods.

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[165] *See* Reg. § 26.2601-1(b)(4)(i)(E) *Ex.* 4.

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Theoretically, the Delaware Tax Trap might be triggered in a state that still follows the common-law rule against perpetuities. For example, Parent creates a trust for the lifetime benefit of Child, remainder to Grandchild, and grants Child the power to appoint trust property either outright or in further trust to Grandchild. As part of this power, Child can grant Grandchild a nongeneral power of appointment. The trust is subject to the laws of a jurisdiction under which Grandchild's exercise of a nongeneral power of appointment starts a new perpetuities period. If Child exercises the First Power by creating a trust for Grandchild and granting Grandchild a Second Power, then the property of Grandchild's trust will be includible in Child's estate under § 2041(a)(3) because Child has exercised the First Power by creating a Second Power that may be exercised so as to suspend absolute ownership of trust property without reference to the date of the trust created by Parent. [166]

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[166] *See* 825 T.M., *Powers of Appointment — Estate, Gift, and Income Tax Considerations*.

Therefore, a donee who is exercising a First Power must consider the Delaware Tax Trap in almost every state. Given the prevalence of the issue, attorneys who draft new trusts or instruments exercising powers of appointment should include language to alert donees and their attorneys to this concern.

The Delaware Tax "Trap" might be the Delaware Tax "Opportunity" for a Nonexempt Dynasty Trust given the substantial increase in the federal estate tax exemption ($10 million indexed for inflation). [167] An individual's federal tax liability might sometimes be lower if the trust assets are subject to estate tax and might sometimes be lower if they are subject to GST tax. Various mechanisms have been suggested to minimize a trust beneficiary's total transfer-tax liability, but these mechanisms usually depend on the inclusion of a formula in the original trust instrument or the exercise of discretion by a trustee who might possess less than complete information.

[167] § 2010(c)(3)(C), added by Pub. L. No. 115-97, § 11061. This exemption amount will revert to $5 million (plus an inflation adjustment) in 2026. For the inflation-adjusted gift-tax, estate-tax, and GST exclusion amounts for recent years, see 800 T.M., *Estate Planning,* Worksheet 1.

The Delaware Tax Trap might provide the ideal mechanism because it gives the donee the ability to choose between estate tax and GST tax in light of circumstances as they are at the time of the choice. Thus, if the donee's tax liability will be lower if the trust is subject to estate tax (which might be the case if the estate is below the exemption amount in the year of death and if a stepped-up income tax basis is desirable), then he or she might exercise a First Power to trigger the Delaware Tax Trap. Conversely, if the donee's tax liability will be lower if a trust were subject to the GST tax (which might be the case if he or she lives in a state that has a death tax), then he or she might refrain from exercising a First Power (or exercise it in a way that does not spring the Delaware Tax Trap).

### e. Current Delaware Law

The common-law rule against perpetuities has been abolished in Delaware. The basic rule is as follows: [168]

[168] Del. Code Ann. tit. 25, § 503(a).

No interest created in real property held in trust shall be void by reason of the common-law rule against perpetuities or any common-law rule limiting the duration of noncharitable purpose trusts, and no interest created in personal property held in trust shall be void by reason of any rule, whether the common-law rule against perpetuities, any common-law rule limiting the duration of noncharitable purpose trusts, or otherwise.

Trust interests in personal property may be perpetual, but trust interests in real property must be distributed "at the expiration of 110 years from the later of the date on which a parcel of real property or an interest in real property is added to or purchased by a trust or the date the trust became irrevocable." [169]The 110-year limitation may be circumvented by contributing a parcel of real property to an entity because "real property does not include any intangible personal property such as an interest in a

corporation, limited liability company, partnership, statutory trust, business trust or other entity, regardless of whether such entity is the owner of real property or any interest therein." [170]

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[169] Del. Code Ann. tit. 25, § 503(b).

[170] Del. Code Ann. tit. 25, § 503(e). The subsection addresses what happens if such an entity ceases to exist.

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Delaware law generally measures violations of the rule against perpetuities from the date of exercise (rather than from the date of creation) of powers of appointment. The basic rule is: [171]
(a) Except as otherwise provided in subsection (b) of this section, every estate or interest in property, real or personal, created through the exercise, by will, deed or other instrument, of a power of appointment, irrespective of:

(1) Whether such power is nongeneral or general as to appointees;

(2) The manner in which such power was created or may be exercised;

(3) Whether such power was created before or after the passage of this section, shall, for the purpose of any rule of law against perpetuities, remoteness in vesting, restraint upon the power of alienation or accumulations now in effect or hereafter enacted be deemed to have been created at the time of the exercise and not at the time of the creation of such power of appointment. No such estate or interest shall be void on account of any such rule unless the estate or interest would have been void had it been created at the date of the exercise of such power of appointment otherwise than through the exercise of a power of appointment.

(b) Subsection (a) of this section shall not apply to the exercise of a power over property held in a trust if the instrument of exercise of any such power makes express reference to this section and expressly states that the provisions of this subsection shall apply. If the provisions of this subsection apply, every estate or interest in property, real or personal, created through the exercise, by will, deed or other instrument, of a power of appointment, irrespective of:

(1) Whether such power is nongeneral or general as to appointees;

(2) The manner in which such power was created or may be exercised;

(3) Whether such power was created before or after the passage of this section, shall, for the purpose of any rule of law against perpetuities, remoteness in vesting, restraint upon the power of alienation or accumulations now in effect or hereafter enacted, be deemed to have been created at the time of the creation and not at the time of the exercise of such power of appointment.

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[171] Del. Code Ann. tit. 25, § 501. Rules are set for releasing powers of appointment (Del. Code Ann. tit. 25, § 502).

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Regarding the above rule, another section provides that "trusts created by the exercise of a power of appointment, whether nongeneral or general, and whether by will, deed or other instrument, shall be

deemed to have become irrevocable by the trustor or testator on the date on which such exercise became irrevocable." [172]

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[172] Del. Code Ann. tit. 25, § 503(c).

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The law is mindful of not falling into the Delaware Tax Trap through the exercise of First Powers over Grandfathered Dynasty Trusts and Exempt Dynasty Trusts in most situations. Accordingly, the general rule is reversed for these trusts as follows: [173]

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[173] Del. Code Ann. tit. 25, § 504(a) (citation omitted).

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Notwithstanding any other provision of this chapter, and except as otherwise provided in subsection (b) of this section, in the case of a power of appointment over property held in trust (the "first power"), if the trust is not subject to, or has an inclusion ratio of zero for purposes of, the tax on generation-skipping transfers imposed pursuant to Chapter 13 of the Internal Revenue Code or any successor provision thereto and the first power may not be exercised in favor of the donee, the donee's creditors, the donee's estate or the creditors of the donee's estate, then every estate or interest in property, real or personal, created through the exercise, by will, deed or other instrument, of the first power, irrespective of:

(1) The manner in which the first power was created or may be exercised, or

(2) Whether the first power was created before or after the passage of this section, shall, for the purpose of any rule of law against perpetuities, remoteness in vesting, restraint upon the power of alienation or accumulations now in effect or hereafter enacted, be deemed to have been created at the time of the creation of, and not at the time of the exercise of, the first power. For purposes of applying the foregoing rule, if any part of an estate or interest in property created through the exercise of the first power includes another power of appointment (the "second power"), then the second power of appointment and any estate or interest in property (including additional powers of appointment) created through the exercise of the second power shall be deemed to have been created at the time of the creation of the first power.

Elsewhere, the law provides: [174]

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[174] Del. Code Ann. tit. 25, § 503(c).

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Notwithstanding the foregoing, in the case of a power of appointment described in § 504 of this title as a "first power," and subject to § 504(a) of this title, trusts created by the exercise of the power of appointment, whether by will, deed or other instrument, shall be deemed to have become irrevocable by the trustor or testator on the date on which the first power was created.

But the law recognizes that it might be desirable to spring the Delaware Tax Trap over Grandfathered Dynasty Trusts and Exempt Dynasty Trusts: [175]

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[175] Del. Code Ann. tit. 25, § 504(b) (citation omitted). The law addresses the manner in which powers of appointment may be exercised (Del. Code Ann. tit. 25, § 505).

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Subsection (a) of this section shall not apply to the exercise of a first power or Second Power over property held in a trust that is not subject to, or has an inclusion ratio of zero for purposes of, the tax on generation-skipping transfers imposed pursuant to Chapter 13 of the Internal Revenue Code or any successor provision thereto if the instrument of exercise of any such power makes express reference to subsection (a) of this section and expressly states that subsection (a) of this section shall not apply to the exercise of the power or makes express reference to § 501 of this title and expressly states that § 501 of this title shall apply to the exercise of the power.

### f. State of the Delaware Tax Trap in Some Other States

In the author's experience, Alaska, Delaware, Nevada, and South Dakota are viewed as leading personal trust states. As described above, the donee of a First Power over a Delaware trust can exercise the power to spring the Delaware Tax Trap and get a stepped-up income tax basis. This option does not appear to be available in Alaska, Nevada, or South Dakota.

A testator or trustor may create a perpetual Alaska trust, [176] but trusts created via the exercise of nongeneral powers of appointment are limited to 1,000 years. [177] The donee of a First Power over an Alaska Trust cannot spring the Delaware Tax Trap because the duration of trusts created by First Powers and Second Powers relates back to the creation of the First Power under the following provision: [178]

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[176] Alaska Stat. § 34.27.075, § 34.27.100.

[177] Alaska Stat. § 34.27.051(a).

[178] Alaska Stat. § 34.27.051(c).

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If a nongeneral power of appointment is exercised to create a new or successive nongeneral power of appointment...all property interests subject to the exercise of that new or successive nongeneral...power of appointment are invalid unless, within 1,000 years from the time of creation of the original instrument or conveyance creating the original nongeneral power of appointment that is exercised to create a new or successive nongeneral...power of appointment, the property interests that are subject to the new or successive nongeneral...power of appointment either vest or terminate.

A Nevada statute [179] allows trusts created by Will, inter vivos trust instruments, and exercises of nongeneral powers of appointment to last for 365 years. For the reasons given in V.D., below, the statute may very well be invalid. In any event, the following statute [180] prevents the donee of a First Power over a Nevada trust from triggering the Delaware Tax Trap: “For purposes of NRS 111.103 to 111.1039, inclusive, a nonvested property interest or a power of appointment arising from a transfer of property to a previously funded trust or other existing property arrangement is created when the nonvested property interest or power of appointment in the original contribution was created.”

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[179] Nev. Rev. Stat. § 111.1031(1)(b), (3)(b).

[180] Nev. Rev. Stat. § 111.1033(3).

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South Dakota permits trusts created by Will, inter vivos trust instruments, and exercises of powers of appointment to be perpetual. [181] Nevertheless, the donee of a First Power over a South Dakota trust cannot spring the Delaware Tax Trap as a result of the following statute: "If a future interest or trust is created by exercise of a power of appointment, the permissible period is computed from the time the power...is created if the power is not a general power." [182] Nor can the Delaware Tax Trap be sprung in the states described below.

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[181] S.D. Codified Laws § 43-5-8.

[182] S.D. Codified Laws § 43-5-5.

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Connecticut follows the Uniform Statutory Rule Against Perpetuities (USRAP). Thus, a trust created by a Will or inter vivos trust instrument [183] or by the exercise of a power of appointment [184] must vest at the expiration of the common-law rule against perpetuities or at the expiration of 90 years after creation. The Delaware Tax Trap cannot be triggered because the date of creation relates back to the creation of the original trust under the following statute: "For purposes of sections 45a-490 to 45a-496, inclusive, a...power of appointment arising from a transfer of property to a previously funded trust or other existing property arrangement is created when the...power of appointment in the original contribution was created." [185]

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[183] Conn. Gen. Stat. § 45a-491(a). The Uniform Law Commission provides a copy of the USRAP at https://www.uniformlaws.org/home.

[184] Conn. Gen. Stat. § 45a-491(c).

[185] Conn. Gen. Stat. § 45a-492(c).

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A Florida statute [186] allows trusts created by Will, inter vivos trust instruments, and exercises of nongeneral powers of appointment to last for 360 years. The Delaware Tax Trap cannot be triggered because the date of creation relates back to the creation of the original trust under the following statute: [187]

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[186] Fla. Stat. § 689.225(2)(f).

[187] Fla. Stat. § 689.225(3)(e).

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For purposes of this section, if a nongeneral or testamentary power of appointment is exercised to create another nongeneral or testamentary power of appointment, every nonvested property interest or power of

appointment created through the exercise of such other nongeneral or testamentary power is considered to have been created at the time of the creation of the first nongeneral or testamentary power of appointment.

In Maryland, trusts created by Will, inter vivos trust instruments, and exercises of powers of appointment may be perpetual, [188] but caselaw prevents the donee of a First Power over a Maryland trust from springing the Delaware Tax Trap. [189]

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[188] Md. Code Ann., Est. & Trusts § 11-102(b)(5).

[189] *See*, *e.g.*, *Arrowsmith v. Mercantile-Safe Deposit & Tr. Co.*, 545 A.2d 674, 678 (Md. 1988) ("The period of the Rule is calculated from the date of the deed of trust creating the power and not from the exercise of the power by the will").

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In New Hampshire, a trust may be perpetual if the governing instrument expressly exempts the trust from the application of the rule against perpetuities and if the trustee or another person has the power to sell, mortgage, or lease trust property for any period beyond the period that would be required for an interest in the trust to vest in order to be valid under the rule against perpetuities. [190] Given that New Hampshire has no statute regarding the beginning date for measuring the validity of the exercise of a power of appointment or when a First Power becomes irrevocable, the Delaware Tax Trap cannot be sprung in New Hampshire because, under the common law, the duration of trusts created by powers of appointment dates back to the creation of the original trust. [191]

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[190] N.H. Rev. Stat. Ann. § 564-B:4-402A, § 564:24, § 547:3-k.

[191] 850 T.M., *Generation-Skipping Transfer Tax*.

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In New Jersey, trusts created by Will, inter vivos trust instruments, and exercises of powers of appointment may be perpetual, [192] but the donee of a First Power over a New Jersey trust cannot spring the Delaware Tax Trap by reason of the following statute: [193]

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[192] N.J. Stat. Ann. § 46:2F-9.

[193] N.J. Stat. Ann. § 46:2F-10(a)(3).

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If a future property interest or trust is created by exercise of a power of appointment, the permissible period is computed from the time the power is exercised if the power is a general power exercisable in favor of the donee, the donee's estate, the donee's creditors or the creditors of the donee's estate, whether or not it is exercisable in favor of others, and even if the general power is exercisable only by will; in the case of other powers the permissible period is computed from the time the power is created.

Trusts created by Will, inter vivos trust instruments, and exercises of powers of appointment in New York are subject to the common-law rule against perpetuities. [194] A donee who exercises a First Power over a

New York trust cannot trigger the Delaware Tax Trap pursuant to the following statute: [195]

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[194] N.Y. Est. Powers & Trusts Law § 9-1.1

[195] N.Y. Est. Powers & Trusts Law § 10-8.1(a).

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Where an estate is created by an instrument exercising a power of appointment, the permissible period of the rule against perpetuities begins:

(1) In the case of an instrument exercising a general power which is presently exercisable, on the effective date of the instrument of exercise.

(2) In all other cases, at the time of the creation of the power.

It appears that the Delaware Tax Trap can be sprung in Pennsylvania, however, where trusts created by Will, inter vivos trust instruments, and exercises of powers of appointment may be perpetual. [196] A donee who exercises a First Power over a Pennsylvania trust may trigger the Delaware Tax Trap under the following statute: “If a power of appointment is exercised to create a new power of appointment, any interest created by the exercise of the new power of appointment is invalid if it does not vest within 360 years of the creation of the original power of appointment, unless the exercise of the new power of appointment expressly states that this provision shall not apply to the interests created by the exercise.” [197]

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[196] 20 Pa. Cons. Stat. § 6107.1(b)(1).

[197] 20 Pa. Cons. Stat. § 6107.1(b)(3).

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## g. Related Issues

The regulations under § 2041 define “power of appointment” expansively. [198] As a result, attorneys who advise trustees regarding trust modifications, exercises of decanting powers, [199] and changes of trust situs (as well as donees who exercise First Powers) must be mindful of § 2041(a)(3) and § 2514(d). Nevertheless, the provision's legislative history indicates that the rules do not apply to powers exercised by trustees: “The existing statute contains a provision which was intended to cover this situation, but it is too broadly worded. Under it, for example, the exercise of an otherwise exempt power might be taxed if it were exercised by giving a trustee discretionary power to invade principal.” [200]

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[198] Reg. § 20.2041-1(b)(1).

[199] *See* PLR 200744020 (exercise of decanting power over grandfathered trust did not fall within § 2041(a)(3)).

[200] S. Rep. No. 82-382 (1951).

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The practitioner should be aware of any creditor issues related to the exercise of First Powers. Under Delaware law, for example, the exercise of a nongeneral power of appointment does not cause trust assets to be subject to creditor claims. [201] The exercise of a general power — lifetime or testamentary — only subjects trust assets to the claim of a creditor in favor of whom the power is exercised. [202] Practitioners in other jurisdictions should be aware of the rights of a beneficiary's creditors to assets over which the beneficiary exercises a power of appointment.

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[201] *See* Del. Code Ann. tit. 12, § 3536(d)(1)–§ 3536(d)(2).

[202] Del. Code Ann. tit. 12, § 3536(d)(1)–§ 3536(d)(2).

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The planner should also pay close attention to how federal estate tax will be paid if a donee triggers the Delaware Tax Trap as well as to how GST tax will be paid if a donee does not spring the Delaware Tax Trap over a Nonexempt Dynasty Trust. Charging all taxes to the residue of the probate estate will be ill-advised in almost every case. If the donee of a First Power triggers the Delaware Tax Trap (and thereby generates federal estate tax), then § 2207 is available. It provides that an executor can recover any tax due on the decedent's estate that is attributable to property subject to a power of appointment from the recipient of such property. [203]

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[203] § 2207.

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Similarly, if a taxable termination occurs in a Nonexempt Dynasty Trust, then § 2603(b) is available. It provides that, unless otherwise provided in the governing instrument, the GST tax will be charged against the property generating the tax. [204]

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[204] § 2603(b).

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In many ways, the Delaware Tax Trap is an ideal way to minimize the payment of federal transfer taxes because it puts the decision as to whether to subject assets to federal estate tax or to GST tax in the hands of the person who is best able to make that determination. That might involve reviewing the situation periodically and signing appropriate estate-planning documents (which will grow difficult if the donee of a First Power becomes incompetent). With that in mind, donees of First Powers might want to include provisions in durable powers of attorney in which they authorize attorneys-in-fact to amend exercises of powers of appointment (which might be as minimal as specifying whether the duration of trusts will be measured from the creation rather than from the exercise of powers or vice versa); or they might want to include language in instruments of appointment in which they authorize court-appointed guardians to make any appropriate decisions. It also might be prudent to include language in new trusts in which trustees are authorized to make appropriate distributions.

Some national commentators have expressed reluctance to rely on the Delaware Tax Trap to obtain a stepped-up income tax basis because the Delaware Tax Trap was designed to prevent tax savings rather than to generate such savings and because there is so little case law or regulatory authority. The Sixth

Circuit's decision in *Summa Holdings, Inc. v. Commissioner* [205] early in 2017 should allay those concerns. There, the IRS sought to prevent taxpayers from saving income taxes through a strategy employing a domestic international sales corporation ("DISC") and a Roth individual retirement account ("IRA") through the use of the substance-over-form doctrine. The Sixth Circuit rejected the IRS's contention "because *Summa Holdings* used the DISC and Roth IRAs for their congressionally sanctioned purposes — tax avoidance — the Commissioner had no basis for recharacterizing the transactions and no basis for recharacterizing the law's application to them." [206]

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[205] 848 F.3d 779 (6th Cir. 2017). *But see Mazzei v. Commissioner*, 150 T.C. No. 7, 2018 BL 80932, 2018 WL 1168766, at *24 (Mar. 5, 2018) ("We have not found, nor have petitioners or the dissent identified, support in the Code or the regulations for their claim that the Roth IRAs' purchase of the FSC stock need have no substance").

[206] *Summa Holdings, Inc. v. Commissioner*, 848 F.3d at 782.

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Estates, Gifts and Trusts Portfolios
Trusts
Portfolio 867-2nd: Choosing a Domestic Jurisdiction for a Long-Term Trust
Detailed Analysis
III. Client's Ability to Choose a Jurisdiction For a Trust

## A. Introduction

When someone is creating a trust, the Will or inter vivos instrument, as the case may be, should designate the law of a jurisdiction to govern various aspects of the trust's operation. This section discusses the effectiveness of such a designation under the *Restatement (Second) of Conflict of Laws* [207] and the Uniform Trust Code (UTC). [208]

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[207] *Restatement (Second) of Conflict of Laws* (1971). In this III. and in IV., below, a reference to the "*Restatement*" refers to the *Restatement (Second) of Conflict of Laws*.

[208] UTC (amended 2018). The text of the UTC and a list of the jurisdictions that have adopted the UTC is available at, https://my.uniformlaws.org/committees/community-home?communitykey=193ff839-7955-4846-8f3c-ce74ac23938d& tab=groupdetails. *See* DiChello, *The UTC—Anything but Uniform in the Courts*, 157 Tr. & Est. 64 (Sept. 2018). For a detailed discussion of the UTC and differences adopted by enacting jurisdictions, see 864 T.M., *Uniform Trust Code.* Citations for the various state versions of the UTC are in Worksheet 3, below.

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According to the Scott treatise, [209] the various considerations that govern the choice of a jurisdiction for a trust were "well summed up" in *Wilmington Trust Co. v. Wilmington Trust Co.*, as follows: [210]

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[209] 7 Scott, Fratcher & Ascher, *Scott and Ascher on Trusts* § 45.4.2.1 at 3238 (5th ed. 2010) (hereafter "7 *Scott and Ascher on Trusts*").

[210] 24 A.2d 309, 313 (Del. 1942).

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Contracting parties, within definite limits, have some right of choice in the selection of the jurisdiction under whose law their contract is to be governed. And, where the donor in a trust agreement has expressed his desire, or if it pleases, his intent to have his trust controlled by the law of a certain state, there seems to be no good reason why his intent should not be respected by the courts, if the selected jurisdiction has a material connection with the transaction. More frequently, perhaps, the trust instrument contains no expression of choice of jurisdiction; but, again, there is no sufficient reason why the donor's choice should be disregarded if his intention in this respect can be ascertained from an examination of attendant facts and circumstances provided that the same substantial connection between the transaction and the intended jurisdiction shall be found to exist.

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## B. Restatement Approach

### 1. Introduction

To determine how much latitude a client who resides in one state ("Home State") has to select the law of another state ("Trust State") to govern a trust, the attorney must analyze the conflict-of-laws principles that have been developed in trust matters. These matters are covered in Chapter 10 of the *Restatement*, [211] Chapters 44–46 of the Scott treatise, [212] and Chapter 16 of the Bogert treatise. [213]

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[211] *Restatement* § 267–§ 282.

[212] 7 *Scott and Ascher on Trusts* § 44.1–§ 46.9.

[213] Abramson, Gary, Bogert & Bogert, *The Law of Trusts and Trustees* § 291–§ 301 (3d ed. 2014) (hereafter "*Bogert on Trusts*").

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The *Restatement*'s objective is to carry out — rather than to defeat — the testator's or trustor's intent. Accordingly, the Introductory Note to Chapter 10 of the *Restatement* provides in pertinent part that: [214]

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[214] *Restatement* Ch. 10, Introductory Note (1971).

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The chief purpose in making decisions as to the applicable law is to carry out the intention of the creator of the trust in the disposal of the trust property. It is important that his intention, to the extent to which it can be ascertained, should not be defeated, unless this is required by the policy of a state which has such an interest in defeating his intention, as to the particular issue involved, that its local law should be applied. The policy may relate to the capacity of the testator or settlor to create the trust, to the formalities required for the creation of the trust, or to the validity of the trust in other respects.

Under the *Restatement*, the client's freedom to select the law of a Trust State to govern a trust is a function of the following:
(a) *Type of Asset.* Whether the trust holds personal property or real property (the *Restatement* refers to them as "movables" and "land," respectively);

(b) *Type of Trust.* Whether the trust is created by Will or an inter vivos agreement or declaration; and

(c) *Type of Question.* Whether the issue involves:

(1) The "validity" of a trust provision;

(2) The “administration” of the trust;

(3) The “construction” of a trust provision; or

(4) Restraints on alienation of a beneficiary's interest.

## 2. Type of Asset

The *Restatement* contains one set of rules for trusts that hold movables and another set of rules for trusts that hold land. Regarding trusts of movables, the *Restatement* provides in pertinent part: [215]

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[215] *Restatement* Introductory Note to Topic 1 — Movables. *See* 7 *Scott and Ascher on Trusts* § 44.2 at 3054–3055.

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The subject matter of the trust is ordinarily not a single movable but rather a group of movables which at the time of the creation of the trust may be situated in different states. It is desirable that a trust should be treated as a unit, and, to this end, that the same law should be applied to all the movables included in the trust. Although the state in which a chattel or a right embodied in a document is situated has power, when it is the forum, to apply its local law to the validity and administration of a trust, insofar as it includes such chattel or document, it is generally accepted doctrine that it will apply the law selected in accordance with the rules stated in this Topic. Hence the location of the movables at the time of the creation of the trust, whether it is created inter vivos or by Will, is ordinarily unimportant in determining issues as to the validity or the administration of the trust or the construction of the will or trust instrument.

Although the same law is applied to all of the movables included in a trust, no matter where they are located, the choice of the law to be applied to them may depend upon the particular issue involved. The local law of one state may be applied to an issue of validity and the local law of another state applied to an issue of administration or to an issue of construction. Moreover, the local law of different states may be applicable to different issues of validity, depending upon the particular ground for the claim that the trust or one of its provisions is invalid. So also, the local law of different states may be applied in determining different issues as to construction.

In determining the law applicable to a trust of movables created inter vivos, the settlor's domicil is ordinarily not of the first importance, whereas in the case of a trust of movables created by Will the domicil of the testator is very important. It will be noted, however, that both in the case of inter vivos trusts and of trusts created by Will the place of administration of the trust is of great importance.

Regarding trusts of interests in land, the *Restatement* says in relevant part: [216]

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[216] *Restatement* Introductory Note to Topic 2 — Land.

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As has been stated, it is desirable that all of the movables included in a trust, although they may be situated in different states at the time of the creation of the trust, should be subject to the same law. As to trusts of interests in land, it has been felt that each parcel of land should be subject to the state in which it

is situated, and that the law which would be applied by the courts of that state, whether its own local law or the local law of some other state, should be applied by the courts of all states. The courts of the state of the situs will usually apply its local law; but in some situations, as will appear hereafter, they may apply the local law of some other state. Whatever law is applied by the courts of the state of the situs will be applied by the courts of other states in which the question arises in litigation.

It then covers public policy issues, intestacy, the validity of a disposition of land by Will or conveyance, trusts funded with the proceeds from the sale of land, and situations in which interests in land are treated as personal property. [217]

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[217] *Id.*

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### 3. Type of Trust

For each type of asset, the *Restatement* offers rules for trusts created by Will and trusts created inter vivos. It also covers situations in which a Will pours over assets at the testator's death to an inter vivos trust.

### 4. Type of Question — Definitions

### a. Validity

The *Restatement* describes questions relating to the "validity" of trust provisions as follows: [218]

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[218] *Restatement* § 269 cmt. d. *See id.* § 270 cmt. d. *See also* 7 *Scott and Ascher on Trusts* § 45.4 at 3181; *Bogert on Trusts* § 293 at 37.

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Some questions of validity relate only to the trust provisions and not to the will as a testamentary disposition. A trust may be invalid, in whole or in part, because it violates the rule against perpetuities or a rule against the suspension of the absolute ownership or of the power of alienation; because it violates a rule against accumulations; because the purpose is illegal; because of an illegal condition, such as one promoting divorce or restraining marriage. A trust may be invalid because there are no beneficiaries to enforce it, or because the purpose is merely capricious. A legacy for charitable purposes may be invalid, either on the ground that there is no beneficiary to enforce it or on the ground that it involves a perpetuity, as it was under the local law of New York and a few other States until changed by statute. A legacy to an unincorporated association may be invalid. A trust for charitable purposes may be invalid for indefiniteness. All trusts may be invalid as under the civil law which formerly prevailed in Louisiana.

Conspicuously absent from the list of issues that the *Restatement* says involve the validity of trust provisions is the issue regarding the ability of creditors to reach a beneficiary's interest in the trust or the trust assets themselves. Commentators who oppose the recognition of self-settled spendthrift or asset-protection trusts sometimes contend that the ability of creditors to defeat such trusts should be analyzed as a matter of trust validity. Nothing in the *Restatement*, the Bogert treatise, or the Scott treatise appears to support that view, which is not surprising because, as will be seen shortly, the *Restatement* treats this issue as a separate type of question.

The Bogert treatise discusses the issue as follows: [219]

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[219] *Bogert on Trusts* § 293 at 44–45 (footnotes omitted; emphasis added).

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Another example of characterization relates to the question of the validity or application of a trust spendthrift clause. Such a clause denies creditors of a beneficiary the right to reach the beneficiary's interest and restricts the beneficiary's right to voluntarily assign his interest. In a few states, spendthrift clauses are not enforced. If the domicile of the settlor or testator and the situs of trust administration are in the same state, it is unlikely any question will arise as to the validity or invalidity of the spendthrift clause under the law of the state. If, however, two states are involved and their laws differ on the matter, the forum court can characterize the problem as one relating to validity of the restrictions under the law of the settlor or testator's domicile, especially if that state has a strong public policy against protecting trust beneficiaries, or under the law of the situs where real estate is involved. *The question has usually been treated as one to be governed by the trust law of the state in which the trust is administered or the trust land has its situs, often the residence or domicile of the trustee, on the ground that the matter relates solely to trust administration rather than the validity of the clause or construction of the extent of the beneficiary's interests under the terms of the trust instrument.*

The Scott treatise paraphrases favorably dictum in the 1892 New York case of *Cross v. United States Trust Co.* [220] indicating that “the question here presented was not one of validity but one of reaching the beneficiary's interest.” [221]

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[220] 131 N.Y. 330 (1892).

[221] 7 *Scott and Ascher on Trusts* § 45.7.1.1 at 3346.

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## b. Administration

The *Restatement* defines questions of trust “administration” as follows: [222]

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[222] *Restatement* § 271 cmt. a (citations omitted). *See id.* § 272 cmt. a, *id.* § 279 cmt. a; 7 *Scott and Ascher on Trusts* § 45.5 at 3265–3266; *Bogert on Trusts* § 293 at 36–37.

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The term “administration of a trust,” as it is used in the *Restatement* of this Subject, includes those matters which relate to the management of the trust. Matters of administration include those relating to the duties owed by the trustee to the beneficiaries. They include the powers of a trustee, such as the power to lease, to sell and to pledge, the exercise of discretionary powers, the requirement of unanimity of the trustees in the exercise of powers, and the survival of powers. They include the liabilities which may be incurred by the trustee for breach of trust. They include questions as to what are proper trust investments. They include the trustee's right to compensation. They include the trustee's right to indemnity for expenses incurred by him in the administration of the trust. They include the removal of the trustee and the appointment of successor trustees. They include the terminability of the trust.

### c. Construction

For purposes of the *Restatement*, "where the question is as to who are beneficiaries of the trust and as to the extent of their interests, the question is one of construction rather than of administration... ." [223]

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[223] *Restatement* § 271 cmt. a. *See Bogert on Trusts* § 293 at 35–36.

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Regarding allocations to income or principal, "it is generally held that it is a question of construction." [224]

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[224] *Restatement* § 268 cmt. h. *See* 7 *Scott and Ascher on Trusts* § 45.3.10 at 3169–3175.

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### d. Restraints on Alienation of a Beneficiary's Interest

The *Restatement* contains no special definitions regarding a trust beneficiary's ability to assign his or her interest or creditors' ability to reach that interest. As discussed above, the *Restatement* addresses this subject separately and does not treat it as a matter of trust validity.

### 5. Type of Question — Effectiveness of Designation

### a. Validity

### (1) Trust of Movables Created by Will

Section 269 of the *Restatement* provides in relevant part as follows: [225]

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[225] *Restatement* § 269. *See id.* cmt. f; 7 *Scott and Ascher on Trusts* § 45.1 at 3060–3064, § 45.4.1 at 3181–3182, § 45.4.1.3 at 3200–3204, § 45.4.1.8 at 3222–3225; *Bogert on Trusts* § 296 at 58–59. The principles described in III.B.5., are summarized in III.B.6., below.

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

...

(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 ...

A comment under § 269 adds that: [226]

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[226] *Restatement* § 269 cmt. f.

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Despite the absence of an express designation, it may otherwise be apparent from the language of the trust provisions of the will or from other circumstances, such as the extent of the contacts with a particular state, that the testator wished to have the local law of a particular state govern the validity of the trust.

Another comment describes the section's rationale as follows: [227]

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[227] *Restatement* § 269 cmt. e.

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It is desirable that a trust should be treated as a unit and, to this end, that the trust of all of the movables included therein should be governed by a single law. The validity of a trust of movables created by will should not be held valid as to some of the movables included in the trust and invalid as to others. This is true whether the movables consist of chattels, rights embodied in documents or intangibles. The rule of this Section is applicable to all these types of movables, no matter where they are situated at the time of the testator's death. It does not follow, however, that all questions of validity are determined by the same law.

Nevertheless, a testator may not circumvent restrictions that the Home State places on charitable bequests and bequests that exclude certain members of his or her family by designating the law of a Trust State to govern the validity of his or her trusts. [228]

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[228] *Restatement* § 269 cmt. c.

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## (2) Trust of Movables Created Inter Vivos

Section 270 of the *Restatement* provides in pertinent part as follows: [229]

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[229] *Restatement* § 270. *See id.* cmt. b; 7 *Scott and Ascher on Trusts* § 45.1 at 3060–3064, § 45.4.2.1 at 3234–3242; *Bogert on Trusts* § 297 at 71.

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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 ...

One of § 270's comments notes that: [230]

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[230] *Restatement* § 270 cmt. b.

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Despite the absence of an express designation, it may otherwise be apparent from the language of the trust instrument or from other circumstances, such as the extent of the contacts with a particular state, that the settlor wished to have the local law of a particular state govern the validity of the trust.

Another comment gives the general principle underlying the section as follows: [231]

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[231] *Restatement* § 270 cmt. a (cross-reference omitted).

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It is desirable that a trust should be treated as a unit and, to this end, that the trust as to all of the movables included therein, no matter where they happen to be at the time of the creation of the trust, should be governed by a single law. The creation of a trust is different from an outright conveyance, which is either valid or invalid at the outset. In the case of a trust there is something more. In the first place, the creation of a trust establishes a continuing relationship between the trustee and the beneficiaries, and the state in which the trust is to be administered or which is otherwise connected with the trust may be different from the state in which the trust property is situated when the trust is created. In the second place, the trust property is ordinarily not a single movable but includes a group of movables which may be situated in different states at the time of the creation of the trust. The validity of a trust of movables, therefore, should be governed by a single law and not held valid as to some of the movables included in the trust and invalid as to others. This is true whether the movables consist of chattels, rights embodied in a document or intangibles. The rule of this Section is applicable to all these types of movables, no matter where they are situated at the time of the creation of the trust. It does not follow, however, that all questions of validity are determined by the same law.

### (3) Substantial Relation to the Trust

As mentioned above, for the designation of a Trust State's law to govern the validity of the provisions of a testamentary trust [232] or an inter vivos trust [233] to be respected, the Trust State must have "a substantial relation to the trust." For a testamentary trust, a comment under § 269 provides in relevant part as follows: [234]

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[232] *Restatement* § 269(b)(i).

[233] *Restatement* § 270(a).

[234] *Restatement* § 269 cmt. f. *See* 7 *Scott and Ascher on Trusts* § 45.4.1.3 at 3200–3242.

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A state has a substantial relation to a trust when it is the state in which the trust is to be administered; or that of the place of business or domicil of the trustee at the time of the testator's death, or that of the domicil of the testator at that time, or that of the domicil of the beneficiaries. There may be other contacts or groupings of contacts which will likewise suffice.

For an inter vivos trust, a comment under § 270 provides in pertinent part as follows: [235]

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[235] *Restatement* § 270 cmt. b. *See* 7 *Scott and Ascher on Trusts* § 45.4.2.1 at 3239.

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A state has a substantial relation to a trust when it is the state, if any, which the settlor designated as that in which the trust is to be administered, or that of the place of business or domicil of the trustee at the time of the creation of the trust, or that of the location of the trust assets at that time, or that of the domicil of the settlor, at that time, or that of the domicil of the beneficiaries. There may be other contacts or groupings of contacts which will likewise suffice.

## (4) Strong Public Policy

As mentioned above, the designation of a Trust State's law to govern the validity of a trust that holds personal property will be honored unless the issue in question contravenes a “strong public policy” of the testator's domicile, in the case of a testamentary trust, [236] or the state with which, as to the matter at issue, the trust has its most significant relationship, in the case of an inter vivos trust. [237] Thus, for testamentary trusts, a comment under § 269 says in part that: [238]

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[236] *Restatement* § 269(b).

[237] *Restatement* § 270(a).

[238] *Restatement* § 269 cmt. c (cross-reference omitted). *See Restatement* § 269 cmt. i, *id.* § 270 cmts. b, e; 7 *Scott and Ascher on Trusts* § 45.4.1.8 at 3222–3225, § 45.4.2.4 at 3254–3260; *Bogert on Trusts* § 297 at 70, § 301 at 113.

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The law that would be applied by the courts of the state of the testator's domicil at death determines whether and to what extent a testator may by will prevent his surviving spouse from receiving the share of his movables which she would receive if he had died intestate.

The same law also determines whether a legacy for charitable purposes is invalid, in whole or in part, because of statutory restrictions on the power of a testator to make charitable dispositions by Will.

A comment under § 269 emphasizes that: [239]

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[239] *Restatement* § 269 cmt. i. *See* 7 *Scott and Ascher on Trusts* § 45.4.1.5 at 3209–3214.

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A trust provision in a will is invalid to the extent that it is invalid under the strong public policy of the state of the testator's domicil at death, even though it would be valid under the local law of the state designated in the will to govern the validity of the trust or under the local law of the state where the trust is to be administered.

The mere fact, however, that the provision would be invalid under the local law of the state of the

testator's domicil does not invalidate the provision. If the provision is valid under the local law of the state designated by the testator or under the local law of the place of administration, it will be held to be valid if it does not contravene a strong policy of the state of the testator's domicil. No such strong policy is involved in rules against perpetuities or rules against accumulations or rules as to indefiniteness of beneficiaries.

The *Restatement*, the Scott treatise, and the Bogert treatise do not cover whether the designation of a Trust State's law to govern the ability of creditors to reach trust assets might offend a strong public policy of the Home State. As noted above, this is consistent with the *Restatement*'s framework that addresses this issue separately rather than as an issue of validity.

### (5) Most Significant Relationship

For inter vivos trusts, a designation of a Trust State's law to govern the validity of trust provisions will stand even if doing so would violate a strong public policy of the trustor's domicile if the Trust State rather than the Home State is "the state with which, as to the matter at issue, the trust has its most significant relationship under the principles stated in § 6." [240] Section 6(2) of the *Restatement* provides that: [241]

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[240] *Restatement* § 270(a).

[241] *Restatement* § 6(2). *See id.* § 6 cmts. d–j.

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[T]he factors relevant to the choice of the applicable rule of law include

(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.

Although the above factors are analyzed in IV.D.3.b., below, it is important to note here that the trustor's domicile is only one factor that warrants consideration and that most of the other factors weigh in favor of honoring the designation even if doing so will offend a strong public policy of the Home State.

### (6) Trust of Land Created by Will

Section 278 of the *Restatement* provides that: [242]

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[242] *Restatement* § 278. *See id.* cmt. a; 7 *Scott and Ascher on Trusts* § 46.1 at 3368–3371, § 46.4.1 at 3402, § 46.4.1.2 at 3418–3422; *Bogert on Trusts* § 296 at 65–69.

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.

A comment under § 278 provides in relevant part that: [243]

[243] *Restatement* § 278 cmt. b (cross-reference omitted).

If the will is otherwise valid, a further question may arise as to the validity of a trust of an interest in land created by the will. Where the land is to be retained in the trust, the courts of the situs have applied its local law. That law has been applied to determine whether there is a violation of the rule against perpetuities, or a rule against accumulations, or a rule as to illegal conditions or purposes, or a rule precluding the creation of a trust, or a rule invalidating charitable trusts.

### (7) Trust of Land Created Inter Vivos

Section 278 also covers the validity of trusts of land created by living trusts. [244] A comment under the section provides in pertinent part that: [245]

[244] *Restatement* § 278. *See id.* cmt. a; 7 *Scott and Ascher on Trusts* § 46.1 at 3368–3371, § 46.4.2 at 3422–3427; *Bogert on Trusts* § 297 at 76–78.

[245] *Restatement* § 278 cmt. c.

If the trustee is to retain the land in the trust, the substantial validity of the trust is determined by the law that would be applied by the courts of the situs, and usually those courts would apply their local law. Thus, as in the case of a testamentary trust, the local law of the situs is applicable on the question whether the disposition of the land violates the rule against perpetuities, or a rule against accumulations, or a rule as to illegal conditions or purposes, or a rule precluding the creation of a trust, or a rule invalidating charitable trusts.

## b. Administration

### (1) Trust of Movables Created by Will

Section 271 of the *Restatement* provides in relevant part as follows: [246]

[246] *Restatement* § 271. *See id.* cmt. c; 7 *Scott and Ascher on Trusts* § 45.1 at 3060–3064, § 45.5.1 at 3266, § 45.5.1.1 at 3266–3270; *Bogert on Trusts* § 296 at 63–64.

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

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

One of the comments to the section gives the following general rule: [247]

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[247] *Restatement* § 271 cmt. b.

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It is desirable that a trust should be treated as a unit, and, to this end, that the trust as to all of the movables included therein should be governed by a single law. The administration of a trust of movables, therefore, should be governed by a single law, and different rules should not be applied to some of the movables included in the trust and not applied to others. This is true whether the movables consist of chattels, rights embodied in a document, or intangibles. The rule of this Section is applicable to all these types of movables no matter where they are situated at the time of the testator's death.

Another comment describes the matters that cannot be controlled by the terms of a trust as follows: [248]

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[248] *Restatement* § 271 cmt. h. *See* 7 *Scott and Ascher on Trusts* § 45.6.6 at 3323–25.

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Certain matters of administration may be such that the testator cannot regulate them by any provision in the terms of the trust. Thus, by a statute of the testator's domicil it may be provided that the attempted grant to a testamentary trustee of exoneration from liability for failure to exercise reasonable care, diligence and prudence, or a power to make a binding and conclusive fixation of the value of any asset for purposes of distribution or allocation, shall be deemed contrary to public policy. So also, under the local law of the state of the testator's domicil there may be unusually strict rules as to self-dealing. If a testator fixes the administration of a trust in a state other than that of his domicil, it is not certain whether the courts will apply the rule of the domicil or the rule of the place of administration.

## (2) Trust of Movables Created Inter Vivos

Section 272 of the *Restatement* provides in pertinent part: [249]

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[249] *Restatement* § 272. *See id.* cmt. c; 7 *Scott and Ascher on Trusts* § 45.1 at 3060–3064, § 45.5.2 at 3283, § 45.5.2.1 at 3283–3286; *Bogert on Trusts* § 297 at 74.

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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 ...

A comment summarizes the rationale of the section as follows: [250]

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[250] *Restatement* § 272 cmt. b.

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It is desirable that a trust should be treated as a unit, and, to this end, that the trust as to all of the movables included therein should be governed by a single law. The administration of a trust of movables, therefore, should be governed by a single law, and different rules should not be applied to some of the movables included in the trust and not applied to others. This is true whether the movables consist of chattels, rights embodied in a document or intangibles. The rule of this Section is applicable to all these types of movables, no matter where they are situated at the time of the creation of the trust.

A later comment summarizes matters that cannot be controlled by the terms of the trust as follows: [251]

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[251] *Restatement* § 272 cmt. f (cross-reference omitted). *See* 7 *Scott and Ascher on Trusts* § 45.6.6 at 3323–3325.

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Certain matters of administration may be such that the settlor cannot regulate them by any provision in the terms of the trust. In the case of an inter vivos trust the applicable law is probably the local law of the state in which the administration of the trust is fixed.

### (3) Trust of Land Created by Will

Section 279 of the *Restatement* reads as follows: [252]

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[252] *Restatement* § 279. *See id.* cmt. b; 7 *Scott and Ascher on Trusts* § 46.1 at 3368–3371, § 46.6 at 3455–3456; *Bogert on Trusts* § 296 at 68.

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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.

A comment expands on the general rule as follows: [253]

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[253] *Restatement* § 279 cmt. b.

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The courts of the situs would usually apply their own local law to determine issues of administration. But if the testator or settlor provides that the local law of some other state shall be applied to govern the administration of the trust, or certain issues of administration, the courts of the situs would apply the designated law as to issues which can be controlled by the terms of the trust.

### (4) Trust of Land Created Inter Vivos

The rules regarding the resolution of issues involving the administration of trusts of land created by Will apply to such issues for inter vivos trusts as well. [254]

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[254] *See Restatement* § 279, *id.* cmt. b; 7 *Scott and Ascher on Trusts* § 46.1 at 3368–3371, § 46.6 at 3455–3456; *Bogert on Trusts* § 297 at 77.

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## c. Construction

### (1) Trust of Movables Created by Will

Section 268(1) of the *Restatement* provides as follows: [255]

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[255] *Restatement* § 268(1). *See id.* § 268 cmt. b; 7 *Scott and Ascher on Trusts* § 45.1 at 3060–3064, § 45.3.1 at 3136–3139; *Bogert on Trusts* § 296 at 64.

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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.

A comment elaborates upon the general rule as follows: [256]

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[256] *Restatement* § 268 cmt. b.

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The courts will give effect to a provision in a trust instrument or will that it should be construed in accordance with the rules of construction of a particular state. It is not necessary that this state have any connection with the trust. This is because construction is a process for giving meaning to an instrument in areas where the intentions of the party, or parties, would have been followed if they had been made clear.

Despite the absence of an express designation, it may otherwise be apparent from the language of the trust instrument or will or from other circumstances that the settlor or testator wished to have the local law of a particular state govern its construction. In such a case, the rules of construction of this state will be applied.

### (2) Trust of Movables Created Inter Vivos

Restatement § 268(1), quoted above, also applies to the determination of the law that is used to resolve a question regarding the construction of an inter vivos trust that holds movables. [257]

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[257] *Restatement* § 268(1). *See id.* § 268 cmt. b; 7 *Scott and Ascher on Trusts* § 45.1 at 3060–3064, § 45.3.5 at 3151–3157; *Bogert on Trusts* § 297 at 75–76.

### (3) Trust of Land Created by Will

Section 277(1) of the *Restatement* provides: [258]

[258] *Restatement* § 277(1). *See id.* § 277 cmt. b; 7 *Scott and Ascher on Trusts* § 46.1 at 3368–3371, § 46.3 at 3391–3392; *Bogert on Trusts* § 296 at 68.

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.

According to a comment under § 277: [259]

[259] *Restatement* § 277(1) cmt. b (cross-reference omitted).

The courts will give effect to a provision in a trust instrument or will that it should be construed in accordance with the rules of construction of a particular state. This is true of a trust of interests in land, as it is in the case of interests in movables.

### (4) Trust of Land Created Inter Vivos

The rules for trusts of land created inter vivos regarding the determination of what law is used to resolve construction issues are the same as for trusts of land created by Will described above. [260]

[260] *Restatement* § 277(1). *See id.* § 277 cmt. b; 7 *Scott and Ascher on Trusts* § 46.1 at 3368–3371, § 46.3 at 3391–3392; *Bogert on Trusts* § 297 at 78.

## d. Restraints on Alienation of a Beneficiary's Interest

### (1) Trust of Movables Created by Will

Section 273 of the *Restatement* provides in relevant part that: [261]

[261] *Restatement* § 273. *See id.* cmts. b, d; 7 *Scott and Ascher on Trusts* § 45.7 at 3337–3338, § 45.7.1–§ 45.7.1.4 at 3338–3359, § 45.7.2 at 3359–3365, § 45.7.3 at 3365–3366; *Bogert on Trusts* § 293 at 44–45.

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 domicil 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 ....

A comment elaborates in pertinent part as follows: [262]

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[262] *Restatement* § 273 cmt. b.

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Where the trust is to be administered in a state other than that of the testator's domicil, the applicable law is the local law of the place of administration rather than the local law of his domicil.

A later comment provides in relevant part: [263]

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[263] *Restatement* § 273 cmt. d.

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On the question whether the interest of a beneficiary can be assigned by him, the same principles are applicable... . . Where the testator fixes the administration of the trust in a state other than that of his domicil, such as by naming as trustee a trust company of that state, the applicable law is the local law of the state of administration.

## (2) Trust of Movables Created Inter Vivos

*Restatement* § 273 reads in relevant part: [264]

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[264] *Restatement* § 273. *See id.* cmts. c, d; 7 *Scott and Ascher on Trusts* § 45.7 at 3337–3338, § 45.7.1–§ 45.7.1.4 at 3338–3359, § 45.7.7 at 3359–3365, § 45.7.3 at 3365–3366; *Bogert on Trusts* § 293 at 44–45.

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

(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 ....

A comment continues: [265]

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[265] *Restatement* § 273 cmt. d.

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In the case of an inter vivos trust, if the settlor has fixed its administration in a particular state, the local law of that state is applicable to the assignability of a beneficiary's interest. Thus if the settlor domiciled in one state transfers property to a trust company of another state, the law applicable to the assignability of a beneficiary's interest is ordinarily the local law of the state in which the trust company was incorporated and does business.

### (3) Trust of Land Created by Will

Section 280 of the *Restatement* provides: [266]

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[266] *Restatement* § 280. *See id.* cmt. a; 7 *Scott and Ascher on Trusts* § 46.7 at 3457–3458; *Bogert on Trusts* § 293 at 44–45.

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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.

The section's comment expands as follows: [267]

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[267] *Restatement* § 280 cmt. a.

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In the case of land the applicable law is the law that would be applied by the courts of the situs if it is to be retained in the trust. These courts would apply their own local law to determine this question.

### (4) Trust of Land Created Inter Vivos

The rules here are comparable to those for trusts of land created by Will. [268]

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[268] *See Restatement* § 280, *id.* cmt. a; 7 *Scott and Ascher on Trusts* § 46.7 at 3457–3458; *Bogert on Trusts* § 293 at 44–45.

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## 6. Type of Question — Summary

The Bogert treatise summarizes the above principles as follows: [269]

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[269] *Bogert on Trusts* § 301 at 107–108 (emphasis in original). *See* Redd, *Choice of Law*, 156 Tr. & Est. 11, 11–12 (Nov. 2017).

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(A) As to interests in personal property held in a testamentary trust:

1. A testator may designate the local law to govern the validity of the trust, except that (a) the testator's designation will not control if application of the designated law would be contrary to a “strong public policy” of the state of his domicile at death and (b) the designated state must have a “substantial relation” to the trust. A substantial relation exists when the designated state is that in which the trust is administered or in which the trustee has his or her place of business or domicile at death, or is the state of the domicile of the beneficiaries.

2. A testator may designate the state whose local law is to govern construction of the terms of the trust, and it is not required that the designated state have any connection with the trust.

3. A testator may designate the local law of one state to govern administration of the trust even though that state has no relation to the trust, except that on public policy grounds certain matters of administration cannot be controlled by the trust terms. These matters include attempts to grant the testamentary trustee exoneration from liability for failure to exercise prudence or for acts of self-dealing, or a power to fix the value of trust assets for all purposes.

(B) As to interests in personal property held in a revocable trust:

1. The settlor of a revocable trust may designate the local law of one state to govern the validity of the trust (a) if that state has a substantial relation to the trust and (b) if application of its local 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.

2. As in the case of a testamentary trust, a settlor may designate the state whose local law is to govern construction under the terms of the trust; the designated state need not have any connection with the trust.

3. Except where matters of administration cannot be controlled by the trust terms on public policy grounds, a settlor may designate the local law of one state to govern administration of the trust even though that state has no relation to the trust.

(C) As to trust interests in real property:

The opportunity of a testator or settlor of a trust of land to effectively designate a local law of a state other than that of the situs of the land to govern the validity and administration of a trust of land is more limited. The effectiveness of such a designation will depend upon whether the forum court recognizes the designated state as having a more significant relationship to the particular issue than the situs state.

## 7. Pour Over by Will

If a bequest under a Will to the trustee of a trust (i.e., a pour over) is valid under the law of the testator's domicile, “the effect is to enlarge the assets of the original trust.” [270] Thereafter, “[t]he administration of the trust thus enlarged is governed by the local law of the state which governs the administration of the original trust, and it is subject to the supervision of the court, if any, which has supervision over the original trust.” [271] A court in the Home State might be able to interfere if a provision of the trust offends a strong public policy of that state, [272] but, as noted above, this should not extend to issues involving the rule against perpetuities or the rule against accumulations. [273]

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[270] *Restatement* § 269 cmt. b. *See* 7 *Scott and Ascher on Trusts* § 45.5.1.4 at 3281–3283; *Bogert on Trusts* § 296 at 58.

[271] *Restatement* § 269 (cross-references omitted).

[272] *Restatement* § 269 cmt. c.

[273] *Restatement* § 269 cmt. i.

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## 8. Application of the Rules — The Peierls Case

### a. Introduction

On October 4, 2013, the Supreme Court of Delaware issued the following three decisions involving Peierls family trusts:

• *In re Peierls Family Testamentary Trusts* ("*Peierls I*") [274]

• *In re Peierls Charitable Lead Unitrust* ("*Peierls II*") [275]

• *In re Peierls Family Inter Vivos Trusts* ("*Peierls III*") [276]

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[274] *In re Peierls Family Testamentary Tr.*, 77 A.3d 223 (Del. 2013) ("*Peierls I*").

[275] *In re Peierls Charitable Lead Unitrust*, 77 A.3d 232 (Del. 2013) ("*Peierls II*").

[276] *In re Peierls Family Inter Vivos Tr.*, 77 A.3d 249 (Del. 2013) ("*Peierls III*").

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Among other things, *Peierls I* confirmed that Delaware courts follow the *Restatement* on whether a Delaware court has and should exercise jurisdiction in a matter involving a trust, [277] while *Peierls III* confirmed that Delaware courts consult the *Restatement* to determine when Delaware law applies. [278]

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[277] *Peierls I*, 77 A.3d at 227 ("In cases such as these where a trust maintains contacts with multiple states, we prefer to consult the *Restatement (Second) of Conflict of Laws* to resolve the issue of jurisdiction").

[278] *Peierls III*, 77 A.3d at 255 ("When confronted with a choice-of-law issue, Delaware courts adhere to the *Restatement (Second) of Conflict of Laws*").

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### b. Peierls I

In *Peierls I*, the Supreme Court of Delaware had to decide whether Delaware courts had and should exercise jurisdiction over seven testamentary trusts created by members of the Peierls family. After noting that these questions should be resolved under § 267 of the *Restatement*, [279] the court found that Delaware courts possessed jurisdiction [280] for the following reason: [281]

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[279] *Restatement* § 267 cmt. e. *See* IV.C., below.

[280] *Peierls I*, 77 A.3d at 227.

[281] *Peierls I*, 77 A.3d at 228 (footnote omitted).

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All interested parties consented to the Court of Chancery's jurisdiction: Trustees Brian and Jeffrey filed the Petitions in the Court of Chancery; the beneficiaries provided written consent to the court's jurisdiction; Northern Trust [(a co-trustee)] is a Delaware entity; and Bank of America (corporate successor to US Trust Co.), though not subjecting itself to jurisdiction, filed written acknowledgment of its removal as corporate trustee. Having obtained jurisdiction over the trustees, the Court of Chancery had jurisdiction to adjudicate issues of administration of the Trusts under the Restatement.

The court then turned to the question of whether Delaware courts should exercise jurisdiction in the circumstances. It first observed: [282]

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[282] *Peierls I*, 77 A.3d at 228 (internal quotation marks and footnotes omitted).

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Distinct from whether the Court of Chancery had jurisdiction to evaluate the Petitions is the issue of whether the Vice Chancellor should have exercised jurisdiction to do so. This question is largely one of which court has primary supervision over the Trusts. One indication that a particular court has primary supervision over the administration of a trust is if the trustee is required to render regular accountings in the court in which he has qualified. If the court in which the trustee has qualified does not exercise active control over the administration of the trust, then the court of the place of administration may exercise primary supervision. A court having primary supervisory power has and will exercise jurisdiction as to all questions which may arise in the administration of a trust.

Referring to Comment (e) under § 267, the court continued: [283]

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[283] *Peierls I*, 77 A.3d at 228 (footnotes omitted; emphasis in original).

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The *Restatement* further recognizes the need to “promote comity and respect for other states’ laws”:

A court of a state other than that of the testator's domicil or that in which the trust is to be administered will not exercise jurisdiction if to do so would be an undue interference with the supervision of the trust by the court which has primary supervision. Whether there is such interference depends on the relief sought. Thus, if a court acquires jurisdiction over the trustee it may entertain a suit to compel him to redress a breach of trust, even though the trustee has qualified as trustee in a court of another state or the administration of the trust is in another state. It may compel the trustee to render an accounting or it may even remove the trustee**.** On the other hand*, it will ordinarily decline to deal with questions of construction or validity or administration of the trust, leaving these matters to be dealt with by the court of primary supervision.* Thus, it will not ordinarily give instruction to the trustee as to his powers and duties

## c. Peierls III

In *Peierls III*, the Supreme Court of Delaware confirmed that Delaware courts should look to the *Restatement* to resolve any conflict-of-laws issues in trust matters. [284] It first considered the applicability of Del. Code Ann. tit. 12, § 3332(b), which then said, "[e]xcept as otherwise expressly provided by the terms of a governing instrument or by court order, the laws of this State shall govern the administration of a trust *while the trust is administered in this State*." [285] The court found that the statute was inapplicable for the following reason: [286]

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[284] *Peierls III*, 77 A.3d at 255.

[285] Del. Code Ann. tit. 12, § 3332(b) (emphasis added).

[286] *Peierls III*, 77 A.3d at 256.

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Notably, the statute imposes a precondition upon its application — namely that the trust "[be] administered" in Delaware. The Petitions in part seek orders approving the resignation of the current trustees — resignations that are conditioned on judicial approval — and the appointment of a successor trustee, whose acceptance is also conditioned on judicial approval. Because the current trustees have not actually resigned and the successor trustee has not yet assumed its role, the Trusts are not yet "in Delaware" for purposes of deciding whether to permit a transfer of administration and a change in the law of administration. Accordingly, Section 3332(b) is not yet applicable. We, therefore, must look to our conflict-of-laws jurisprudence to determine whether a Delaware court can exercise jurisdiction over and approve the Peierls' Petitions.

The court then turned to identifying issues that constitute matters of administration under the *Restatement.* [287] It said: [288]

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[287] *Id*.

[288] *Id*. (footnotes and internal quotation marks omitted).

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Section 272 of the Restatement specifically addresses which state's law governs the administration of inter vivos trusts. Section 272's Comment *a* directs us to Section 271's Comment *a* (which discusses testamentary trusts) to determine what matters are administrative in nature. Administrative matters are those matters which relate to the management of the trust, including a trustee's powers, the liabilities a trustee may incur for breach of trust, what constitutes a proper investment, a trustee's compensation and indemnity rights, a trust's terminability, and, importantly, a trustee's removal and successor trustees' appointment.

The court continued: [289]

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[289] *Peierls III*, 77 A.3d at 256–257.

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We note that the Peierls' Petitions seek to change the existing trustees; declare that Delaware is the Trusts' situs and that Delaware law governs administrative matters; modify the Trusts' provisions to allow for particular management changes under the Delaware trust statutes; and accept jurisdiction over the Trusts. All of these are administrative matters. Accordingly, we must determine which state's law governs the Trusts' administrative provisions to determine whether the Vice Chancellor properly denied the Petitions.

Regarding whether the law that governs the administration of a trust changes upon the change of trustee, the court said: [290]

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[290] *Peierls III*, 77 A.3d at 259 (footnotes and internal quotation marks omitted; emphasis added).

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A trust instrument may expressly authorize a change in the law governing administration of the trust. The trust instrument may also implicitly authorize the change, such as when the trust instrument contains a power to appoint a trustee in another named state. As the Restatement notes, even a simple power to appoint a successor trustee may be construed to include a power to appoint a trust company or individual in another state. Whether the trust instrument expressly or implicitly authorizes a change in the trust's administrative governing law, the law governing the administration of the trust thereafter is the local law of the other state and not the local law of the state of original administration. *That rule applies even when the trust instrument contains a choice-of-law provision. Therefore, when a settlor does not intend his choice of governing law to be permanent and the trust instrument includes a power to appoint a successor trustee, the law governing the administration of the trust may be changed.*

For present purposes, the three *Peierls* decisions have the following two implications. First, a Delaware trustee must actually be in office for a Delaware court to adjudicate a trust matter. Second, unless the governing instrument specifies that the law of another state applies in all circumstances, Delaware law will govern the administration of a trust once a Delaware corporate trustee is in place. This means that a Delaware directed trust, silent trust, unitrust, or other arrangement might become available.

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## C. UPC Approach

Section 2-703 of the Uniform Probate Code (UPC) [291] provides guidance on how to select the state whose law governs the meaning and effect of the terms of a trust. It says: [292]

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[291] UPC § 2-703 (amended 2010). The text of the UPC and a list of jurisdictions that have enacted the UPC may be viewed at, https://my.uniformlaws.org/committees/community-home?CommunityKey=a539920d-c477-44b8-84fe-b0d7b1a4cca8.

[292] UPC § 2-703 (amended 2010).

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The meaning and legal effect of a governing instrument is determined by the local law of the state selected in the governing instrument, unless the application of that law is contrary to the provisions relating to the elective share described in [Part] 2, the provisions relating to exempt property and allowances described in [Part] 4, or any other public policy of this state otherwise applicable to the disposition.

At least three states have statutes based on the provision. [293]

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[293] Colo. Rev. Stat. § 15-11-703; Haw. Rev. Stat. § 560:2-703; Mich. Comp. Laws § 700.2705.

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## D. UTC Approach

Section 107 of the UTC provides in relevant part that: [294]

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[294] UTC § 107(1) (amended 2018). *See Morris v. Morris*, 756 S.E.2d 616, 620 (Ga. Ct. App. 2014) ("Georgia law [rather than North Carolina law] governs the meaning and effect of the provisions of the Trust"); *Commerce Bank, N.A. v. Bolander*, 239 P.3d 83, 90 (Kan. Ct. App. 2007) ("the district court did not err in holding that. . . .Kansas [rather than Oklahoma or Texas] had jurisdiction to resolve the issues in this case").

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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 ....

Section 107's comment describes the general rule as follows: [295]

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[295] UTC § 107 cmt. (amended 2018).

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Paragraph (1) allows a settlor to select the law that will govern the meaning and effect of the terms of the trust. The jurisdiction selected need not have any other connection to 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. 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.

UTC § 107 is concerned with matters of "meaning and effect," which seem to correspond most closely to matters of "construction" under the *Restatement*. Regarding other matters, § 107's comment provides: [296]

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[296] *Id.*

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Usually, the law of the trust's principal place of administration will govern administrative matters and the law of the place having the most significant relationship to the trust's creation will govern the dispositive provisions.

To determine a trust's "principal place of administration," UTC § 108(a) stipulates: [297]

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[297] UTC § 108(a) (amended 2018). *See, e.g.*, *Fellows v. Colburn*, 34 A.3d 552, 563 (N.H. 2011) ("the plaintiffs failed to provide sufficient evidence to demonstrate that the trust's principal place of administration was New Hampshire"); *Queen v. Schmidt*, No. 10-2017, 2015 BL 286543, 2015 WL 5175712, at *9 (D.D.C. Sept. 3, 2015) ("the Trust's principal place of administration clearly lay in the District of Columbia").

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(a) Without precluding other means for establishing a sufficient connection with the designated jurisdiction, terms of a trust designating the principal place of administration are valid and controlling if:

(1) a trustee's principal place of business is located in or a trustee is a resident of the designated jurisdiction; or

(2) all or part of the administration occurs in the designated jurisdiction.

Regarding the governance of the trust's "dispositive provisions," which seems to correspond to "validity" under the *Restatement*, UTC § 107's comment refers to "the law of the place having the most significant relationship to the trust's creation." [298]

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[298] UTC § 107 cmt. (amended 2018).

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No UTC section or comment addresses what state's law governs the ability of creditors to reach a trust beneficiary's interest, but UTC § 106 provides that matters not covered by the UTC are to be resolved under common-law principles, [299] so that the above discussion of the *Restatement*'s treatment of these issues remains relevant.

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[299] UTC § 106 (amended 2018).

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Section 107's comment offers guidance when the relative interests of two jurisdictions are being weighed (e.g., to determine which state's law governs a trust's "dispositive provisions" or their "meaning and effect"). [300] The factors to be considered are based on (and therefore are quite similar to) the *Restatement* guidelines. The author quotes and analyzes them in IV.D.3.b., below.

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[300] UTC § 107 cmt. (amended 2018) (cross-references omitted).

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## E. Suggested Language

If a client wants an inter vivos trust to be governed by the law of a particular state and to have all issues involving the trust adjudicated there, he or she might include the following language:

This agreement creates a [Trust State] trust, and all matters pertaining to the validity, construction, and application of this agreement or to the administration of the trusts created by it shall be governed by [Trust State] law. The courts of [Trust State] shall have exclusive jurisdiction over any action brought with respect to a trust hereunder.

If the client wants the law that governs questions of administration and the supervising court to change if the trust's situs is moved to another state, the following sentence might be inserted after the above sentences:

However, if the successor trustee hereunder is located in any state other than the State of [Trust State], the situs of such trust shall become that of the location of the successor trustee, and thereafter the laws governing the administration of such trust shall be those of the new situs and the courts of that state shall have exclusive jurisdiction over any action brought with respect to a trust hereunder.

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IV. Beneficiaries' Ability to Defeat Clients' Selection of Trust States

## A. Introduction

Suppose that a client's Will or inter vivos trust designates the law of a Trust State to govern the validity, administration, and construction of trusts created thereunder as well as restraints on alienation of beneficiaries' interests. Also suppose that one or more beneficiaries are unhappy with one or more of the Trust State's laws and seek redress by bringing an action in a court of the Home State. Under what circumstances may a beneficiary defeat a testator's or trustor's designation of a Trust State's law and what may the client and the attorney do in the planning process to counter such an attack? This section will explore these issues in the context of four substantial legal obstacles that the beneficiary and the Home State court must surmount to defeat the designation. [301]

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[301] The author would like to thank John E. Sullivan, III, Esquire, Sullivan & Sullivan, Ltd., Beachwood, Ohio, for his substantial contributions to the author's understanding of the material covered in this section.

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## B. Obstacle 1: Home State Court Might Lack Jurisdiction

### 1. Introduction

Comment a to § 104 of the *Restatement (Second) of Conflict of Laws* states in relevant part: [302]

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[302] *Restatement (Second) of Conflict of Laws* § 104 cmt. a (1971) (citation omitted). *See Wilkes v. Phoenix Home Life Mut. Ins. Co.*, 902 A.2d 366, 382 (Pa. 2006); *Estate of Waitzman*, 507 So.2d 24, 25 (Miss. 1987).

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Due process forbids the rendition of a judgment within the United States unless the State of rendition has judicial jurisdiction. ... A judgment rendered in violation of these requirements is void in the State of rendition itself, and due process forbids the recognition and enforcement of such a judgment in sister States.

Hence, a Home State court may render a valid judgment against a trustee of a trust only if that court has jurisdiction. Such jurisdiction might be based on in rem jurisdiction over trust assets or personal jurisdiction over a trustee. Four U.S. Supreme Court decisions since 2011 highlight the importance of jurisdictional considerations, as discussed below.

### 2. In Rem Jurisdiction

A Home State court will have in rem jurisdiction over trust assets that are held in the court's jurisdiction. [303]To prevent a Home State court from having in rem jurisdiction over a trust, the trustee should hold all assets in the Trust State because "[a] court sitting in [one state] ... cannot assert jurisdiction over the corpus of a trust with a situs outside the State." [304]

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[303] *Hanson v. Denckla*, 357 U.S. 235, 246 (1958).

[304] *Walker v. W. Mich. Nat'l Bank & Tr.*, 324 F. Supp. 2d 529, 534 n.3 (D. Del. 2004), *aff'd*, 145 Fed. Appx. 718 (3d Cir. 2005).

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### 3. Personal Jurisdiction — General Principles

State courts, federal courts sitting in diversity, [305] and federal courts considering many federal questions [306] may exercise personal jurisdiction over a defendant only if constitutional due process requirements are satisfied. [307] The classic *International Shoe Company v. Washington* [308] test determines whether a nonresident defendant has "certain minimum contacts with [the forum state] such that the maintenance of

the suit does not offend traditional notions of fair play and substantial justice." A court may satisfy this test under either of two theories: general jurisdiction or specific jurisdiction.

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[305] 28 U.S.C. § 1332.

[306] 28 U.S.C. § 1331.

[307] *See, e.g.*, *Ins. Corp. of Ireland, Ltd. v. Compagnie des Bauxites de Guinee*, 456 U.S. 694 (1982); *World-Wide Volkswagen Corp. v. Woodson*, 444 U.S. 286 (1980); *Int'l Shoe Co. v. Washington*, 326 U.S. 310 (1945). This discussion assumes that the applicable long-arm statute has also been satisfied, which is another prerequisite for the exercise of personal jurisdiction over out-of-state defendants by a state court or a federal court sitting in diversity. *See, e.g.*, Fed. R. Civ. P. 4(k)(2); *Matter of Beatrice B. Davis Family Heritage Tr.*, 394 P.3d 1203, 1207 (Nev. 2017); *Herman v. BRP, Inc.*, No. N13C-11-105, 2015 BL 104658, 2015 WL 1733805, at *3 (Del. Super. Ct. Apr. 13, 2015); *Innovation Ventures, LLC v. Custom Nutrition Labs, LLC*, 946 F. Supp. 2d 714, 718 (E.D. Mich. 2013); *Covenant Tr. Co. v. Guardianship of Ihrman*, 45 So.3d 499, 502 (Fla. Dist. Ct. App. 2010).

[308] *Int'l Shoe Co.,* 326 U.S. at 316 (1945) (internal quotation marks omitted).

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Chief Justice Strine of the Supreme Court of Delaware described the two bases for asserting personal jurisdiction over a nonresident defendant — general jurisdiction and specific jurisdiction: [309]

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[309] *Genuine Parts Co. v. Cepec*, 137 A.3d 123, 129–30 (Del. 2016) (footnotes and internal quotation marks omitted; emphasis added).

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Personal jurisdiction refers to the court's power over the parties in the dispute. There are two bases a state can use to exercise personal jurisdiction over a nonresident defendant. The first is *general jurisdiction*, which grants authority to a state's courts to assert jurisdiction over a nonresident defendant on the basis of wholly unrelated contacts with the forum. This all-purpose jurisdiction exists where a corporation's continuous corporate operations within a state are so substantial and of such a nature as to justify suit against it on causes of action arising from dealings entirely distinct from those activities. Until recently, a foreign corporation could be subject to general jurisdiction if it had continuous and systematic business contacts in the forum state. That is, merely doing business in a state was a basis for general jurisdiction there. But as we will later discuss, two recent decisions of the U.S. Supreme Court established that that is no longer enough. Courts can also exercise *specific jurisdiction* over a corporate defendant where the suit arises out of or relates to the corporation's contacts with the forum.

The two U.S. Supreme Court decisions involving general jurisdiction to which Chief Justice Strine referred are *Goodyear Dunlop Tire Operations, S.A. v. Brown* (2011) [310] and *Daimler AG v. Bauman* (2014). [311] Writing for a unanimous Court, Justice Ginsburg held in *Goodyear* that defendants' affiliations with the state must be "so continuous and systematic as to render them essentially at home in the forum state" to warrant the exercise of general jurisdiction. [312] Writing for eight Justices three years later (Justice Sotomayor concurred in the judgment), Justice Ginsburg confirmed the "essentially at home" test in *Daimler*. [313]

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[310] 564 U.S. 915 (2011).

[311] 571 U.S. 117 (2014).

[312] *Goodyear*, 564 U.S. at 919.

[313] *Daimler*, 571 U.S. at 122.

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Since 2011, the U.S. Supreme Court also has acknowledged the limits of specific jurisdiction. In 2014, the Court revisited specific personal jurisdiction jurisprudence in *Walden v. Fiore*. [314] Writing for a unanimous Court, Justice Thomas laid out the issue and the Court's conclusion at the beginning of his opinion: [315]

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[314] 571 U.S. 277 (2014). *See* Calhoun & Yates, *More Adventures in Due Process*, 2014 State Tax Today 101-9 (May 27, 2014); Carr, *News Analysis: U.S. Supreme Court Continues Trend in Cases With Nexus Implications*, 2014 State Tax Today 41-2 (Mar. 3, 2014). Another recent case in which the U.S. Supreme Court recognized restrictions on the exercise of specific personal jurisdiction is *J. McIntyre Mach., Ltd. v. Nicastro*, 564 U.S. 873 (2011).

[315] *Walden*, 571 U.S. at 279 (citation and internal quotation marks omitted).

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This case asks us to decide whether a court in Nevada may exercise personal jurisdiction over a defendant on the basis that he knew his allegedly tortious conduct in Georgia would delay the return of funds to plaintiffs with connections to Nevada. Because the defendant had no other contacts with Nevada, and because a plaintiff's contacts with the forum State cannot be decisive in determining whether the defendant's due process rights are violated, we hold that the court in Nevada may not exercise personal jurisdiction under these circumstances.

At the end of the opinion, Justice Thomas stressed that the focus of due process analysis is the defendant's — not the plaintiff's — conduct. He wrote: [316]

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[316] *Walden*, 571 U.S. at 291 (citation and internal quotation marks omitted).

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Well-established principles of personal jurisdiction are sufficient to decide this case. The proper focus of the minimum contacts inquiry in intentional-tort cases is the relationship among the defendant, the forum, and the litigation. And it is the defendant, not the plaintiff or third parties, who must create contacts with the forum State. In this case, the application of those principles is clear: Petitioner's relevant conduct occurred entirely in Georgia, and the mere fact that his conduct affected plaintiffs with connections to the forum State does not suffice to authorize jurisdiction.

A court will have personal jurisdiction over a foreign trustee in certain situations, such as when it appointed the trustee. [317] But, the foregoing cases demonstrate that nonresident trustees should not automatically concede that personal jurisdiction exists in the Home State.

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[317] *See Ohlheiser v. Shepherd*, 228 N.E.2d 210, 215 (Ill. App. Ct. 1967).

Courts consider various factors to determine whether sufficient minimum contacts exist to establish personal jurisdiction. These are catalogued, in part, in *World-Wide Volkswagen v. Woodson* and include the following acts in the forum state:

• Closing sales;

• Performing services;

• Soliciting business;

• Availing themselves of the privileges and benefits of the forum state's law;

• Indirectly, through others, serving or seeking to serve the forum state's market; and

• Delivering products into the stream of commerce with the expectation that they will be purchased by consumers in the forum state. [318]

[318] *World-Wide Volkswagen*, 444 U.S. 286, 295–98. *See, e.g.*, *Emberton v. Rutt*, No. 1:07-cv-01200, 2008 BL 348180, 2008 WL 4093714 (D.N.M. Mar. 31, 2008).

However, not all acts within a state create an adequate nexus for jurisdiction. As a general proposition, occasional trips into a state or receipt of payments issued from inside a state will be insufficient. [319] And, as shown in the trustee-specific cases discussed below, the fact that "several bits of trust administration" [320] may be carried on is also routinely inadequate to establish jurisdiction.

[319] *See Helicopteros Nacionales de Colombia, S.A. v. Hall*, 466 U.S. 408 (1984).

[320] *Hanson v. Denckla*, 357 U.S. 235, 252 (1958)

## 4. Personal Jurisdiction — Trustee Concerns

A Home State court might be able to adjudicate a matter if it has personal jurisdiction over a trustee. One way in which a client may avoid this pitfall is to use only trustees with little or no contact with the Home State. If the trustor wants a co-trustee from outside the Trust State, then the co-trustee should be from outside the trustor's Home State as well. This situation gives courts in the Home State substantially less basis to assert general jurisdiction over the trustees, and the court may be able to assert only specific personal jurisdiction over them. This is not always an easy task, however. Although the issue turns on the specific facts of each case, many opinions have shown that specific personal jurisdiction may not be established over an out-of-state trustee merely because of routine trustee activities such as mailings and phone calls from the defendant trustee's state into the plaintiff's state.

The leading case in this area is *Hanson v. Denckla*, [321] which involved a controversy concerning the right to part of the principal of a trust established in Delaware by a Pennsylvania trustor who subsequently

moved to Florida. The U.S. Supreme Court held that a Delaware court was under no obligation to give full faith and credit to a judgment of a Florida court that lacked jurisdiction over the trust's assets and the trustee. The Court, affirming the decision of the Supreme Court of Delaware, [322] discussed the jurisdictional issues as follows: [323]

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[321] 357 U.S. 235, 253 (1958). *See* Malloy, *Dora and William Donner Were Busy People*, 42 Cumb. L. Rev. 245 (2011–2012).

[322] *Lewis v. Hanson*, 128 A.2d 819 (Del. 1957), *aff'd sub nom. Hanson v. Denckla*, 357 U.S. 235 (1958).

[323] *Hanson*, 357 U.S. at 253–54 (citation omitted).

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[I]t is essential in each case that there be some act by which the defendant purposefully avails itself of the privilege of conducting activities within the forum State, thus invoking the benefits and protections of its laws. The settlor's execution in Florida of her power of appointment cannot remedy the absence of such an act in this case.

*Hanson* remains controlling precedent. In fact, it was cited as such numerous times in at least three U.S. Supreme Court cases that have been decided since 2011. [324] *Hanson* continues to be the starting point for analyzing whether personal jurisdiction exists in trust cases. Since *Hanson*, numerous cases have found that insufficient minimum contacts existed to create personal jurisdiction.
(a) *In re Estate of Ducey* (1990). [325] The Montana Supreme Court held that Montana lacked jurisdiction over the Nevada corporate trustee of a trust created by a Montana testator. The court reached this conclusion even though the Nevada trustee mailed payments to the Montana beneficiary and also telephoned the decedent in Montana in connection with modifications to her estate plan, including changes designed to benefit other Montana residents.

(b) *In re Frumkin* (1993). [326] The Tennessee Court of Appeals held that Tennessee lacked jurisdiction over the Florida corporate trustee of a trust created by a Florida testator. The court so ruled even though the Florida trustee mailed some checks and letters to the Tennessee beneficiary.

(c) *Dreher v. Smithson* ( 1999). [327] The Oregon Court of Appeals held that Oregon lacked jurisdiction over the individual trustees of a trust created by a Massachusetts trustor. The court so ruled even though the trustees: (1) accepted the trusteeship knowing that the trust had an Oregon beneficiary; (2) wrote and telephoned the beneficiary in Oregon; and (3) mailed distribution checks to the Oregon beneficiary.

(d) *Rose v. Firstar Bank* (2003). [328] The Rhode Island Supreme Court held that Rhode Island lacked jurisdiction over the Ohio corporate trustee of a trust created by an Ohio testator. The court so ruled even though the trustee: (1) mailed checks, statements, and other trust documents to Rhode Island; and (2) periodically communicated with the Rhode Island beneficiaries.

(e) *Nastro v. D'Onofrio* (2003). [329] A Connecticut federal district court held that it lacked jurisdiction over the trustee of a Jersey, Channel Islands, trust created by a Connecticut trustor. The court found insufficient contacts between Connecticut and the trustee, even though the trust was funded with stock in Connecticut corporations.

(f) *Walker v. West Michigan National Bank & Trust* (2004). [330] A Delaware federal district court lacked jurisdiction over the Michigan corporate trustee of a trust created by a Montana resident even though the Delaware beneficiary bringing the action had contributed assets to the trust and the trustee filed income tax returns for the trust. The court noted that a plaintiff's "mere beneficial interest in a trust is insufficient to assert personal jurisdiction over a nonresident trustee." [331]

(g) *Walker v. The Northern Trust Co.* (2004). [332] In a companion case to *Walker v. West Michigan National Bank & Trust*, another Delaware federal district judge ruled that the court lacked jurisdiction over the Illinois corporate trustee of a trust created by a Montana resident to which the Delaware beneficiary bringing the action had not contributed assets.

(h) *Andreas v. Stisser (In re Estate of Stisser)* (2006). [333] A Florida intermediate appellate court held that Florida courts did not have jurisdiction to adjudicate the claim by the personal representative of a Florida decedent against the trustees of the Minnesota trust that she created while she resided in Minnesota for funds to pay estate expenses. The court did so because the trustees were indispensable parties over which Florida courts lacked personal and in rem jurisdiction. [334]

(i) *Walker v. The Northern Trust Co.* (2007). [335] In a subsequent proceeding to the case discussed in (g), above, an Illinois federal district court ruled that it lacked personal jurisdiction over the nonresident trustor of an irrevocable trust regarding a beneficiary's claim that the trustor was unjustly enriched through the payment of his attorney fees from the trust.

(j) *Fellows v. Colburn* (2011). [336] In a negligence action against successor trustees, the Supreme Court of New Hampshire held that New Hampshire courts lacked jurisdiction over the defendants because "the facts pled by the plaintiffs were insufficient to justify the exercise of in personam jurisdiction over the defendants, as either successor trustees or beneficiaries." [337]

(k) *Bernstein v. Stiller* (2013). [338] Trust beneficiaries sought accountings and removal of the trustees in a Pennsylvania federal district court and contended that the trustees' filing of a state income tax return declaring the trust to be a resident trust gave the court jurisdiction. [339] The court held: [340]

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[324] *See McIntyre*, 564 U.S. at 877, 878, 880, 882; *Goodyear*, 564 U.S. at 924; *Walden*, 571 U.S. at 284, 285, 288, 291. *See also Innovation Ventures, LLC*, 946 F. Supp. 2d at 719.

[325] 787 P.2d 749, 752 (Mont. 1990).

[326] 912 S.W.2d 138 (Tenn. Ct. App. 1995).

[327] 986 P.2d 721 (Or. Ct. App. 1999).

[328] 819 A.2d 1247, 1255 (R.I. 2003).

[329] 263 F. Supp. 2d 446, 453 (D. Conn. 2003).

[330] 324 F. Supp. 2d 529 (D. Del. 2004), *aff'd*, 145 Fed. Appx. 718 (3d Cir. 2005).

[331] *Walker*, 324 F. Supp. 2d at 534.

[332] 2004 WL 1588287 (D. Del. July 14, 2004), *aff'd*, 145 Fed. Appx. 718 (3d Cir. 2005).

[333] 932 So.2d 400 (Fla.2d Dist. Ct. App. 2006).

[334] *Id.* at 402.

[335] No. 06-C-4901, 2007 BL 310409, 2007 WL 178392, at *5 (N.D. Ill. Jan. 18, 2007).

[336] 34 A.3d 552 (N.H. 2011).

[337] *Id.* at 562.

[338] No. 09-659, 2013 BL 172426, 2013 WL 3305219 (E.D. Pa. June 27, 2013).

[339] *Id.* at *1.

[340] *Id.* at *7.

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The declared residency of the trust assets is insufficient to give the Court personal jurisdiction over Respondent Trustees.

In contrast, courts held in numerous cases that they did have personal jurisdiction over a trustee.
(a) *Ohlheiser v. Shepherd* (1967). [341] An intermediate appellate court in Illinois held that it had personal jurisdiction over a Wisconsin individual successor trustee in an action by the beneficiaries to compel the successor trustee to deliver trust principal for the following reasons: [342]

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[341] 228 N.E.2d 210 (Ill. App. Ct. 1967).

[342] *Id.* at 215.

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[W]e consider that defendant, as successor trustee of a testamentary trust, became an officer of the court appointing him when he accepted the appointment by entering upon his duties as successor trustee. Although these duties did not require him to perform any act while physically within the State of Illinois, he impliedly submitted himself to the in personam jurisdiction of the court of appointment until discharged from his office. He exercised the right of acting as successor trustee by the appointment of an Illinois court and has enjoyed the benefits and protection of the laws of Illinois. The exercise of that right gave rise to the obligation to respond to the court that appointed him. We think defendant had sufficient contact with the State of Illinois to subject him to its in personam jurisdiction and to satisfy due process. To hold that an appointing court be found to have jurisdiction in personam over its officer does not offend traditional notions of fair play and substantial justice, provided he is adequately notified of the action against him so that he may defend himself.

(b) *Johnson v. Witkowski* (1991). [343] In an action involving alleged breaches of fiduciary duties, a Massachusetts intermediate appellate court concluded that Massachusetts courts had personal jurisdiction over a nonresident individual trustee as follows: [344]

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[343] 573 N.E.2d 513 (Mass. Ct. App. 1991).

[344] *Id.* at 523–24 (citations and internal quotation marks omitted).

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In regard to the constitutional requirements, the touchstone remains whether the defendant purposefully established minimum contacts in the forum State and whether specific jurisdiction over the defendant

comports with “fair play and substantial justice.” Here, the activity conducted by the defendants, including the corporation, in regard to the trust gave them sufficient warning that a particular activity may subject them to the jurisdiction of a foreign sovereign. The trust was formed in Massachusetts and was funded by the estate of a Massachusetts resident. Most of the beneficiaries are Massachusetts residents. Witkowski signed the trust in Massachusetts and has continued to manage and administer the trust while maintaining numerous contacts with the plaintiff in Massachusetts. Consequently, the courts of Massachusetts could constitutionally exercise jurisdiction over the defendant Witkowski.

(c) *Seijo v. Miller* ( 2006). [345] The Federal District Court for the District of Puerto Rico denied the Louisiana trustees’ motion to dismiss for lack of specific personal jurisdiction claims brought by the heirs of the income beneficiary of a trust created by a Puerto Rican trustor in Louisiana for Puerto Rican beneficiaries. The court concluded: [346]

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[345] 425 F. Supp. 2d 194 (D.P.R. 2006).

[346] *Id.* at 201 (citations and internal quotation marks omitted).

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[T]his court finds that in the instant case, they point to the exercise of jurisdiction. First, the defendants are not burdened by appearing before this Court because they travel to Puerto Rico to conduct business activities. The possibility that most of the evidence will have to be brought from Louisiana to Puerto Rico does not overly burden defendants. Second, Puerto Rico has an interest in having a Puerto Rico-based court adjudicate this dispute because a State has a ‘manifest interest’ in providing its residents with a convenient forum for redressing injuries inflicted by out-of-state actors. Third, the plaintiffs’ choice of forum must be accorded a degree of deference regarding their own convenience, and without a doubt, it is more convenient for the plaintiffs to litigate in Puerto Rico than in Louisiana. Fourth, the judicial system's interest in obtaining the most effective resolution of the controversy does not cut in either direction. Fifth, there is shared interest that Puerto Rico provide its residents a means of redress against out-of-state tortfeasors. Taken collectively, the gestalt factors discussed above indicate that the exercise of personal jurisdiction over the defendants in this case does not offend due process.

(d) *Cummings v. Pitman* (2007). [347] The Supreme Court of Kentucky held that Kentucky courts had personal jurisdiction over the individual trustee of a trust created by a Kentucky trustor even though the trustee resided in New York and the trust was governed by New York law. The court summarized its analysis at the beginning of its opinion as follows: [348]

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[347] 239 S.W.3d 77 (Ky. 2007).

[348] *Id.* at 80.

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Due process of law imposes limitations on a court's exercise of personal jurisdiction over nonresident defendants. In the instant case, a nonresident attorney engaged in significant legal and fiduciary activities in Kentucky. Conceding that he is subject to personal jurisdiction in Kentucky for claims arising from legal services performed, he seeks to avoid personal jurisdiction in this forum for actions in his role as trustee

of the trust agreement he drafted. Appellee, R. Andrew Boose, analogizes himself to one with two hats and posits that in Kentucky he wore only his "attorney hat" but never donned his trustee hat except for one brief moment. As Mr. Boose appears to have engaged in a fully anticipated continuing course of conduct in Kentucky sufficient to meet statutory and federal due process standards for personal jurisdiction, we are unable to accept his contention that though he acted as an attorney in Kentucky, only in New York did he act as trustee.

Along the way, the court distinguished the case at bar from *Hanson v. Denckla* as follows: [349]

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[349] *Id.* at 89 (footnotes and internal quotation marks omitted).

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We have not overlooked *Hanson v. Denckla*, a case regarding the validity of a trust agreement without any connection with the forum state. In *Hanson*, the trustee's contact with the forum at issue came not as a result of doing or soliciting business there, but rather as a result of the settlor's decision to move there after the trust agreement had been executed. The Court held that the mere fact that the beneficiary resides in a forum state is not of itself sufficient to justify long-arm jurisdiction over the trustee. However, even *Hanson* suggested that if the agreement was negotiated with a settlor residing in the forum state at the time of formation of the trust, long-arm jurisdiction would be appropriate. From the facts in evidence, we have no doubt that Kentucky is a reasonable forum choice. Mr. Boose admitted in his answer that the Kentucky court had personal jurisdiction over him in his individual capacity. We are unable to divide his responsibilities between attorney and trustee so as to make the distinction meaningful.

In the course of the opinion, the court noted that: [350]

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[350] *Id.* at 82 n.3 (citation and internal quotation marks omitted).

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While the trust agreement provided for application of the substantive law of New York, the determination of whether Kentucky may exercise personal jurisdiction is a matter of state law, particularly where, as here, the trust agreement is silent with respect to forum selection, Paragraph 15, according to its plain language is a choice of law provision rather than a forum selection clause. The provision relates only to what law is to govern a dispute between the parties, it is silent concerning where the parties may bring an action.

The failure of a Will or trust instrument to designate a jurisdiction in which legal proceedings involving a trust are to be brought to establish personal jurisdiction over an out-of-state trustee has been given significance in no other case discussed in this section. Given that this court did so, it would do no harm — and might be beneficial — to include such a designation. [351]

(e) *Sloan v. Segal* (2008). [352] A Delaware Vice Chancellor held that the court had specific personal jurisdiction over a Florida resident for the following reasons: [353]

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[351] *See* III.D., above.

[352] CA. No. 2319-VCS, 2008 BL 662, 2008 WL 81513 (Del. Ch. Jan. 3, 2008).

[353] *Id.* at 9 (footnote omitted).

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Segal's continuous course of Delaware-directed conduct makes it obviously reasonable for this court to exercise jurisdiction over him. Indeed, this state has an important interest at stake in this case. Patricia Sloan was a Delaware resident for virtually her entire life. Segal appears to have moved Patricia Sloan from this state at a time when she had started to display the symptoms of Alzheimer's and may have been unable to make an informed, uncoerced judgment about departing. In a situation such as this, Delaware has a legitimate interest in applying its law to determine whether its longtime resident exercised her right of appointment over a Delaware-based trust in an uncoerced and knowing manner. Having repeatedly engaged in conduct in Delaware relevant to the Martin Sloan Trust and having brought suit in this very court to obtain a position as one of the trustees of that Trust, Segal has no colorable basis to claim that his due process rights will be violated if he has to defend this lawsuit in this court.

(f) *Anglo Irish Bank Corp., PLC v. Superior Court* (2008). [354] A California intermediate appellate court held that it had specific personal jurisdiction over two offshore banks, an offshore trust company, and associated individuals in a fraud and deceit action involving leveraged investments through a foreign trust brought by California residents. The court concluded that defendants purposefully availed themselves of forum benefits, that the dispute was substantially connected to their California activities, and that the exercise of personal jurisdiction was fair and reasonable in the circumstances. [355]

(g) *Matter of Beatrice B. Davis Family Heritage Trust* (2017). [356] In an action in which a beneficiary sought information about a trust and an LLC from a nonresident individual investment trust advisor, the Supreme Court of Nevada held: [357]

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[354] 165 Cal. App. 4th 969 (Cal. Ct. App. 2008).

[355] *Id.* at 981–85.

[356] 394 P.3d 1203 (Nev. 2017). *See* LaPiana, *Statute Gave Specific Personal Jurisdiction Over Trust Advisor*, 44 Est. Plan. 42 (Nov. 2017).

[357] *Id.* at 1208.

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Nevada courts may exercise specific personal jurisdiction over a person accepting a position as an ITA under NRS 163.5555 should the suit arise out of a decision or action of that ITA.

Another basis for jurisdiction is a state's version of UTC § 202(a), the model version of which provides that “by accepting the trusteeship of a trust having its principal place of administration in this State, the trustee submits personally to the jurisdiction of the courts of this State regarding any matter involving the trust. [358]

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[358] UTC § 202(a) (amended 2018).

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The following cases are also instructive:
(a) *Emberton v. Rutt* (2008). [359] In a dispute between the beneficiaries of a New Mexico trust and a nonresident individual trustee, a federal district judge in New Mexico concluded: [360]

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[359] 2008 BL 348180, 2008 WL 4093714 (D.N.M. March 31, 2008)

[360] *Id.* at *8.

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There is no dispute that at one time Rutt submitted to New Mexico courts' jurisdiction. There is also insufficient evidence that Rutt's actions since that consent has vitiated that previous consent. Moreover, Rutt continues to have sufficient minimum contacts with New Mexico such that exercise of personal jurisdiction over him does not violate due process.

(b) *Queen v. Schmidt* (2015). [361] A federal district judge in the District of Columbia held that, pursuant to D.C. Code § 19-1302.02, the court had jurisdiction over two of the co-trustees who had accepted trusteeship of a trust that held real estate in the District of Columbia and was administered there. [362]

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[361] 2015 BL 286543, 2015 WL 5175712 (D.D.C. Sept. 3, 2015).

[362] *Id.* at *10.

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In 2012, a New York trial court concluded that it could exercise personal jurisdiction over a Cook Islands corporate trustee for the following reason: [363]

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[363] *Weitz v. Weitz*, 2012 WL 1079302 (N.Y. Sup. Ct. Mar. 19, 2012).

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The Court concludes that the exercise of jurisdiction over Southpac is appropriate in light of the allegations that Southpac participated in the fraudulent conveyance of assets in an effort to avoid the satisfaction of the judgment in the New York divorce action.

A 2014 decision of an intermediate appellate court in Kentucky illustrates how proper corporate structure can defeat personal jurisdiction. Hence, in *Kloiber v. Daniel Kloiber Dynasty Trus*t, [364] the court considered whether or not the trial court had personal jurisdiction over the Delaware trustee of a trust created by the husband's father in a divorce proceeding. In affirming the lower court's dismissal of the wife's claim against the trustee, [365] the court opined: [366]

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[364] 2014 BL 341661, 2014 WL 6882265 (Ky. Ct. App. Dec. 5, 2014).

[365] *Id.* at *8.

[366] *Id.* at *8 n.11.

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Beth presented to the trial court internet printouts concerning PNC's wealth management services, of which establishing a trust was one such service. We note that PNC does indeed offer wealth management services in some Kentucky locations and provided appropriate Kentucky-based contact information, but the website concerning PNC Delaware Trust Co. clearly listed its contact information in Delaware. Given that PNC Delaware Trust Co. is a distinct corporate entity from PNC Financial Services Group, Inc., we are unprepared to say that such printouts were sufficient to sustain Beth's burden of proof.

The author's employer has a comparable corporate structure. Thus, Wilmington Trust Company, which conducts Delaware trust business, operates in Delaware only. Wilmington Trust, N.A., operates in California, Florida, Georgia, Massachusetts, New Jersey, New York, Pennsylvania, and elsewhere. [367]

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[367] *See* www.wilmingtontrust.com/wtcom/.

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## 5. Rules in Federal District Court

The circumstances under which a federal district court in the Home State may assert personal jurisdiction over a trustee in a Trust State under federal question jurisdiction [368] or diversity jurisdiction [369] will often be as described above. [370] In 2014, the U.S. Supreme Court described the limits on such a court's exercise of jurisdiction as follows: “Federal courts ordinarily follow state law in determining the bounds of their jurisdiction over persons.” [371] For diversity purposes, a national association is deemed to be a citizen of the state of its headquarters. [372] In an action to remove a trustee, the “amount in controversy” for diversity purposes is capped at the value of the trust. [373] The citizenship of the trustee, not of the beneficiaries, is determinative for diversity purposes. [374]

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[368] 28 U.S.C. § 1331.

[369] 28 U.S.C. § 1332.

[370] Fed. R. Civ. P. 4(k)(1)(A).

[371] *Daimler*, 571 U.S. at 125. *See Wells Fargo Bank, N.A. v. Barber*, 85 F. Supp. 3d 1308, 1316 (M.D. Fla. 2015); *State Farm Mut. Auto Ins. Co. v. Snyder*, 2013 BL 308898, 2013 WL 5948089, at *2 (E.D. Pa. Nov. 6, 2013); *Metex Mfg. Corp. v. Manson Envtl. Corp.*, 2008 BL 298665, 2008 WL 474100, at *7 (D.N.J. Feb. 15, 2008).

[372] *Wachovia Bank, N.A. v. Schmidt*, 546 U.S. 303 (2006).

[373] *See Moore v. Chase*, 2014 BL 169378, 2014 WL 2759960, at *3 (D. Kan. June 18, 2014); *Glass v. Steinberg*, 2010 BL 8593, 2010 WL 6592935, at *2 (W.D. Ky. Jan. 14, 2010).

[374] *See Americold Realty Tr. v. Conagra Foods, Inc.*, 136 S. Ct. 1012, 1016 (2016); *Raymond Loubier Irrevocable Tr. v. Loubier*, 858 F.3d 719, 732 (2d Cir. 2017); *Wang by and through Wong v. New Mighty U.S. Trust*, 843 F.3d 487, 487 (D.C. Cir. 2016), *cert. denied*, 137 S. Ct. 2266 (2017). *See also* LaPiana, *Citizenship of a Trust for Diversity Purposes*, 44 Est. Plan. 46 (Oct. 2017).

## 6. Implications

If the trustee of a trust has extensive contacts in the Home State, the Home State court will have jurisdiction, but if all trustees and trust assets are located in the Trust State and if the trustees have insufficient contacts in the Home State, the Home State court will fail to have jurisdiction over the trust. Admittedly, the minimum contacts issue can provoke sharp debate, but this is still a significant hurdle for plaintiffs to overcome.

Nonetheless, although the facts may sometimes be murky, the law is very clear: courts from Home States can't enter valid orders or judgments against a trustee unless the court has personal jurisdiction over the trustee, nor can it enter orders or judgments against trust assets that are safely beyond the forum state's borders. This will indeed be a serious obstacle in many cases. But, even if jurisdiction exists, the court's analysis is only beginning.

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## C. Obstacle 2: Home State Court Should/Must Decline Jurisdiction

### 1. Restatement Approach — Movables

For trusts of movables (i.e., personal property) created by Will or inter vivos, § 267 of the *Restatement* provides that: [375]

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[375] *Restatement* § 267. *See* 7 *Scott and Ascher on Trusts* § 45.2.2.4.1 at 3102–14, § 45.2.2.4.2 at 3114–22, § 45.2.2.5 at 3122–25; *Bogert on Trusts* § 292 at 26–27.

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The administration of a trust of interests in movables is usually supervised ... by the courts of the state in which the trust is to be administered.

A comment to § 267 provides the following guidance for determining where a trust is to be administered: [376]

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[376] *Restatement* § 267 cmt. c.

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The question frequently arises whether a testator or settlor has manifested an intention that the trust be administered in a state other than that of his domicil. It may be expressly provided in the will or trust instrument that the trust is to be administered in a particular state. In the absence of such a provision, it is reasonable to infer in most situations that the testator or settlor expected the trustee to administer the trust at his or its place of business or domicil. This is especially true of a corporate trustee which will ordinarily administer its trust business at its principal trust office.

A later comment describes the implications of § 267 as follows: [377]

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[377] *Restatement* § 267 cmt. d.

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If the trust is to be administered in a particular state, that state has jurisdiction to determine through its courts not only the interests of the beneficiaries in the trust property but also the liabilities of the trustee to the beneficiaries, even though it does not have jurisdiction over the beneficiaries, or some of them...

So also a court of the state in which the trust is administered may give instructions as to the powers and

duties of the trustee, although the beneficiaries or some of them are not subject to the jurisdiction of the court, provided they are given opportunity to appear and be heard.

Another comment discusses the role of the court of primary supervision as follows: [378]

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[378] *Restatement* § 267 cmt. e.

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Where the trustee has not qualified as trustee in any court and the trust is to be administered in a particular state, the courts of that state have primary supervision over the administration of the trust. They have and will exercise jurisdiction as to all questions which may arise in the administration of the trust. Thus, if an inter vivos trust is created with a trust company as trustee, the courts of the state in which the trust company was organized and does business will exercise jurisdiction over the administration of the trust.

Accordingly, if a Trust State trust is administered exclusively in the Trust State, then the Trust State will have primary supervision over the administration of the trust and will have (and will exercise) jurisdiction as to all questions that may arise in the administration of the trust. [379] Hence, if a Trust State trust is created with a Trust State trust company as trustee, then the Trust State courts will exercise jurisdiction over the administration of the trust. [380] If a Home State court also has jurisdiction over the trustee or the trust, a Comment to § 267 suggests that the court should defer to Trust State courts as follows: [381]

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[379] *Id.*

[380] *Id.*

[381] *Id. See In re Holdeen Tr.*, 58 Pa. D. & C.2d 602, 622–25 (Ct. Com. Pl. Phila. 1972) (summarizes cases in which Home State court deferred to court of primary supervision).

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A court of a state other than that of the testator's domicil or that in which the trust is to be administered will not exercise jurisdiction if to do so would be an undue interference with the supervision of the trust by the court which has primary supervision. Whether there is such interference depends on the relief sought. Thus, if a court acquires jurisdiction over the trustee it may entertain a suit to compel him to redress a breach of trust, even though the trustee has qualified as trustee in a court of another state or the administration of the trust is in another state. It may compel the trustee to render an accounting or it may even remove the trustee. On the other hand, it will ordinarily decline to deal with questions of construction or validity or administration of the trust, leaving these matters to be dealt with by the court of primary supervision. Thus, it will not ordinarily give instructions to the trustee as to his powers and duties.

The Scott treatise summarizes the applicable principles as follows: [382]

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[382] 7 *Scott and Ascher on Trusts* § 45.2.2.6 at 3125.

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Trust administration is ordinarily governed by the law of the state of primary supervision, and the rights of

the parties ought not depend on the fact that a court of some other state happens to have acquired jurisdiction. Such a court may give a judgment based on its own local law, or it may attempt to apply the law of the state of primary supervision but apply it incorrectly.

Case law confirms that courts are cautious about construing trust questions governed by the laws of other states and that consequently they often abstain from exercising jurisdiction. For example, in *Bartlett v. Dumaine*, [383] the New Hampshire Supreme Court deferred to Massachusetts courts in a suit regarding the duties of trustees of a Massachusetts trust to account to its beneficiaries, even though the New Hampshire court had personal jurisdiction over all interested parties. The Scott treatise cites cases from Illinois, New York, Pennsylvania, and Texas that reached comparable results. [384] In 2013, the Supreme Court of Delaware confirmed that: [385]

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[383] 523 A.2d 1, 14–15 (N.H. 1986); *Balt. Nat'l Bank v. Cent. Pub. Util. Corp*., 28 A.2d 244, 246 (Del. Ch. 1942) (Delaware Court of Chancery deferred to Maryland courts in case involving trust to be administered in Maryland). *But see Flaherty v. Flaherty*, 638 A.2d 1254, 1255–57 (N.H. 1994) ("Since the New Hampshire Superior Court issued the divorce decree, it should decide every facet of the property division," but Massachusetts law governed construction, administration, and creditor rights issues).

[384] 7 *Scott and Ascher on Trusts* § 45.2.2.4.1 at 3112 n.36. *See, e.g*., *Walton v. Harris*, 647 N.E.2d 65, 67–69 (Mass. App. Ct. 1995) (Massachusetts courts had jurisdiction because Massachusetts continued to be situs even though assets had been moved to Florida); *Holdeen Tr*., 58 Pa. D. & C.2d 602, 612–22 (Ct. Com. Pl. Phila. 1972) (Pa. courts had jurisdiction because settlor set administration in Pa. even though assets were in N.Y.).

[385] *In re Peierls Family Testamentary Tr*., 77 A.3d 223, 227 (Del. 2013).

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[I]n cases such as these where a trust maintains contacts with multiple states, we prefer to consult the*Restatement (Second) of Conflict of Laws* [particularly § 267] to resolve the issue of jurisdiction.

If it is important for proceedings involving a trust to be handled in Trust State courts, the trustee and beneficiaries might commence a proceeding (e.g., to appoint a successor trustee, to make a unitrust conversion) early in the trust's existence to confirm jurisdiction.

In this regard, a Delaware Vice Chancellor wrote in 2016: [386]

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[386] *IMO Ronald J. Mount 2012 Irrevocable Dynasty Tr*, 2016 BL 18383, 2016 WL 297655, at *3 (Del. Ch. Jan. 21, 2016), quoting *Pipal Tech. Ventures Private Ltd. v. MoEngage, Inc*., 2015 BL 413630, 2015 WL 9257869, at *5 (Del. Ch. Dec. 17, 2015) (footnote and internal quotation marks omitted).

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[A] court — in the absence of a prior-filed action elsewhere — should respect a plaintiff's choice of forum except in the rare case where the defendant demonstrates with particularity that it will be subjected to overwhelming hardship and inconvenience if required to litigate in Delaware, thereby warranting drastic relief.

## 2. Restatement Approach — Land

The testator or trustor is much more constrained for trusts that hold interests in land created by Will or

inter vivos. Hence, § 276 of the *Restatement* provides as follows: [387]

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[387] *Restatement* § 276. *See id.* cmt. b; 7 *Scott and Ascher on Trusts* § 46.2.2–§ 46.2.2.2 at 3373–3382, 46.2.3–46.2.3.2 at 3382–3389; *Bogert on Trusts* § 292 at 20–21.

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The administration of a trust of an interest in land is supervised by the courts of the situs as long as the land remains subject to the trust.

One of § 276's comments expands upon the general rule as follows: [388]

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[388] *Restatement* § 276 cmt. b.

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[T]he courts of the situs have jurisdiction over the administration of the trust as long as the land remains subject to the trust. The courts of the situs have and will exercise jurisdiction to determine the construction, validity and effect of the will or trust instrument insofar as interests in the land are concerned. A court of the situs has power to remove the trustee and vest the title to the land in a substitute trustee, even though it does not have jurisdiction over the trustee personally. It has and will exercise jurisdiction over the administration of the trust. It can determine the powers and duties of the trustee and the rights of the beneficiaries.

That comment describes the role of courts outside the situs as follows: [389]

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[389] *Id.*

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A court of a state other than that of the situs may exercise jurisdiction if this does not unduly interfere with the control by the courts of the situs. Thus, if it has jurisdiction over the trustee it may entertain a proceeding to surcharge the trustee for a breach of trust, although in determining whether the trustee has incurred a liability it will apply the law that would be applied by the courts of the situs. It may even remove the trustee and compel him to make a conveyance to a successor trustee. It cannot, however, by its judgment directly affect interests in the land.

A court other than that of the situs will not exercise jurisdiction, if to exercise it would be an undue interference with the supervision of the trust by the courts of the situs. Thus, it will not ordinarily deal with questions of construction or validity or administration of the trust, leaving these matters to be dealt with by the courts of the situs. It will not ordinarily give instructions to the trustee as to his powers and duties.

## 3. UPC Approach

The above principles have been codified in some states. Section 7-203 of the UPC provides as follows: [390]

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[390] UPC § 7-203 (amended 2010).

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The Court will not, over the objection of a party, entertain proceedings under Section 7-201 involving a trust registered or having its principal place of administration in another state, unless (1) when all appropriate parties could not be bound by litigation in the courts of the state where the trust is registered or has its principal place of administration or (2) when the interests of justice otherwise would seriously be impaired. The Court may condition a stay or dismissal of a proceeding under this section on the consent of any party to jurisdiction of the state in which the trust is registered or has its principal place of business, or the Court may grant a continuance or enter any other appropriate order.

Currently, § 7-203 is in effect in the above form in at least seven states. [391] Applying Michigan's version of § 7-203, [392] the Court of Appeals of Michigan held in 2015: [393]

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[391] Alaska Stat. § 13.36.045; Haw. Rev. Stat. Ann. § 560:7-203; Idaho Code § 15-7-203; Mass. Gen. L. ch. 203E, § 203, Mich. Comp. Laws § 700.7205; N.C. Gen. Stat. § 36C-2-203; Utah Code Ann. § 75-7-204.

[392] Mich. Comp. Laws § 700.7205.

[393] *In re Seneker Tr.*, 2015 BL 51771, 2015 WL 847129, at *1 (Mich. Ct. App. Feb. 26, 2015).

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Appellant argues, and we agree, that the Trust's principal place of administration is in Florida and, therefore, the Michigan probate court was without subject-matter jurisdiction over appellees' petition.

## 4. UTC Approach

No UTC provision covers this subject. Indeed, in enacting their versions of the UTC, several states repealed and, except for Massachusetts and Michigan, did not replace their versions of UPC § 7-203, quoted above.

## 5. Federal District Court

When a case involving a trust meets the requirements for diversity jurisdiction [394] so that the case may be removed from state to federal court, the federal district court must decide whether to exercise jurisdiction. Sometimes such courts decline to do so, [395] other times they do not. [396]

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[394] *See* 28 U.S.C. § 1332. *See* Rubenstein & Chmil, *Getting Out of Federal Court*, 156 Tr. & Est. 14 (Dec. 2017).

[395] *See, e.g.*, *Norton v. Bridges*, 712 F.2d 1156 (7th Cir. 1983).

[396] *See, e.g.*, *Barnes v. Brandrup*, 506 F. Supp. 396 (S.D.N.Y. 1981).

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## D. Obstacle 3: Home State Court Should Apply Trust State Law

### 1. Restatement Approach — Movables

### a. Introduction

Section III., above, quotes many of the provisions of the *Restatement* regarding the effectiveness of a designation by a testator or trustor of a law to govern the validity, administration, and construction of a trust of movables as well as restraints on alienation of beneficiaries' interests.

### b. Section 269 and § 270 — Validity

### (1) Introduction

Section 269 of the *Restatement* addresses questions involving the validity of provisions of a trust of movables created by Will, [397] and § 270 covers the law that is used to resolve questions involving the validity of provisions of a trust of movables created inter vivos. [398]

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[397] *Restatement (Second) of Conflict of Laws* § 269 (1971).

[398] *Restatement* § 270. *See Toledo Tr. Co. v. Nat'l Bank of Detroit*, 362 N.E.2d 273, 278–279 (Ohio Ct. App. 1976).

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When analyzing the validity of a trust provision under § 269 or § 270, it is necessary to answer the following three questions:
(a) Is the question one of "validity"?

(b) Does the Trust State have a substantial relation to the trust?

(c) Does the trust provision in question violate a strong public policy of the Home State?

For an inter vivos trust, it also is necessary to determine whether the Trust State or the Home State has the most significant relationship to the matter at issue.

### (2) Questions of Validity

The "validity" of trust clauses is a defined term and is limited to matters such as whether the trust violates the rule against perpetuities or a rule against accumulations. [399] The ability of creditors to reach trust assets is not a matter of validity but is addressed separately by the Restatement.

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[399] *Restatement* § 269 cmt. d.

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### (3) Substantial Relation to the Trust

The Trust State has a substantial relation to the trust if, inter alia, the trustor designated it as the place of the trust's administration, the trustee lives or does business in the Trust State when the trust is created, or the trust assets are located in the Trust State at that time. [400]

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[400] *Restatement* § 270 cmt. b. *See Annan v. Wilmington Tr. Co.*, 559 A.2d 1289, 1293–1294 (Del. 1989) (Delaware courts recognized trust agreement's designation of Quebec law because trust was created and initially administered in Quebec).

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### (4) Strong Public Policy

According to the authorities, the strong public policy issues that justify a departure from § 270's general rule involve trust provisions designed to defeat a surviving spouse's right of election and violate a state's restrictions on testamentary gifts to charity, [401] but they do not include jurisdictional differences in the rule against perpetuities or the rule against accumulations. [402] Moreover, the spousal elective share exception is not always followed as a matter of common law, and courts have sometimes allowed deceased spouses from one state to establish inter vivos trusts under the law of another state to defeat their surviving spouse's elective shares. [403]

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[401] *Restatement* § 269 cmts. c, i, *id.* § 270 cmts. b, e; 7 *Scott and Ascher on Trusts* § 45.4.2.4 at 3254–3260; *Bogert on Trusts* § 297 at 70 n.6, § 301 at 113.

[402] *Restatement* § 269 cmt. i. *See 2002 Lawrence R. Buchalter Alaska Tr. v. Phila. Fin. Life Assurance Co.*, 96 F. Supp. 3d 182, 209 (S.D.N.Y. 2015) ("The party seeking to invoke the doctrine bears the heavy burden of establishing that the foreign law is repugnant").

[403] *See* V.L., below.

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### (5) Most Significant Relationship to the Matter at Issue

Section 270 refers to § 6 of the *Restatement* quoted above on this issue. [404] This subject is discussed in detail below with respect to the UTC.

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[404] *Restatement* § 6(2).

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## c. Section 271 and § 272 — Administration

A trustor's designation of a state's law to govern questions regarding the administration of a testamentary trust [405] or inter vivos trust [406] of personal property will be respected, even if the designated state has no connection with the trust. Administration questions involve the duties, powers, and liability of the trustee; trust investments; the trustee's right to compensation and indemnity; the replacement of the trustee; and the beneficiaries' power to terminate the trust. [407]

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[405] *Restatement* § 271(a). *See Pitts v. First Union Nat'l Bank*, 262 F. Supp. 2d 593, 596 (D. Md. 2003) ("In the absence of a written choice of law provision in the applicable document, Maryland will apply the law of the state whose law governs the administration of the trust").

[406] *Restatement* § 272.

[407] *Restatement* § 271 cmt. a.

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## d. Section 268 — Construction

A testator's or trustor's designation of the law of a state to govern questions regarding the construction of a trust that holds personal property will be respected, even if the designated state has no connection with the trust. [408] Construction questions involve the identity of the beneficiaries and, generally, decisions involving allocations between principal and income. [409]

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[408] *Restatement* § 268. *See In re Dumaine*, 600 A.2d 127, 129 (N.H. 1991) (New Hampshire court honored designation of New Hampshire law on construction question); *In re Estate of Lykes*, 305 A.2d 684 (N.H. 1973) (N.H. court honored designation of Texas law on construction question).

[409] *Restatement* § 268.

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## e. Section 273 — Restraints on Alienation of a Beneficiary's Interest

For trusts that hold personal property, the analytical starting point for determining whether creditors may reach trust assets is § 273 of the *Restatement*. [410] Section 273 and its comments specify that the law of the place of administration designated by the testator or trustor is to be respected and do not contemplate that a different rule might apply if the law of the Trust State violates a strong public policy of the Home State. Consequently, the law that governs a trust should be determinative with respect to the ability of creditors to reach its assets without further inquiry.

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[410] *Restatement* § 273. *See Estate of German v. United States*, 7 Cl. Ct. 641 (Cl. Ct. 1985) (in suit to establish whether estate was entitled to estate tax refund, court, without discussion, applied Maryland law (law designated by trust) not Florida law (law of trustor's domicile) to determine whether creditors could reach trustor's interest).

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For inter vivos trusts, the Scott treatise suggests that there might be a strong public policy exception to the rule in § 273. It says: [411]

[411] 7 *Scott and Ascher on Trusts* § 45.7.1.2 at 3350 (footnotes omitted).

If the settlor creates a trust to be administered in a state other than that of his domicil, the law of the place of administration, rather than that of the settlor's domicil, should ordinarily apply. Thus, a settlor domiciled in one state may create an inter vivos trust by conveying property to a trust company of another state, as trustee, and delivering the property to it, for administration in the other state. In that case, the law of the other state ordinarily applies as to the rights of creditors to reach a beneficiary's interest.

It is true that this permits a person who is domiciled in a jurisdiction in which restraints on alienation are not permitted, to create an inter vivos trust in another jurisdiction, in which they are permitted, and thereby to take advantage of the law of the latter jurisdiction. It would seem, however, that there is ordinarily nothing wrong with this, at least if there is no strong public policy against doing so in the state of the settlor's domicil.

The Scott treatise does not discuss whether a state's provision of greater protection from creditor claims for an inter vivos trust amounts to a violation of a forum state strong public policy, but, in discussing the issue for testamentary trusts (where the law of the testator's domicile traditionally is given more weight than the law of the domicile of the trustor of an inter vivos trust), the Scott treatise takes the position that a difference in the effectiveness of spendthrift clauses should not justify a departure from the general rule: [412]

[412] 7 *Scott and Ascher on Trusts* § 47.7.1.1 at 3345 (footnote omitted).

Ordinarily, it would seem, such a policy, whether to allow restraints on alienation, in order to protect a beneficiary, or to permit alienation in order to protect creditors and assignees, is not so strong as to preclude the application in another jurisdiction of its own law.

Indeed, the Scott treatise criticizes dictum in *Erdheim v. Mabee*, [413] which suggested that forum courts should have more latitude, as follows: [414]

[413] 113 N.E.2d 433 (N.Y. 1953).

[414] 7 *Scott and Ascher on Trusts* § 45.7.1.1 at 3347 (footnote omitted).

If this means that any court that acquires jurisdiction over the trust property can properly apply its own law as to the rights of creditors to reach the trust property, regardless of the law of the situs of the trust, we submit that the dictum is unsupportable.

The Scott treatise summarizes the applicable principles as follows: [415]

[415] *7 Scott and Ascher on Trusts* § 45.7.3 at 3365–3366 (footnote omitted).

There are conflicting policies in the various states as to the rights of creditors of a beneficiary of a trust of movables to reach the beneficial interest, and as to the rights of an assignee of such an interest. In some jurisdictions, the policy is to protect the beneficiary; in others, the policy is to protect creditors and assignees; and yet others, the policy attempts to protect all of them, within limits. When more than one jurisdiction is involved, the question is which jurisdiction's law should apply.

Although the matter is not entirely clear, we submit that the applicable law should, ordinarily at least, be that of the situs of the trust. To the extent that under that law a beneficiary's interest cannot be reached by creditors or assignees, it ought not be possible to reach that interest simply by choosing a different forum.

If under the law of the situs of the trust a beneficiary's interest cannot be reached, it should ordinarily be immaterial that the plaintiff chooses to bring the proceeding in a jurisdiction in which the result would or might have been differed. The law of the forum, merely because it is the law of the forum, should not apply. It should also generally be immaterial where the beneficiary is domiciled, where the creditor or assignee is domiciled, and where the debt was incurred or the assignment was made.

Until very recently, the effectiveness of spendthrift clauses in third-party trusts was quite controversial; when the 4th edition of the Scott treatise was published in 1989, some states did not respect spendthrift trusts at all, whereas others did so to one degree or another. Scott nevertheless suggested that differences between these laws did not constitute differences of “strong public policy.”

### 2. Restatement Approach — Land

Section III., above, quotes many of the provisions of the Restatement regarding the effectiveness of a designation by a testator or trustor of a law to govern the validity, administration, and construction of a trust of land as well as of restraints on alienation of beneficiaries’ interests. Although the law that governs questions of construction for a trust of land is the law designated by the testator or trustor, [416] the law that governs questions of validity, [417] administration, [418] or restraints on alienation [419] for such a trust is the law that would be applied by the courts of the situs of the land.

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[416] *Restatement* § 277.

[417] *Restatement* § 278.

[418] *Restatement* § 279.

[419] *Restatement* § 280.

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### 3. UTC Approach

### a. In General

Under the UTC, a Home State's public policy may not bar application of a Trust State's law regarding the “meaning and effect” of a trust provision unless the Home State has the “most significant relationship” to the trust. [420] More significantly for present purposes, a trust's “dispositive provisions” are governed by the law of “the place having the most significant relationship to the trust's creation.” [421]

[420] UTC § 107(1) (amended 2018).

[421] UTC § 107 cmt. (amended 2018).

As a general rule of trust law, the overriding principle of construction is that courts should discern and honor a testator's or trustor's intent whenever possible. [422] This rule applies in choice of law issues as well, [423] and "[t]he jurisdiction selected need not have any other connection to the trust." [424] Any other considerations are typically just factors used to divine intent when it is not expressed. [425] This rule honoring intent is well-established in Delaware. [426]

[422] *See, e.g.*, *Hodges v. Johnson*, 177 A.3d 86, 93 (N.H. 2017); *Shriners Hosps. for Children v. First N. Bank of Wyo.*, 373 P.3d 392, 406 (Wyo. 2016); *In re Peierls Family Inter Vivos Tr.*, 77 A.3d 249, 263 (Del. 2013); *Ladysmith Rescue Squad, Inc. v. Newlin*, 694 S.E.2d 604, 608 (Va. 2010); *In re Cohen*, 188 A.3d 1208, 1214 (Pa. Super. Ct. 2018); *Millstein v. Millstein*, 2018-Ohio-2295, 2018 WL 1567801, at *2 (Ohio Ct. App. Mar. 29, 2018); *Bradley v. Shaffer*, 535 S.W.3d 242, 247 (Tex. App. 2017); *Church of Little Flower v. U.S. Bank*, 979 N.E.2d 106, 110 (Ill. App. Ct. 2012); *Miami Children's Hosp. Found., Inc. v. Estate of Hillman*, 101 So.3d 861, 863 (Fla. Dist. Ct. App. 2012); *In re Estate of Stewart*, 286 P.3d 1089, 1093 (Ariz. Ct. App. 2012); *In re Tr. Under Will of Flint*, 118 A.3d 182, 194 (Del. Ch. 2015).

[423] *Rudow v. Fogel*, 426 N.E.2d 155, 160 (Mass. Ct. App. 1981) ("In estate or commercial planning areas, the intentions of the settlor-testator or the contracting parties are significant both for local law and choice-of-law decisions."); *The First Nat'l Bank of Mount Dora v. Shawmut Bank of Boston*, 389 N.E.2d 1002, 1008 (Mass. 1979) ("In construing a trust instrument and rights and obligations under it, the law of the situs of the trust would often be given recognition, particularly when, as here, the trust expressly so directs"); *Nat'l Shawmut Bank v. Cumming*, 91 N.E.2d 337, 341 (Mass. 1950) (noting that Vermont settlor "had expressed an intent in the trust instrument that it should be construed and interpreted according to the laws of this Commonwealth [of Massachusetts]"). *See also Conflict of Laws as to Trusts Inter Vivos*, 139 A.L.R. 1129, 1130 (1942).

There is also apparent in the more recent cases a tendency to give effect to any expressed or necessarily implied intention or desire of the creator of the trust to have the trust governed by the law of a particular jurisdiction with which one or more of the elements of the trust are connected.

[424] UTC § 107 cmt. (amended 2018).

[425] *Conflict of Laws*, 139 A.L.R. at 1130 ("Indeed, it may be said that any rule referring the validity, interpretation, or effect of the trust to the law of the situs of particular elements of the trust, such as the law of the donor's domicil or the law of the situs of the administration of the trust, is not an absolute or primary rule, but a secondary rule based upon the presumed intention of the donor, in the absence of indications to the contrary, that the law of that jurisdiction be the governing law of the trust").

[426] *See, e.g.*, *In re Peierls Family Inter Vivos Tr.*, 77 A.3d 249, 263 (Del. 2013); *In re Tr. Under Will of Flint for the Benefit of Shadek*, 118 A.3d 182, 194 (Del. Ch. 2015).

## b. Application

When the relative interests of jurisdictions are being weighed, the UTC sets the following guidelines for determining which state has the most significant relationship to a trust: [427]

[427] UTC § 107 cmt. (amended 2018) (citations omitted).

Factors to consider in determining the governing law include the place of the trust's creation, the location of the trust property, and the domicile of the settlor, the trustee, and the beneficiaries. Other more general factors that may be pertinent in particular cases include the relevant policies of the forum, the relevant policies of other interested jurisdictions and degree of their interest, the protection of justified expectations and certainty, and predictability and uniformity of result.

These factors can be managed or addressed in ways that maximize the Trust State's relation to a trust and/or minimize the Home State's relation.

## (1) Place of Trust's Creation

A trust executed by a trustee in a particular state is typically deemed to be created in that state. [428] Accordingly, so long as a trustee executes its trust in the Trust State, the "place of creation" test is satisfied. To be safe, a testator or trustor could also execute the Will or trust in the Trust State. [429] Because a prudent client should meet with his or her trustee in any event, a trip to the trustee's place of business is hardly a serious burden. Additionally, a trust's situs, which arises from the creation of a trust, is based on the trustee's domicile and the trust's place of administration. [430] Hence, accepting and administering a trust from within the Trust State will also in many cases be the same as creating the trust in the Trust State.

[428] *See, e.g.*, *Cumming*, 91 N.E.2d at 341 (referring to "the completion of the trust agreement by final execution by the trustee"); *In re Gower*, 184 B.R. 163, 164 (Bankr. M.D. Fla. 1995) (noting that decedent "created and executed [trust] in Colorado").

[429] *See, e.g.*, *Toledo Tr. Co. v. Nat'l Bank of Detroit*, 362 N.E.2d 273, 278–279 (Ohio Ct. App. 1976) (trustor's execution of trust in Toledo, Ohio, helped establish that trust had its "most significant contacts with ... Ohio").

[430] *Warner v. Fla. Bank & Tr. Co.*, 160 F.2d 766, 771 (5th Cir. 1947) ("Matters of administration are determined by the law of the situs or the seat of the trust, and the domicile of the trustee of intangible personal property including shares of stock is usually the seat of the trust").

## (2) Location of Trust Property

"[T]he situs of intangibles is often a matter of controversy." [431] The common-law maxim is that "movables follow the person," [432] and hence personalty is situate where the legal title holder is located. [433]Although this view has been somewhat displaced in recent years by the notion that property is situate where it is physically located, [434] personal property is still often considered situate with the owner. [435] In keeping with this rule, personalty can be situated in a Trust State simply by retitling it in the name of a trustee. [436]

[431] *Hanson v. Denckla*, 357 U.S. 235, 246–247 (1958).

[432] *Appraisal Review Bd. of Galveston County. v. Tex-Air Helicopters, Inc.*, 970 S.W.2d 530 (Tex. 1998);

*Delaware v. New York*, 507 U.S. 490, 503 (1993).

[433] *Zanes v. Mercantile Bank & Tr. Co. of Tex.*, 49 S.W.2d 922, 926 (Tex. Civ. App. 1932). *See also Sadler v. Indus. Tr. Co.*, 97 N.E.2d 169, 170 (Mass. 1951) (noting that trust "consist[ed] entirely of personal property which was transferred to the trustee by the settlor at the times the trusts were executed" and that trust property was in Rhode Island).

[434] *See, e.g.*, 16 *Am. Jur.2d Conflict of Laws* § 52; *Bogert on Trusts* § 291 at 8 ("The word 'situs' usually refers to the state in which trust assets are physically located ... .").

[435] *See* 16 Am. Jur.2d Conflict of Laws § 52.

[436] *Cf. Cumming*, 91 N.E.2d at 339 (noting that trustor executed trust in Vermont while trustee executed trust in Massachusetts).

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Situs selection may be reinforced by good planning. Certain tangible assets (such as valuables held in a safe deposit box) are easily located within the Trust State. Cash, securities, and comparable assets can be placed in accounts maintained in the Trust State.

### (3) Trustee's Domicile

The fact that a trustee is located, incorporated, or organized in the Trust State will make this factor weigh in the Trust State's favor. [437]

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[437] *See, e.g.*, *Toledo Tr. Co.*, 362 N.E.2d at 278–79 (trustee's incorporation in Ohio helped establish that trust had its "most significant contacts with ... Ohio"); *Cumming*, 91 N.E.2d at 339 (trustee's domicile and place of business in Massachusetts supported application of Massachusetts law).

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### (4) Testator's/Trustor's Domicile

A testator's or trustor's domicile in the Home State admittedly lessens the Trust State's relation to a trust. However, in an increasingly mobile society, the weight accorded to a testator's or trustor's domicile, which may be transient, can often be considered a less important consideration, and hence given less weight, than the trustee's domicile, particularly that of an institutional trustee with a more-or-less permanent presence in the Trust State. The impact of a testator's or trustor's domicile may be further lessened by other considerations.

### (5) Beneficiaries' Domiciles

Not all beneficiaries will necessarily live in the Home State. A scattered group of beneficiaries residing in multiple states dilutes the relationship of any one beneficiary's Home State to the trust. If the beneficiaries are also mobile, then the permanency and primacy of the trustee's relationship is further heightened. This dilution effect is also manipulable to an extent. A testator or trustor can always name charitable or institutional beneficiaries that reside outside his or her Home State, and perhaps even one or more who reside in his or her Home State. Such planning will reduce the impact of any one beneficiary's state.

### (6) Policies of Forum State — Trust State Not the Forum

This factor's impact is clearly based on which state is the forum for a dispute. If someplace other than the Trust State is the forum, then the Trust State's relation to the trust is arguably diminished, and a local judge may conclude that the forum state — and hence its policy, if any, has a greater relation to the trust. [438]

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[438] *See In re Smith*, 415 B.R. 222, 234–35 (Bankr. N.D. Tex. 2009); *Dexia Credit Local v. Rogan*, 624 F. Supp. 2d 970, 975–76 (N.D. Ill. 2009); *In re Lawrence*, 227 B.R. 907, 917 (Bankr. S.D. Fla. 1998); *In re Brooks*, 217 B.R. 98, 101–02 (Bankr. D. Conn. 1998); *In re Portnoy*, 201 B.R. 685, 698 (Bankr. S.D.N.Y. 1996) (U.S. courts applied their law rather than foreign law designated in the trust instrument to determine whether creditors could reach trust assets).

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## (7) Policies of Forum State — Trust State as the Forum

If the Trust State is the forum, then that state's relation to a trust, and hence the interest in advancing its policies, is obviously enhanced. This, in turn, suggests that trustors expecting challenges to their trusts might preemptively sue in that state. A preemptive suit could take the form of an action for a declaratory judgment that the Trust State's law applies. [439]

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[439] *See* Unif. Declaratory Judgments Act § 4 (1922), which is in effect in Alabama (Ala. Code § 6-6-225); Arizona (Ariz. Rev. Stat. Ann. § 12-1834); Arkansas (Ark. Code Ann. § 16-111-105); Colorado (Colo. Rev. Stat. § 13-51-108); Delaware (Del. Code Ann. tit. 10; § 6504); Florida (Fla. Stat. § 86.041); Georgia (Ga. Code Ann. § 9-4-4); Idaho (Idaho Code § 10-1204); Illinois (735 ILCS 5/2-701); Indiana (Ind. Code Ann. § 34-14-1-4); Iowa (Iowa R. Civ. P. 1.1104); Kansas (Kan. Stat. Ann. § 60-1706); Louisiana (La. Civ. Code Ann. art. 1874); Maine (Me. Rev. Stat. Ann. tit. 14, § 5956); Maryland (Md. Code Ann., Cts. & Jud. Proc. § 3-408); Massachusetts (Mass. Gen. L. ch. 231A, § 2); Minnesota (Minn. Stat. Ann. § 555.04); Missouri (Mo. Ann. Stat. § 527.040); Montana (Mont. Code Ann. § 27-8-204); Nebraska (Neb. Rev. Stat. § 25-21,152); Nevada (Nev. Rev. Stat. § 30.060); New Jersey (N.J. Rev. Stat. § 2A:16-55); New Mexico (N.M. Stat. Ann. § 44-6-4) North Carolina (N.C. Gen. Stat. § 1-255); North Dakota (N.D. Cent. Code § 32-23-04); Ohio (Ohio Rev. Code Ann. § 2721.05); Oklahoma (Okla. Stat. Ann. tit. 12, § § 1651–1657); Oregon (Or. Rev. Stat. § 28.040); Pennsylvania (42 Pa. Cons. Stat. § 7535); Rhode Island (R.I. Gen. Laws § 9-30-4); South Carolina (S.C. Code Ann. § 15-53-50); South Dakota (S.D. Codified Laws § 21-24-5); Tennessee (Tenn. Code Ann. § 29-14-105); Texas (Tex. Civ. Prac. & Rem. Code Ann. § 37.005); Utah (Utah Code Ann. § 78B-6-410); Vermont (Vt. Stat. Ann. tit. 12, § 4714); Virginia (Va. Code Ann. § 8.01-184); Washington (Wash. Rev. Code § 7.24.020); West Virginia (W. Va. Code § 55-13-4); Wisconsin (Wis. Stat. § 806.04); Wyoming (Wyo. Stat. Ann. § 1-37-105). The text of the act is available at, www.uniformlaws.org/shared/docs/declatory%20judgments/udja%201922.pdf. For a list of the states that have enacted the Act, go to www.uniformlaws.org/LegislativeFactSheet.aspx?title=Declaratory Judgments Act.

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Preemptive suits might raise nettlesome questions of whether (1) the prospective challenger is a necessary or indispensable party to the suit, (2) the Trust State had good jurisdiction, and (3) a case has become ripe for adjudication. Nonetheless, if a preemptive suit can be filed in the Trust State, then it should be. This will plainly enhance the Trust State's relation to the trust and give that state's law the legal advantage as to the forum state's policies.

A preemptive suit may also create a very practical advantage — Trust State judges are likely to think long and hard before finding that their own state's relation to a trust is somehow displaced by another state's interest. This is evident in the following passage from the 1957 decision of the Delaware Supreme Court in *Lewis v. Hanson*: [440]

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[440] 128 A.2d 819, 835 (Del. 1957), *aff'd*, 357 U.S. 235 (1958). *See Sloan v. Segal*, 2008 WL 81513 (Del. Ch. Jan. 3, 2008).

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[W]e think the public policy of Delaware precludes its courts from giving any effect at all to the Florida judgment of invalidity of the 1935 trust. We are dealing with a Delaware trust. The trust res and trustee are located in Delaware. The entire administration of the trust has been in Delaware. The attack on the validity of this trust raises a question of first impression in Delaware and one of great importance in our law of trusts. To give effect to the Florida judgment would be to permit a sister state to subject a Delaware trust and a Delaware trustee to a rule of law diametrically opposed to the Delaware law. It is our duty to apply Delaware law to controversies involving property located in Delaware, and not to relinquish that duty to the courts of a state having at best only a shadowy pretense of jurisdiction.

*Comment:* If the filing of a preemptive suit smacks of forum shopping, then so be it. Plaintiffs show no remorse over this practice; there is no reason why trustees should be less willing to use this tool to their advantage.

### (8) Policies of Nonforum State

The forum court should consider the relevant policies of other interested states and the degree of their interest. Thus, a Home State court must consider the Trust State's policies and interests. [441] The reverse, of course, also is true — a Trust State court must consider the policies and interests of the Home State. As suggested above, there will sometimes be little conflict between the laws and policies of the Trust State and the Home State. In other instances, there might be. Such conflict merely means that the competing policies may cancel out each other as factors regarding which state has the most significant relationship to a trust, which leaves the outcome determined by other factors, most of which strongly cut in the Trust State's favor.

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[441] *See Bartlett v. Dumaine*, 523 A.2d 1, 14–15 (N.H. 1986).

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### (9) Justified Expectations, Certainty, Predictability, and Uniformity of Results

These final factors strongly weigh in favor of a Trust State being deemed the state with the most significant relationship to a trust.

As noted above, the primary duty of a court is to discern and apply a testator's or trustor's intent. If a testator or trustor intended a trust to be governed by the Trust State's law, to contain property legally situate in the Trust State, and to be administered by a Trust State trustee, then it seems probable that the testator or trustor intended that the Trust State have the most significant relationship with the trust. Moreover, these factors also show that both the testator or trustor and the trustee have an expectation that the law will govern.

Considerations of certainty, predictability, and uniformity also point to finding the Trust State's relationship more significant than the Home State. Although Home State courts may only occasionally deal with the Trust State's law in question, Trust State trustees and their many testators, trustors, and beneficiaries have a constant need to know which body of law governs their rights and duties. The knowledge that

trusts are governed by Trust State law will facilitate stability, predictability, and uniformity in connection with trust planning and administration. In contrast, an ad hoc, result-oriented approach will create much uncertainty, unpredictability, and inconsistency. Such chaos simply is not good for interstate commerce and transactions. As noted by a Massachusetts court: [442]

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[442] *Rudow v. Fogel*, 426 N.E.2d 155, 160 (Mass. Ct. App. 1981).

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[T]he interests of our interstate system... are furthered by applying a single law in determining whether a given situation creates a fiduciary relationship. It is desirable that the same law apply to all property involved in the same transaction wherever situated.

### c. Comment

In sum, then, it will be very hard to deny that the Trust State is the state with the most significant relationship to a trust, even if the Home State has a strong public policy regarding the matter at issue.

### d. Rights of Creditors

Article 5 of the UTC [443] covers the ability of creditors to reach the assets of third-party and self-settled trusts, and UTC § 105(b)(5) [444] prohibits a governing instrument from departing from that rule. Therefore, residents of states that have enacted the foregoing provisions may not create trusts with different terms under those states' laws. Nevertheless, trustors may explore creating domestic asset-protection trusts or third-party trusts containing more protective provisions in other states because the UTC does not offer choice-of-law rules for these issues.

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[443] UTC § 501–§ 507 (amended 2018).

[444] UTC § 105(b)(5) (amended 2018).

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## 4. Rules in Federal Court

The conflict of laws analysis essentially is the same if a controversy ends up in federal district court due to diversity of citizenship. The U.S. Supreme Court laid down the governing principles in *Klaxon Co. v. Stentor Electric Manufacturing Co.* as follows: [445]

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[445] *Klaxon Co. v. Stentor Elec. Mfg. Co.*, 313 U.S. 487, 496–97 (1941). *See* 2002 *Lawrence R. Buchalter Alaska Tr. v. Phila. Fin. Life Assurance Co.*, 96 F. Supp. 3d 182, 199 (S.D.N.Y. 2015); *Wells Fargo Bank, N.A. v. Barber*, 85 F. Supp. 3d 1308, 1316 (M.D. Fla. 2015); *State Farm Mut. Auto. Ins. Co. v. Snyder*, 2013 WL 5948089, at *2 (E.D. Pa. Nov. 6, 2013); *Campbell v. Fawber*, 975 F. Supp. 2d 485, 504 (M.D. Pa. 2013); *Broaddus v. Shields*, 2012 WL 28694, at *5 (N.D. Ill. Jan. 5, 2012).

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The conflict of laws rules to be applied by the federal court in Delaware must conform to those prevailing in Delaware's state courts. Otherwise, the accident of diversity of citizenship would constantly disturb

equal administration of justice in coordinate state and federal courts sitting side by side. Any other ruling would do violence to the principle of uniformity within a state, upon which the *Tompkins* decision is based. Whatever lack of uniformity this may produce between federal courts in different states is attributable to our federal system, which leaves to a state, within the limits permitted by the Constitution, the right to pursue local policies diverging from those of its neighbors. It is not for the federal courts to thwart such local policies by enforcing an independent general law of conflict of laws. Subject only to review by this Court on any federal question that may arise, Delaware is free to determine whether a given matter is to be governed by the law of the forum or some other law. This Court's views are not the decisive factor in determining the applicable conflicts rule. And the proper function of the Delaware federal court is to ascertain what the state law is, not what it ought to be.

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Portfolio 867-2nd: Choosing a Domestic Jurisdiction for a Long-Term Trust
Detailed Analysis
IV. Beneficiaries' Ability to Defeat Clients' Selection of Trust States

## E. Obstacle 4: Trust State Court Might Not Have to Give Full Faith and Credit to Judgment of Home State Court

Under the United States Constitution, "Full Faith and Credit shall be given in each State to the public Acts, Records, and judicial Proceedings of every other State." [446]

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[446] U.S. Const. art. IV, § 1. *See* 28 U.S.C. § 1738.

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### 1. Respect Due Statutes

The Full Faith and Credit Clause applies to statutes and to judgments of another state, but it does not operate in the same manner with respect to them. The U.S. Supreme Court examined the Full Faith and Credit Clause's application to state statutes in *Franchise Tax Board v. Hyatt*, [447] in which the Court unanimously held that the Nevada Supreme Court's refusal to extend full faith and credit to California's statute immunizing its tax-collection agency from suit did not violate the Full Faith and Credit Clause. In contrasting the application of the Full Faith and Credit Clause to statutes and to judgments, the Court stated: [448]

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[447] 538 U.S. 488 (2003). *See* Hamilton, *The Long, Strange Trip of Franchise Tax Board v. Hyatt*, 389 State Tax Notes 343 (Jul. 23, 2018).

[448] *Hyatt*, 538 U.S. at 494 (citations and internal quotation marks omitted).

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[O]ur precedent differentiates the credit owed to laws (legislative measures and common law) and to judgments. Whereas the full faith and credit command is exacting with respect to a final judgment ... rendered by a court with adjudicatory authority over the subject matter and persons governed by the judgment, it is less demanding with respect to choice of laws. We have held that the Full Faith and Credit Clause does not compel a state to substitute the statutes of other states for its own statutes dealing with a subject matter concerning which it is competent to legislate.

Although the Full Faith and Credit Clause does not compel a court in one state to adopt a statute of another state, a court may not simply ignore a sister state's law and apply its own, and it must satisfy two criteria before its statute may constitutionally displace another state's statute. First, as noted above, a state must be "competent to legislate" regarding the subject matter in question. This criterion is usually easy to satisfy in the absence of some form of preemption or constitutional prohibition. Second, full faith and credit and due process require "that for a State's substantive law to be selected in a constitutionally permissible manner, that State must have a significant contact or significant aggregation of contacts, creating state interests, such that choice of its law is neither arbitrary nor fundamentally unfair." [449]It's

often a close question whether, and to what extent, a state court may apply its own law to the exclusion of another state's law that is arguably more applicable, and, as a constitutional matter, states will be given significant leeway in developing local conflict-of-laws rules that satisfy the broad constitutional mandates. [450] Nonetheless, one state cannot disregard another state's statutes when the other state had sufficiently significant contacts to the issues being litigated and the first state's interest was weak. [451]

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[449] *Allstate Ins. Co. v. Hague*, 449 U.S. 302, 313 (1981). *Accord Hyatt*, 538 U.S. at 494.

[450] *See, e.g.*, *Hague*, 449 U.S. 302.

[451] *See, e.g.*, *Phillips Petroleum Co. v. Shutts*, 472 U.S. 797 (1985) (Kansas not allowed to apply its statutes to oil and gas lease controversies involving properties located in Texas, Oklahoma, and elsewhere).

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## 2. Implications

Although a Home State court often will have constitutional discretion to apply or ignore a Trust State's statutes, the facts of some cases will strongly suggest (or perhaps require, as in *Phillips Petroleum Co. v. Shutts* [452]) the application of the Trust State's law rather than the Home State's law. On the one hand, a forum court in a defendant's Home State may have a strong argument for applying forum law because of the defendant's residence and because the plaintiff, whatever his or her residence, chose the forum. On the other hand, the argument for applying forum law is weaker when a defendant's contact with the forum is limited and the defendant's conduct took place outside the forum state. This observation has a potentially significant impact for out-of-state trustees with limited and minimal ties to the Home State. Even if the United States Constitution doesn't mandate adherence to a Trust State's statute, someone arguing against application of Trust State law must still satisfy the choice-of-law rules that will often weigh in the Trust State's favor, as outlined above.

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[452] 472 U.S. 797 (1985).

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## 3. Respect Due Judgments

As noted above, the U.S. Supreme Court declared in *Franchise Tax Board v. Hyatt* that: [453]

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[453] *Hyatt*, 538 U.S. at 494. *See Matter of Vale*, 2015 WL 721038, at *3 (Del. Ch. Feb 19, 2015).

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[T]he full faith and credit command ‘is exacting’ with respect to a final judgment ... rendered by a court with adjudicatory authority over the subject matter and persons covered by the judgment.

However, this “exacting” requirement has its limits. To begin, Trust State courts may disregard judgments entered against trustees by Home State courts if the judgment did not satisfy the requirements of due process. [454] Hence, any failure to join a trustee in an action regarding a trust, or any defect in service of process on or jurisdiction over a trustee, can open a Home State court's judgment to collateral attack.

[454] *Hanson*, 357 U.S. 235, 255–56 (1958). *See also Nastro v. D'Onofrio*, 822 A.2d 286, 292–94 (Conn. App. Ct. 2003); *Toledo Tr. Co. v. Nat'l Bank of Detroit*, 362 N.E.2d 273, 280 (Ohio Ct. App. 1976).

Further, a Trust State court might not have to give full faith and credit to a judgment rendered by a Home State court. In this regard, § 103 of the *Restatement* states: [455]

[455] *Restatement* § 103. *Accord Bartlett v. Dumaine*, 523 A.2d 1 (N.H. 1986).

A judgment rendered in one State of the United States need not be recognized or enforced in a sister State if such recognition or enforcement is not required by the national policy of full faith and credit because it would involve an improper interference with important interests of the sister State.

Section 103's comments emphasize that it has an extremely narrow scope of application [456] and would probably include such things as one state refusing to respect a judgment from another state that "purport[s] to accomplish an official act within the exclusive province of that other State or interfere[s] with litigation over which the ordering State had no authority." [457] Nevertheless, authorities indicate that § 103 might apply if a Trust State court is asked to give full faith and credit to a judgment rendered by a Home State court.

[456] *Restatement* § 103 cmts. a–b.

[457] *Baker v. Gen. Motors Corp.*, 522 U.S. 222, 235 (1998).

The Scott treatise frames the issue as follows: [458]

[458] 7 *Scott and Ascher on Trusts* § 45.2.2.6 at 3126.

In some situations, however, the court that has primary supervision over the administration of the trust may regard the judgment as an undue interference with its power to control trust administration. It may take the position that the court rendering the judgment applied its own local law, though it should have applied the law of the state of primary supervision, or that it incorrectly applied the law of the state of primary supervision. The question then is whether the court of primary supervision is bound to give full faith and credit to the judgment. The final determination of this question rests, of course, with the Supreme Court of the United States.

As noted above, *Hanson v. Denckla* held that Delaware did not have to give full faith and credit to a judgment of a Florida court that lacked jurisdiction over the trustee and the trust property. The Scott treatise states that: [459]

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[459] 7 *Scott and Ascher on Trusts* § 45.2.2.6 at 3128.

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It seems clear that the Florida court, in applying its own local law and holding that the Delaware trust and the exercise of the power of appointment were invalid, unduly interfered with the administration of the trust by the Delaware courts.

It describes the implications of the above observation as follows: [460]

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[460] 7 *Scott and Ascher on Trusts* § 45.2.2.6 at 3128–29 (footnotes omitted).

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Since the Delaware court could properly regard the judgment of the Florida court as unduly interfering with the administration of a trust that was fixed in Delaware, it was not bound by that judgment, notwithstanding the fact that the Florida court had jurisdiction over some or all of the beneficiaries. Indeed, it may well be argued that the Delaware court would not be bound by the Florida judgment even if the Florida court had jurisdiction over the trustee as well. A court might acquire jurisdiction over an individual trustee who happens to be in the state or over a corporate trustee that happens to have such a connection with the state as to give the state jurisdiction over it, or the trustee may appear in the action. We submit, however, that such a judgment would unduly interfere with supervision of the administration of the trust. It might, indeed, be held that not only would the Delaware courts not be bound to give full faith and credit to the Florida judgment, but that the Florida judgment would so interfere with the administration of the trust that it would be invalid as a denial of due process of law.

The Scott treatise suggests that the same principle should apply in other contexts: [461]

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[461] 7 *Scott and Ascher on Trusts* § 45.2.2.6 at 3129.

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In *Hanson v. Denckla*, the issue was the validity of the disposition of the trust property. A similar question may arise as to the effect of a judgment rendered by a court, other than that which has primary supervision, instructing the trustee as to the trustee's powers and duties or authorizing or directing the trustee to deviate from the terms of the trust. These matters are ordinarily for determination by the court that has primary supervision over the administration of the trust. Certainly in most cases the courts of other states would decline to exercise jurisdiction, though they happened to have jurisdiction over the trustee or some or all of the beneficiaries. If, however, such a court exercises jurisdiction, the Supreme Court might well hold that the court of primary supervision is not bound to give full faith and credit to the judgment. Indeed, it might hold that the judgment is invalid, even in the state in which it was rendered, on the ground that it unduly interferes with the administration of the trust and thus constitutes a denial of due process of law.

In the related case of *Lewis v. Hanson*, [462] the Delaware Supreme Court unequivocally stated that Delaware courts would not have been required to give full faith and credit to the Florida judgment even if the Florida courts had jurisdiction over the trustee and/or the trust property. The court declared: [463]

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[462] 128 A.2d 819 (Del. 1957) (citation omitted).

[463] *Id.* at 835.

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[W]e think the public policy of Delaware precludes its courts from giving any effect at all to the Florida judgment of invalidity of the 1935 trust. We are dealing with a Delaware trust. The trust *res* and trustee are located in Delaware. The entire administration of the trust has been in Delaware. The attack on the validity of this trust raises a question of first impression in Delaware and one of great importance in our law of trusts. To give effect to the Florida judgment would be to permit a sister state to subject a Delaware trust and a Delaware trustee to a rule of law diametrically opposed to the Delaware law. It is our duty to apply Delaware law to controversies involving property located in Delaware, and not to relinquish that duty to the courts of a state having at best only a shadowy pretense of jurisdiction.

The Supreme Court of New Hampshire applied the above principles in the 1986 case of *Bartlett v. Dumaine*. [464] There, the beneficiaries of a New Hampshire trust (the Dumaine Trust) and a Massachusetts trust (the Dexter Trust) brought claims against the trustees of the two trusts. After affirming findings that the claims against the trustees of the New Hampshire trust were meritless, [465]the court, citing § 103 of the *Restatement* and pertinent sections of a prior edition of the Scott treatise, dismissed the request for an accounting for the Massachusetts trust, even though it had personal jurisdiction over all interested parties. The court reasoned as follows: [466]

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[464] 523 A.2d 1 (N.H. 1986).

[465] *Id.* at 14.

[466] *Id.* at 14–15 (citations omitted).

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In determining whether the superior court should have exercised or declined to exercise its jurisdiction in this case, we consider the relationships which New Hampshire and Massachusetts have with the Dexter Trust. New Hampshire's interest in the proper administration of Dexter is substantial because Dumaines, a New Hampshire trust, has the vested remainder interest in Dexter. Nevertheless, we cannot help but conclude that Massachusetts' interest in the administration of Dexter is greater. Both the petitioners and the respondents acknowledge that Dexter is a Massachusetts trust which is administered in Massachusetts, and which is governed by the trust law of that commonwealth. The question we are asked to decide is whether the Dexter trustees need only account to the Dumaines' trustees under the Massachusetts general rule that in matters involving the trust and the outside world the trustees represent the beneficiaries, or whether the Dexter trustees must account directly to the Dumaines' beneficiaries under exceptions to the general rule which govern when certain conflicts of interest exist. It is our conclusion that the Massachusetts courts, and not those of New Hampshire, are the courts of "primary supervision" over the Dexter Trust and the satellite trusts, and that this question should be left to a Massachusetts court to decide.

Both New Hampshire and Massachusetts jealously seek to preserve jurisdiction over their own trusts. Both States also willingly decline jurisdiction over another State's trust. Both practices are sound. Although there is a strong policy favoring an end to litigation, there is an equally strong policy favoring the orderly administration of trusts.

The court concluded its discussion of this issue as follows: [467]

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[467] *Id.* at 15 (citations and internal quotation marks omitted).

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A final consideration stays our hand from divining the law of Massachusetts in this area; namely, what effect that Commonwealth is likely to give any judgment we might render. A judgment rendered in one State of the United States need not be recognized or enforced in a sister State if such recognition or enforcement is not required by the national policy of full faith and credit because it would involve an improper interference with important interests of the sister State. There is ample evidence that the Massachusetts Supreme Judicial Court would consider a decision by this court regarding the Dexter trustees' duty to account as improper interference with the Commonwealth's important interests.

Estates, Gifts and Trusts Portfolios
Trusts
Portfolio 867-2nd: Choosing a Domestic Jurisdiction for a Long-Term Trust
Detailed Analysis
V. Factors to Consider in Selecting a Trust State

## A. Introduction

Some attorneys do not look beyond the states where they are admitted to practice when they advise clients regarding the creation of trusts. But, as shown in I.E., above, other attorneys actively work with clients to find advantageous Trust States.

This section summarizes factors that attorneys and clients should consider in choosing Trust States. [468]

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[468] *See* Redd, *Choice of Law*, 156 Tr. & Est. 11,11) (Nov. 2017). This Portfolio does not cover the Private Trust Company ("PTC"), an option that is considered by many wealthy families. *See* Grayson, Brynn & Petrovic, *Avoid Private Trust Company Pitfalls*, 157 Tr. & Est. 27 (Nov. 2018). For a primer on the PTC, see Weeg, *The Private Trust Company: A DIY for the Über Wealthy*, 52 Real Prop., Tr. & Est. L.J. 121 (Spring 2017).

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Estates, Gifts and Trusts Portfolios
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## B. Favorable Trust Climate

When an attorney is developing an estate plan with a client that involves the use of trusts, the attorney should help the client to find a Trust State where the client's trusts will be more likely to accomplish what the client wants them to achieve. Such a Trust State should have a well-thought-out body of trust statutes; an ongoing commitment to update those statutes to respond to changing federal tax laws, financial conditions, and other circumstances; a competent judiciary; a supportive legislature, executive branch, and legal and banking community; and numerous financial institutions that compete for trust business. Delaware developed such a system early in the 20th century; [469] South Dakota did so starting in about 1983. [470] Since 1997, several other states, Alaska (1997), [471] Nevada (1999), [472] and New Hampshire (2004), [473] in particular, have taken steps to attract trust business.

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[469] *See* Nenno, *Delaware Trusts 2017* (Wilm. Tr. Co. 2017); Schanzenbach, *Evaluating the Impact of Trust Business on Delaware's Economy* (May 25, 2011), http://www.leimbergservices.com/docs/report-5-25-11b.pdf; Sitkoff & Schanzenbach, *Perpetuities, Taxes, and Asset Protection: An Empirical Assessment of the Jurisdictional Competition for Trust Funds*, 42 U. Miami Inst. on Est. Plan. ¶ 1407.1 at 14-19, ¶ 1407.2 at 14-19–14-20, ¶ 1407.5 at 14-22–14-23 (2008);

[470] *See* Goetzinger, *A Dynamic Duo: South Dakota's Trust Laws & Business Entity Statutes*, 61 S.D. L. Rev. 339 (2016). Sitkoff & Schanzenbach, *Perpetuities, Taxes, and Asset Protection: An Empirical Assessment of the Jurisdictional Competition for Trust Funds*, 42 U. Miami Inst. on Est. Plan. ¶ 1407.3 at 14-20–14-21.

[471] *See* Blattmachr, Chapman, Gans & Shaftel, *New Alaska Law Will Enhance Nationwide Estate Planning — Part 2*, 40 Est. Plan. 20 (Oct. 2013); Blattmachr, Chapman, Gans & Shaftel, *New Alaska Law Will Enhance Nationwide Estate Planning — Part 1*, 40 Est. Plan. 3 (Oct. 2013); Lee, *Alaska on the Asset Protection Trust Map: Not Far Enough for a Regulatory Advantage, But Too Far For Convenience?,* 29 Alaska L. Rev. 149 (June 2012).

[472] *See* www.mcdonaldcarano.com.

[473] *See* Burke, Brassard, Sanborn & Shields, *Why the Granite State Rocks at Trust Administration*, 43 Est. Plan. 3 (June 2016).

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While it might not be possible to house a trust in a state that will meet all of a client's goals, this section and the Worksheets will help attorneys to find the most appropriate Trust State for each client given all pertinent circumstances.

## C. Client Objectives

### 1. Introduction

Some clients want their trusts to promote definite objectives (e.g., to prevent a concentrated block of publicly traded stock from being diversified, to prevent stock in a closely held company from being sold except in specified circumstances, or to prevent a beneficiary from being provided with details about trusts until reaching a "responsible" age). Not only do such clients want to see language in the trust instrument that is in keeping with their wishes, but they also want assurance that the provisions in question will be respected. The testator's or trustor's intent might be frustrated either by inadequate trust design or by overly-liberal rules for trust modification. Two prime examples, which involve very large South Dakota trusts, of how intent can be defeated are described in 2., below. In both instances, the trustor was deceased and South Dakota law might not provide the trustor's representatives with the tools to set things right.

### 2. Proper Trust Design Is Key

#### a. McDevitt v. Wellin (2016)

The first case involving a South Dakota trust is the ongoing litigation involving the *Wellin Family 2009 Irrevocable Trust*, which the trustor, Keith Wellin, intended to be a South Dakota dynasty trust. In January of 2016, the United States District Court for the District of South Carolina summarized the sad saga as follows: [474]

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[474] *McDevitt v. Wellin*, 2016 WL 199626, at *1–2 (D.S.C. Dec. 15, 2016) (citations omitted).

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On November 2, 2009, Keith Wellin ("Keith") created the *Wellin Family 2009 Irrevocable Trust* (the "Trust") for the benefit of his children and grandchildren. In late 2013, defendants Peter J. Wellin, Cynthia W. Plum, and Marjorie W. King (the "Wellin children"), acting as co-trustees, liquidated and distributed over $95.6 million of the Trust's estimated $154 million in assets to themselves. On December 17, 2013, then-plaintiff Schwartz, acting as trust protector, initiated the present action, claiming that the Wellin children's liquidation of the Trust assets was both tortious and in violation of the Trust. The action also sought to remove the Wellin children from their positions as co-trustees. Notably, at the time Schwartz was hired by Keith as trust protector, and at all times since, Keith has pursued a separate action — *Wellin v. Wellin et. al.*, — seeking to declare the Trust void ab initio. Recognizing this conflict, Keith released any claims he may have against Schwartz for reimbursement of Schwartz's fees and attorney fees in the event Keith's separate action is successful.

In May 2014, after the court found that Schwartz did not qualify as a real party in interest and dismissed the action, Schwartz exercised his powers under the Trust and appointed Larry S. McDevitt ("McDevitt") as an additional trustee. McDevitt quickly ratified the commencement of the action. On October 10, 2014, McDevitt filed a new complaint seeking actual and punitive damages from the Wellin children and

asserting a cause of action for the recovery of attorney's fees. The Wellin children counterclaimed that Schwartz was not properly appointed trust protector because Keith lacked capacity at the time of his appointment, and that Schwarz was "subordinate" to Keith in violation of the Trust requirements. The Wellin children also sought to have the trust plaintiffs removed from their fiduciary positions based on various actions taken in bad faith and against the best interests of the Trust.

The Wellin children are currently holding the distributed Trust assets in certain UBS accounts, and have used millions of dollars in Trust assets to pay their own attorneys, experts, and consultants in this litigation. The trust plaintiffs and their attorneys have not been paid or reimbursed by the Trust. However, the trust plaintiffs and their attorneys are being paid, pursuant to letter agreements between Keith and the trust plaintiffs, which provide that Keith will pay the trust plaintiffs' fees and expenses, and their attorneys' fees. The letter agreements further state that these advances must only be repaid to the extent the trust plaintiffs are able to recover such fees from the Trust assets or the Wellin children.

Hence, the salient facts of this case are as follows:
• The trustor created an enormous dynasty trust for his children and their issue in 2009.

• Four years later, the children, as co-trustees, liquidated the trust assets and distributed the bulk of the proceeds to themselves.

• The trustor spent the last few years of his life suing his children to restore or revoke the trust.

• The children are paying their litigation costs from the proceeds of the trust assets; the trustor and his widow are bearing the litigation costs of the protector and the trustee appointed by the protector.

• The South Dakota corporate co-trustee apparently made no attempt to intervene.

## b. Marvin M. Schwan Charitable Foundation v. Burgdorf (2016)

The second South Dakota case is the ongoing litigation involving the Marvin M. Schwan Charitable Foundation. There, the trustor, Marvin M. Schwan, created the foregoing trust in 1992 for seven named charitable institutions and died the following year. [475] After the trustor's death, the trust was funded with nearly $1 billion but, "[t]he parties do not dispute that certain investments made by the Trustees over several years caused approximately $600 million in losses to the Foundation." [476] At all relevant times, the trust had five individual trustees and a Trust Succession Committee, which consisted of seven members, two of whom are sons of the trustor. [477]

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[475] *Marvin M. Schwan Charitable Found. v. Burgdorf*, 880 N.W.2d 88, 89–90 (S.D. 2016).

[476] *Id.* at 90.

[477] *Id.*

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In June of 2014, the trustor's sons, as members of the Trust Succession Committee, petitioned a circuit court for court supervision of the trust pursuant to South Dakota Codified Laws § 21-22-9. [478] Thereafter, the trustees, the beneficiaries, and the South Dakota Attorney General entered into a settlement agreement and disingenuously asked the court to dismiss the petition, inter alia, because court supervision, "would needlessly waste additional assets." [479] The court subsequently dismissed the petition for lack of standing, finding that the petitioners were neither fiduciaries nor beneficiaries for purposes of

the statute. [480] The Supreme Court of South Dakota reversed because it found that the petitioners in fact were "beneficiaries" within the meaning of the statute. [481]

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[478] *Id.* at 91.

[479] *Id.*

[480] *Id.* at 92.

[481] *Id.* at 95.

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All of this means that, in a case in which the trustees admitted to $600 million of investment losses, the trustor's representatives had to go all the way to the Supreme Court of South Dakota even to be allowed to petition for court supervision, which petition might very well be denied.

### c. In re Trust Under Will of Flint (2015)

In 2015, the Court of Chancery of Delaware had to balance testator intent against a request for change in *In re Trust of Flint*. [482] At the outset, the court said: [483]

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[482] 118 A.3d 182 (Del. Ch. 2015).

[483] *Id.* at 183.

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The current income beneficiary of a testamentary trust petitioned for an order that would modify the trust's terms by rewriting its administrative provisions, thereby converting the trust from the traditional trustee-managed structure that the settlor contemplated into a directed trust where the trustee would serve only an administrative role. . . .The petition is denied.

The trust was established under the 1934 Will of a New York individual who died in 1938. At the time of the petition, over 80% of the trust's assets consisted of IBM stock. The corporate trustee wanted to diversify, but the individual co-trustee/current beneficiary and her descendants resisted. Conversion to a directed trust seemed to be the solution.

The court discussed the significance of intent in trust law generally as well as in Delaware trust law specifically: [484]

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[484] *Id.* at 193–194 (footnote and citations omitted).

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Whether the wishes of living beneficiaries should prevail over the wishes of a dead settlor is a contestable issue where reasonable minds can disagree. Different jurisdictions have reached different results. English law has long made the wishes of the beneficiaries paramount. By contrast, under the *Claflin* doctrine, the majority rule in the United States has long prioritized the settlor's intent. Recent statutory initiatives,

including the Uniform Trust Code, have eroded the *Claflin* doctrine and moved towards prioritizing the wishes of beneficiaries.

In Delaware, the settlor's intent controls. Our Supreme Court has stated repeatedly that "[t]he cardinal rule of law in a trust case is that the intent of the settlor controls." Our Trust Code makes it the policy of the State of Delaware "to give maximum effect to the principle of freedom of disposition and to the enforceability of governing instruments." It would undercut this policy, and might well be described as duplicitous, for our State to represent to a settlor that our law will respect his dispositions and enforce his governing instrument, only to enable his beneficiaries to rewrite that instrument after his death.

### d. Vito v. Grueff (2017)

The trustor's intent, as interpreted by the court, has prevailed so far in *Vito v. Grueff,* [485] in which the trust instrument allowed the trust to be amended by a vote of 75% of the beneficiaries. Pursuant to that provision, three of the trustor's four children sought to modify the trust to exclude the fourth child. The court held: [486]

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[485] 160 A.3d 592 (Md. Ct. App. 2017).

[486] *Id.* at 614.

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[W]e hold that Item Tenth of the irrevocable trust does not authorize 75% of the beneficiaries to remove the remaining beneficiary. Our holding is grounded in the well-established principle that the settlor's intent controls the disposition of the trust property.

### e. In re Trust Under Agreement of Taylor (2017)

The trustor's intent prevailed again in *In re Trust Under Agreement of Taylor*, [487] in which the beneficiaries attempted to add a provision to an irrevocable trust to give themselves the power to replace the corporate trustee. Reversing the Superior Court, [488] the Supreme Court of Pennsylvania held: [489]

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[487] 164 A.3d 1147 (Pa. 2017). *See* LaPiana, *Modification Cannot Be Used to Remove a Trustee*, 44 Est. Plan. 43 (Nov. 2017).

[488] *In re Trust Under Agreement of Taylor*, 124 A.3d 334, 342 (Pa. Sup. Ct. 2015).

[489] *Taylor*, 164 A.3d at 1161 (internal quotation marks omitted).

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For these reasons, we conclude that the scope of section 7740.1 of the UTA does not extend to modification of trust agreements to permit the removal and replacement of trustees. Instead, as the UTC comment to section 7740.1 reflects, section 7766 of the UTA is the exclusive provision regarding removal of trustees.

## 3. Permitted Provisions

The UTC [490] contains a variety of optional provisions, [491] as well as 14 mandatory provisions from which a

testator or trustor who creates a trust in that state is forbidden to depart. [492] The drafting attorney may not opt out of, or draft around, these mandatory provisions.

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[490] UTC (amended 2018). The text of the UTC and a list of the jurisdictions that have adopted it are available at, www.uniformlaws.org/LegislativeFactSheet.aspx?title=Trusthttps://my.uniformlaws.org/committees/community-home?communitykey=193ff839-7955-4846-8f3c-ce74ac23938d& tab=groupdetails. Worksheet 3 gives citations for the statutes of the states that have enacted the UTC.

[491] UTC § 105(a) (amended 2018). For a detailed discussion of the UTC, see 864 T.M., *Uniform Trust Code.*

[492] UTC § 105(b) (amended 2018).

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For example, the UTC specifies instances in which creditors may reach the assets of a third-party spendthrift trust [493] or a discretionary trust, [494] prohibits a client from creating an effective asset-protection trust ("APT"), [495] and forbids resident testators and trustors to adopt different terms. [496]

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[493] UTC § 503 (amended 2018).

[494] UTC § 504 (amended 2018).

[495] UTC § 505(a)(2) (amended 2018).

[496] UTC § 105(b)(5) (amended 2018).

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Similarly, the UTC requires a trustee to furnish a beneficiary with certain information by age 25 [497] and suggests that a client not be able to override that requirement. [498]

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[497] UTC § 813(b), § 105(b)(8) (amended 2018). *See* Redd, *Answering to Beneficiaries*, 156 Tr. & Est. 13 (Sept. 2017); McEwan, *The UTC and the Duty to Inform and Report,* 156 Tr. & Est. 33 (Apr. 20, 2017); Newman, *Trust Law in the Twenty-First Century: Challenges to Fiduciary Accountability*, 29 Quinnipiac Prob. L.J. 261, 269–270 (2016); Treu, *The Mandatory Disclosure Provisions of the Uniform Trust Code: Still Boldly Going Where No Jurisdiction Will Follow – A Practical Tax-Based Solution*, 82 Miss. L.J. 597 (2013).

[498] UTC § 105(b)(8) (amended 2018). *See* Fitzsimons, *UTC Reporting Requirements: Default vs. Mandatory by Enacting Jurisdiction & State Law Variations* (As of Feb. 2016), www.actec.org/assets/1/6/Fitzsimons-UTC-Reporting-Requirements-Default-vs-Mandatory-by-Enacting-Jurisdiction-and-State-Law-Variation.pdf.

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Courts in two UTC states — North Carolina and Ohio — have held that specific language in a governing instrument does not override the statutory duty to disclose. [499] An intermediate appellate court in Maryland (which since has enacted its version of the UTC) came to a similar result. [500] However, an

intermediate appellate court in Ohio held that the trustor was not entitled to receive financial accountings for two trusts that he had created [501] and an intermediate appellate court in a non-UTC state — Indiana — denied a request for further information by a recipient of a specific distribution who had received a certification of trust from the trustee. [502] Finally, the Supreme Court of Nebraska held that providing schedule K-1s did not satisfy disclosure requirements under pre-UTC and post-UTC Nebraska law, [503] and that a trustee had violated his pre-UTC and post-UTC Nebraska law duties to report. [504]

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[499] *Zimmerman v. Zirpolo Tr.*, 2012-Ohio-346, at *7 (App. 5th Dist2012) ("Once the requirements of RC 5808.13 were satisfied, the Trustee had a duty to provide the requested documents to the beneficiaries"); *Wilson v. Wilson*, 690 S.E.2d 710, 716 (N.C. Ct. App. 2010) ("The information sought by plaintiffs was reasonably necessary to enforce their rights under the trust, and therefore could not legally be withheld, notwithstanding the terms of the trust instrument").

[500] *Johnson v. Johnson*, 967 A.2d 274, 283 (Md. Ct. Spec. App. 2009), judgment *vacated* on procedural grounds, 32 A.3d 1072 (Md. 2011) ("despite the language in the Trust attempting to eliminate Catherine's duty to account, James is entitled to request an accounting and Catherine is required to provide it").

[501] *Millstein v. Millstein*, 2018-Ohio-2295, 2018 WL 1567801, at *5 (Ohio Ct. App Mar. 29, 2018) ("the trial court did not err when it granted summary judgment to Kevan").

[502] *Schrage v. Seberger Living Tr.*, 52 N.E.3d 45, 54 (Ind. Ct. App. 2016) ("Based on that interest alone, she is entitled to nothing further from the Trustee").

[503] *Abbot v. Brenneman (In re Brenneman Testamentary Tr.)*, 849 N.W.2d 458, 468 (Neb. 2014).

[504] *In re Estate of Forgey*, 906 N.W.2d 618, 632 (Neb. 2018) ("Lyle clearly violated the requirement, prior to 2005, to keep the beneficiaries of the trust reasonably informed; and after 2005, he violated his duty to send to distributees a report at least annually").

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Regarding the disclosure of information to beneficiaries, a 2005 article notes that: [505]

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[505] Covey & Hastings, *Notice, Disclosure and Trustee Reporting Requirements Under Various State Laws and Trust Codes*, Prac. Drafting App. B 8001 (Jan. 2005).

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[S]tates with statutes regarding the responsibility of a trustee to provide information and reports to a beneficiary vary considerably and are often unclear concerning the ability of the creator to negate the statutory requirements. The Delaware statute provides the creator with the greatest flexibility.

A 2011 article reiterates the flexibility that Delaware offers in this area: [506]

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[506] Bieber, *Trustee's Duties Extend to Remainder Beneficiaries Too*, 38 Est. Plan. 23, 30 (Nov. 2011) (footnote omitted). *See* Mann & Zhao, *Can You Keep a Secret? Working With Silent Trusts*, 43 Tax Mgmt. Est., Gifts & Tr. J. 311 (Nov. 8, 2018); Soled, et al., *Quiet Trusts: When Mum's the Word to Trust Beneficiaries*, 40 Est. Plan. 13 (July 2013); Burford, *Pacifying a Silent Trust*, 151 Tr. & Est. 14 (Nov. 2012).

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At least one state [Delaware] now has a statute that specifically does allow a settlor to keep trust information wholly confidential. . .Despite the Delaware statute, the trend, as shown in Restatement (Third) of Trusts and the Uniform Trust Code, is towards more disclosure, not less. Maybe Delaware will lead the way in this area; perhaps it will become a competitive area among states, as was eliminating the rule against perpetuities.

The Delaware statute referred to above now provides that: [507]

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[507] Del. Code Ann. tit. 12, § 3303(a). Absent specific language to the contrary in the governing instrument, a trustee must provide current beneficiaries with relevant information about trusts (*McNeil v. McNeil*, 798 A.2d 503 (Del. 2002)).

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(a) Notwithstanding any other provision of this Code or other law, the terms of a governing instrument may expand, restrict, eliminate or otherwise vary any laws of general application to fiduciaries, trusts and trust administration, including, but not limited to, any such laws pertaining to:

(1) The rights and interests of beneficiaries, including, but not limited to, the right to be informed of the beneficiary's interest for a period of time, as set forth in subsection (c) of this section;

(2) The grounds for removal of a fiduciary;

(3) The circumstances, if any, in which the fiduciary must diversify investments;

(4) The manner in which a fiduciary should invest assets, including whether to engage in one or more sustainable or socially responsible investment strategies, in addition to, or in place of, other investment strategies, with or without regard to investment performance; and

(5) A fiduciary's powers, duties, standard of care, rights of indemnification and liability to persons whose interests arise from that instrument; provided, however, that nothing contained in this section shall be construed to permit the exculpation or indemnification of a fiduciary for the fiduciary's own willful [sic] misconduct or preclude a court of competent jurisdiction from removing a fiduciary on account of the fiduciary's wilful misconduct. The rule that statutes in derogation of the common law are to be strictly construed shall have no application to this section. It is the policy of this section to give maximum effect to the principle of freedom of disposition and to the enforceability of governing instruments.

Accordingly, if Delaware law governs a trust, the terms of the trust instrument will be carried out regardless of other statutes or laws. Delaware law now illustrates the periods of time for which the dissemination of information may be deferred and allows designated representatives to receive information during such periods. [508] Given that a trustee's duty to keep beneficiaries informed is a matter of trust administration if the trust holds personal property, [509] the trust instrument's designation of the Delaware law or the law of a state having comparable legislation (e.g., Nevada, Ohio, or South Dakota [510]) on this issue should be respected for such a trust.

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[508] Del. Code Ann. tit. 12, § 3303(c)–§ 3303(e), § 3339.

[509] *Restatement* § 271 cmt. a.

[510] *See e.g.*, Nev. Rev. Stat. § 163.004(1); Ohio Rev. Code § 5801.04(C); S.D. Codified Laws § 55-2-13.

Notice to beneficiaries is one of the aspects of the UTC that can be most troubling to clients who wish to protect their children from full knowledge of their wealth. Thus, clients may wish to consider moving a trust to a state that allows disclosure to beneficiaries to be restricted or changing the law that governs the administration of the trust.

In any event, testators and trustors who want to accomplish specific goals that might be frustrated in their Home States should consider creating trusts in Trust States where their wishes will be honored. In this regard, a 2010 article counsels that: [511]

[511] Berry, English & Fitzsimons, Jr., *Disclose. Disclose! Disclose? Longmeyer Distorts the Trustee's Duty to Inform Trust Beneficiaries*, 24 Prob. & Prop. 12, 16 (July/Aug. 2010).

[I]f the client resides in a state with undesirable law, the instrument could include a choice of law provision adopting "better" law in line with the client's wishes. Such a provision is most likely to be effective if the trustee is located in the state with the desirable law so that the choice of law clause has a relationship to the trust and the validity of the provision would likely have to be litigated in that state.

## 4. Modification or Termination of a Trust

### a. Introduction

It may be well and good for a testator or trustor to set specific requirements in a Will or trust, but the attorney must be mindful of ways in which the trustee or beneficiaries might undo those provisions or terminate the trust altogether after the testator or trustor is gone. Set forth below are three such dangers.

### b. Beneficiaries' Power to Amend or Terminate a Trust

The UTC [512] and the codified and/or common law in certain states [513] authorize beneficiaries to amend or terminate trusts rather easily. UTC § 411(b), a version of which has been adopted by 32 states, [514] provides as follows: [515]

[512] UTC § 411(b) (amended 2018). Under the "*Claflin* doctrine," "[i]t is very difficult to terminate or modify an irrevocable trust in jurisdictions that follow the traditional rules." (Ausness, *Sherlock Holmes and the Problem of the Dead Hand: The Modification and Termination of "Irrevocable" Trusts*, 28 Quinnipiac Prob. L.J. 237, 263 (2015)). For an analysis of what constitutes a "material purpose," see id. at 245–246.

[513] *See* Worksheet 15, below. *See also* Hayward & Pena, *Methods for Modifying Trusts Under Delaware Law*, 15 Del. L. Rev. 95 (2015); Barnes, *Repairing Broken Trusts and Other Fallen Estate Plans*, 41 Est. Plan. 3 (Nov. 2014).

[514] *See* Worksheet 15, below.

[515] UTC § 411(b) (amended 2018).

A noncharitable irrevocable trust may be terminated upon consent of all of the beneficiaries if the court concludes that continuance of the trust is not necessary to achieve any material purpose of the trust. A noncharitable irrevocable trust may be modified upon consent of all of the beneficiaries if the court concludes that modification is not inconsistent with a material purpose of the trust.

An optional UTC provision suggests that "a spendthrift provision ... is not presumed to constitute a material purpose of the trust." [516] In *In re Trust D* (2010), [517] the Supreme Court of Kansas denied a petition to increase trust distributions under Kansas's version of the UTC provision [518] that, unlike the UTC provision, said that a spendthrift clause did constitute a material purpose. The court held: [519]

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[516] UTC § 411(c) (amended 2018). *See Restatement (Third) of Trusts* § 65 (2003).

[517] 234 P.3d 793 (Kan. 2010).

[518] Kan. Stat. Ann. § 58A-411(b).

[519] *In re Trust D*, 234 P.3d at 800.

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[T]he proposed modification increasing Alford's annual distribution is inconsistent with material purposes of the trust and cannot be validated under K.S.A. 2009 Supp. 58a-411(b).

Subsequently, the Kansas statute was amended to conform to the UTC view. [520]

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[520] Kan. Stat. Ann. § 58A-411(c).

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A Florida intermediate appellate court disapproved a settlement agreement that, inter alia, would have removed the requirement that a trust have a corporate trustee because the trust prohibited modifications [521] and a request to terminate a trust that was not justified under Florida law. [522] But, the Supreme Judicial Court of Maine, over the trustee's objection, granted the beneficiaries' petition to terminate trusts even though the governing instrument had a spendthrift clause. [523] Similarly, an intermediate appellate court in Kansas held that modifying the successor trustee provision did not violate a material purpose of a trust. [524] In denying a petition to terminate a trust, the Supreme Court of Wyoming wrote: [525]

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[521] *Bellamy v. Langfitt*, 86 So.3d 1170, 1175 (Fla. Dist. Ct. App. 2012) ("As Paragraph 18 of the Trust prohibits the judicial modification of the Trust, even if it is in the best interest of the beneficiaries, we conclude that the trial court erred by modifying Paragraph 2").

[522] *Horgan v. Cosden*, 249 So.3d 683, 687 (Fla. Dist. Ct. App. 2018) ("neither section 736.04113 nor section 736.04115 supports the termination of the Trust").

[523] *In re Pike Family Tr.*, 38 A.3d 329, 332 (Me. 2012) ("Even in the absence of any presumption, a court may conclude that a spendthrift provision was a material purpose of the settlor. Here, however, Buhrman has failed to meet his burden") (citation omitted).

[524] *Matter of Tr. of Hildebrandt*, 388 P.3d 918, 922 (Kan. Ct. App. 2017) ("Modifying the successor trustee does not violate a material purpose of the Trust"). *See* LaPiana, *Successor Trustee May Be Modified by*

*Consent*, 44 Est. Plan. 48 (June 2017).

[525] *Shriners Hosps. for Children v. First N. Bank of Wyo.*, 373 P.3d 392, 408 (Wyo. 2016) (citations omitted).

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This argument fails first and foremost because termination of a trust is not permitted under Wyoming law if the continuance of the trust is necessary to carry out a material purpose of the trust. Holding the ranch in the Trust until the year 2100 is a material purpose of the Trust and requires continuation of the Trust. Sale of the ranch and termination of the Trust would obviously defeat that material purpose.

Moreover, the Supreme Court of Nebraska refused to terminate a trust because: [526]

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[526] *Shire v. Unknown/Undiscovered Heirs*, 907 N.W.2d 263, 274 (Neb. 2018) (emphasis added). *See* LaPiana, *Modification of Trust Fails for Lack of Consent*, 45 Est. Plan. 47 (July 2018).

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[T]he court did not err in determining that the Trust could not be modified, under § 30-3837, *because the beneficiaries did not unanimously consent to the modification* and the modification would not adequately protect the interests of the nonconsenting beneficiaries.

South Dakota and Delaware are not UTC states. Under South Dakota statutes, "[a]n irrevocable trust may be modified or terminated upon the consent of all of the beneficiaries if continuance of the trust on its existing terms is not necessary to carry out a material purpose," and, "upon a finding that the provisions of § 55-3-24 have been met, the court shall affirm the proposed modification or termination of the trust." [527]

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[527] S.D. Codified Laws § 55-3-24–§ 55-3-25.

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In contrast, a petition to the Court of Chancery for modification of a trust in Delaware must be accompanied by consents of all trustees, other fiduciaries, and other interested persons as well as of all beneficiaries. [528] Testators and trustors who favor beneficiary control will prefer the South Dakota approach; testators and trustors who want their wishes to be respected will prefer the Delaware approach.

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[528] Del. Ch. Ct. R. 101(a)(7).

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UTC § 111 [529] and the codified and/or common law in certain states, [530] also allow irrevocable trusts to be modified or terminated without court involvement via nonjudicial settlement agreement. Section 111, a version of which is in effect in 33 states, [531] provides: [532]

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[529] UTC § 111 (amended 2018). *See* Kotis, *Nonjudicial Settlement Agreements: Your Irrevocable Trust Is Not Set in Stone*, 31 Prob. & Prop. 32 (Mar./Apr. 2017).

[530] *See* Worksheet 15, below

[531] *See* Worksheet 15, below.

[532] UTC § 111 (amended 2018).

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(a) For purposes of this section, "interested persons" means persons whose consent would be required in order to achieve a binding settlement were the settlement to be approved by the court.

(b) Except as otherwise provided in subsection (c), interested persons may enter into a binding nonjudicial settlement agreement with respect to any matter involving a trust.

(c) A nonjudicial settlement agreement is valid only to the extent it does not violate a material purpose of the trust and includes terms and conditions that could be properly approved by the court under this [Code] or other applicable law.

(d) Matters that may be resolved by a nonjudicial settlement agreement include:

(1) The interpretation or construction of the terms of the trust;

(2) The approval of a trustee's report or accounting;

(3) Direction to a trustee to refrain from performing a particular act or the grant to a trustee of any necessary or desirable power;

(4) The resignation or appointment of a trustee and the determination of a trustee's compensation;

(5) Transfer of a trust's principal place of administration; and

(6) Liability of a trustee for an action relating to the trust.

(e) Any interested person may request the court to approve a nonjudicial settlement agreement, to determine whether the representation as provided in [Article] 3 was adequate, and to determine whether the agreement contains terms and conditions the court could have properly approved.

Even though they are not UTC states, South Dakota [533] and Delaware [534] authorize nonjudicial settlement agreements. Given that the consent requirements under them are the same as for court proceedings as described above, beneficiary consent alone suffices in South Dakota which has led one commentator to observe: [535]

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[533] S.D. Codified Laws § 55-3-24.

[534] Del. Code Ann. tit. 12, § 3338.

[535] Krogstad & Bock, *Modern Trust Governance*, 61 S.D. L. Rev. 370, 371 (2016) (footnote omitted).

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South Dakota allows a trust to be modified without court approval if all the beneficiaries consent.

As with a court proceeding, trustees, other fiduciaries, and other interested persons must participate in a nonjudicial settlement agreement in Delaware. [536]

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[536] Del. Code Ann. tit. 12, § 3338.

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Nevada, which also has not enacted a version of the UTC, has legislation that permits indispensable parties to enter into a nonjudicial settlement agreement. [537] In 2017, the Supreme Court of Nevada clarified the circumstances in which an irrevocable trust may be modified by holding in *Matter of Frei Irrevocable Trust Dated October 29, 1996* that: [538]

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[537] Nev. Rev. Stat. § 164.942.

[538] 390 P.3d 646, 648–649 (Nev. 2017) (citation omitted). *See* LaPiana, *Spendthrift Trust Can Be Modified Even if Undoing Spendthrift Protection*, 44 Est. Plan. 46 (July 2017).

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We adopt Restatement (second) of Trusts § 338 and hold that an irrevocable trust, spendthrift or not, may be modified with the consent of the surviving settlor(s) and any beneficiaries whose interests will be directly prejudiced.

Delaware and South Dakota also have legislation in this area. [539]

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[539] *See* Del. Code Ann. tit. 12, § 3342; S.D. Codified Laws § 55-3-24.

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Modification or termination of a trust will be all the easier if the state's virtual representation statute eliminates the need to involve a guardian or trustee ad litem in a judicial or nonjudicial proceeding. [540]

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[540] *See* Bart, *Virtual Representation Statutes Chart* (Oct. 1, 2018), www.actec.org/assets/1/6/Bart-Virtual-Representation-Statutes-Chart.pdf.

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## c. Decanting Power

A “decanting power” authorizes a trustee to transfer the assets of a trust to a new or existing trust. [541] Such a power might be granted by the governing instrument, caselaw, [542] or a state statute. [543] Trustees might use a decanting power to:

• Postpone a distribution until a beneficiary is more “responsible”;

• Revise a trust's administrative provisions;

• Consolidate or divide trusts;

• Fix drafting mistakes;

• Change the trust's governing law;

• React to changed circumstances. [544]

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[541] *See* Akkerman, *Decanting: A Practical Roadmap for Modernizing Trusts in South Dakota*, 61 S.D. L. Rev. 413 (Fall 2016); Skeary, *The Power of Trust Decanting: The Authority for the Power, Its Scope, and the Fiduciary Duty and Tax Implications of Its Use*, 32 Prob. & Prop. 22 (Sept./Oct. 2018); Redd, Decanting Dilemmas, 157 Tr. & Est. 12 (Mar. 2018); Sterk, Trust Decanting: A Critical Perspective, 38 Cardozo L. Rev. 1993 (Aug. 2017); Ross, *Practical Considerations for Decanting*, 30 Prob. & Prop. 36 (Mar./Apr. 2016); Taback & Pratt, *When the Rubber Meets the Road: A Discussion Regarding a Trustee's Exercise of Discretion*, 49 Real Prop., Tr. & Est. L.J. 491 (Jan. 2015); Ross, *Decanting a Revocable Trust: Useful Even if Counterintuitive*, 41 Est. Plan. 24 (Oct. 2014); Culp & Mellen, *Decanting From Trusts With Perpetuities Savings Provisions*, 41 Est. Plan. 28 (Oct. 2014). For a more in-depth discussion of decanting, *see* 871 T.M., *Trust Decanting*.

[542] *See Ferri v. Powell-Ferri*, 72 N.E.3d 541, 552 (Mass. 2017); *Morse v. Kraft*, 992 N.E.2d 1021, 1026 (Mass. 2013); *In re Estate of Spencer*, 232 N.W.2d 491, 498 (Iowa 1975); *Wiedenmayer v. Johnson*, 254 A.2d 534, 536 (N.J. Super. Ct. App. Div. 1969); *Phipps v. Palm Beach Tr. Co.*, 196 So. 299, 301 (Fla. 1940).

[543] *See* Worksheet 13, below. *See also* Bart, *Summaries of State Decanting Statutes* (Oct. 15, 2018), www.actec.org/assets/1/6/Bart-State-Decanting-Statutes.pdf; Culler, *List of States With Decanting Statutes Passed or Proposed* (Aug. 20, 2018), www.actec.org/assets/1/6/Culler-Decanting-Statutes-Passed-or-Proposed.pdf.

[544] *See* Newman, *Trust Law in the Twenty-First Century: challenges to Fiduciary Accountability*, 28 Quinnipiac Prob. L. J. 261, 287 (2016); Ausness, *Sherlock Holmes and the Problem of the Dead Hand: The Modification and Termination of "Irrevocable" Trusts*, 28 Quinnipiac Prob. L.J. 237, 286 (2015).

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Decanting powers present GST tax, gift tax, and income tax issues. [545]

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[545] *See* II.F.2., above. The IRS has indicated that it is studying and, thus, will not rule on (until it publishes guidance) whether a trustee's distribution of property from an irrevocable GST tax-exempt trust to another irrevocable trust (sometimes referred to as a decanting) resulting in a change in beneficial interests is a loss of such exempt status or constitutes a § 2612 taxable termination or taxable distribution for GST tax purposes. Rev. Proc. 2019-3, § 5.01(13). The same ruling limitation applies to whether a trustee's distribution of property from an irrevocable trust to another irrevocable trust resulting in a change in beneficial interests is: (1) a distribution for which a § 661 deduction is allowable or § 662 gross income inclusion is required; and (2) a gift under § 2501. Rev. Proc. 2019-3, § 5.01(7), § 5.01(12).

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In 2015, the Uniform Law Commission ("ULC") issued the Uniform Trust Decanting Act ("UTDA"). [546]

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[546] The text of the UTDA and a list of states that have enacted it may be viewed at, https://my.uniformlaws.org/committees/community-home?CommunityKey=5b248bac-9251-47fb-bad8-57a23f3df540. As of this writing, seven states have enacted versions of the UTDA.

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Although Massachusetts does not have a decanting statute, two decisions of its Supreme Judicial Court indicate that trustees may exercise decanting powers in certain circumstances.

Thus, in *Morse v. Kraft* (2013), [548] the court concluded that the terms of the trust in question gave the trustee a power to decant. It held: [549]

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[548] 992 N.E.2d 1021.

[549] *Id.* at 1026 (footnote omitted).

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We conclude that the terms of the 1982 Trust authorize the plaintiff to transfer property in the subtrusts to new subtrusts without the consent of the beneficiaries or a court. As did the trust in *Wiedenmayer*, supra, arts. III and VI give the disinterested trustee discretion to distribute property directly to, or applied for the benefit of, the trust beneficiaries, limited only in that such distributions must be "for the benefit of" such beneficiaries. We regard this broad grant of almost unlimited discretion as evidence of the settlor's intent that the disinterested trustee have the authority to distribute assets in further trust for the beneficiaries' benefit. Such interpretation is in keeping with the reading of similar trust language in *Phipps*, supra, and *Wiedenmayer*, supra, and our comparable holding in *Loring*, supra, all of which preceded the drafting of the 1982 Trust.

The Supreme Judicial Court revisited the issue four years later in *Ferri v. Powell-Ferri* (2017). [550] There, the trustee of a Massachusetts trust sought to exercise a decanting power to reduce a beneficiary's interests in order to limit the exposure of trust assets to the claims of a divorcing wife in a Connecticut divorce proceeding. The Supreme Court of Connecticut certified three questions to the Supreme Judicial Court, the first of which was: [551]

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[550] 72 N.E.3d 541 (Mass. 2017). *See* Abati & Lumpau, *Common-Law Decanting of Trusts: Lessons From Massachusetts*, 44 Est. Plan. 3 (Oct. 2017); LaPiana, *Common-Law Decanting Avoids Possible Matrimonial Claim*, 44 Est. Plan. 44 (July 2017).

[551] *Ferri*, 72 N.E.3d at 543.

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Under Massachusetts law, did the terms of the Paul John Ferri, Jr. Trust (1983 Trust) ...empower its trustees to distribute substantially all of its assets (that is, to decant) to the Declaration of Trust for Paul John Ferri, Jr. (2011 Trust)?

The latter court concluded that the trustee did have the power to decant. [552]

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[552] *Id.*

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In appropriate circumstances, courts do invalidate trustees' exercises of decanting powers.

Hence, in *Matter of Johnson* (2015), [553] the Surrogate invalidated the trustees' exercises of decanting powers over two trusts. Regarding the first trust, she concluded that the class of beneficiaries in the receiving trust was broader than that of the initial trust. Thus, the decanting was invalid. [554]

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[553] 2015 N.Y. Misc. Lexis 51 (N.Y. Sur. Ct. Jan. 13, 2015).

[554] *Id.* at *15.

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Regarding the second trust, the Surrogate held: [555]

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[555] *Id.* at *22.

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Under the terms of the 1997 instrument, the class of permissible appointees of the trust remainder consisted of petitioner's spouse and issue. By contrast, under the terms of the instrument of the appointed trust, the class of permissible appointees consisted of the issue of petitioner's father. Thus, except to the extent petitioner's spouse is excluded, the class of permissible appointees under the appointed instrument is broader than that under the 1997 instrument. Accordingly, for the reason stated hereinbefore, the decanting of the 1997 trust violated the version of EPTL § 10-6.6(b)(1) in effect as of July 25, 2011.

Later in the same year, a Florida intermediate appellate court held that a trustee's exercise of a decanting power was ineffective for procedural and substantive reasons in *Harrell v. Badger* (2015). [556] The Court first concluded: [557]

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[556] *Harrell v. Badger*, 171 So.3d 764 (Fla. Dist. Ct. App. 2015).

[557] *Id.* at 769 (internal quotation marks omitted).

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Here, section 736.04117(4) plainly and unambiguously requires a trustee to provide notice to all qualified beneficiaries of his intent to invade the principal of a trust at least 60 days prior to the invasion. Appellants are qualified beneficiaries, as defined in section 736.0103(16), Florida Statutes (2008), of the Trust because of their interest in the distribution of any principal remaining after Wilson's death. Badger improperly exercised his power to invade the principal of the Trust by failing to provide any notice to Appellants prior to transferring the entire contents of the Trust to the FFSNT.

The court then held: [558]

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[558] *Id.* (internal quotation marks and footnote omitted).

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Additionally, under section 736.04117(1)(a)1., the decantation of trust principal is limited to situations where the beneficiaries of the second trust include only beneficiaries of the first trust. Here, the first trust defined Wilson as the primary beneficiary and Appellants as the contingent remainder beneficiaries. The second trust — the FFSNT sub-account — also defined Wilson as the primary beneficiary but provided a contingent remainder interest to beneficiaries of the other FFSNT sub-accounts. The second trust clearly included beneficiaries not contemplated by the original Trust, rendering Badger's decantation of all assets from the original Trust invalid.

More recently, the Supreme Court of New Hampshire explained its reasons for invalidating the exercise of a decanting power: [559]

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[559] *Hodges v. Johnson*, 177 A.3d 86, 98 (N.H. 2017) (citations omitted). *See* LaPiana, *Balancing the Duty of Impartiality and Decanting to Eliminate an Interest*, 45 Est. Plan. 41 (Mar. 2018)

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The trial court's determination that the trustees failed to give any consideration to the plaintiffs' future beneficial interests, contrary to the statutory duty of impartiality, is supported by the record and is not plainly erroneous as a matter of law. Therefore, we uphold it.

### d. Change of Situs

Even if a trust begins in a state where the beneficiaries may not defeat the testator's or trustor's intent by modifying or terminating a trust or where a trustee may not do so by exercising a decanting power, the trustee or beneficiaries might change the trust's situs to a state where such a modification, termination, or decanting is available. [560] A situs change might be accomplished through a provision in the governing instrument, a nonjudicial settlement agreement, or a court proceeding. However, a court might not always accommodate beneficiaries' wishes. Accordingly, in *Harold J. Allen Trust Number Three ex rel. Allen v. Brooks* (2006), [561] an intermediate appellate court in Iowa rejected a beneficiary's petition for a change of situs as follows: [562]

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[560] *See* VII., below.

[561] 728 N.W.2d 60 (Iowa Ct. App. 2006).

[562] *Id.* at 63–64.

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As Bruce and Charles note on appeal, the trust instrument does not allow Kathleen to change the situs of the trust in a way that would require management contrary to the purpose of the trust. Kathleen's proposal would break up the trusts and the farms. A transfer of the trust situs to Canada would necessarily have adverse effects on Bruce's and Charles's trusts. Such a transfer would require either a partition of the real estate or a liquidation of the trusts' assets. Harold acquired five farms during hard economic times,

maintained them throughout his life, and preserved them in trusts granted to his three children. Furthermore, Harold, who was himself an experienced trusts and estates attorney, provided for the ability of Kathleen to receive part of the principal of the trust if her income from the trust was otherwise insufficient to support her. Allowing her the ability to liquidate the entire trust for her healthcare would be contrary to this provision. Also, if the trust situs was transferred to Canada, Charles and Bruce, for all intents and purposes, would have to be removed as trustees. This is clearly contrary to Harold's express intent as indicated by his naming all three children as trustees in each of their three trusts. Finally, the settlor's requirement that the trust be interpreted by California law could be thwarted if the trust situs were moved to Canada since full faith and credit would have no application.

## 5. Preventing Modification or Termination of a Trust

### a. Introduction

Clients who want trust terms to be respected should choose Trust States that do not give beneficiaries such powers and should include language in trust instruments that discourage courts, trustees, and beneficiaries from modifying or eliminating those terms and that prevent trusts from being moved to more permissive states. Other actions may be taken as well.

### b. Lifetime Proceeding

If a client wants certain trust provisions to be respected, it is desirable to establish the validity of the trust while the best witness — the client — is living. Some states have procedures to accomplish this. Thus, a Delaware statute provides in pertinent part that: [563]

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[563] Del. Code Ann. tit. 12, § 3546.

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(a) A judicial proceeding to contest whether a revocable trust or any amendment thereto, or an irrevocable trust was validly created may not be initiated later than the first to occur of:

(1) One hundred twenty days after the date that the trustee notified in writing the person who is contesting the trust of the trust's existence, of the trustee's name and address, of whether such person is a beneficiary, and of the time allowed under this section for initiating a judicial proceeding to contest the trust....

To date, the use of the statute has resulted in a court proceeding only once. In that case, a disgruntled brother contended that his mother's restatement of her revocable trust had resulted from his sister's undue influence. [564] The Court of Chancery held that the trustee had complied with the notice requirements and that the brother's objection to the trustee's action was untimely. [565] The Supreme Court of Delaware affirmed. [566]

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[564] *Matter of Ravet*, 2014 BL 158410, 2014 WL 2538887 (Del. Ch. June 4, 2014).

[565] *Id.* at *5.

[566] *Ravet v. N. Tr .Co. of Del.*, 2015 BL 36413, 2015 WL 631588 (Del. Feb. 12, 2015).

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Delaware practitioners have found this procedure to be useful in confirming trust provisions by getting beneficiaries to "put up or shut up" while the trustor is alive. As shown in Worksheet 14, below, several other states offer a similar procedure.

A 2008 California case illustrates how the validity of a trust may be confirmed during the trustor's lifetime through a conservatorship proceeding. [567] At the outset, the court described the facts and its conclusion as follows: [568]

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[567] *Murphy v. Murphy*, 164 Cal. App. 4th 376 (Cal. Ct. App. 2008). *See* Baer & Johnson, *Wake-Up Call*, 147 Tr. & Est. 59 (Aug. 2008).

[568] *Murphy*, 164 Cal. App. 4th at 383 (footnotes omitted).

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Pursuant to Probate Code section 2580 et seq., a person subject to a conservatorship may invoke the jurisdiction of the probate court to execute a testamentary instrument. The probate court has discretion, circumscribed by the statutory scheme, to order a "substituted judgment" that authorizes a conservator on behalf of a conservatee to take necessary or desirable action to facilitate estate planning, when a reasonably prudent person in the conservatee's position would do so. In 2003, the probate court issued such an order on behalf of William J. Murphy, the father of the two parties. The probate court's order authorized William's conservator to execute a living trust and pour-over will implementing an estate plan that effectively disinherited William's son, William J. Murphy, Jr. (respondent). In 2004, following William's death, respondent sued his sister, Maureen Murphy, individually and as trustee of the William J. Murphy Revocable Living Trust (appellant), alleging breach of an oral contract, undue influence, intentional interference with contract, and fraud. Following a lengthy trial, the court issued a judgment in favor of respondent imposing a constructive trust over one-half of William's real and personal property in existence on the date of his death.

Appellant raises a host of challenges to the probate court's ruling. We conclude, as a matter of first impression, that the instant action is barred by principles of collateral estoppel, and reverse.

## c. No-Contest Clause

A client might also try to prevent beneficiaries from challenging certain provisions by including a no-contest clause in the trust. [569] *Black's Law Dictionary* defines such a clause as follows: [570]

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[569] A no-contest clause also may be called an in terrorem, penalty, or forfeiture clause. *See, e.g.*, *Matter of Tr. of Hildebrandt*, 388 P.3d 918 (Kan. Ct. App. 2017); *In re Shaheen Tr.*, 341 P.3d 1169 (Ariz. Ct. App. 2015). *See also* Gordon, *Forfeiting Trust*, 57 Wm. & Mary L. Rev. 455 (Nov. 2015); Viviano, *The Use of Declaratory Judgments to Test the Enforceability of No-Contest Clauses*, 50 Real Prop. Tr. & Est. L.J. 75 (Spring 2015). For a detailed discussion of no-contest clauses, see 824 T.M., *Testamentary Capacity, Undue Influence and Validity of Wills.*

[570] *Black's Law Dictionary* at 1209 (10th ed. 2014).

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A provision designed to threaten one into action or inaction; esp., a testamentary provision that threatens to dispossess any beneficiary who challenges the terms of the will.

For a no-contest clause to be effective, the client must make the provision for a beneficiary large enough that he or she will not risk losing that gift by challenging undesirable trust provisions.

Beginning in 1991, California honored no-contest clauses by statute in specified circumstances [571] and provided a judicial procedure for establishing whether a challenge constituted a "contest." [572] That legislation spawned an enormous amount of litigation. California's no-contest clause legislation was therefore completely revamped in 2010. [573]

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[571] Cal. Prob. Code § 21300–§ 21308.

[572] Cal. Prob. Code § 21320–§ 21322.

[573] Cal. Prob. Code § 21310–§ 21315. *See, e.g.*, *Donkin v. Donkin*, 314 P.3d 780 (Cal. 2013).

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Other states enforce no-contest clauses as well. For instance, Alaska will enforce a penalty clause in a Will or trust "even if probable cause exists for instituting the proceedings," [574] and other states will enforce one, subject to specified exceptions. [575] Under Georgia law, a no-contest clause is honored provided that the Will or trust disposes of a forfeited gift. [576] Some states prohibit forfeiture clauses altogether. [577]

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[574] Alaska Stat. § 13.36.330 (Wills and trusts). The author wonders how an Alaskan court would apply the statute in a situation in which the testator or settlor truly lacked capacity or the instrument was forged. *See EGW v. First Federal Savings Bank of Sheridan*, 413 P.3d 106, 115 (Wyo. 2018) ("Wyoming does not recognize an exception to enforceability of no-contest clauses where a will contest is made in good faith").

[575] *See Sandstead-Corona v. Sandstead*, 415 P.3d 310, 323 (Colo. 2018) ("the no-contest clause in the Trust did not prevent Corona from contesting the 2000 Will"). *See also* Covey and Hastings, Summary of State (Other Than Georgia Rules Regarding In Terrorem Provisions, Prac. Drafting App. A 13258 (July 2018); Challis & Zaritsky, *State Laws: No-Contest Clauses* (Mar. 24, 2012), www.actec.org/assets/1/6/State_Laws_No_Contest_Clauses_-_Chart.pdf. Worksheet 14 compiles the state no-contest clause statutes.

[576] Ga. Code. Ann. § 53-4-68(b), § 53-12-22(b). *See, e.g.*, *Norton v. Norton*, 744 S.E.2d 790 (Ga. 2013) (no-contest clause in Will enforced).

[577] *See* Fla. Stat. § 732.517 (Wills), § 736.1108 (trusts); Ind. Code Ann. § 29-1-6-2 (Wills), § 30-4-2.1-3 (trusts). *See, e.g.*, *Dinkins v. Dinkins*, 120 So.3d 601 (Fla. Dist. Ct. App. 2013).

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*Comment:* As a practical matter, no-contest clauses should not be enforced indiscriminately because they should not work if they result from undue influence, inadequate capacity, or forgery. Not only might unscrupulous beneficiaries forge Wills or trusts that unduly benefits them, but they also might include no-contest clauses to deter challenges. [578] This should not be allowed to stand.

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[578] *See Harrison v. Morrow*, 977 So.2d 457 (Ala. 2007) (no-contest clause does not bar Will contest based on alleged forgery).

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## 6. Striking a Balance

In a 2011 article, a law professor observed that a shift has occurred in trust law from respecting the testator's or trustor's intent to satisfying the desires of the beneficiaries: [579]

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[579] Gallanis, *The New Direction of American Trust Law*, 97 Iowa L. Rev. 215, 216 (Nov. 2011). For an overview of the subject, see Ausness, *Sherlock Holmes and the Problem of the Dead Hand: The Modification and Termination of "Irrevocable" Trusts*, 28 Quinnipiac Prob. L.J. 237 (2015).

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I shall argue that American trust law, after decades of favoring the settlor, is moving in a new direction, with a reassertion of the interests and rights of the beneficiaries. I shall also argue that this new direction is appropriate and welcome.

Many people, including the author, disagree with Professor Gallanis. From a Delaware perspective, Vice Chancellor Laster pointed out in 2015 that "it would undercut this policy [of honoring intent] and might well be described as duplicitous, for our State to represent to a settlor that our law will respect his dispositions and enforce his governing instrument, only to enable his beneficiaries to rewrite that instrument after his death." [580] In that same year, a Missouri practitioner described the planner's dilemma as follows: [581]

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[580] *In re Trust of Flint*, 118 A.3d 182, 194 (Del. Ch. 2015).

[581] Redd, *Flexibility v. Certainty — Has the Pendulum Swung Too Far?*, 154 Tr. & Est. 10, 11 (Mar. 2015).

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Flexibility in estate planning is almost universally touted as the greatest thing since sliced bread. Estate-planning professionals seem consistently to accept and promote the use of techniques and strategies, enabled or enhanced by the developments described above, which can be and sometimes are used to eviscerate a trust. Of course, changes to irrevocable trust instruments are often objectively desirable or necessary. Errors need to be corrected, antiquated, obsolete provisions need to be updated and unanticipated changes in applicable law and beneficiaries' circumstances need to be addressed. Sometimes, though, the motivation to make changes, and the changes themselves, may transcend that which is desirable or necessary. Beneficiaries may simply decide they don't care for the terms of a trust established by an ancestor and want to relax the rules or eliminate restrictions altogether. Indeed, a determined coalition of beneficiaries who are willing to expend sufficient time, effort and money may be able to effectuate virtually any change in trust provisions they desire.

How should estate planners formulate an estate plan in a legal environment in which the concept of irrevocability is so porous? On one hand, it would be unwise and impossible to foreclose the making of any and all changes to an irrevocable trust. On the other hand, most estate-planning clients would be shocked to their core to learn that their beneficiaries, with little or no regard for the client's dispositive desires, could drastically change the client's carefully considered and crafted estate plan.

Another law professor put the issue more bluntly in 2016: [582]

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[582] Fogel, *Terminating or Modifying Irrevocable Trusts by Consent of the Beneficiaries*, 50 Real Prop., Tr. & Est. L.J. 337, 378 (Winter 2016) (footnote omitted). For a summary of factors that should be considered in balancing testator-trustor intent and beneficiary needs, see Kelly, *Restricting Testamentary Freedom: Ex Ante Versus Ex Post Justifications*, 82 Fordham L. Rev. 1125, 1184–1185 (Dec. 2013).

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To respect the primacy of the settlor's intent, courts and legislatures should abandon trust termination by consent of the beneficiaries. The basic concept — allowing beneficiaries to terminate a trust because they feel it does not meet their needs — is inapposite in trust law. The settlor's intent is the touchstone. The beneficiaries in most of these cases are simply dissatisfied beneficiaries. Their efforts to alter the trust to better suit their needs — even if sympathetic — must be rejected.

Equitable deviation should be allowed to take the place of trust modification or termination by consent of the beneficiaries. Thus, a trust will be modified or terminated only in the case of relevant circumstances not anticipated by the settlor. In this manner, trusts are only modified if the court determines that such modification furthers the settlor's intent.

Most clients understand that, whereas they might want their trusts to further certain objectives, it also might be necessary for trusts to be modified due to unanticipated circumstances. In 2006, a third professor described the tension between incentive provisions and the need to respond to change as follows: [583]

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[583] Tate, *Conditional Love: Incentive Trusts and the Inflexibility Problem*, 41 Real Prop., Prob. & Tr. J. 445, 451–452 (Fall 2006) (footnotes omitted).

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This Article questions whether the current trend toward trust modification reform adequately takes into account the particular difficulties posed by contemporary incentive trusts. Scholars who have examined recent reforms in the area of trust modification generally have assumed that allowing greater latitude to courts is a positive development, especially given the rise of perpetual dynasty trusts. In the case of an incentive trust, however, mandatory modification rules may enable the beneficiaries to undo the scheme created by the settlor and remove conditions that encourage certain types of positive behavior. One might argue that some of the conditions imposed by settlors are actually good for the beneficiaries and that the ability of courts to tinker with the provisions of an incentive trust should be limited. A valid case can be made in support of the dead hand. Nonetheless, sound arguments also exist for allowing the courts to step in when the terms of the trust are more of a hindrance than a benefit to the beneficiaries. The inflexibility problem posed by incentive trusts is not easy to resolve.

A year earlier the same professor also recognized that this tension might arise if a testator or trustor wants to create a dynasty trust. [584]

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[584] *See* Tate, *Perpetual Trusts and the Settlor's Intent*, 53 Kan. L. Rev. 595, 620–621 (Apr. 2005).

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A possible approach to resolving this tension might be to charge a corporate trustee, adviser, or protector with responsibility for representing the testator's or trustor's wishes; to require that person's consent to a modification, termination, unitrust conversion, exercise of a decanting power, or change of situs; and to

prohibit removal for refusing to give such consent.

In any event, if a testator or trustor wants to limit the ability of trustees and beneficiaries to modify trusts, then language such as the following might be included in the governing instrument: [585]

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[585] *See* Redd, *Flexibility vs. Certainty — Has the Pendulum Swung Too Far?*, 154 Tr. & Est. 10, 10–11 (Mar. 2015).

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Trustor has crafted the terms of this Agreement carefully and therefore wants to restrict the mechanisms by which this Agreement can be modified. Accordingly, in no circumstances shall the situs of a trust hereunder be changed or the provisions of this Agreement be modified under Delaware's merger statute (12 Del. C. § 3325[29], as amended, or any corresponding provision of future law), Delaware's decanting statute (12 Del. C. § 3528, as amended, or any corresponding provision of future law), Delaware's nonjudicial settlement agreement statute (12 Del. C. § 3338, as amended, or any corresponding provision of future law); Delaware's consent-petition procedure prescribed by any standing order or rule of the Delaware Court of Chancery; or any similar statute or procedure.

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## D. Trust Duration

### 1. Introduction

Clients should be able to create trusts of movables in Trust States that have different perpetuities rules from those of their Home States because:
• The determination of whether a trust violates the rule against perpetuities is a matter of trust validity; [586]

• The trust instrument may designate the law of a state that governs matters of validity that will be effective unless the Trust State's statute offends a strong public policy of a state that has a closer connection to the trust; [587] and

• It generally is the case that no strong public policy is involved in differences in the rule against perpetuities. [588]

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[586] *Restatement (Second) of Conflict of Laws* § 269 cmt. d (Am. Law Inst. 1971). In the remainder of this V.D. "*Restatement*" refers to the *Restatement (Second) of Conflict of Laws*. *See generally* Shapo, Bogert & Bogert, *The Law of rusts and Trustees* § 213, § 214, § 219 (3d ed. 2007).

[587] *Restatement* § 269–§ 270.

[588] *Restatement* § 269 cmt. i.

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### 2. Perpetuities Statutes

The perpetuities rules in the states vary considerably. Since 1983, a number of states have repealed the rule against perpetuities for trusts. Several others have enacted statutes that permit testators and trustors to opt out of the rule. As shown in Worksheet 4, below, 24 states permit perpetual trusts, 11 states allow very long trusts, 13 states follow the USRAP, four states follow the common-law rule against perpetuities, and one state — Louisiana — allows trusts to last for up to three generations. [589] But, the Simes & Smith treatise points out: [590]

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[589] *See Shriners Hosps. for Children v. First N. Bank of Wyo.*, 373 P.3d 392, 405 (Wyo. 2016). ("Because the interest of Shriners and Kalif in the Trust property was fixed and vested upon Jack Cooksley's death, the Trust does not violate the rule against perpetuities"). *See also* Zaritsky, *The Rule Against Perpetuities: A Survey of State (and D.C.) Law* (Mar. 2012), www.actec.org/assets/1/6/Zaritsky_RAP_Survey.pdf.

[590] Borron, *Simes & Smith: The Law of Future Interests* § 1410 at 326 (3d ed. 2004) (footnotes omitted). *Contra Brown Bros. Harriman Tr. Co. v. Benson*, 688 S.E.2d 752 (N.C. Ct. App. 2010).

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In several states are found constitutional provisions to the effect that perpetuities shall not be allowed. The North Carolina constitution contains the following clause: “Perpetuities and monopolies are contrary to the genius of a free state and ought not to be allowed.” If no legislation, other than such a constitutional provision, exists in a given state on the subject of perpetuities, the constitutional provision would seem, as a practical matter, to be without effect. However, if legislative modification of the common law rule is attempted, then such a constitutional provision might be held to restrict its operation.

The nine states that have constitutional prohibitions on perpetuities are: Arizona, Arkansas, Montana, Nevada, North Carolina, Oklahoma, Tennessee, Texas, and Wyoming. [591] Texas adheres to the common law rule against perpetuities; Montana follows the USRAP; Tennessee (360 years), Nevada (365 years), Arizona (500 years), and Wyoming (1,000 years) allow very long trusts; and Arkansas, North Carolina, and Oklahoma permit perpetual trusts. Of the eight states that have enacted legislation that departs from the common law rule, Montana's statute probably is acceptable because it does not represent much of a departure, but the other seven statutes certainly appear to be vulnerable to constitutional attack because they authorize trusts that are much longer than what was permitted at common law.

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[591] Ariz. Const. art. 2, § 29, Ariz. Rev. Stat. Ann. § 33-261; Ark. Const. art. 2, § 19; Mont. Const. art. 13, § 6; Nev. Const. art. 15, § 4; N.C. Const. art. 1, § 34; Okla. Const. art. 2, § 32; Tenn. Const. art. 1, § 22; Tex. Const. art. 1, § 26; Wyo. Const. art. 1, § 30. *See Bradley v. Shaffer*, 535 S.W.3d 242, 250 (Tex. Ct. App. 2017) (“the trust does not violate the rule against perpetuities”).

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With so many choices, practitioners should be cautious about directing clients to those seven states with constitutional prohibitions. [592] This concern is particularly acute in Nevada where voters disapproved a ballot initiative to repeal the constitutional prohibition in 2002. Regarding this issue, Professor Sitkoff of Harvard Law School and a co-author wrote in 2014 that: [593]

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[592] An intermediate appellate court upheld North Carolina's statute in *Brown Bros. Harriman Tr. Co. v. Benson*, 688 S.E.2d 752 (N.C. Ct. App. 2010). But, commentators advise the Supreme Court of North Carolina and other courts not to rely on the case because it is “deeply flawed” (Horowitz & Sitkoff, *Unconstitutional Perpetual Trusts*, 67 Vand. L. Rev. 1769, 1811 (Nov. 2014)). Another commentator points out that “the inclusion of a separate clause, copied from the Pennsylvania Constitution, providing that the legislature ‘shall regulate entails, in such a manner as to prevent perpetuities’ shows that the framers of the North Carolina Constitution of 1776 were hostile to perpetuities as conventionally defined” (Tate, *Perpetuities and the Genius of a Free State*, 67 Vand. L. Rev. 1823, 1833 (Nov. 2014)). For an analysis of these constitutional prohibitions, see Raatz, *State Constitutional Perpetuities Provisions: Derivation, Meaning, and Application*, 48 Ariz. St. L.J. 803 (Fall 2016).

[593] Horowitz & Sitkoff, 67 Vand. L. Rev. at 1803. *Accord* Blattmachr, Gans & Lipkin, *What If Perpetual Trusts Are Unconstitutional?*, LISI Est. Plan. Newsl. #2263 (Dec. 18, 2014), www.leimbergservices.com.

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[L]egislation authorizing perpetual or long-enduring dynasty trusts is constitutionally suspect in a state with a constitutional prohibition of perpetuities.

A Nevada practitioner contends that a 1941 decision of the Supreme Court of Nevada — *Sarrazin v. First National Bank of Nevada* [594] — and a 2015 decision of the same court — *Bullion Monarch Mining, Inc. v. Barrick Gold Strike Mines, Inc.* [595] — mean that the constitutional limitation no longer is relevant.

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[594] 111 P.2d 49 (Nev. 1941). *See* Oshins, *The Rebuttal to Unconstitutional Perpetual Trusts*, LISI Est. Plan. Newsl. #2265 (Dec. 22, 2014), www.leimbergservices.com.

[595] 345 P.3d 1040 (Nev. 2015). *See* Oshins, *Unconstitutional Perpetual Trusts — Not So Fast Says the Nevada Supreme Court*, LISI Est. Plan. Newsl. #2297 (Apr. 6, 2015), www.leimbergservices.com.

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The *Sarrazin* case was decided long before Nevada adopted a 365-year period for trust interests. Its entire description of the law of perpetuities in Nevada is as follows: [596]

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[596] *Sarrazin*, 111 P.2d at 51 (citation omitted; emphasis added).

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Section 4 of article XV of the constitution of Nevada reads: “No perpetuities shall be allowed except for eleemosynary purposes.” There is no Nevada statute defining the rule against perpetuities. The common-law rule is usually stated thus: “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.” *Other than the constitutional provision above quoted, there have not been called to our attention any other provisions, either constitutional or statutory, invalidating interests which vest too remotely, or forbidding restraints on alienation.*

The above emphasized sentence is dictum at best because the court concluded that all interests in the trust in question would vest within the common law rule against perpetuities period. [597]

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[597] *Id.* at 53.

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The *Bullion Monarch Mining* case involved the applicability of Nevada's rule against perpetuities to “commercial mining agreements for the payment of area-of-interest royalties.” [598] Not surprisingly given the nature of the interest, the court held that the rule against perpetuities did not apply. [599] In the course of the opinion, the court discussed a 1974 case — *Rupert v. Stienne* [600] — as endorsing statutes that depart from the common law. Nevertheless, *Rupert*, which dealt with the, “old common-law rule of interspousal immunity,” [601] did not involve a common-law rule that had been codified in Nevada's constitution.

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[598] *Bullion Monarch Mining*, 345 P.3d at 1041.

[599] *Id.* at 1044.

[600] 528 P.2d 1013 (Nev. 1974).

[601] *Bullion Monarch Mining*, 345 P.3d at 1042.

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A decision of the Supreme Court of Nevada validating 365-year trusts might be helpful. The best way to resolve the issue, of course, would be for the voters to repeal the constitutional prohibition.

As discussed in II.F.3.b., above, Delaware first made it possible to create a perpetual trust through the exercise of nongeneral powers of appointment in 1933. In 1995, Delaware enacted legislation that permits stocks, bonds, and other personal property to remain in trust forever. [602] Although a parcel of real property may stay in trust for only 110 years under Delaware law, [603] this limitation may be avoided by putting the property in a limited-liability company ("LLC") or a family limited partnership ("FLP") because an interest in such an entity is personal property. [604]

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[602] Del. Code Ann. tit. 25, § 503.

[603] Del. Code Ann. tit. 25, § 503(b).

[604] Del. Code Ann. tit. 25, § 503(e).

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Regarding the current status of the rule against perpetuities, a 2008 article observes that: [605]

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[605] Sitkoff & Schanzenbach, *Perpetuities, Taxes, and Asset Protection: An Empirical Assessment of the Jurisdictional Competition for Trust Funds*, 42 U. Miami Inst. on Est. Plan. ¶ 1413.3 at 14-28–14-29 (2008). *See* McCouch, *Tax Advice for the Second Obama Administration: Who Killed the Rule Against Perpetuities?*, 40 Pepp. L. Rev. 1291 (2013).

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Even if some states retain the Rule Against Perpetuities, the Rule will apply, in effect, only to real property within those states. When it matters, people move their financial assets to escape the Rule's reach. The evidence indicates that the demand for perpetual trusts was sparked chiefly by tax considerations, not solely by dynastic impulses. However, an intent to extend tax benefits to lineal descendants is clearly evident.

The federal wealth transfer taxes have thus mortally wounded the once-mighty Rule by reducing it to a mere transaction cost. As a result, Congress has inadvertently transformed the question of trust duration into an issue of federal tax law.

In critiquing a proposal to limit the duration of trusts, a professor opined in 2013 that, "I think the ALI's project, and its proposal, to be both unwise and fairly hopeless." [606]

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[606] Shepard, *A Uniform Perpetuities Reform Act*, 16 N.Y.U. J. Legis. & Pub. Pol'y 89, 92 (2013).

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## 3. Creating a Long-Term Trust

### a. Introduction

Suppose that a testator or trustor wants to create a trust in a Trust State that will last longer than the period permitted by the common-law rule against perpetuities or the USRAP that is in effect in the Home State. If the Home State is one of the four states that still have the common-law rule or is one of the 13 states that follow the USRAP, may a beneficiary successfully challenge in a Home State court the creation of a long-term trust elsewhere? To the author's knowledge, no court has yet considered this question, which is not surprising because, until the mid-1990s, only a handful of states had departed from the common-law rule or the USRAP and because the issue is unlikely to arise until the death of an original beneficiary of such a trust. Will the result differ depending on whether the testator or trustor lives in a state that has a constitutional prohibition on perpetuities?

The resolution of the question will depend on whether the trust is funded with movables or land and might arise in the following four contexts:
• If a testator creates the trust by Will;

• If a testator's Will pours over assets in the probate estate to a revocable or irrevocable trust created during life;

• If a trustor funds a revocable trust in the Trust State during life; or

• If a trustor funds an irrevocable trust in the Trust State during life (e.g., to use part or all of the gift tax exemption or the GST exemption).

## b. Trust of Movables

### (1) Trust Under Will

Under the *Restatement (Second) of Conflict of Laws*, because the duration of a trust is a matter of trust validity, [607] a testator's designation of a Trust State's law to govern the duration of trusts established under the Will will stand unless, inter alia, the Trust State's provision offends a strong public policy of the Home State. [608] A Home State court is not justified in departing from a testator's designation merely because Home State law and Trust State law differ on an issue, [609] and differences between perpetuities rules normally don't justify applying Home State law. [610] However, when the *Restatement* was promulgated in 1971, virtually every state followed the common-law rule against perpetuities so that state law differences were not as significant as they are now. Consequently, a constitutional prohibition of perpetuities might now amount to a matter of strong public policy. [611] (As just noted, however, such prohibitions did not deter legislatures in Arizona, Arkansas, Nevada, North Carolina, Oklahoma, Tennessee, and Wyoming from leaving the traditional rule far behind.) For these reasons and because funding of the trusts will be within the control of a Home State court, attempting to create a trust in a Trust State that is substantially longer than what is allowed in the Home State through a testamentary trust is not without significant risk.

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[607] *Restatement (Second) of Conflict of Laws* § 269 cmt. d (1971).

[608] *Restatement* § 269(b).

[609] *Restatement* § 269 cmt. i.

[610] *Id.*

[611] The author would like to thank Carol A. Harrington, Esq., McDermott Will & Emery LLP, Chicago, Illinois, for sharing these insights.

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### (2) Pour Over to Existing Trust

This approach is not without substantial risk either. Under the *Restatement*, whereas the law of the Home State should govern whether a pour-over Will is valid, the law of the Trust State should govern issues that come up in the administration of the trust (e.g., whether the perpetuities period is acceptable) and there is no strong public policy exception. [612] Nonetheless, a Home State court again might get involved and impose Home State law. Therefore, the testator should minimize the assets to be poured over at death.

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[612] *Restatement* § 269 cmt. b, § 271 cmt. f.

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### (3) Revocable Trust Funded During Life

If a trustor funds a revocable trust in a Trust State during life, the courts of the Trust State should supervise the administration of the trust [613] and the Home State's perpetuities rule should prevail only if the Home State, not the Trust State, has the more significant relationship to the trust on the matter at issue. [614] In normal circumstances, this will not be the case. [615] To strengthen the case, the trustor should appoint a trustee that is not subject to personal jurisdiction in the Home State. [616]

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[613] *Restatement* § 267.

[614] *Restatement* § 270(a).

[615] *See* IV.D.3.b., above.

[616] *See* IV.B.4., above.

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### (4) Irrevocable Trust Funded During Life

Because there should be little, if any, interaction between the Home State and the Trust State regarding an irrevocable trust created and funded during life, this vehicle should offer the best chance of success.

## c. Trust of Land

Because courts of the situs supervise the administration of trusts funded with interests in land, [617] and because the validity of provisions of trusts that hold land is controlled by the law of such state, [618] funding a trust with Home State land in a Trust State with the hope of getting a longer perpetuities period probably will fail. Some suggest that this problem may be avoided by putting such an interest in an FLP or LLC and thereby converting it into personal property. Research in this area has not identified a single instance in which this strategy has succeeded, and the author fears that a Home State court might be able to pierce the entity's veil. Moreover, this strategy is under attack in analogous situations. For example, attorneys sometimes suggest that real property be placed in an FLP or LLC to eliminate a state's estate or inheritance tax on real property owned by nonresidents. To counter this strategy, a Maine statute provides that: [619]

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[617] *Restatement* § 276.

[618] *Restatement* § 278.

[619] Me. Rev. Stat. Ann. tit. 36, § 4064.

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When real or tangible personal property is owned by a pass-through entity, the entity must be disregarded and the property must be treated as personally owned by the decedent if the entity does not actively carry on a business for the purpose of profit and gain; the ownership of the property in the entity was not for a valid business purpose; or the property was acquired by other than a bona fide sale for full and adequate consideration and the decedent retained a power with respect to or interest in the property that would bring the real or tangible personal property located in this State within the decedent's federal gross estate.

### d. UTC Approach

Under the UTC, "the law of the place having the most significant relationship to the trust's creation will govern the dispositive provisions" [which should include the trust's duration]. [620] Of the four funding options, establishing a revocable trust or an irrevocable trust in a Trust State should offer the best prospect for success.

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[620] UTC § 107 cmt. (amended 2018).

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### e. Planning Point

Remember that the IRS says that a Grandfathered Dynasty Trust will lose its grandfathered status if it is moved in a way that will increase its duration [621] and that the IRS applies the rules for Grandfathered Dynasty Trusts to Exempt Dynasty Trusts. [622] Accordingly, to preserve flexibility, clients probably should create new trusts in states that permit perpetual trusts rather than in states that limit the duration of trusts.

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[621] Reg. § 26.2601-1(b)(4)(i)(E), *Ex.* 4.

[622] *See, e.g.*, PLR 201829005.

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## 4. Rule Against Accumulations

When clients are creating long-term trusts, attorneys must ensure that they will not violate the rule against accumulations, which forbids the accumulation of income beyond the rule against perpetuities. [623] The continued relevance of the rule against accumulations came to light in the 1999 case of *White v. Fleet Bank of Maine*, [624] in which the Supreme Judicial Court of Maine held that a direction to accumulate 25% of the income of the trust violated the rule. Among states that allow perpetual trusts, Delaware, Illinois (provided that it is a qualified perpetual trust), Michigan, Missouri, New Hampshire, North Carolina, Pennsylvania, South Dakota, Tennessee, and Wisconsin also permit income to be accumulated

perpetually. [625] Other states that permit perpetual or long-term trusts may not yet have dealt with the rule against accumulations.

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[623] *See Black's Law Dictionary* at 26 (10th ed. 2014). *See also* Sitkoff, *The Lurking Rule Against Accumulations of Income*, 100 Nw. U. L. Rev. 501 (2006); Sneddon, *The Sleeper Has Awakened: The Rule Against Accumulations and Perpetual Trusts*, 76 Tul. L. Rev. 189 (Nov. 2001). *See generally*, Shapo, Bogert & Bogert, *The Law of Trusts and Trustees* § 215–§ 217 (3d ed. 2007).

[624] 739 A.2d 373, 380 (Me. 1999).

[625] Del. Code Ann. tit. 25, § 506; 765 ILCS 315/1; Mich. Comp. Laws § 554.93(1)(d), § 554.93(2)(f); Mo. Ann. Stat. § 456.025(2); N.H. Rev. Stat. Ann. § 564-B:4-402A(c)–§ 564-B:4-402A(d); N.C. Gen. Stat. § 41-23(h); 20 Pa. Cons. Stat. § 6107.1(b)(2); S.D. Codified Laws § 43-6-7; Tenn. Code Ann. § 35-15-106(b)(1); Wis. Stat. § 701.1136(2).

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## E. State Income Tax

## 1. Introduction

### a. Background

Most states impose a tax on the income of nongrantor trusts. In 2017, rates ranged from a lowest top rate of 2.90% in North Dakota [626] and 3.07% in Pennsylvania [627] to a highest top rate of 9.90% in Oregon, [628] 12.696% in New York City, [629] and 13.30% in California. [630] With proper planning, this tax may be minimized or eliminated in many instances. Conversely, without proper planning, the income of a trust might be subject to tax by more than one state.

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[626] N.D. Cent. Code § 57-38-30.3(1)(e). *See* Boyle, Blattmachr & Gans, *Planning Opportunities With ESBTs: Saving State and Local Income Taxes*, 129 J. Tax'n 20 (July 2018). For a comprehensive discussion of this subject, see Nenno, *Reprise! The State Taxation of Trust Income Five Years Later*, 51 Heckerling Inst. on Est. Plan. ¶ 1500 (2017); 869 T.M., *State Income Taxation of Trusts*.

[627] 72 P.S. § 7302(b).

[628] Or. Rev. Stat. § 316.037.

[629] N.Y. Tax Law § 601(c)(1)(A), § 1304.

[630] Cal. Rev. & Tax. Code § 17041(a)(1), § 17041(e), § 17041(h), § 17043(a); Cal. Const. Art. XIII, § 36(f)(2). *See* Tax Foundation, *Facts & Figures 2018: How Does Your State Compare?* Table 12 (Jan. 1, 2018), https://taxfoundation.org/publications/facts-and-figures/.

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All income of a trust that is treated as a grantor trust for federal-income tax purposes is generally taxed to the trustor, distributed ordinary income of a nongrantor trust is generally taxed to the recipient, and source income of a trust (e.g., income attributable to business activity) is generally taxed by the state where the activity occurs. [631] Thus, this section V.E., focuses on the tax savings opportunities for accumulated nonsource ordinary income and capital gains of nongrantor trusts.

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[631] *See Corrigan v. Testa*, 73 N.E.3d 381, 289 (Ohio 2016) (nonresident individual not subject to income tax on sale of interest in LLC that conducted business in Ohio under Due Process Clause). *See also* Thistle, et al., *Blurred Lines: State Taxation of Nonresident Partners*, 81 State Tax Notes 689 (Aug. 29, 2016).

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### b. Problem

In some instances, minimizing state fiduciary income tax will not be important, but, in others, proper planning might produce large tax savings.

For example, if a nongrantor trust that had a California trustee but no California beneficiaries, incurred a $1 million long-term capital gain in 2017, had no other income, and paid its California income tax by the end of the year, the trust would have paid $108,775 of California income tax on December 29, 2017, and $232,860 of federal income tax on April 17, 2018. If the trust had had a non-California trustee, however, then the trustee would have owed $0 of state tax and $236,514 of federal income tax.

Similarly, if a nongrantor trust, which was created by a New York City resident and was subject to New York State and City tax incurred a $1 million long-term capital gain in 2017, had no other income, and paid its New York State and City income tax by year-end, the trustee would have owed $107,124 of New York State and City tax on December 29, 2017, and $232,922 of federal income tax on April 17, 2018. If the trust had been structured so that New York tax was not payable, however, the trustee would have owed no state or city tax and $236,514 of federal income tax.

### c. Scope

The rest of this section V.E., will summarize:
(1) The circumstances, if any, in which states tax the nonsource accumulated ordinary income and capital gains of nongrantor trusts based on state statutes, regulations, and 2017 fiduciary income tax return instructions;

(2) Pertinent cases and rulings;

(3) The taxation schemes of particular states; and

(4) Planning and other issues for new trusts.

## 2. Rules for Taxation of Trusts

### a. Introduction

Eight states — Alaska, Florida, Nevada, New Hampshire (which taxes interest and dividends of grantor trusts), South Dakota, Texas, Washington, and Wyoming — do not tax the income of nongrantor trusts; [632] Tennessee taxes interest and dividends only. [633]

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[632] For citations to the pertinent statutes for the information summarized in this section, see Worksheet 5, below.

[633] Tenn. Code Ann. § 67-2-101–§ 67-2-122.

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As just noted, if a trust is a grantor trust for federal income tax purposes, then all income (including accumulated ordinary income and capital gains) will be taxed to the trustor, thus making planning difficult, if not impossible, while that status continues. With the exception of Pennsylvania, which does not follow the federal grantor trust rules at all for irrevocable trusts, all the states that tax trusts essentially honor the federal grantor trust rules. Nevertheless, it might be possible to exploit differences between the federal and the applicable state grantor-trust rules in a particular case. Hence, even though a trust might be a

grantor trust for federal purposes in a given situation, it might be possible to structure it as a nongrantor trust for state purposes and to arrange matters so that the trust is not subject to that state's tax. For instance, Massachusetts classifies a trust as a grantor trust based on § 671–§ 678 only, which means that a trust that falls under § 679 will be a grantor trust for federal but not for state purposes. [634]

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[634] Mass. Gen. L. ch. 62, § 10(e).

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### b. Bases of Taxation

All 43 taxing states, including Tennessee, tax a nongrantor trust based on one or more of the following five criteria:

- If the trust was created by the Will of a testator who lived in the state at death;
- If the trustor of an inter vivos trust lived in the state;
- If the trust is administered in the state;
- If one or more trustees live or do business in the state;
- If one or more beneficiaries live in the state.

Worksheet 5, below, summarizes the criteria that the 43 taxing states employ in taxing trust income.

## 3. Determining Whether Imposition of Tax is Constitutional

### a. Introduction

In some situations, how best to escape a state's tax will be plain. For example, if a state taxes trusts administered within the state or that have resident trustees, then tax may be escaped by establishing administration elsewhere or by appointing nonresident trustees.

Significantly, a state cannot tax a trustee on income of a trust simply by saying so. Thus, a state that taxes a trustee because the testator or trustor was a resident may not collect tax in all circumstances. This is because a state may tax the income of a trust only if doing so will not violate limits set by the United States Constitution. The constitutionality of various state approaches to the income taxation of trusts has not been directly addressed by the U. S. Supreme Court, but the Court's rulings on other forms of state taxation and the decisions of various state and federal courts on the state income taxation of trusts have focused on two constitutional restraints on the right of a state to tax the income of a trust: the Due Process Clause of the Fifth or Fourteenth Amendment [635] and the Commerce Clause. [636] Admittedly, taking on a constitutional challenge is daunting, but if the amount of tax involved is substantial and if the trustee's contacts with the taxing state are minimal, then doing so might be worth the effort.

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[635] U.S. Const. Amend. V, Amend. XIV, § 1. The Due Process Clauses of the Fifth and Fourteenth Amendments are coextensive (*Hibben v. Smith*, 191 US 310, 325 (1903)).

[636] U.S. Const. Art. I, § 8, cl. 3.

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The author recommends that practitioners approach whether a trust is subject to state income tax in three steps: (1) identify which states' tax statutes, if any, potentially apply; (2) determine whether imposition of each tax would violate the Due Process Clause or the Commerce Clause; and (3) determine if the taxing state has jurisdiction over the trustee. [637]

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[637] *See Bernegger v. Thompson*, 884 N.W.2d 535 (Wis. Ct. App. 2016) (Wisconsin courts lack jurisdiction over Mississippi Department of Revenue).

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## b. Early U.S. Supreme Court Decisions

The following four early U.S. Supreme Court decisions, although they did not involve the income taxation of trusts, are relevant to this analysis.
• *Brooke v. City of Norfolk* (1928). [638] The Court held that a Virginia tax on the value of a trust created by the Will of a Maryland decedent that had Virginia beneficiaries but a Maryland trustee violated the Due Process Clause. [639]

• *Safe Deposit and Trust Company of Baltimore v. Virginia* (1929). [640] The Court held that a Virginia tax on the value of an inter vivos trust created by a Virginia domiciliary that had Virginia beneficiaries but a Maryland trustee violated the Due Process Clause. [641]

• *Guaranty Trust Co. v. Virginia* (1938). [642] The Court upheld Virginia's right to tax income received by a resident beneficiary from a nonresident trustee.

• *Greenough v. Tax Assessors of City of Newport* (1947). [643] The Court held that a municipality could impose a tax upon a resident trustee with respect to the trustee's interest in a trust.

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[638] 277 U.S. 27 (1928).

[639] *Id.* at 28–29.

[640] 280 U.S. 83 (1929).

[641] *Id.* at 92–93.

[642] 305 U.S. 19 (1938).

[643] 331 U.S. 486 (1947).

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## c. State Court Cases

Between 1964 and 1992, state courts decided seven pertinent cases. [644] For example, in *Mercantile-Safe Deposit & Trust Company v. Murphy* (1964), [645] the New York Court of Appeals (the highest court in the state) held that the Due Process Clause prohibited New York from taxing the accumulated income of an inter vivos trust (funded in part during life and in part by a pourover of assets under the decedent's Will)

that had no New York trustee, no New York assets, and no New York source income, even though the current discretionary beneficiary was a New York resident.

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[644] *Mercantile-Safe Deposit & Tr. Co. v. Murphy*, 203 N.E.2d 490 (N.Y. 1964); *Matter of Taylor v. State Tax Comm'n*, 445 N.Y.S.2d 648 (N.Y. App. Div. 1981); *Pennoyer v. Tax'n. Div. Dir.*, 5 N.J. Tax 386 (Tax Ct. 1983); *Potter v. Tax'n Div. Dir,* 5 N.J. Tax 399 (Tax Ct. 1983); *In re Swift*, 727 S.W.2d 880 (Mo. 1987); *Blue v. Dep't of Treasury*, 462 N.W.2d 762 (Mich. Ct. App. 1990); *Westfall v. Dir. of Revenue*, 812 S.W.2d 513 (Mo. 1991).

[645] 203 N.E.2d 490 (N.Y. 1964).

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Rightly or wrongly, the state income taxation of trusts changed with the U.S. Supreme Court's 1992 decision in *Quill Corporation v. North Dakota*. [646] There, the Court considered the constitutionality of North Dakota's use tax on an out-of-state mail-order business that had no outlets or sales representatives in the state. The Court found that a business did not need to have a physical presence in the state in order to permit the state to require it to collect use tax from its in-state customers under the minimum-contacts test of the Due Process Clause but that a physical presence in the state was required for a business to have "substantial nexus" with the taxing state under the Commerce Clause.

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[646] 504 U.S. 298 (1992).

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In *District of Columbia v. Chase Manhattan Bank* (1997), [647] the first relevant case decided after *Quill*, the District of Columbia Court of Appeals denied a $324,315 District of Columbia income tax refund claimed by the trustee under the Will of a resident of the District. The court, citing the Due Process Clause of the Fifth Amendment, held that the District of Columbia could base its income taxation of a trust on the domicile of the testator.

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[647] 689 A.2d 539 (D.C. 1997). The court noted that the considerations were the same under the Due Process Clauses of the Fifth and Fourteenth Amendments (*id.* at 541 n.6) and that the Commerce Clause did not apply because the District of Columbia is part of the federal government and therefore not subject to that limitation (*id.* at 542 n.7).

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The case dealt exclusively with the income taxation of a trust created by the Will of a District of Columbia decedent that had no trustees, no beneficiaries, and no assets in the District. Nevertheless, the case is sometimes cited erroneously to support the taxation of an inter vivos trust in the same circumstances. The court was careful to note, however, that it might not have upheld the District's right to tax an inter vivos trust, as follows: [648]

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[648] *Id.* at 547 n.11.

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We express no opinion as to the constitutionality of taxing the entire net income of inter vivos trusts based solely on the fact that the settlor was domiciled in the District when she died and the trust therefore became irrevocable. In such cases, the nexus between the trust and the District is arguably more attenuated, since the trust was not created by probate of the decedent's will in the District's courts. An irrevocable inter vivos trust does not owe its existence to the laws and courts of the District in the same way that the testamentary trust at issue in the present case does, and thus it does not have the same permanent tie to the District. In some cases the District courts may not even have principal supervisory authority over such an inter vivos trust. The idea of fundamental fairness, which undergirds our due process analysis, therefore may or may not compel a different result in an inter vivos trust context.

Similarly, in *Chase Manhattan Bank v. Gavin* (1999), [649] the Supreme Court of Connecticut denied the trustees' request under both the Due Process Clause and the Commerce Clause for Connecticut income tax refunds with respect to four testamentary trusts and one inter vivos trust. Even though *Gavin*'s constitutional analysis is wanting, it remains the law in Connecticut.

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[649] 733 A.2d 782 (Conn. 1999).

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But the following four recent taxpayer victories indicate that trusts can be successful in eliminating state taxation based on the residence of the testator or trustor pursuant to constitutional and other challenges.
• *Residuary Trust A v. Director, Division of Taxation* (2015). [650] A New Jersey intermediate appellate court held on nonconstitutional grounds that New Jersey could not tax the income of a testamentary trust for a year in which the trustee was a nonresident and all administration took place outside New Jersey because such taxation violated the square corners doctrine.

• *Linn v. Department of Revenue* (2013). [651] An Illinois appellate court held that the Due Process Clause prevented that state from taxing the income of an inter vivos trust created by an Illinois trustor for a year in which the trust had minimal Illinois contacts.

• *Fielding v. Commissioner of Revenue* (2017). [652] The Minnesota Tax Court held that Minnesota's imposition of income tax on the nonresident trustee of four trusts would violate the Due Process Clause of the U. S. Constitution even though the trustor of all four trusts and the current beneficiary of one of the trusts were domiciled in Minnesota.

• *McNeil v. Commonwealth* (2013). [653] A Pennsylvania intermediate appellate court held that the Commerce Clause prevented the Commonwealth from taxing the income of two inter vivos trusts created by a Pennsylvania resident for a year in which the trusts had no Pennsylvania trustees, assets, or source income, even though the trust had resident discretionary beneficiaries.

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[650] 28 N.J. Tax 541 (Super. Ct. App. Div. 2015), *aff'g,* 27 N.J. Tax 68 (Tax Ct. 2013). *See* Nenno, *Richard Nenno on the Taxpayer Victory in New Jersey Kassner Case: More Than One Way to Skin a Cat and Save State Income Taxes on Trusts*, LISI Est. Plan. Newsl. #2331 (Aug. 11, 2015), www.leimbergservices.com.

[651] 2 N.E.3d 1203, 1211 (Ill. App. Ct. 2013).

[652] 916 N.W.2d 323 (Minn. 2018), *aff'g*, 2017 BL 194423, 2017 WL 2484593 (Minn. Tax Ct. May 31, 2017). *See* Muse, *Court Holds Trust is Not Resident, Lacks Sufficient Contacts, 89 State Tax Notes* 389 (July 23, 2018).

[653] 67 A.3d 185, 198 (Pa. Commw. Ct. 2013).

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On June 21, 2018, the U.S. Supreme Court eliminated the physical-presence requirement for substantial nexus to justify sales taxation under the Commerce Clause in *South Dakota v. Wayfair, Inc*. [654] In the author's view, the *Wayfair* decision will have minimal impact on the state income taxation of trusts. [655] This is because a taxing state still must satisfy the yet-to-be-developed new substantial-nexus test and, as demonstrated by *McNeil*, the other three prongs of *Complete Auto Transit, Inc. v. Brady*. [656] Furthermore, *Linn* and *Fielding* show that a nonresident trustee may win under the Due Process Clause, which has not required physical presence since the *Quill* decision in 1992. [657] In fact, less than a month after the Court decided *Wayfair*, the Supreme Court of Minnesota affirmed the Minnesota Tax Court's decision for the taxpayer in *Fielding*.

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[654] 138 S. Ct 2080, 2099 (2018). *See* Thimmesch, Shanske & Gamage, *Wayfair: Substantial Nexuws and Undue Burden*, 89 State Tax Notes 447 (July 30, 2018); Reed, *What Is the New Constitutional Test After Wayfair?*, 89 State Tax Notes 335 (July 23, 2018); Calhoun & Kolarik, *Implications of the Supreme Court's Historic Decision in Wayfair*, 89 State Tax Notes 125 (July 9, 2018); Chamseddine, *U.S.Supreme Court Overturns Quill*, 88 State Tax Notes 1273 (June 25, 2018).

[655] *Accord*, Katzenstein & Pennell, *How Does South Dakota v. Wayfair Impact a State's Ability to Tax Undistributed Trust Income?*, LISI Inc. Tax Plan. Newsl. #148 (July 12, 2018), www.leimbergservices.com ("there does not appear to be a change in the standards that will apply in the future").

[656] *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274 (1977).

[657] *Quill Corp. v. North Dakota*, 504 U.S. 298 (1992).

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Given that two state appellate courts have held that the due process requirements are met by the domicile of the testator of a testamentary trust, practitioners should assume that testamentary trusts are likely to be valid subjects for income taxation by the state in which the testator was domiciled at death. In most states, no state action is involved in the creation of an inter vivos trust, however, even if that trust is revocable during the trustor's lifetime. The analysis of the Connecticut Supreme Court in *Gavin* would not appear to extend taxability to a trust where the only contact was the domicile of the trustor at the time the trust was created.

Finally, a nonresident trustee should not concede that a state has the power to tax the trust. It is true that a state has jurisdiction over a trustee whom it has appointed, [658] but there is no jurisdiction simply because a nonresident trustee files a resident trust tax return. [659] In addition, as discussed in IV.B.3., above, the U.S. Supreme Court has decided four cases since 2011 in which it held that personal jurisdiction did not exist over nonresident trustees.

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[658] *See Ohlheiser v. Shepherd*, 228 N.E.2d 210, 215 (Ill. App. Ct. 1967).

[659] *See Bernstein v. Stiller*, 2013 BL 172426, 2013 WL 3305219, at *4 (E.D. Pa. June 27, 2013); *Walker v. West Michigan Nat'l Bank & Tr.*, 324 F. Supp. 2d 529, 534 (D. Del. 2004).

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So far, this section has focused on the validity of state taxation based solely on the existence of a resident testator or trustor. Three recent state court decisions involve other aspects of the subject.

The first involved North Carolina, which purports to tax resident and nonresident trustees on income "that is for the benefit of a resident of this state." [660] In *Kimberley Rice Kaestner 1992 Family Trust v. North Carolina Department of Revenue* (2018), [661] the Supreme Court of North Carolina considered whether North Carolina could tax the accumulated income of a trust having a nonresident trustee but resident discretionary beneficiaries. The court held that imposition of the tax in the circumstances would violate the Due Process Clause of the federal constitution and a provision of the North Carolina constitution. [662]

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[660] N.C. Gen. Stat. § 105-160.2.

[661] 814 S.E.2d 43 (N.C. 2018), *aff'g*, 789 S.E.2d 645 (N.C. Ct. App. 2016), *aff'g*, 2015 NCBC 36, 2015 WL 1880607 (N.C. Sup. Ct. Apr. 23, 2015). *See* LaPiana, *North Carolina Tax Statute Held to Violate Due Process*, 45 Est. Plan. 42 (Sept. 2018); Muse, *Court Holds Trust is Not Resident, Lacks Sufficient Contacts*, 89 State Tax Notes 389 (July 23, 2018); Willens, *North Carolina Cannot Tax the Income of "Foreign" Trust*, 128 Daily Tax Rep. 9 (July 3, 2018); Fox, *North Carolina Supreme Court Decalres Tax on Accumulated Trust Income Unconstitutional*, 122 Daily Tax Rep. 14 (June 25, 2018); Muse, *Trust Lacks Minimum Contacts to Tax, State High Court Holds*, 88 State Tax Notes 1248 (June 18, 2018).

[662] 814 S.E.2d at 51.

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This case suggests that a North Carolina testator or trustor may eliminate North Carolina income tax on accumulated ordinary income and capital gains by using a non-North Carolina trustee. The case's reasoning should extend to Georgia as well because that state taxes in a similar manner. [663]

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[663] *See* Ga. Code Ann. § 48-7-22(a)(1)(C).

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The second case involved Massachusetts, which classifies an inter vivos nongrantor trust created by an inhabitant of the Commonwealth as a resident trust if, inter alia, a trustee is also an inhabitant. [664] The Supreme Judicial Court of Massachusetts held in *Bank of America, N.A. v. Commissioner of Revenue* that: [665]

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[664] Mass. Gen. L. ch. 62, § 10(c).

[665] 54 N.E.3d 13, 21 (Mass. 2016).

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We interpret the three interrelated statutes that apply in this case, § § 1(f)(2), 10, and 14, to mean that a corporate trustee will qualify as an "inhabitant" of the Commonwealth within the meaning and for the purposes of these statutes if it: (1) maintains an established place of business in the Commonwealth at which it abides, i.e., where it conducts its business in the aggregate for more than 183 days of a taxable year; and (2) conducts trust administration activities within the Commonwealth that include, in particular,

material trust activities relating specifically to the trust or trusts whose tax liability is at issue.

Under the above test, a Massachusetts trustor may escape Massachusetts income tax on a trust's accumulated ordinary income and capital gains by appointing a non-Massachusetts trustee.

The third case was *T. Ryan Legg Irrevocable Trust v. Testa* decided by the Supreme Court of Ohio. [666] The court held that the trust in question was a nonresident trust rather than a resident trust [667] and parsed the categories of Ohio taxable income. [668]

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[666] 75 N.E.3d 184 (Ohio 2016).

[667] *Id.* at 197.

[668] *Id.* at 193–194.

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## 4. Specific State Considerations

### a. New York

In 2017, the top rate for a nongrantor trust created by a resident of New York State (but not of New York City) was 8.82%, and that rate applied to taxable income over $1,077,550. [669] If the creator resided in New York City, then the trust was also subject to New York City tax at a rate of up to 3.876%, with that rate applying to income over $50,000. [670] Hence, a New York City resident trust was taxable at a rate of up to 12.696%, and that rate applied to taxable income over $1,077,550. N.Y. Tax Law § 605(b)(3) taxes trusts created by New York testators and trustors, but subparagraph (D) of N.Y. Tax Law § 605(b)(3), added in 2003 and effective January 1, 1996, creates an exemption for an Exempt Resident Trust. The relevant statutory language is: [671]

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[669] N.Y. Tax Law § 601(c)(1)(A). For planning considerations for all 43 states that tax trust income, see 869 T.M., *State Income Taxation of Trusts*. *See also* Noonan & Eberl, *Trust Us: New York's Residency Rules for Trusts Are Complicated*, 81 State Tax Notes 631 (Aug. 22, 2016); Nenno, *Planning for New York Trusts to Escape State Income Tax*, 42 Est. Plan. 12 (Oct. 2015).

[670] N.Y. Tax Law § 1304(a)(3)(A), § 1304-B(a)(1)(ii); Admin. Code City of N.Y. § 11-1701(a)(3)(A), § 11-1704.1; instructions to 2017 N.Y. Form IT-205 at 10, 17. *See* N.Y. TSB-M-10(7)I, 2010 State Tax Today 161-19 (Aug. 17, 2010), available at www.tax.ny.gov/pdf/memos/income/m10_7i.pdf.

[671] N.Y. Tax Law § 605(b)(3)(D)(i).

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(D)(i) Provided, however, a resident trust is not subject to tax under this article if all of the following conditions are satisfied:

(I) all the trustees are domiciled in a state other than New York;

(II) the entire corpus of the trusts, including real and tangible property, is located outside the state of New York; and

(III) all income and gains of the trust are derived from or connected with sources outside of the state of New York, determined as if the trust were a non-resident trust.

(ii) For purposes of item (II) of clause (i) of this subparagraph, intangible property shall be located in this state if one or more of the trustees are domiciled in the state of New York.

The above provision codifies the holdings of the *Taylor* [672] and *Murphy* [673] cases cited in V.E.3., above, which were later implemented by administrative regulations. Commentators have succinctly summarized the reach of the New York fiduciary income tax as follows: [674]

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[672] *Matter of Taylor v. State Tax Comm'n*, 445 N.Y.S.2d 648 (N.Y. Sup. Ct. 1981).

[673] *Mercantile-Safe Deposit & Tr. Co. v. Murphy*, 203 N.E.2d 490 (N.Y. 1964).

[674] Michaels & Twomey, *How, Why, and When to Transfer the Situs of a Trust*, 31 Est. Plan. 28, 29 (Jan. 2004). *See*, *e.g.*, N.Y. TSB-A-10(4)I, 2010 WL 2557532 (June 8, 2010), www.tax.ny.gov/pdf/advisory_opinions/income/a10_4i.pdf (trust became nonresident as of date trustee ceased to be New York domiciliary); *Matter of Joseph Lee Rice III Family 1992 Tr.*, DTA No. 822892 (Nov. 4, 2010), https://www.dta.ny.gov/pdf/archive/Determinations/822892.det.pdf (Division of Tax Appeals denied trust refund for closed years during which trustee had ceased to be New York resident but continued to use New York office address on returns).

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Essentially, New York will not tax a trust that has no New York trustees, no New York assets, and no New York source income.

Effective January 1, 2010, a resident trust not subject to personal income tax under N.Y. Tax Law § 605(b)(3)(D) must file an informational return. [675]

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[675] N.Y. Tax Law § 658(f)(2); N.Y. TSB-A-11(4)I, 2011 WL 7113861 (July 27, 2011), www.tax.ny.gov/pdf/advisory_opinions/income/a11_4i.pdf; N.Y. TSB-M-10(5)I, 2010 State Tax Today 145-10 (July 23, 2010), www.tax.ny.gov/pdf/memos/income/m10_5i.pdf.

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Numerous cases have held that a trust that meets the above requirements at the outset is not taxable and that a trust ceases to be taxable upon the death, resignation, or move of the last New York resident trustee. [676] The New York Tax Services Bureau has ruled that an adviser, committee member, or protector will be treated as a trustee under certain circumstances [677] and that the residence of the donor of a nongeneral power of appointment and of a donee of a general power of appointment determines taxability. [678]

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[676] *See, e.g.*, *Matter of Joseph Lee Rice III Family 1992 Tr.*, DTA No. 822892 (Nov. 4, 2010), www.nysdta.org/Determinations/822892.det.pdf (trustee moved); N.Y. TSB-A-11(4)I, 2011 WL 7113861 (July 27, 2011), www.tax.ny.gov/pdf/advisory_opinions/income/a11_4i.pdf (trustee resigned); N.Y. TSB-A-10(4)I, 2010 WL 2557532 (June 8, 2010), www.tax.ny.gov/pdf/advisory_opinions/income/a10_4i.pdf (trustee died).

[677] N.Y. TSB-A-04(7)I, 2004 N.Y. Tax Lexis 259 (Nov. 12, 2004), www.tax.ny.gov/pdf/advisory_opinions/income/a04_7i.pdf.

[678] N.Y. TSB-A-03(6)I, 2003 WL 22970581 (Nov. 21, 2003), www.tax.ny.gov/pdf/advisory_opinions/income/a03_6i.pdf.

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The 2014–2015 New York budget bill [679] now requires New York State and New York City residents to pay tax on accumulation distributions from Exempt Resident Trusts [680] and imposes reporting requirements on the trustees of such trusts. [681] Nevertheless, New York testators and trustors should continue to plan their trusts to qualify as Exempt Resident Trusts. This planning should *not* cease in light of the addition of the "throwback" tax rules because:
• The throwback tax does not extend to capital gains and accumulations during minority;

• Tax rates might go down in the future;

• Beneficiaries might leave New York;

• Distributions might go to non-New York beneficiaries. [682]

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[679] 2014 N.Y. Laws 59, Part I (Mar. 31, 2014).

[680] 2014 N.Y. Laws 59, Part I, § 1, § 6 (Mar. 31, 2014).

[681] 2014 N.Y. Laws 59, Part I, § 4 (Mar. 31, 2014).

[682] *See* Steiner, *Coping With the New York Tax Changes Affecting Estates and Trusts*, LISI Est. Plan. Newsl. #2225 (May 19, 2014), www.leimbergservices.com; Mensch & Karibjanian, *New York Tax Changes for Estates and Trusts*, LISI Est. Plan. Newsl. #2222 (May 8, 2014), www.leimbergservices.com.

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## b. New Jersey

New Jersey follows New York's approach. [683] The top rate for a New Jersey resident trust in 2017 was 8.97% (that rate applied to taxable income over $500,000). [684] The relevant part of the instructions for the 2017 New Jersey Gross Income Tax Fiduciary Return provides that: [685]

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[683] *See* N.J. Stat. Ann. § 54A:1-2(o).

[684] N.J. Stat. Ann. § 54A:2-1(b)(5).

[685] Instructions to 2017 NJ-1041 at 1 (emphasis in original).

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A resident estate or trust is not subject to New Jersey tax if it:
• Does not have any tangible assets in New Jersey;

• Does not have any income from New Jersey sources; and

• Does not have any trustees or executors in New Jersey.

However, the fiduciary must file Form NJ-1041 for such estate or trust, enclose a statement certifying that the estate or trust is not subject to tax, and check the box on Line 26.

The *Residuary Trust A* decision in New Jersey discussed in V.E.3., above, indicates that planning to minimize the state's income tax is viable. [686]

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[686] *Residuary Trust A v. Dir., Div. of Taxation*, 28 N.J. Tax 541 (N.J. Super. Ct. App. Div. 2015), *aff'g*, 27 N.J. Tax 68 (Tax Ct. 2013).

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## c. Connecticut

Connecticut's approach is also similar to New York's. Accordingly, Connecticut taxes the income of the following types of resident trusts: [687]

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[687] Conn. Gen. Stat. Ann. § 12-701(a)(4)(C), § 12-701(a)(4)(D).

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(C) a trust, or a portion of a trust, consisting of property transferred by will of a decedent who at the time of his death was a resident of this state, and (D) a trust, or a portion of a trust, consisting of the property of (i) a person who was a resident of this state at the time the property was transferred to the trust if the trust was then irrevocable, (ii) a person who, if the trust was revocable at the time the property was transferred to the trust, and has not subsequently become irrevocable, was a resident of this state at the time the property was transferred to the trust or (iii) a person who, if the trust was revocable when the property was transferred to the trust but the trust has subsequently become irrevocable, was a resident of this state at the time the trust became irrevocable.

For inter vivos trusts, the statute apportions the tax based on the number of resident and nonresident noncontingent beneficiaries. [688] In 2017, the tax rate was 6.99%. [689] In the *Gavin* case mentioned in V.E.3., above, [690] the Connecticut Supreme Court confirmed that the state could tax a testamentary trust solely because the testator was a resident at death and that the state could tax an inter vivos trust created by a resident if the sole noncontingent beneficiary was a resident. Nevertheless, it might be possible to plan around *Gavin* in certain circumstances.

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[688] Conn. Gen. Stat. Ann. § 12-701(a)(4).

[689] Conn. Gen. Stat. Ann. § 12-700(a)(9)(E), § 12-700(a)(10).

[690] *Chase Manhattan Bank v. Gavin*, 733 A.2d 782 (1999).

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## d. Delaware

A trust is a resident trust in Delaware if it was created by the Will of a Delaware resident or by an inter vivos instrument created by such a resident or if the trust has a resident trustee. [691] In 2017, the top rate was 6.60% on income over $60,000. [692] The trustee of a Delaware resident trust may deduct income (including capital gains) set aside for future distribution to nonresident beneficiaries. [693] In calculating comparable deductions, some states deem all unknown or unascertained beneficiaries as residents, [694] but Delaware makes this determination based on the residences of relevant existing beneficiaries on the last day of the tax year. [695] Because of the foregoing deduction, few Delaware trusts created by nonresidents pay Delaware income tax.

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[691] Del. Code Ann. tit. 30, § 1601(8).

[692] Del. Code Ann. tit. 30, § 1102(a)(14).

[693] Del. Code Ann. tit. 30, § 1636.

[694] *See, e.g.*, Mass. Gen. L. ch. 62, § 10(a).

[695] Del. Code Ann. tit. 30, § 1636(b).

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### e. Illinois

The combination of the 4.35% net-income tax and the 1.5% net-replacement tax meant that Illinois taxed the net income of nongrantor trusts at 5.85% in 2017. [696] The rate is 6.45% for 2018 and later years. [697] Also following the New York pattern, Illinois defines "resident trust" as follows: [698]

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[696] 35 ILCS 5/201(a), 35 ILCS 5/201(b)(5.3), 35 ILCS 5/201(c) and 35 ILCS 5/201(d). *See* Ill. Dep't of Rev. Informational Bulletin FY 2015-09 (Jan. 2015), www.revenue.state.il.us/Publications/Bulletins/2015/FY-2015-09.pdf.

[697] 35 ILCS 5/201(a), (b)(5.4).

[698] 35 ILCS 5/1501(a)(20)(C)–35 ILCS 5/1501(a)(20)(D).

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(C) A trust created by a will of a decedent who at his death was domiciled in this State; and

(D) An irrevocable trust, the grantor of which was domiciled in this State at the time such trust became irrevocable. For purpose of this subparagraph, a trust shall be considered irrevocable to the extent that the grantor is not treated as the owner thereof under Sections 671 through 678 of the Internal Revenue Code.

The 2013 *Linn* case summarized in V.E.3., above, suggests that it is now possible to take steps to escape the state's income tax on trusts. [699]

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[699] *Linn v. Dep't of Revenue*, 2 N.E.3d 1203, 1211 (Ill. App. Ct. 2013).

## f. California

Thanks to California's Proposition 30 [700] (which increased the top marginal rate to 12.30%) and the additional 1.00% Mental Health Services Tax, [701] a California resident trust was taxed in 2017 at rates up to 13.30% (the top rate began at taxable income over $1 million [702]) on two bases: [703]

[700] Cal. Const. Art. XIII, § 36(f)(2).

[701] Cal. Rev. & Tax. Code § 17043(a).

[702] Cal. Rev. & Tax. Code § 17041(a)(1), § 17041(e). § 17041(h).

[703] Cal. Rev. & Tax. Code § 17742(a). *See* Cal. Rev. & Tax. Code § 17743–§ 17744.

The tax applies to the entire taxable income...of a trust, if the fiduciary or beneficiary (other than a beneficiary whose interest in such trust is contingent) is a resident, regardless of the residence of the settlor.

The law provides rules for determining the residence of a corporate fiduciary [704] and for other purposes. [705] Even if a Californian is receiving current income distributions from a trust that has a non-California trustee, the trustee should be able to defer or eliminate California taxation of accumulated ordinary income and capital gains if the distribution of such income and gains is within the trustee's discretion. [706] In this connection, in a 2006 Technical Advice Memorandum, the California Franchise Tax Board ruled that:
1. A resident beneficiary of a discretionary trust has a noncontingent interest in the trust only as of the time, and to the extent of the amount of income, that the trustee actually decides to distribute;

2. Accumulated income is taxable to a trust when the income is distributed or distributable to a resident beneficiary;

3. The conclusion in point 1 above is unaffected if the trustee may or does distribute principal (capital gains) to the current beneficiary. [707]

[704] Cal. Rev. & Tax. Code § 17742(b).

[705] Cal. Rev. & Tax. Code § 17745.

[706] Cal. Franchise Tax Board, TAM 2006-0002 (Feb. 17, 2006), www.ftb.ca.gov/law/Technical_Advice_Memorandums/2006/20060002.pdf.

[707] Cal. Franchise Tax Board, TAM 2006-0002 (Feb. 17, 2006), www.ftb.ca.gov/law/Technical_Advice_Memorandums/2006/20060002.pdf. *Accord In the Matter of the Appeal of: Yolanda King Family Tr. and Mary L. Tunney Junior Tr.*, 2007 WL 3275358 (Cal. St. Bd. Eq. Oct. 4, 2007).

## 5. Planning, Ethical, and Other Issues

The state fiduciary income tax implications of a trust should be considered in the planning stage because it is much easier not to pay a tax in the first place than to obtain a refund. In some instances, it will be clear that a trust will not be taxable. In other situations, however, it will not be clear whether the tax applies to the trust or, if it does, whether imposition of the tax is valid under the circumstances. The ABA Committee on Ethics and Professional Responsibility has advised that: [708]

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[708] ABA Comm. on Ethics and Prof'l Responsibility, Formal Op. 85-352 (1985). *See* Ventry, *Lowering the Bar: ABA Formal Opinion 85-352*, 112 Tax Notes 69 (July 3, 2006).

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[A] lawyer may advise reporting a position on a return even where the lawyer believes the position probably will not prevail, there is no "substantial authority" in support of the position, and there will be no disclosure of the position in the return. However, the position to be asserted must be one which the lawyer in good faith believes is warranted in existing law or can be supported by a good faith argument for an extension, modification or reversal of existing law. This requires that there is some realistic possibility of success if the matter is litigated. In addition, in his role as advisor, the lawyer should refer to potential penalties and other legal consequences should the client take the position advised.

Estates, Gifts and Trusts Portfolios
Trusts
Portfolio 867-2nd: Choosing a Domestic Jurisdiction for a Long-Term Trust
Detailed Analysis
V. Factors to Consider in Selecting a Trust State

## F. Investment Return

All U.S. jurisdictions now follow the prudent-investor rule. As shown in Worksheet 6, below, seven states have a stand-alone statute and 43 states and the District of Columbia have enacted the 1994 Uniform Prudent Investor Act (UPIA), [709] which includes the following components:
(1) In managing investments, a trustee must invest as a prudent person would in the circumstances; [710]

(2) A trustee may acquire any type of investment, and each investment is considered as part of an overall investment strategy; [711]

(3) The propriety of a particular investment is assessed on what the trustee knew or should have known when it made the investment, and any determination of liability must consider the performance of the whole Portfolio not just the particular investment; [712] and

(4) The governing instrument may expand or restrict the trustee's investment responsibilities. [713]

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[709] The text of the UPIA and a list of jursidictions that have enacted it may be viewed at https://my.uniformlaws.org/committees/community-home?CommunityKey=58f87d0a-3617-4635-a2af-9a4d02d119c9. For a detailed discussion of the UPIA, see 861 T.M., *Trustee Investments.*

[710] UPIA § 2(a) (1994).

[711] UPIA § 2(e), § 2(b) (1994).

[712] UPIA § 8, § 2(b) (1994).

[713] UPIA § 1(b) (1994). *See Shriners Hosps. for Children v. First N. Bank of Wyo.*, 373 P.3d 392, 411 (Wyo. 2016) ("We find no error in the district court's conclusion that First Northern Bank did not breach a fiduciary duty to diversify trust investments by rejecting Shriners' demands to sell the ranch or terminate the Trust").

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Because so many states have enacted the UPIA, most state statutes are quite similar. But, some differences do exist. For example, Delaware law permits a trustee to consider beneficiaries' other trust interests and resources in establishing the investment policy for a trust and no longer requires the trustee to determine such a policy for each trust without regard to other factors. [714] In addition, to recognize younger beneficiaries' desire to participate in impact investing, Delaware law now authorizes trustees to "engage in sustainable investing strategies that align with the beneficiaries' social, environmental, governance or other values or beliefs." [715] The author understands that Illinois is developing a similar rule.

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[714] Del. Code Ann. tit. 12, § 3302(c).

[715] Del. Code Ann. tit. 12, § 3302(a). *See* Del.Code Ann. tit. 12, § 3303(a) ("[T]he terms of a governing instrument may expand, restrict, eliminate, or othrwise vary any laws of general application to fiduciaries, trusts and trust administration, including, but not limited to, any such laws pertaining to: . . . (4) The manner in which a fiduciary should invest assets, including whether to engage in one or more sustainable or socially responsible investment strategies, in addition to, or in place of, other investment strategies, with or without regard to investment performance").

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## G. Division of Responsibilities

### 1. Introduction

Clients sometimes want to appoint a corporate trustee but also want to have a separate an adviser, committee, or protector (not the corporate trustee) control certain trust decisions. [716] Here are a few examples:

• A client might want to fund an inter vivos dynasty trust with stock in the family company but wants to continue to make decisions regarding the purchase, sale, and voting of such stock;

• A family might have a long-standing relationship with a successful money manager and wants that manager (not the trustee) to make investment decisions for trust assets;

• A client might want someone other than the trustee to decide when to make income or principal distributions to beneficiaries.

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[716] *See* Flubacher & Brown, *If You Can't Beat 'Em, Join 'Em*, 157 Tr. & Est. 32 (Nov. 2018); Nenno, *Good Directions Needed When Using Directed Trusts*, 42 Est. Plan. 12 (Dec. 2015); Redd, *Directed Trusts — Who's Responsible?,* 154 Tr. & Est. 11 (Sept. 2015); Flubacher, *Directed Trusts: Panacea or Plague?,* 154 Tr. & Est. 4 (Feb. 2015).

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In a 2008 article, a Kentucky attorney observed that: [717]

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[717] Gilman, *Effective Use of Trust Advisors Can Avoid Trustee Problems*, 35 Est. Plan. 18, 23 (Mar. 2008) (emphasis in original).

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Despite the fact that there is no perfect solution to the question of trustee appointment and supervision, it is the author's opinion that the best course of action for our clients and their families is to appoint a single trustee—a trustee who is trained for the job—preferably a corporate institution, who will be responsible for all trust administration issues, *and* then appoint an advisor or a committee of advisors who will provide the corporate fiduciary with the necessary insight into the clients' family members and will provide meaningful oversight of the trustee's administrative services.

The combination of a corporate trustee with a competent group of advisors should produce the best results for clients' families. The approach combines the strength of the corporate trust department and the personal touch that we humans demand and expect. While the use of an advisory committee might not solve all the problems, the recommended action has substantial merit and should be thoroughly evaluated with clients.

In these situations, the client wants to minimize the trustees' involvement in such decisions and wants such trustees to lower their fees to reflect their reduced duties. Unfortunately, depending on the state law that governs these issues, even if a trust (directed trust) directs the trustee (directed trustee) to make investments or distributions on the direction of someone else (directing person) and relieves the trustee from liability for following such directions, such a trustee might have considerable monitoring or other responsibilities. Thus, the trustee might be placed in the unenviable position of being pressured to charge low fees while being subject to substantial potential liability.

The terminology for multiparticipant trusts can best be described as confused. In states such as Delaware, investment advisers have been part of trust arrangements since early in the twentieth century. Thus, the 1958 U.S. Supreme Court decision in *Hanson v. Denckla* [718] considered a revocable trust with investment advisers created in 1935, [719] and a 1965 Harvard Law Review article analyzed the adviser concept. [720] In contrast, the new player in multiparticipant trusts in many states is the protector, a role that has immigrated to this country from abroad over the past few decades.

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[718] 357 U.S. 235 (1958).

[719] *Id.* at 238–239.

[720] *Note: Trust Advisers*, 78 Harvard L. Rev. 1230 (1965).

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This section V.G., uses the following definitions:
• *Direction investment adviser* — an individual or entity (other than a trustee) who directs a trustee on how to buy and sell trust assets, vote stock, borrow money, and make other investment decisions;

• *Direction distribution adviser* — an individual or entity (other than a trustee) who directs a trustee on when to distribute income and principal to beneficiaries and, in many cases, when to exercise a decanting power, a power to adjust between income and principal, and/or a power to convert an income trust into a unitrust;

• *Protector* — an individual or entity (other than a trustee) who may amend the trust, replace trustees and advisers, receive trust information in "quiet" trusts, and/or carry out other supervisory duties

The author will not consider the consent trust — a trust in which a trustee makes investment, distribution, or other decisions only after obtaining the consent of an adviser, committee, etc., nor will the author cover the delegated trust — a trust in which the trustee, pursuant to the governing instrument or state law, hires someone to assist with the trust's administration and in which the trustee retains potential liability for an agent's activities.

This discussion refers to provisions of the UTC and the UPC. Because tates and the District of Columbia have often enacted these provisions in forms different from the model forms, attorneys should carefully study the relevant statutes of all pertinent jurisdictions in a particular case.

## 2. The State Statutes

## a. UTC Approach

The UTC differentiates between multiparticipant trusts that have two or more trustees and multiparticipant

trusts that have a single trustee and advisers, protectors, committees, etc.

The multitrustee arrangement is covered by UTC § 703, [721] under which:
• "A cotrustee must participate in the performance of a trustee's function unless...the cotrustee has properly delegated the performance of the function to another trustee"; [722]

• "A trustee may not delegate to a cotrustee the performance of a function the settlor reasonably expected the trustees to perform jointly"; [723]

• "Each trustee shall exercise reasonable care to:

• Prevent a cotrustee from committing a serious breach of trust; and

• Compel a cotrustee to redress a serious breach of trust." [724]

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[721] UTC § 703 (amended 2018).

[722] UTC § 703(c) (amended 2018).

[723] UTC § 703(e) (amended 2018).

[724] UTC § 703(g) (amended 2018).

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The above continuing responsibilities make § 703 unsuitable for directed trusts.

The other arrangement is covered by subsection (b) of UTC § 808, which provides: [725]

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[725] UTC § 808(b) (amended 2018) (emphasis added).

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If the terms of a trust confer upon a person other than the settlor of a revocable trust power to direct certain actions of the trustee, the trustee shall act in accordance with an exercise of the power *unless the attempted exercise is manifestly contrary to the terms of the trust or the trustee knows the attempted exercise would constitute a serious breach of a fiduciary duty that the person holding the power owes to the beneficiaries of the trust*.

Section 75 of the *Third Restatement of Trusts* contains similar rules. [726]

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[726] *Restatement (Third) of Trusts* § 75 (2007).

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Section 808(b) and § 75 are not comforting to directed trustees. This is because a directed trustee must devote considerable resources to ensure that the directing person's action is not "manifestly contrary to the terms of the trust" or "a serious breach of a fiduciary duty." Section 808's Comment describes this

situation as, “minimal oversight responsibility,” but investment and trust officers who provide such oversight have assured the author that it would be far more challenging to review someone else's investment and distribution decisions than to make those decisions themselves. The Comment to § 808 does contemplate that the governing instrument may further restrict the directed trustees’ responsibilities, however. [727]

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[727] UTC § 808 cmt. (amended 208).

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### b. Protective Approach

At the time of this writing, 31 states afford more protection to directed trustees than UTC § 808(b) and *Restatement* § 75 provide. For example, a directed trustee of a Delaware trust is liable for following a distribution or investment direction only if such a trustee engages in wilful misconduct.

### c. No Statute

A few states, including California, Connecticut, and New York, currently have no directed trust statute, and the effectiveness of directed trust language in trusts governed by the laws of these states is unpredictable. In New York, for instance, one case respected a directed trust arrangement, [728] whereas a later case did not. [729] Worksheet 7, below, contains citations for the foregoing statutes.

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[728] *Matter of Rubin*, 540 N.Y.S.2d 944 (N.Y. Sur. Ct. Nassau Cty. 1989), *aff'd*, 570 N.Y.S.2d 996 (N.Y. App. Div. 1991).

[729] *Matter of Rivas*, 958 N.Y.S.2d 648 (N.Y. Sur. Ct. Monroe Cty. 2011), *aff'd*, 939 N.Y.S.2d 918 (N.Y. App. Div. 2012).

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## 3. Delaware's Experience

Delaware's long-standing directed trust law permits someone other than the trustee to make distribution and investment decisions for particular assets (e.g., closely held stock) or with the hope of maximizing the trust's investment performance; the law also makes it clear that a trustee may follow the direction of an adviser who is authorized by the governing instrument to provide such direction without breaching the trustee's fiduciary responsibility. [730] To recognize this diminished responsibility, Delaware corporate trustees customarily charge less to administer directed trusts than trusts over which they have investment duties.

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[730] Del. Code Ann. tit. 12, § 3313(b). Perhaps reflecting its early adoption, the Delaware statute uses “adviser” rather than “advisor,” which is the norm elsewhere.

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The primary rule for directed trusts currently reads as follows: [731]

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[731] Del. Code Ann. tit. 12, § 3313(b) (emphasis added).

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If a governing instrument provides that a fiduciary is to follow the direction of an adviser or is not to take specified actions except at the direction of an adviser, and the fiduciary acts in accordance with such a direction, *then except in cases of wilful misconduct on the part of the fiduciary so directed*, the fiduciary shall not be liable for any loss resulting directly or indirectly from any such act.

The term *wilful misconduct* is defined as follows: [732]

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[732] Del. Code Ann. tit. 12, § 3301(g).

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The term 'wilful misconduct' shall mean intentional wrongdoing, not mere negligence, gross negligence or recklessness and 'wrongdoing' means malicious conduct or conduct designed to defraud or seek an unconscionable advantage.

A directed trustee is relieved from monitoring and related duties in the following way: [733]

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[733] Del. Code Ann. tit. 12, § 3313(e).

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Whenever a governing instrument provides that a fiduciary is to follow the direction of an adviser with respect to investment decisions, distribution decisions, or other decisions of the fiduciary or shall not take specified actions except at the direction of an adviser, then, except to the extent that the governing instrument provides otherwise, the fiduciary shall have no duty to:

(1) Monitor the conduct of the adviser;

(2) Provide advice to the adviser or consult with the adviser; or

(3) Communicate with or warn or apprise any beneficiary or third party concerning instances in which the fiduciary would or might have exercised the fiduciary's own discretion in a manner different from the manner directed by the adviser.

Absent clear and convincing evidence to the contrary, the actions of the fiduciary pertaining to matters within the scope of the adviser's authority (such as confirming that the adviser's directions have been carried out and recording and reporting actions taken at the adviser's direction), shall be presumed to be administrative actions taken by the fiduciary solely to allow the fiduciary to perform those duties assigned to the fiduciary under the governing instrument and such administrative actions shall not be deemed to constitute an undertaking by the fiduciary to monitor the adviser or otherwise participate in actions within the scope of the adviser's authority.

The statute recognizes the protector and describes protector powers as follows: [734]

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[734] Del. Code Ann. tit. 12, § 3313(f).

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For purposes of this section, the term “adviser” shall include a “protector” who shall have all of the power and authority granted to the protector by the terms of the governing instrument, which may include but shall not be limited to:

(1) The power to remove and appoint trustees, advisers, trust committee members, and other protectors;

(2) The power to modify or amend the governing instrument to achieve favorable tax status or to facilitate the efficient administration of the trust; and

(3) The power to modify, expand, or restrict the terms of a power of appointment granted to a beneficiary by the governing instrument.

The statute defines an “investment decision.” [735] The statute also specifies that an adviser or protector is a fiduciary unless the governing instrument provides otherwise. [736] In *IMO Ronald J. Mount Irrevocable Dynasty Trust* (2017), [737] the Delaware Court of Chancery confirmed that a protector may serve in a nonfiduciary capacity under Delaware law. The court wrote: [738]

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[735] Del. Code Ann. tit. 12, § 3313(d).

[736] Del. Code Ann. tit. 12, § 3313(a).

[737] *IMO Ronald J. Mount Irrevocable Dynasty Tr.*, 2017 BL 331356, 2017 WL 4082886 (Del. Ch. Sept. 7, 2017).

[738] *Id.* at *7–8 (footnotes and internal quotation marks omitted).

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[U]nder the clear and unambiguous terms of the Dynasty Trust Instrument, the Trust Protector serves in a non-fiduciary capacity. Specifically, the Trust Instrument states that “the Trust Protector, acting as such, shall serve in a non-fiduciary capacity. A settlor's decision to allow the trust protector to serve in a non-fiduciary capacity is valid and will be enforced under Delaware law. The public policy of our State, as articulated by the General Assembly, is to give maximum effect to the principle of freedom of disposition and to the enforceability of governing instruments. As relevant here, 12 Del. C. § 3313(a) provides that the governing instrument may provide that any such adviser (including a protector) shall act in a non-fiduciary capacity.

Here, Ronald, as Settlor of the Dynasty Trust, clearly and unambiguously provided that the Trust Protector would fulfill that role in a non-fiduciary capacity.

An unreported 2004 case that is summarized in V.G.4.b., below, upheld the Delaware statute. [739]

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[739] *Duemler v. Wilmington Tr. Co.*, 2004 BL 31983, 2004 WL 5383927 (Del. Ch. Nov. 24, 2004). Delaware courts give unpublished opinions substantial precedential weight (*Crystallex Int'l Corp. v. Petroleos De Venezuela, S.A.*, 879 F.3d 79, 85 n.8 (3d Cir. 2018).

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Effective in 2017, Delaware has a comparable structure for directed trusts in which a trustee directs another trustee. [740]

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[740] Del. Code Ann. tit. 12, § 3313(a).

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## 4. Case Law

### a. Introduction

To the author's knowledge, only two courts have decided whether a directed trust statute afforded protection to a directed trustee.

### b. Rollins v. Branch Banking and Trust Company of Virginia (2001)

In *Rollins v. Branch Banking and Trust Company of Virginia*, [741] a Virginia trial court held that a trustee was not liable for the $25 million loss caused by the retention of stock as directed by the beneficiaries. The court did not dismiss the beneficiaries' claim that the trustee had breached a duty to warn them about the deteriorating condition of trust investments, however, and the case was settled on this issue. The case's precedential value is uncertain because Virginia has revised its directed trust statute since it was issued. In light of *Rollins*, several states have modified their statutes to absolve directed trustees of monitoring and other duties.

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[741] 56 Vir. Cir. 147 2001 WL 34037931 (Va. Cir. Ct. Apr. 30, 2001).

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### c. Duemler v. Wilmington Trust Company (2004)

In *Duemler v. Wilmington Trust Company*, [742] a Delaware vice chancellor ruled that a corporate trustee was not liable for the failure of a sophisticated investment adviser (a securities lawyer in this case) to direct the trustee on an investment decision where the trustee forwarded relevant information to the adviser. Vice Chancellor Strine held: [743]

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[742] *Duemler v. Wilmington Tr. Co.*, 2004 BL 31983, 2004 WL 5383927 (Del. Ch. Nov. 24, 2004).

[743] *Id.* at *1.

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The Court...finds that section 3313(b) of title 12 of the Delaware Code insulates fiduciaries of a Delaware trust from liability associated with any loss to the trust where a governing instrument provides that the fiduciary is to follow the direction of an advisor, the fiduciary acts in accordance with such direction and the fiduciary did not engage in willful misconduct. The trust agreement involved in this case appointed Plaintiff as the investment advisor to the Trust and, at all times, Plaintiff made all of the investment decisions for the Trust, including not to tender the securities in the Exchange Offer. In connection with

Plaintiff's decision not to tender the securities in the Exchange Offer, Wilmington Trust acted in accordance with Plaintiff's instructions, did not engage in willful misconduct by not forwarding the Exchange Offer materials to Plaintiff and had no duty to provide information or ascertain whether Plaintiff was fully informed of all relevant information concerning the Exchange Offer. Accordingly, 12 Del. C. § 3313(b) insulates Wilmington Trust from all liability for any loss to the Trust resulting from plaintiff's decision not to tender the securities in the Exchange Offer.

### d. Commentary

Commenting attorneys wrote in 2012 that: [744]

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[744] Covey & Hastings, *Power to Direct Trustee Action: Virginia Law*, Prac. Drafting, July 2012, 10910, 10913.

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While the Delaware Chancery Court may well be willing to construe its directed trust statute in a manner contemplated by the legislature, it remains to be seen how other state courts will interpret similar 'bifurcation' type statutes, including the degree of protection conveyed by them.

## 5. Uniform Directed Trust Act

In 2014, the ULC initiated a project (for which the author was an observer) to draft a Uniform Directed Trust Act (UDTA), [745] which was approved by the ULC in the summer of 2017. The drafting committee considered various options in deciding what residuary standard of liability, if any, should be imposed on a directed trustee: [746]

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[745] The text of the UDTA and a list of jurisdictions that have enacted the UDTA may be viewed at https://my.uniformlaws.org/committees/community-home?CommunityKey=ca4d8a5a-55d7-4c43-b494-5f8858885dd8.

[746] UDTA § 9 cmt. (Unif. Law Comm'n 2017).

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The drafting committee settled upon the "willful misconduct" standard after a review of the existing directed trust statutes.

Roughly speaking, the existing directed trust statutes fall into two groups. In one group, which constitutes a majority, are the statutes that fully relieve a directed trustee from duty or liability for complying with an action of a trust director. This group includes the statutes in Alaska, New Hampshire, Nevada, and South Dakota. The policy rationale for these statutes is that duty should follow power. A director who possesses a power of direction should be the exclusive bearer of fiduciary duty in the exercise or nonexercise of that power. Moreover, the settlor of a directed trust could have made the trust director the sole trustee instead. Thus, on greater-includes-the-lesser reasoning, the settlor should also be able to eliminate a directed trustee's duty and liability for complying with an action of a trust director. Under these statutes, a beneficiary's only recourse for misconduct by the trust director is an action against the director for breach of the director's fiduciary duty to the beneficiary.

In the other group, which includes Delaware, Illinois, Colorado, North Carolina, Texas, and Virginia, are the statutes under which a directed trustee is not liable for complying with a direction of a trust director,

unless by so doing the directed trustee would personally engage in “willful” or “intentional” misconduct. The policy rationale for these statutes is that, because a trustee stands at the center of a trust, the trustee must bear at least some duty even if the trustee is directed. Although the settlor could have made the trust director the sole trustee, the settlor did not actually do so — and under traditional understandings of trust law, a trustee must always be accountable to a beneficiary in some way. *See, e.g.*, *Restatement (Third) of Trusts* § 96 cmt. c (Am. Law Inst. 2012) (“Notwithstanding the breadth of language in a trust provision relieving a trustee from liability for breach of trust, for reasons of policy trust fiduciary law imposes limitations on the types and degree of misconduct for which the trustee can be excused from liability.”).

The states in the second group also recognize, however, that to facilitate the settlor's intent that the trust director rather than the directed trustee be the primary or even sole decision maker, it is appropriate to reduce the trustee's duty and liability below the usual level with respect to a matter subject to a power of direction. Accordingly, under these statutes a beneficiary's main recourse for misconduct by the trust director is an action against the director for breach of the director's fiduciary duty to the beneficiary. The beneficiary also has recourse against the trustee, but only if the trustee's compliance with the terms of the power of direction amounted to “willful misconduct” by the trustee. Relative to a non-directed trust, this second approach has the effect of increasing the total fiduciary duties owed to a beneficiary. All of the usual duties of trusteeship are preserved in the trust director, but in addition the directed trustee also has a duty to avoid willful misconduct.

The outcome was as follows: [747]

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[747] UDTA § 9 cmt. (Unif. Law Comm'n 2017).

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After extensive deliberation and debate, the drafting committee opted to follow the second group of statutes, which includes the prominent Delaware act, on the grounds that this model does more to protect a beneficiary and is more consistent with traditional fiduciary policy. The popularity of directed trusts in Delaware establishes that a directed trust regime that preserves a “willful misconduct” safeguard is workable and that a total elimination of duty in a directed trustee is unnecessary to satisfy the needs of directed trust practice.

Commentators opined in 2017 that: [748]

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[748] Covey & Hastings, *Uniform Directed Trust Act; Liability of Directed Trustee and Trust Director*, Prac. Drafting 12,895, 12,900 (July 2017).

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We believe the approach of Sections 8 and 9, as discussed above, is sound. Care should be taken in describing the scope of authority conferred upon the trust director so that the responsibilities of that person and the trustee are clearly delineated.

## 6. Designing the Directed Trust

In operation, the directed trustee executes the directed trust. Thus, the directed trustee buys and sells trust assets and makes other investment changes as directed by the direction investment adviser and distributes income and principal as directed by the direction distribution adviser.

The Will or inter vivos trust instrument that establishes the directed trust must clearly identify the powers that are to be directed currently and over time. The terms should include any administrative acts that are to be directed. For example, if the direction investment adviser has the power to choose the entity that will have custody of trust assets, then the governing instrument should contain language instructing the direction investment adviser to direct the directed trustee to sign custody agreements. In addition, the governing instrument should specify:
• Who has the deciding vote when investment and distribution decisions are made by different parties;

• What, if anything, direction investment advisers or direction distribution advisers will be paid for their services as well as the extent to which such advisers will be reimbursed for out-of-pocket expenses [749];

• That the advisers and the directed trustee share information that each party requires in order to fulfill their responsibilities (e.g., a directed trustee must often provide asset values for nonmarketable assets on reports that must be filed with regulators; direction investment advisers who choose such investments should be required to furnish their values on request);

• The procedure to be used to confirm that directions have been given and received;

• That an adviser must accept an appointment in writing (this will ensure that advisers are willing and able to undertake their duties).

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[749] A common arrangement in many Delaware trusts is to appoint a beneficiary as direction investment adviser and to authorize him or her to hire an investment manager. In such cases, the direction investment adviser might serve without compensation but will be reimbursed for expenses, including investment counsel fees. Language in the governing instrument that specifies that a direction investment adviser will receive “reasonable” compensation is too vague to be helpful.

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Because direction investment advisers or direction distribution advisers bear considerable responsibility for the ultimate success of trusts, the persons who are given that responsibility must have the resources to stand behind their performance in case of dishonesty, negligence, inattention, or other failings. Advisers should be chosen with this in mind because, in a properly constructed directed trust, the directed trustee should not (and will not) be held liable in the event of catastrophe. Although the adviser's liability might be limited to cases of wilful misconduct or gross negligence, the adviser should usually serve in a fiduciary capacity. An entity such as an LLC is sometimes appointed as an adviser to limit the members’ potential liability. Such an entity should be funded sufficiently to protect the trust and its beneficiaries.

## 7. Related Issues

### a. A Caveat

The relief that even the most protective statute provides to a directed trustee is not unlimited. A directed trust statute is a state law creation and thus will only protect a directed trustee from state-law claims. Specifically, it will not shield a directed trustee from any claims that arise under federal law, such as tax laws and anti-money-laundering penalties.

### b. Conflict-of-Laws Principles

If a resident of one state concludes that the needs of his or her family will be best served by creating a

directed trust in another state, the attorney must take steps to ensure that the law of the latter state will apply in evaluating the directed trust arrangement and that that state's courts (rather than the courts of the former state or some other state) will make such assessment. The operation of a directed trust and the directed trustee's liability to beneficiaries under it are matters of trust administration. [750] A testator's or trustor's designation of a state's law to govern administration matters for a trust that holds movables is almost always respected. [751]

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[750] *See Restatement (Second) of Conflict of Laws* § 271 cmt. a (Am. Law Inst. 1971).

[751] *See Restatement* § 271 cmt. h, *id.* § 272 cmt. f; *Matter of Rubin*, 540 N.Y.S.2d 944, 946–947 (Sur. Ct. Nassau Cty. 1989), *aff'd*, 570 N.Y.S.2d 996 (N.Y. App. Div. 1991).

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The author covers choice-of-laws principles in III. and IV., above, and specifically addresses those principles for directed trusts elsewhere. [752]

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[752] Richard W. Nenno, *Good Directions Needed When Using Directed Trusts*, 42 Est. Plan. 12, 21–26 (Dec. 2015).

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### c. CRT and Advisers

From time to time, the author is asked whether a Charitable-Remainder Trust (CRT) may have a direction investment adviser. The IRS has ruled that a CRT in which the trustee would invest on direction of an investment manager would qualify, provided that such a manager exercised powers in a fiduciary capacity. [753] Attorneys should draft CRTs with this ruling in mind. However, it should be noted that prior to the 1994 ruling, the IRS had ruled that the investment of assets on the direction of investment counsel would disqualify a CRT. [754]

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[753] *See* PLR 9442017.

[754] *See* PLR 8041100.

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## 8. The Protector

Since the turn of the twenty-first century, the “protector” — which has long been a feature of offshore trusts — has begun to appear in trusts created in the United States, and several states have begun to enact statutes in which the protector's role is defined. The protector sometimes becomes involved in decisions (e.g., directing investments or distributions) that have traditionally fallen within the domain of the adviser or committee; at other times, the protector is charged with responsibilities such as replacing trustees and advisers, amending trust provisions, and changing situs that used to require court involvement.

Given that protector statutes do not contain default powers, the governing instrument must clearly spell out the powers, rights, duties, and responsibilities of the trustee, the direction investment adviser, the

direction distribution adviser, and the protector. Matters that should be addressed include:
• The protector's powers and duties, including the power to enforce the trust.

• Whether the protector has ongoing monitoring responsibilities regarding the exercise of one or more powers (e.g., to remove an adviser or trustee).

• The amount and source of the protector's compensation.

• The extent to which the protector will be reimbursed for out-of-pocket expenses, including counsel fees and court costs that are incurred in carrying out duties.

• Whether the protector will serve in a fiduciary capacity for some or all duties.

• How successor protectors will be chosen.

Much has been written on whether or not a protector should serve in a fiduciary capacity. [755] In the author's view, this will depend on the power that is being exercised. Protectors should certainly serve in a fiduciary capacity if they are discharging the powers of a direction investment adviser or a direction distribution adviser. Even if protectors are handling protector functions, protectors should do so in a fiduciary capacity, but there are exceptions to the rule. For example, if a protector is given the power under § 675(4)(C) to swap trust assets in order to acquire grantor-trust treatment, then the protector must hold this power in a nonfiduciary capacity. Courts have decided several cases involving protectors in recent years. Relevant cases include the following:
• *Robert T. McLean Irrevocable Trust v. Ponder* (Mo. 2013). [756] Although the protector could replace the trustee, a Missouri intermediate appellate court held that the protector did not have a duty to monitor the trustee's activities to determine if the protector should exercise that power.

• *Schwartz v. Wellin* (S.C. 2014). [757] Given that the protector was not a “real party in interest” under South Dakota law, a federal district judge in South Carolina held that the protector could not prevent the individual trustees from terminating a huge South Dakota dynasty trust.

• *SEC v. Wyly* (N.Y. 2014). [758] A federal district judge in New York held that the trustors’ control over the protectors of foreign trusts caused the trusts to be grantor trusts for federal income tax purposes, subjecting the trustors owed the IRS billions of dollars of federal income tax.

• *Minassian v. Rachins* (Fla. 2014). [759] A Florida intermediate appellate court concluded that the trustee's appointment of a protector pursuant to the trust instrument and the protector's modification of the trust terms during litigation were allowed to resolve the dispute because these actions were in accordance with the trustor's intent.

• *In re IMO Daniel Kloiber Dynasty Trust* (Del. 2014). [760] The Delaware Court of Chancery deferred deciding various questions that involved the effectiveness of the exercise of the protector's powers pending the outcome of a divorce proceeding in Kentucky.

• *In re Eleanor Pierce (Marshall) Stevens Living Trust* (La. 2015). [761] An intermediate appellate court held that the role of protector is allowed by Louisiana law and therefore upheld a protector's removal of the trustee.

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[755] *See* Richard C. Ausness, *When Is a Trust Protector a Fiduciary?* 27 Quinnipiac Prob. L.J. 277 (2014).

[756] 418 S.W.3d 482 (Mo. Ct. App. 2013).

[757] 2014 BL 107668, 2014 WL 1572767 (D.S.C. Apr. 17, 2014).

[758] 56 F. Supp. 3d 394 (S.D.N.Y. 2014). *See* Keenen & Zeydel, *Is Designating an Independent Trustee a Tax Panacea?,* 43 Est. Plan. 3 (Feb. 2016).

[759] 152 So.3d 719 (Fla. Dist. Ct. App. 2014).

[760] 98 A.3d 924 (Del. Ch. 2014). *See* LaPiana, *The Directed Trust in Divorce Court*, 42 Est. Plan. 44 (Jan. 2015).

[761] 159 So.3d 1101 (La. Ct. App. 2015).

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## H. Asset Protection — Third-Party Trusts

### 1. Introduction

Clients may protect interests in a trust that they create for others ("third-party trust") from claims by the beneficiaries' creditors by subjecting the interest to spendthrift clauses or by them wholly discretionary. The degree of protectiveness of spendthrift trusts and discretionary trusts differs from state to state, and the underlying concepts have been threatened by the *Restatement (Third) of Trusts*. [762]

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[762] *See* Nelson, *Summary of States That Adopted the Uniform Trust Code and Those States' Treatment of Exception Creditors (Sections 503–504)* (Mar. 2013), www.actec.org/assets/1/6/Nelson_UTC_State_Laws.pdf.

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### 2. Spendthrift Trusts

### a. Restatement (Second) of Trusts Approach

The *Restatement (Second) of Trusts* defines a "spendthrift trust" as follows: [763]

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[763] *Restatement (Second) of Trusts* § 152(2) (Am. Law Inst. 1959). *See* Shapo, Bogert & Bogert, *The Law of Trusts and Trustees* § 222, § 224, § 227 (3d. ed. 2007).

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A trust in which by the terms of the trust or by statute a valid restraint on the voluntary and involuntary transfer of the interest of the beneficiary is imposed is a spendthrift trust.

If a third-party trust contains a spendthrift clause, a beneficiary's right to current income or future principal distributions is not subject to voluntary or involuntary transfer in most circumstances. [764] Even if such a trust contains a spendthrift clause, though, creditors may reach the beneficiary's interest to pay claims for spousal or child support, alimony, necessary services or supplies, costs incurred to protect the beneficiary's trust interest, or governmental obligations. [765] The beneficiary's interest also may be reached to pay claims dictated by public policy (e.g., a claim resulting from the beneficiary's commission of a willful tort). [766]

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[764] *Restatement (Second) of Trusts* § 152(1), § 153(1) (Am. Law Inst. 1959).

[765] *Id.* § 157, *id.* cmts. b–e (Am. Law Inst. 1959).

[766] *Id.* cmt. a (Am. Law Inst. 1959).

## b. Restatement (Third) of Trusts Approach

The *Restatement (Third) of Trusts* defines “spendthrift trust” in substantially the same manner as does the *Second Restatement*. [767] Likewise, creditors may reach a beneficiary's interest in such a trust for the support of a child, spouse, or former spouse; for necessary services and supplies provided to the beneficiary; and for costs incurred to protect the beneficiary's trust interest. [768] The beneficiary's interest also may be reached to pay governmental claims. [769] Ominously from the beneficiary's perspective, the interest might be reachable in the following circumstances: [770]

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[767] *Restatement (Third) of Trusts* § 58(1) (Am. Law Inst. 2003), *id.* cmt. a.

[768] *Restatement* § 59, *id.* cmts. b–d.

[769] Restatement § 59, cmt. a(1).

[770] *Restatement* cmt. a(2).

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The exceptions to spendthrift immunity stated in this Section are not exclusive. Special circumstances or evolving policy may justify recognition of other exceptions, allowing the beneficiary's interest to be reached by certain creditors in appropriate proceedings ...

## c. UTC Approach

UTC § 502 and § 503, respectively, describe spendthrift protection and exceptions to it as follows:

Section 502. Spendthrift Provision.

(a) A spendthrift provision is valid only if it restrains both voluntary and involuntary transfer of a beneficiary's interest.

(b) A term of a trust providing that the interest of a beneficiary is held subject to a ‘spendthrift trust’, or words of similar import, is sufficient to restrain both voluntary and involuntary transfer of the beneficiary's interest.

(c) A beneficiary may not transfer an interest in a trust in violation of a valid spendthrift provision and, except as otherwise provided in this [article], a creditor or assignee of the beneficiary may not reach the interest or a distribution by the trustee before its receipt by the beneficiary.

Section 503. Exceptions to Spendthrift Provision.

(a) In this section, “child” includes any person for whom an order or judgment for child support has been entered in this or another State.

(b) A spendthrift provision is unenforceable against:

(1) a beneficiary's child, spouse, or former spouse who has a judgment or court order against the

beneficiary for support or maintenance;

(2) a judgment creditor who has provided services for the protection of a beneficiary's interest in the trust; and

(3) a claim of this State or the United States to the extent a statute of this State or federal law so provides.

(c) A claimant against which a spendthrift provision cannot be enforced may obtain from a court an order attaching present or future distributions to or for the benefit of the beneficiary. The court may limit the award to such relief as is appropriate under the circumstances.

States sometimes modified these provisions in enacting their versions of the UTC.

### d. State Statutes

The third-party spendthrift trust statutes of the various states differ significantly. Delaware and states with similar laws might offer more protection than the laws of other states. For example, Georgia permits a creditor to reach spendthrift trust assets if he or she is the victim of a willful tort committed by a beneficiary. [771] California permits spendthrift trust assets to be reached to pay claims for spousal or child support, restitution for commission of a felony, and public support, [772] and it limits the amount that may be protected. [773] Oklahoma permits income distributable to a beneficiary of a spendthrift trust to be reached for child and spousal support claims and claims for necessaries, and limits the annual income that may be protected from garnishment to $25,000. [774]

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[771] Ga. Code Ann. § 53-12-80. For a summary of the spendthrift-trust rulesin Texas, see *Bradley v. Shaffer*, 535 S.W.3d 242, 248 (Tex. Ct. App. 2017).

[772] Cal. Prob. Code § 15305, § 15305.5, § 15306.

[773] Cal. Prob. Code § 15306.5–§ 15307. *See In re Hernandez*, 2013 BL 166949, 2013 WL 1490995, at *8 (B.A.P. 9th Cir. Apr. 11, 2013).

[774] Okla. Stat. Ann. tit. 60, § 175.25B.

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Worksheet 8, below, gives citations for state third-party spendthrift trust statutes.

## 3. Discretionary Trusts

### a. Restatement (Second) of Trusts Approach

The *Restatement (Second) of Trust*'s protection of a beneficiary's interest in a discretionary trust from creditor claims rests on two foundations — one is based on the nature of the beneficiary's interest; the other is based on limiting a court's ability to interfere with a trustee's exercise of discretion.

First, § 155(1) of the *Restatement (Second) of Trusts* provides that: [775]

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[775] *Restatement (Second) of Trusts* § 155(1) (Am. Law Inst. 1959). *See* Redd, *Diving Into Discretionary Distributions*, 157 Tr. & Est. 12 (Sept. 2018); Richard C. Ausness, *Discretionary Trusts: An Update* 43 ACTEC L.J. 231 (Winter 2018); Newman, Trust Law in the Twenty-First Century: Challenges to Fiduciary

Accountability), 28 Quinnipiac Prob. L.J. 261, 280–286 (2016). *See generally* Shapo, Bogert & Bogert, *The Law of Trusts and Trustees* § 228 (3d ed. 2007).

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[I]f by the terms of a trust it is provided that the trustee shall pay to or apply for a beneficiary only so much of the income and principal or either as the trustee in his uncontrolled discretion shall see fit to pay or apply, a transferee or creditor of the beneficiary cannot compel the trustee to pay any part of the income or principal.

A trust described in § 155 is a "discretionary trust" not a "spendthrift trust" or a "support trust." [776] The beneficiary's protection results from the nature of the interest and is available whether or not the trust contains a spendthrift clause. [777] A creditor may not reach the beneficiary's interest because the beneficiary cannot force the trustee to make a distribution. [778]

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[776] *Restatement* cmt. b.

[777] *Id.* § 155.

[778] *Id.* § 187.

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Second, § 187 of the *Restatement (Second) of Trusts* provides that: [779]

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[779] *Id.* § 187.

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Where discretion is conferred upon the trustee with respect to the exercise of a power, its exercise is not subject to control by the court, except to prevent an abuse by the trustee of his discretion.

Comment d to § 187 enumerates factors for a court to consider when deciding whether a trustee has abused its discretion, [780] and subsequent comments provide that a court will interfere with a trustee's exercise or nonexercise of discretion only if the trustee acts dishonestly or with an improper motive, fails to exercise judgment, or acts beyond the bounds of a reasonable judgment, even though the court would have acted differently. [781] If the trustee's action is subject to a standard by which its conduct may be judged, the court may interfere if the trustee acts unreasonably. [782] If the trust contains no such standard, though, the court will interfere only if the trustee acts dishonestly or with an improper motive. [783] Inclusion in the trust of language that gives the trustee absolute, unlimited, or uncontrolled discretion relieves it from the duty to act reasonably even if the trust contains a standard by which the trustee's conduct may be judged. [784]

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[780] *Id.* cmt. d.

[781] *Id.* cmts. e–h.

[782] *Id.* § 187 cmt. i.

[783] *Id.* (Am. Law Inst. 1959).

[784] *Id.* cmt. j.

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## b. Restatement (Third) of Trusts Approach

Sections 50 and 60 of the *Restatement (Third) of Trusts* undermine both foundations. [785] This erosion poses a serious threat to the security of trusts in jurisdictions with no discretionary trust statute.

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[785] *Restatement (Third) of Trusts* § 50, § 60 (Am. Law Inst. 2003).

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With respect to the first foundation, comment e to § 60 begins innocuously enough as follows: [786]

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[786] *Id.* § 60 cmt. e.

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A transferee or creditor of a trust beneficiary cannot compel the trustee to make discretionary distributions if the beneficiary personally could not do so.

But, in the very next sentence, it continues that: [787]

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[787] *Id.*

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It is rare, however, that the beneficiary's circumstances, the terms of the discretionary power, and the purposes of the trust leave the beneficiary so powerless.

With respect to the second foundation, the *Restatement (Third) of Trusts* makes it much easier for a court to interfere with a trustee's exercise or nonexercise of discretion. Thus, comment b to § 50 provides that: [788]

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[788] *Id.* § 50 cmt. b.

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It is not necessary ... that the terms of the trust provide specific standards in order for a trustee's good-faith decision to be found unreasonable and thus to constitute an abuse of discretion.

Comment d continues as follows: [789]

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[789] *Id.* § 50 cmt. d.

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Reasonably definite or objective standards serve to assure a beneficiary some minimum level of benefits, even when other standards are included to grant broad latitude with respect to additional benefits... . Sometimes trust terms express no standards or other clear guidance concerning the purposes of a discretionary power, or about the relative priority intended among the various beneficiaries. Even then a general standard of reasonableness, or at least of good-faith judgment, will apply to the trustee ... based on the extent of the trustee's discretion, the various beneficial interests created, the beneficiaries' circumstances and relationships to the settlor, and the general purposes of the trust.

The 2007 edition of the Scott treatise explains the difference between the approaches of the *Restatement (Second) of Trusts* and *Restatement (Third) of Trusts* as follows: [790]

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[790] 3 *Scott and Ascher on Trusts* § 18.2.6 at 1361 n.2 (citations omitted).

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Under the Second Restatement, the relevant inquiry seems to have been whether "reasonable men might differ" on the propriety of the exercise of the power. The inference is that the trustee's decision should stand, in the absence of a judicial finding that no reasonable person could conclude that the trustee had acted reasonably. Under the Third Restatement, the relevant inquiry seems to be whether "the trustee's decision is one that would not be accepted as reasonable by persons of prudence."

### c. UTC Approach

With respect to the first foundation, § 504 of the UTC provides as follows: [791]

(a) In this section, 'child' includes any person for whom an order or judgment for child support has been entered in this or another State.

(b) Except as otherwise provided in subsection (c), whether or not a trust contains a spendthrift provision, a creditor of a beneficiary may not compel a distribution that is subject to the trustee's discretion, even if:

(1) the discretion is expressed in the form of a standard of distribution; or

(2) the trustee has abused the discretion.

(c) To the extent a trustee has not complied with a standard of distribution or has abused a discretion:

(1) a distribution may be ordered by the court to satisfy a judgment or court order against the beneficiary for support or maintenance of the beneficiary's child, spouse, or former spouse; and

(2) the court shall direct the trustee to pay to the child, spouse, or former spouse such amount as is equitable under the circumstances but not more than the amount the trustee would have been required to distribute to or for the benefit of the beneficiary had the trustee complied with the standard or not abused the discretion.

(d) This section does not limit the right of a beneficiary to maintain a judicial proceeding against a trustee

for an abuse of discretion or failure to comply with a standard for distribution.

(e) If the trustee's or cotrustee's discretion to make distributions for the trustee's or cotrustee's own benefit is limited by an ascertainable standard, a creditor may not reach or compel distribution of the beneficial interest except to the extent the interest would be subject to the creditor's claim were the beneficiary not acting as trustee or cotrustee.

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[791] UTC § 504 (amended 2018).

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With respect to the second foundation, § 814(a) provides as follows: [792]

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[792] UTC § 814(a) (amended 2018).

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Notwithstanding the breadth of discretion granted to a trustee in the terms of the trust, including the use of such terms as “absolute”, “sole”, or “uncontrolled”, the trustee shall exercise a discretionary power in good faith and in accordance with the terms and purposes of the trust and the interests of the beneficiaries.

Many states modified the above provisions when they enacted their versions of the UTC.

### d. State Statutes

A few states have had discretionary trust statutes for some time. For example, under California's statutes, which were enacted beginning in 1990, an interest in a discretionary trust may be reached to pay claims for spousal or child support, restitution for commission of a felony, and public support, [793] and the amount that may be protected is limited. [794] Historically, Delaware did not have a statute that covered the ability of creditors to reach a beneficiary's interest in such a trust. Given the uncertainty that now exists on this issue, however, Delaware has adopted legislation in order to provide that:
• A beneficiary who is eligible to receive distributions from a trust in the trustee's discretion has a discretionary interest; [795]

• A creditor may not directly or indirectly compel the distribution of a discretionary interest, except to the extent expressly granted by the terms of a governing instrument in accordance with Delaware's third-party spendthrift-trust statute; [796]

• A court may overturn a trustee's decision regarding a discretionary interest only if the court finds that the trustee abused its discretion within the meaning of *Restatement (Second) of Trusts* § 187, not *Restatement (Third) of Trusts* § 50 and § 60. [797]

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[793] Cal. Prob. Code § 15305, § 15305.5, § 15306. *See United States v. Harris*, 854 F.3d 1053, 1056 (9th Cir. 2017)(“[W]hen a beneficiary has a basic beneficial right to receive payments from a discretionary trust, a government lien may attach to and subsist against that right), *id.* at 1057 (“[A] spendthrift clause does not protect a trust's assets from the enforcement of a federal lien”); *Pratt v. Ferguson*, 206 Cal. Rptr.3d 895, 903 (Cal. Ct. App. 2016) (“The trial court erred by applying the shutdown clause to preclude the use of any of the Trust's assets — whether principal or income — to satisfy the child support judgment”); *Young v. McCoy*, 54 Cal. Rptr.3d 847 (Cal. Ct. App. 2007) (trustee's refusal to exercise discretion to pay

restitution not abuse of discretion); *Ventura Cnty. Dep't of Child Support Servs. v. Brown*, 11 Cal. Rptr.3d 489 (Cal. Ct. App. 2004) (trustee's refusal to exercise discretion to pay child support was abuse of discretion).

[794] Cal. Prob. Code § 15306.5–§ 15307.

[795] Del. Code Ann. tit. 12, § 3315(b).

[796] Del. Code Ann. tit. 12, § 3536.

[797] Del. Code Ann. tit. 12, § 3315(a). *See Merrill Lynch Tr. Co., FSB v. Campbell*, 2009 BL 217734, 2009 WL 2913893, at *10 (Del. Ch. Sept. 2, 2009). Delaware courts give unpublished opinions substantial precedential weight (*Crystallex Int'l Corp. v. Petroleos De Venetuela, S.A.*, 879 F.3d 79 85 n.8 (3d cir. 2018)).

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Thirty-two states have adopted variations of one or both of the UTC provisions. Several states developed their own approaches. Worksheet 8, below, contains citations for state discretionary trust statutes.

## e. Case law

The undermining of the creditor protection that traditionally was afforded by discretionary trusts is of particular concern in a state that has no discretionary trust statute because a court is free to embrace the *Restatement (Third) of Trust*'s approach. This precise issue arose in the case of *Tannen v. Tannen* [798] in New Jersey, which involved whether a beneficiary's discretionary interest in a trust created by her parents should be taken into account in the awarding of alimony to her former husband. The intermediate appellate court described the difference between the *Restatement (Second) of Trusts* and *Restatement (Third) of Trusts* as follows: [799]

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[798] 3 A.3d 1229 (N.J. Super. Ct. App. Div. 2010), *aff'd*, 31 A.3d 621 (N.J. 2011). *See Harrison v. Harrison*, 88 N.E.3d 232, 236 (Ind. Ct. App. 2017) ("[T]he trial court did not abuse its discretion by excluding Wife's interests in the Royal Family Trusts from the marital pot.")

[799] *Id.* at 1242 (citations, internal quotation marks, and brackets omitted).

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Unlike the limited rights of a discretionary beneficiary recognized by the prior Restatement, under the Restatement (Third) of Trusts the benefits to which defendant is entitled, and what may constitute an abuse of discretion by the trustee[s], depend on the terms of the discretion, including the proper construction of any accompanying standards, and on the settlor's purposes in granting the discretionary power and in creating the trust. Defendant has the ability to enforce her rights to these benefits, which, in turn, defines the extent of her interests.

On this difference, the court concluded: [800]

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[800] *Id.* at 1243.

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As a court of intermediate appellate jurisdiction, we do not presume to adopt the Restatement (Third) of Trusts as the law of this state and apply its provisions to the facts of this case. Given the significance of its principles in the context of NJSA 2A:34-23(b)(11), such determination would be more appropriately made by our Supreme Court."

Accordingly, reversing the trial court, the intermediate appellate court held as follows: [801]

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[801] *Id.* at 1243–1244.

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We conclude that under the existing law of this state, defendant's beneficial interest in the WTT was not an asset held by her. It was, therefore, improper to impute income from the WTT to defendant in determining plaintiff's alimony obligation.

The Supreme Court of New Jersey declined the invitation to adopt § 50 of the *Third Restatement of Trusts.* It held that "the judgment of the Appellate Division is affirmed, substantially for the reasons expressed in Judge Messano's opinion..." [802]

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[802] *Tannen v. Tannen*, 31 A.3d 621 (N.J. 2011).

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In 2013, a Florida intermediate appellate court permitted a former wife to garnish discretionary distributions to her former husband from a Florida trust. [803] Subsequently, a highly respected national commentator recommended that Floridians consider establishing new trusts in, and moving existing trusts to, states that forbid the garnishment of third-party trusts. [804]

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[803] *Berlinger v. Casselberry*, 133 So.3d 961, 965–966 (Fla. Dist. Ct. App. 2013).

[804] Nelson, *Protecting Trusts From Claims of Alimony or Child Support*, 153 Tr. & Est. 25, 28 (Mar. 2014).

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The Supreme Judicial Court of Massachusetts addressed a similar issue in the 2016 *Pfannenstiehl v. Pfannenstiehl* case. [805] The court concluded: [806]

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[805] 55 N.E.3d 933 (Mass. 2016). *See* LaPiana*, When a Discretionary Trust Is Not So Discretionary,* 43 Est. Plan. 44 (Jan. 2016); Roman, *Protecting Your Clients' Assets From Their Future Ex-Sons and Daughters-in-Law, 39* ACTEC L.J. 157 (Spring/Fall 2013).

[806] *Id.* 55 N.E.3d at 942 (citations and internal quotation marks omitted).

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Considering the language of the 2004 trust and the particular circumstances here, the ascertainable standard does not render Curt's future acquisition of assets from the trust sufficiently certain such that it

may be included in the marital estate under GL c. 208, § 34. As noted, however, the trust may be considered as an expectancy of future acquisition of capital assets and income in determining what disposition to make of the property that is subject to division.

The assets of third-party trusts are sometimes susceptible to federal claims. Thus, in 2016, the federal district court in Arizona held in *Duckett v. Enomoto* that a federal tax lien attached to a taxpayer's interest in a discretionary-support trust. [807]

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[807] 2016 BL 122633, 2016 WL 1554979, at *8 (D. Ariz. Apr. 18, 2016). *See* LaPiana, *'Shall' Is a Four-Letter Word — at Least for Tax Lien Purposes*, 43 Est. Plan. 43 (Sept. 2016).

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Courts rarely find that trustees have abused discretion. An exception to this rule was *Reliance Trust Co. v. Candler* (2013), [808] where the Supreme Court of Georgia confirmed that the trustee had made excessive distributions to a beneficiary. The court summarized the facts as follows: [809]

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[808] 751 S.E.2d 47 (Ga. 2013).

[809] *Id.* at 48–49 (citations omitted).

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[T]he remainder beneficiaries of the revocable marital trust created by the wife of Charles Howard Candler III sued Reliance Trust Company ("Reliance"), co-trustee of the trust, for breach of trust. They alleged that after the death of the settlor, Reliance made improper distributions from the corpus of the trust to Mr. Candler, who was the life beneficiary. The remainder beneficiaries alleged these improper distributions significantly diminished the value of the trust and thereby damaged them in an amount equal to the improper distributions, plus interest. The case was tried and the jury returned a verdict finding that Reliance did not act in bad faith but otherwise finding in favor of the remainder beneficiaries in the amount of $1,140,924.41. The trial court entered final judgment on the verdict and also awarded the remainder beneficiaries $535,558.15 in pre-judgment interest, which was affirmed by the Court of Appeals. We granted Reliance's petition for a writ of certiorari, directing the parties to address only these points. Did the Court of Appeals err when it upheld the jury's verdict in favor of Respondents/Appellees and when it affirmed the trial court's award of interest?

The court upheld the jury verdict against the trustee on procedural grounds. [810]

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[810] *Id.* at 50.

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## 4. Subsequent Protection

Comment j to § 152 of the *Restatement (Second) of Trusts* provides that: [811]

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[811] *Restatement (Second) of Trusts* § 152 cmt. j (Am. Law Inst. 1959). *See Restatement (Third) of Trusts* § 58 cmts. d, d(2) (Am. Law Inst. 2003). *See also Fannie Mae v. Heather Apartments LP*, 811 N.W.2d 596,

597 (Minn. 2012) (court may "enjoin the disposition of a judgment debtor's property only if that property is in the hands of the judgment debtor"); *Beren v. Beren (In re Estate of Beren)*, 321 P.3d 615, 623 (Colo. App. 2013) ("because the spend-thrift provision . . . no longer protected those trust funds that had become subject to mandatory distribution, the trial court properly allowed garnishment of those funds"); *Cmty. Bank of Elmhurst v. Klein*, 6 N.E.3d 841, 843 (Ill. App. Ct. 2014) ("property that is no longer held in trust (such as principal distributions) may be used for the satisfaction of a judgment").

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After the income of a spendthrift trust has been paid to the beneficiary it can be transferred by him and can be reached by his creditors.

Some states offer protection from creditor claims for funds distributed from discretionary and spendthrift trusts. For instance, in New York, 90% of the income or other payments from a third-party trust is exempt from application to satisfy a money judgment, except to the extent that a court determines that it is needed to meet the reasonable requirements of the judgment debtor and his or her dependents. [812] Moreover, a Delaware statute provides that creditors of non-Delaware residents as well as Delaware residents may not reach assets of accounts in Delaware banks. The current statute provides as follows: [813]

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[812] N.Y. C.P.L.R. § 5205(d)(1).

[813] Del. Code Ann. tit. 10, § 3502(b).

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Banks, trust companies, savings institutions and loan associations ... shall not be subject to the operations of the attachment laws of this State.

This protection is not new. In fact, the earliest predecessor of the statute was enacted in 1871. [814] Over the years, Delaware courts have read the protection broadly. [815]

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[814] 14 Del. Laws 90 (1871).

[815] *Sterling v. Tantum*, 94 A. 176 (Del. Super. Ct. 1915); *Provident Tr. Co. v. Banks*, 9 A.2d 260 (Del. Ch. 1939); *Bank of Del. v. Wilmington Hous. Auth.*, 352 A.2d 420 (Del. Super. Ct. 1976); *Del. Tr. Co. v. Partial*, 517 A.2d 259 (Del. Ch. 1986). *But see Garretson v. Garretson*, 306 A.2d 737, 742 (Del. 1973).

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## 5. Applicable Law

As discussed above, the law that determines whether or not creditors may reach a beneficiary's interest in a trust is the law designated by the trust instrument. [816]Consequently, clients' designations of other states' laws to govern the ability of creditors to reach the assets of third-party trusts should stand.

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[816] *Restatement (Second) of Conflict of Laws* § 273, § 280 (Am. Law Inst. 1971); 7 *Scott and Ascher on Trusts* § 45.7–§ 45.7.3, § 46.7; *Bogert on Trusts* § 293. *See In re Zukerkorn*, 484 B.R. 182, 196 (B.A.P. 9th Cir. 2012) (application of more protective Hawaii spendthrift statute does not violate fundamental California policy).

## 6. California

Given that the Supreme Court of California decided a case involving third-party spendthrift trusts in 2017, it is worth reviewing California's rules for such trusts. California does recognize spendthrift protection for income interests [817] and principal interests [818] in California trusts. But, the legislation provides exceptions for:

• Principal that has become due and payable; [819]

• Claims for child or spousal support; [820]

• Restitution judgment; [821]

• Liability for public support; [822]

• Court order directing trustee to satisfy judgments; [823]

• Income in excess of amount for education and support. [824]

[817] Cal. Prob. Code § 15300.

[818] Cal. Prob. Code § 15301(a).

[819] Cal. Prob. Code § 15301(b).

[820] Cal. Prob. Code § 15305.

[821] Cal. Prob. Code § 15305.5.

[822] Cal. Prob. Code § 15306.

[823] Cal. Prob. Code § 15306.5.

[824] Cal. Prob. Code § 15307.

In *Carmack v. Reynolds* (2017), [825] the Supreme Court of California addressed a question certified to it by the Ninth Circuit as follows: [826]

[825] 391 P.3d 625 (Cal. 2017).

[826] *Id.* at 632.

In sum, after an amount of principal has become due and payable (but has not yet been distributed), a

creditor can petition to have the trustee pay directly to the creditor a sum up to the full amount of that distribution (§ 15301(b)) unless the trust instrument specifies that the distribution is for the beneficiary's support or education and the beneficiary needs the distribution for those purposes (§ 15302). If no such distribution is pending or if the distribution is not adequate to satisfy a judgment, a general creditor can petition to levy up to 25 percent of the payments expected to be made to the beneficiary, reduced by the amount other creditors have already obtained and subject to the support needs of the beneficiary and any dependents. (§ 15306.5).

The court continued by providing the following example: [827]

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[827] *Id.*

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As an illustration, suppose a trust instrument specified that a beneficiary was to receive distributions of principal of $10,000 on March 1 of each year for 10 years. Suppose further that a general creditor had a money judgment of $50,000 against the beneficiary and that the trust distributions are neither specifically intended nor required for the beneficiary's support. On March 1 of the first year, upon the creditor's petition a court could order the trustee to remit the full distribution of $10,000 for that year to the creditor directly if it has not already been paid to the beneficiary, as well as $2,500 from each of the nine anticipated payments (a total of $22,500) as they are paid out. If the creditor were not otherwise able to satisfy the remaining $17,500 balance on the judgment, then on March 1 of the following years, upon the general creditor's petition the court could order the trustee to pay directly to the creditor a sum up the remainder of that year's principal distribution ($7,500), as the court in its discretion finds appropriate, until the judgment is satisfied.

The court concluded: [828]

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[828] *Id. See In re Reynolds*, 867 F.3d 1119 (9th Cir. 2017).

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We conclude that a bankruptcy trustee, standing as a hypothetical judgment creditor, can reach a beneficiary's interest in a trust that pays entirely out of principal in two ways. It may reach up to the full amount of any distributions of principal that are currently due and payable to the beneficiary, unless the trust instrument specifies that those distributions are for the beneficiary's support or education and the beneficiary needs those distributions for each purpose. Separately, the bankruptcy trustee can reach up to 25 percent of any anticipated payments made to, or for the benefit of, the beneficiary, reduced to the extent necessary by the support needs of the beneficiary and any dependents.

In *In re Zukerkorn* (2012), [829] the Bankruptcy Appellate Panel for the Ninth Circuit confirmed that a California resident may choose the law of a state (e.g., Hawaii) that has more protective statutes than California to govern trusts. [830]

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[829] 484 B.R. 182 (B.A.P. 9th Cir. 2012).

[830] *Id.* at 196.

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## 7. Delaware

### a. The Spendthrift Trust Statute

Delaware's third-party spendthrift trust statute [831] contains the following protections for a beneficiary's interest:

• The creditors of a trust beneficiary generally have only such rights against the beneficiary's interest in the trust or the property of the trust as are expressly granted to the creditors by the governing instrument and Delaware law.

• The provision's protections apply regardless of the nature or extent of the beneficiary's interest, whether or not the interest is subject to an exercise of discretion by the trustee or another fiduciary, and regardless of any action that the beneficiary takes or might take in the future.

• The protection is not limited to a certain amount.

• A beneficiary's interest that is not subject to the rights of creditors is exempt from all legal or equitable process instituted by such creditors, including garnishment. [832]

• A beneficiary's creditor may not bring an action against the trustee or the beneficiary in order to:

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[831] Del. Code Ann. tit. 12, § 3536.

[832] Del. Code Ann. tit. 12, § 3536(a).

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(1) Compel the trustee, another fiduciary, or the beneficiary to notify the creditor of a distribution;

(2) Compel the trustee or the beneficiary to make a distribution, whether or not distributions from the trust are subject to the exercise of discretion by a trustee or another fiduciary;

(3) Prohibit the trustee from making a distribution to or for the benefit of the beneficiary, whether or not distributions from the trust are subject to the exercise of discretion by a trustee or another fiduciary; or

(4) Compel the beneficiary to exercise a power of appointment or revocation.

• A beneficiary's voluntary, involuntary, direct, or indirect assignment of an interest that the governing instrument prohibits him or her from assigning is void.

• A beneficiary may not waive a spendthrift clause's protections.

• The provision's protection extends to claims for forced heirship, legitime, marital elective share, or similar rights.

• The provision's protection applies to a trust beneficiary's interest until trust property actually is distributed.

• A trustee may make direct payment of a beneficiary's expenses, even if the beneficiary has outstanding creditors.

• A trustee is not liable to a beneficiary's creditors for paying the beneficiary's expenses.

• A creditor of a trust beneficiary has no right against the beneficiary's interest if the beneficiary has a nongeneral inter vivos or testamentary power of appointment over the trust. [833]

• A creditor of a trust beneficiary has no right against the beneficiary's interest if the beneficiary has a general inter vivos or testamentary power of appointment over the trust unless and to the extent that the beneficiary actually exercises the power. [834]

• A beneficiary of a CRT, a lifetime marital-deduction rust, or other trust may release an interest in favor of succeeding beneficiaries, even if the trust has a spendthrift clause. [835]

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[833] Del. Code Ann. tit. 12, § 3536(d).

[834] Del. Code Ann. tit. 12, § 3536(d)(1), (2).

[835] Del. Code Ann. tit. 12, § 3536(e).

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Three exceptions exist to the protection afforded by the statute — two statutory and one court-made.

### b. Statutory Exceptions to Spendthrift-Trust Protection

The statute states that a creditor of a trust beneficiary may reach the assets of a trust if and to the extent that the beneficiary may revoke the trust in his or her own favor. [836]

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[836] Del. Code Ann. tit. 12, § 3536(d)(3).

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In addition, a spendthrift clause in a self-settled trust does not prevent a creditor of the trustor-beneficiary from satisfying a claim from the trustor-beneficiary's interest to the extent that such interest is attributable to the trustor-beneficiary's contributions, [837] unless a trust meets the requirements of Delaware's Qualified Dispositions in Trust Act [838] or is a lifetime marital-deduction trust, credit-shelter trust, or other trust. [839] Nevertheless, a trust may include a provision authorizing the trustee to reimburse the trustor for income taxes attributable to the trust on a discretionary basis without causing the trust to become self-settled. [840] In addition, the possessor of any power of withdrawal (not just the possessor of a $5,000/5% power) [841] is not treated as the trustor due to the lapse, waiver, or release of the power. [842]

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[837] Del. Code Ann. tit. 12, § 3536(c).

[838] Del. Code Ann. tit. 12, § 3570–§ 3576.

[839] Del. Code Ann. tit. 12, § 3536(c)(1).

[840] Del. Code Ann. tit. 12, § 3536(c)(2). *See* Rev. Rul. 2004-64.

[841] *See* § 2041(b)(2), § 2514(c).

[842] Del. Code Ann. tit. 12, § 3536(c) (flush language)

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## c. Narrow Court-Created Exception to Spendthrift-Trust Protection — Garretson v. Garretson (1973)

The Supreme Court of Delaware created an extremely narrow public-policy exception to the protection provided by Del. Code Ann. tit. 12, § 3536 in the 1973 Garretson v. Garretson case. [843] In Garretson, the wife filed an action in the Court of Chancery for the following reason: [844]

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[843] 306 A.2d 737 (Del. 1973).

[844] *Id.* at 739.

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In order to obtain jurisdiction over the husband, now a resident of the State of Florida, the plaintiff obtained a sequestration order under which the income from the testamentary trust, payable to the husband, was seized in order to coerce his appearance in the Court of Chancery.

The court held that: [845]

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[845] *Id.* at 740.

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It is to be noted that both 3536 and Item II of the will provide in terms that the trust property shall not be subject to the rights of the creditors of (such) beneficiary, (and) shall be exempt from execution, attachment, distress for rent, on behalf of such creditors. The question thus presented is whether or not a wife, seeking support from her husband, is a creditor within the meaning of the word as it is used in s 3536 and in Item II of the will. If the wife is a creditor, then seizure of any of the trust assets on her behalf is prohibited by the terms of s 3536 and of Item II of the will. The Chancellor concluded that the wife was not a creditor in that meaning of the word, and we agree with that conclusion.

An action brought by a wife seeking separate maintenance from her husband who has deserted her is an attempt on her part to compel the performance of a duty imposed by law upon the husband to support his wife and dependents.

The weight of authority is to the effect that a wife seeking such relief is not a creditor and is not bound by the spendthrift provisions of a trust from reaching the trust assets. A wife, under such circumstances, can hardly be a creditor who is defined as one to whom a debt is owing by another person who is the debtor [846]...

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[846] *Id.* at 741 (citations omitted).

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*Garretson* allowed a current — but not a divorced — spouse to reach the assets of a third-party spendthrift trust for support, [847] but some practitioners misrepresent the breadth of this court-created exception by claiming it applies to divorced spouses.

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[847] *Id.* at 737.

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Typical is the following statement in a January 2016 article: [848]

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[848] Oshins & Siegel, *The Anatomy of the Perfect Modern Trust — Part 1*, 43 Est. Plan. 3, 12 (Jan. 2016) (footnote and internal quotation marks omitted).

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Delaware provides that spouses who are beneficiaries of discretionary trusts do not receive protection of their trust assets from alimony claims of a divorced spouse.

In the *Garretson* case, the Supreme Court of Delaware noted that "we...consider that...the record discloses solely that the individual parties are still husband and wife." [849] The court concluded: [850]

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[849] *Garretson*, 306 A.2d at 739.

[850] *Id.* at 742.

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It of course remains to be seen, if the husband appears generally in this litigation and subjects himself to the jurisdiction of the Court of Chancery, whether, on final hearing, his contentions with regard to his Mexican divorce will be ultimately upheld, in which event we assume that the wife would lose her status as wife, and there may be an entirely different situation then facing the Chancellor. This question, however, is not before us, and we make no ruling upon the future outcome of the course of the litigation.

## d. Cases Refusing to Create Exception to Spendthrift-Trust Protection

### (1) Introduction

In Garretson, the Supreme Court of Delaware found that a wife who sought support from a husband who had deserted her was not a "creditor" under Del. Code Ann tit. 12, § 3536. Subsequently, three plaintiffs asked the Court of Chancery to create new judicial exceptions to the statute. All three efforts were unsuccessful.

### (2) Gibson v. Speegle (1984)

In the *Gibson v. Speegle* case, [851] the Delaware Court of Chancery set the stage as follows: [852]

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[851] *Gibson v. Speegle*, 184 Del. Ch. Lexis 475 (Del. Ch. May 30, 1984), *rem'd*, 494 A.2d 165 (Del. 1984).

[852] *Id.*, 184 Del. Ch. Lexis 475 at *1.

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This is the decision on the petition and proof of claim filed by Aetna Casualty and Surety Company of America (“Aetna”) seeking an order requiring the payment of Aetna's outstanding judgment against Gary Barwick (“Barwick”) from the proceeds of a partition sale. One-half of those proceeds, or the sum of $12,799.20, is the share allocated to Arlene B. Gibson (“Gibson”), trustee of a testamentary trust created for the benefit of Barwick by his mother, Virginia Barwick. Gibson contends that Virginia Barwick's will created a spendthrift trust and that Aetna, as a “creditor” within the meaning of 12 Del. C. § 3536, is not entitled to satisfy its judgment from the trust assets.

The vice chancellor first rejected the plaintiff's public-policy argument: [853]

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[853] *Id.* at *5 (citations omitted).

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Aetna contends that ours would be a sorry system of justice if the spendthrift statute were applied to allow a criminal such as Barwick to avoid having to pay for his crimes. Aetna suggests that its position is not unlike that of a wife suing her husband for support and attempting to reach her husband's interest in a spendthrift trust. This Court has concluded that a husband in those circumstances should not be allowed to enjoy the benefits of the trust while neglecting his legal obligation to support his dependents. The husband-wife situation, however, is distinguishable because a spouse has a statutory duty to support the other spouse and their children. Aetna has not cited any authority indicating that a tort-feasor owes a similar duty to a tort claimant.

The court then considered — and expressed sympathy for — the plaintiff's contention that a tort victim should not be considered a “creditor” under the statute: [854]

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[854] *Id.* at *6 (citations omitted).

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The term “creditor” is not defined in the statute and has not been construed in Delaware other than in the context of the husband and wife support situation described above. However, the authors of several respected treatises on trusts have concluded that tort claimants should not be considered “creditors” for purposes of a spendthrift trust provision. Their reasoning is sound. If a business extends credit to a spendthrift trust beneficiary, it does so at its own risk. A person who is injured by a tort-feasor, by contrast, did not choose to do business with the tort-feasor and should not be prevented from receiving compensation for his injuries by the terms of a spendthrift trust.

Nonetheless, the court, deferring to the decision of the general assembly, dismissed this argument as well: [855]

[855] *Id.* at *6–7 (citations omitted).

In the absence of a statute, I would not hesitate to adopt this view and allow Aetna's claim. I am not at all comfortable with the fact that Virginia Barwick, by use of a spendthrift trust, assisted her son in avoiding his obligation to pay for his crimes. However, it is not the Court's function to write the law but only to interpret it. The statute enacted by the General Assembly contains no exceptions, Dean Griswold proposed a form of statute which, he believed, should retain the desirable elements of spendthrift trusts while eliminating most of the levels which accompany such trusts in their unrestrained form as early as 1947. The proposed statute, which contained an exception for tort claimants, among others, was available to the General Assembly in 1959 when § 3536 was amended. The fact that such a modification was not enacted leaves me no choice but to conclude that the General Assembly intended § 3536 to be an "unrestrained" form of spendthrift provision. As a result, I reluctantly conclude that Aetna is a creditor within the meaning of § 3536 and its proof of claim must be denied.

## (3) Parsons v. Mumford (1989)

The next case was the 1989 decision in *Parsons v. Mumford*, [856] in which the court described the controversy as follows: [857]

[856] 1989 WL 63899 (Del. Ch. June 14, 1989). Delaware courts give unpublished opinions substantial precedential weight (*Crystallex Int'l Corp. v. Petroleos De Venezuela, S.A.* 879 F.3d 79 85 n.8 (3d Cir. 2018)).

[857] *Id.* at *1.

Plaintiffs are judgment creditors of the individual defendant. The corporate defendant is trustee of a trust in which the judgment debtor has a remainder interest. The suit seeks, among other relief, an order directing the trustee, upon termination of the trust, to pay over a portion of the remainder interest, if then due to the judgment debtor, to plaintiffs in satisfaction of their judgments.

Following *Gibson*, the court concluded that "while there are strong equities in favor of the limited remedy sought, the provisions of Section 3536 of Title 12 prohibit it in these circumstances." [858]

[858] *Id.* at *5.

## (4) Mennen v. Fiduciary Trust International of Delaware (2017)

The latest controversy involved trusts created by George S. Mennen in 1970. In this case, the beneficiaries of one trust attempted to reach the assets of a second trust in order to remedy investment losses caused by the principal beneficiary of the second trust in his capacity as trustee of the first trust. In a 2015 final report, [859] the master in chancery observed that: [860]

[859] *Mennen v. Wilmington Tr. Co.*, 2015 BL 120928 (Del. Ch. Apr. 24, 2015).

[860] *Id.* at *1-2.

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Whatever my personal views regarding the policy supporting spendthrift clauses, I am bound by state statute and controlling precedent to conclude that the spendthrift clause bars the plaintiffs from satisfying the judgment against the individual trustee from the assets in the individual trustee's trust.

The master therefore recommended that the Court of Chancery hold that:
• A person with a tort claim is a "creditor" under § 3536; [861]

• A public-policy exception to § 3536 should not be created for tort claims; [862]

• A public-policy exception to § 3536 should not be created for claims against a "persistent wrongdoer"; [863] and

• The remedy of "impoundment" is not available. [864]

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[861] *Id.* at *5-7.

[862] *Id.* at *6.

[863] *Id.* at *10.

[864] *Id.* at *11-13.

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After procedural issues were resolved, [865] the Court of Chancery adopted the master's final report as written early in 2017. [866]

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[865] *Mennen v. Wilmington Tr. Co.*, 2017 BL 59205, 2017 WL 751201, at *1 (Del. Ch. Feb. 27, 2017). Delaware courts give unpublished opinions substantial precedential weight (*Crystallex Int'l Corp. v. Petroleos De Venezuela, S.A.* 879 F.3d 79 85 n.8 (3d Cir. 2018)).

[866] *Id.* at *2.

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The Supreme Court of Delaware affirmed: [867]

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[867] *Mennen v. Fiduciary Tr. Int'l of Del.*, 166 A.3d 102, 102 (Del. 2017).

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This 21st day of June 2017, after careful consideration of the parties' briefs and the record on appeal, we have determined that the Court of Chancery's . . .February 27, 2017 Report Pursuant to Delaware Supreme Court Rule 19(c) should be affirmed for the reasons stated . . . by the Master in Chancery in her well-reasoned April 24, 2015 final report on the motion for summary judgment . . ..

### e. Drafting Suggestion

In light of *Garretson*, Delaware attorneys routinely include language, such as that highlighted below, in spendthrift clauses in third-party spendthrift trusts:

A beneficiary may not alienate or in any other manner assign or transfer his or her interest in any trust hereunder, and no one *(including a spouse or former spouse)* may attach or otherwise reach any interest of any beneficiary hereunder to satisfy a claim against that beneficiary, whether the claim is legal or equitable in origin.

## 8. Third-Party Trusts in Divorce

### a. Introduction

Beneficiaries' interests in third-party trusts may come into play in connection with divorce proceedings in at least the three following contexts:
• In identifying "marital property" that family courts may allocate between the divorcing spouses;

• As resources that family courts may take into account in dividing marital property and setting alimony and/or child support;

• As assets that courts may reach to enforce the payment of alimony and child support. [868]

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[868] *See* Roman, *Protecting Your Clients' Assets From Their Future Ex-Sons and Daughters-in-Law: The Impact of Evolving Trust Laws on Alimony Awards*, 39 ACTEC L.J. 157 (Spring/Fall 2013).

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### b. Identifying Marital Property and Nonmarital Property

In rearranging former spouses' assets incident to divorce, family courts first must identify the "marital property" that may be divided between the parties. Interests in third-party trusts often must be evaluated. The following cases are illustrative.
(1) In *In re Goodlander* (2011), [869] the Supreme Court of New Hampshire considered whether an interest in a discretionary trust was marital property subject to division. The court held that the trust interest was not marital property: [870]

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[869] 20 A.3d 199 (N.H. 2011). *See United States v. Baker*, 2017 BL 336616, 2017 WL 4225035, at *3 (D. Mass. Sept. 22, 2017) ("the court . . . reaffirms its decision to divide the Escrowed Funds equally between the government and Robyn Baker").

[870] *Id.* at 205 (citations and internal quotation marks omitted).

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Because the trustee of the EMT Trust has the sole discretion to distribute funds to the beneficiaries, including Tamposi, any interest Tamposi has in future distributions fits squarely within the definition provided by the UTC for a mere expectancy. That is, any distribution to or for the benefit of Tamposi is subject to the exercise of the trustee's discretion, whether or not the terms of a trust include a standard to guide the trustee in making distribution decisions. Accordingly, Tamposi's interest in future distributions of the EMT Trust is neither a property interest nor an enforceable right, but a mere expectancy.

(2) In *Dahl v. Dahl* (2015), [871] the Supreme Court of Utah had to allocate assets of a failed Nevada APT. As relevant here, the court held: [872]

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[871] 345 P.3d 566, 2015 WL 5098249 (Utah Aug. 27, 2015). *See* Borowsky & Nenno, *Myths and Facts About Kloiber*, LISI Asset Prot. Plan. Newsl. #337 (Jan. 5, 2017), www.leimbergservices.com.

[872] *Id.* at *10.

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Because Ms. Dahl contributed marital property to the Trust, she retains the status of settlor and may revoke the Trust as to her contribution of both her separate property and any marital assets.

(3) In IMO Daniel Kloiber Dynasty Trust U/A/D December 20, 2002 (2016), [873] the facts and resolution were as follows: [874]

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[873] C.A. No. 9685-VCL (Del. Ch. Aug. 16, 2016). For related proceedings, see *Kloiber v. Daniel Kloiber Dynasty Tr.*, 2014 BL 341661, 2014 WL 6882265 (Ky. Ct. App. Dec. 5, 2014); *IMO Daniel Kloiber Dynasty Tr. U/A/D December 20, 2002*, 98 A.3d 924 (Del. Ch. 2014).

[874] Borowsky & Nenno, *Myths and Facts About Kloiber*, LISI Asset Prot. Plan. Newsl. #337 (Jan. 5, 2017), www.leimbergservices.com (footnote omitted).

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*Kloiber*, like *Dahl*, involved a husband, Dan Kloiber (“Dan”), who transferred marital assets to a trust during the marriage. Dan's father settled a discretionary trust for Dan, his wife and his descendants. Dan was a primary beneficiary of the trust. Dan sold his interest in his company, a marital asset, to the trust for $6 million. The trust later sold the company interest for a sum in excess of $300 million. Dan's wife, Beth Kloiber (“Beth”), claimed that Dan's transfer to the trust was a fraudulent transfer because he received only $6 million in exchange for an asset worth in excess of $300 million. As noted, the case was settled, and the trust was not pierced. Rather, the trust was divided into a share for Dan and a share for Beth, and each share continues to be held in further trust.

(4) In *Pfannenstiehl v. Pfannenstiehl* (2016), [875] the Supreme Judicial Court of Massachusetts analyzed whether an interest in a discretionary trust was marital property. The court concluded: [876]

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[875] 55 N.E.3d 933 (Mass. 2016).

[876] *Id.* at 942.

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Considering the language of the 2004 trust, and the particular circumstances here, the ascertainable standard does not render Curt's future acquisition of assets from the trust sufficiently certain such that it may be included in the marital estate under G.L. c. 208, § 34.

(5) In *Powell-Ferri v. Ferri* (2017), [877] the trustee decanted a Massachusetts trust into a new Massachusetts trust in order to eliminate a divorcing husband's powers to withdraw trust assets. The Supreme Court of Connecticut held that the divorcing husband's interest in the second trust was not marital property in the Connecticut divorce proceeding because: [878]

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[877] 165 A.3d 1124 (Conn. 2017).

[878] *Id.* at 1130.

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[W]e cannot conclude that the trial court abused its discretion in declining to treat the 2011 trust as a marital asset.

Because the Massachusetts Supreme Judicial Court determined that the decanting was proper, and because those assets could not be reached once placed in the 2011 trust, we need not consider Powell-Ferri's arguments concerning contributions to the 1983 trust.

### c. Taking Trust Interests Into Consideration

Even if an interest in a third-party trust is not classified as marital property, the interest might be taken into account for other purposes. For example, immediately after determining that the trust interest in the *Pfannenstiehl* case mentioned above, was not marital property, the court noted: [879]

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[879] *Pfannenstiehl*, 55 N.E.3d at 942.

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[T]he trust may be considered as an expectancy of future acquisition of capital assets and income in determining what disposition to make of the property that is subject to division.

But, in the *Tannen* case mentioned above, a New Jersey court held: [880]

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[880] *Tannen*, 3 A.3d at 1243–1244.

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[U]nder the existing law of this state, defendant's beneficial interest in the WTT was not an asset held by her. It was, therefore, improper to impute income from the WTT to defendant in determining plaintiff's alimony obligation.

## d. Enforcement of Court Awards

Far too often, parties to a divorce do not live up to their monetary obligations. Courts must then develop ways to ensure compliance. Some examples are summarized below.
(1) In the Garretson case summarized above, the Supreme Court of Delaware described the situation as follows: [881]

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[881] *Garretson*, 306 A.2d at 738.

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The individual parties were married in 1943 and lived together until December 19, 1967, when the husband left the wife. In 1968, while the husband was still a resident of Delaware, the wife commenced a separate maintenance action in the Court of Chancery. Ultimately, the parties negotiated a settlement which was cast in the form of a separation agreement and incorporated by the Vice Chancellor in a final order of September 9, 1969. Under the terms of the settlement, the husband was required to pay the wife $400 a month. Shortly thereafter, the husband left Delaware and established a residence in the State of Florida, and obtained a divorce in the Republic of Mexico dated October 23, 1969.

Prior to these events, in September of 1968, the husband brought an action for divorce against the wife in Delaware on the grounds of incompatibility. Ultimately, a decree nisi was denied. Then followed the separate maintenance action and the final order incorporating the separation agreement.

The husband has paid nothing to the wife since May, 1970. As a result, the wife brought a second action in the Court of Chancery, now before us, seeking a judgment against the husband for the amount of the arrearages and an order upon the Bank of Delaware, Trustee, to pay into Court the amount of any such judgment, and to make payments thereafter directly to her in compliance with the order entered in the separate maintenance action.

The court held that “the trust fund may be sequestered” [882] to encourage the former husband to participate in the proceeding.
(2) In the Goodlander case mentioned above, the Supreme Court of New Hampshire pointed out that: [883]

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[882] *Garretson*, 306 A.2d at 742.

[883] *Goodlander*, 20 A.3d at 210.

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Under the provisions of the UTC, a former spouse is entitled to seek a trust distribution to meet his or her

most basic needs regardless of whether a trustee makes a distribution to the beneficiary.

(3) The court in the Berlinger case mentioned above, recounted the facts as follows: [884]

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[884] *Berlinger*, 133 So.3d at 963.

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Although financially able to pay, Berlinger and his attorneys went to extraordinary lengths to avoid his support obligation to Casselberry.

After thirty years of marriage, Berlinger and Casselberry divorced in 2007. Pursuant to a marital settlement agreement ratified by the court and incorporated into the final judgment of dissolution, Berlinger agreed to pay Casselberry $16,000 a month in permanent alimony. Thereafter, Berlinger and his current wife enjoyed a substantial lifestyle sustained through payments made to Berlinger directly or on his behalf by the Berlinger Discretionary Trusts. The trusts paid for all of his living expenses including, but not limited to, mortgage payments, property taxes, insurance, utilities, food, groceries, and miscellaneous living expenses. Although he continued to live on the substantial proceeds of the Berlinger Discretionary Trust, Berlinger voluntarily stopped paying alimony in May 2011.

The court ordered that the former husband's trust distributions be garnished as follows: [885]

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[885] *Id.* at 966.

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Sections 736.0503 [Exceptions to Spendthrift Provision] and 736.0504 [Discretionary Trusts; Effect of Standard] codified the Florida Supreme Court's holding in *Bacardi*. Neither section protects a discretionary trust from garnishment by a former spouse with a valid order of support.

Following *Berlinger*, a Florida practitioner advised: [886]

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[886] Nelson, *Protecting Trusts From Claims of Alimony or Child Support*, 153 Tr. & Est. 25, 28 (Mar. 2014) (footnote omitted).

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Courts will go out of their way to protect spouses with support judgments if the law isn't absolutely clear. For these reasons, it's important to consider moving trusts to states such as Alaska, Delaware, Nevada and South Dakota.

(4) In *Pratt v. Ferguson* (2016), [887] a former wife was not meeting her obligation to cover child support and other expenses. The court recited the pertinent facts and described its conclusion as follows: [888]

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[887] 206 Cal. Rptr.3d 895 (Cal. Ct. App. 2016).

[888] *Id.* at 897 (emphasis in original).

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David Pratt obtained court orders requiring his ex-wife, Cynthia Vedder, to pay child support and expenses. All those orders are final. Vedder is the beneficiary of a trust established by her grandparents. Pratt filed a petition to compel Robert L. Ferguson, the trustee of the Borgert Vedder and Nellie A. Vedder Revocable Trust (the Trustee), to satisfy the orders from Vedder's share of the trust estate. The trial court denied the petition based on a clause in the trust that prohibited the Trustee from making certain distributions if they would become subject to Vedder's creditors' claims (the shutdown clause). We reverse.

We hold that, notwithstanding the shutdown clause, Probate Code section 15305 gives the trial court discretion to order a trustee to make distributions of income and principal to satisfy the final child support orders. Probate Code section 15305, subdivision (d) expressly states that the section *"applies to a support judgment notwithstanding any provision in the trust instrument."*

As described more particularly in the disposition, we remand to the trial court to exercise its discretion to order satisfaction of the child support orders with respect to all distributions by the trust of income and principal. We agree with the opinion of *Ventura County Dept. of Child Support Services v. Brown* (2004) 117 Cal. App.4th 144, 11 Cal. Rptr.3d 489 (*Ventura County*), that where a trustee has discretion to make or withhold payment, the trustee may not act with an intent to avoid child support.

Estates, Gifts and Trusts Portfolios
Trusts
Portfolio 867-2nd: Choosing a Domestic Jurisdiction for a Long-Term Trust
Detailed Analysis
V. Factors to Consider in Selecting a Trust State

## I. Asset Protection — Self-Settled Trusts

### 1. Introduction

A trust in which the trustor retains a beneficial interest often is referred to as a "self-settled trust." The *Restatement (Second) of Trusts*, the *Restatement (Third) of Trusts*, and the UTC do not extend creditor protection to a trustor-beneficiary's interest in a self-settled discretionary trust. [889] Thus, § 156(2) of the *Restatement (Second) of Trusts* provides as follows: [890]

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[889] *Restatement (Second) of Trusts* § 156(2) (1959), *Id.* § 156 cmt. e (1959); *Restatement (Third) of Trusts* § 60 cmt. f (2003); UTC § 505(a)(2) (amended 2018). *See* Rothschild & Rubin, *Minimize Creditor Challenges to Self-Settled Spendthrift Trusts*, 157 Tr. & Est. 14 (Nov. 2018). *See generally* Shapo, Bogert & Bogert, *The Law of Trusts and Trustees* § 223, § 227 (3d ed. 2007).

[890] *Restatement* § 156(2).

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Where a person creates for his own benefit ... a discretionary trust, his transferee or creditors can reach the maximum amount which the trustee under the terms of the trust could pay to him or apply for his benefit.

Nor do they give any protection to a trustor-beneficiary's interest in a self-settled spendthrift trust. [891] For example, § 156(1) of the *Restatement (Second) of Trusts* says that: [892]

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[891] *Restatement* § 156(1); *Restatement (Third) of Trusts* § 58(2) (2003), *id.* § 58(2) cmt. e; UTC § 505(a)(2) (amended 2018).

[892] *Restatement* § 156(1).

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Where a person creates for his own benefit a trust with a provision restraining the voluntary or involuntary transfer of his interest, his transferee or creditors can reach his interest.

As society became increasingly litigious, Americans began to look for trusts that offered creditor protection *and* continued benefits. Until 1997, trusts settled in foreign countries were the only available option. Since then, however, several states have enacted asset protection trust ("APT") statutes.

### 2. State Statutes

Seventeen states permit trustors to obtain protection from creditors by creating domestic APTs. [893] Worksheet 9, below, gives citations for the domestic APT statutes and for statutes of other states that do

not recognize them.

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[893] *See* 868 T.M., *Domestic Asset Protection Trusts*. For summaries of the domestic APT statutes, see Shaftel, *Eleventh Annual ACTEC Comparison of the Domestic Asset Protection Trust Statutes* (Aug. 2017), www.actec.org/assets/1/6/Shaftel-Comparison-of-the-Domestic-Asset-Protection-Trust-Statutes.pdf.

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### 3. Applicable Law

As noted previously, the general rule is that the law that determines whether or not creditors may reach a beneficiary's interest in a trust is the law designated by the trust instrument. [894] Hence, although the question is controversial, a client's designation of another state's statute to govern the ability of creditors to reach the assets of a self-settled spendthrift trust should be effective.

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[894] *Restatement (Second) of Conflict of Laws* § 273 (1971).

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### 4. Protection for Distributions

As described in V.H.4., above, mandatory or discretionary distributions from self-settled trusts into bank accounts or trusts may enjoy protection from creditor claims under the laws of certain states.

### 5. Crummey Powers

Because the holder of a *Crummey* power has the ability to withdraw property for a period of time, he or she might be treated as contributing property to the trust when the power lapses. Several state statutes provide that a holder of a *Crummey* power will not be treated as the trustor of the trust in these circumstances. [895]

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[895] *See, e.g.*, UTC § 505(b)(2) (amended 2018); Del. Code Ann. tit. 12, § 3536(c)(2); Idaho Code § 15-7-502(5)(b); Tex. Prop. Code § 112.035(e)(2).

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### 6. Income Tax Reimbursement Clause

As discussed in II.E., above, a trustor may greatly enhance the transfer-tax savings provided by a dynasty trust by structuring it as a grantor trust for federal income tax purposes. In Revenue Ruling 2004-64, the IRS confirmed that inclusion of a provision giving the trustee discretion to reimburse the trustor for income taxes attributable to a grantor trust would not result in the trust being included in the gross estate provided that, under applicable state law, inclusion of such a provision would not cause the trust to be self-settled and thereby enable creditors to reach its assets. Several state statutes now provide that inclusion of a discretionary income tax reimbursement clause will not cause a trust to be self-settled. [896]

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[896] *See, e.g.*, Del. Code Ann. tit. 12, § 3536(c)(2); Fla. Stat. § 736.0505(1)(c); N.Y. Est. Powers & Trusts

Law § 7-3.1(d).

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## 7. Lifetime QTIP Trust

Given the increase of the estate tax exemption to $10 million (indexed for inflation) and the addition of portability of this exemption for spouses dying after 2010). [897] wealthy spouses, who are reluctant to make outright gifts to poorer spouses to enable them to use their exemptions, have begun to consider creating inter vivos QTIP, credit-shelter, and other trusts to achieve this objective. Whereas the IRS long has taken the position that a lifetime QTIP trust from which the donor spouse may benefit if he or she outlives the donee spouse is not a self-settled trust for transfer-tax purposes, [898] the question remains whether such a trust will be treated as self-settled (and therefore reachable by creditors) for state-law purposes. Several state statutes now provide that a lifetime QTIP trust or, in some states, a lifetime credit-shelter or other trust is not self-settled. [899]

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[897] § 2010(c)(3)(C). This exemption amount will revert to $5 million (plus an inflation adjustment) in 2026. For the inflation-adjusted gift tax, estate tax and GST tax exclusion amounts for recent years, see 800 T.M., *Estate Planning*, Worksheet 1.

[898] *See* § 2523(f)(5); Reg. § 25.2523(f)-1(d), § 25.2523(f)-1(f) *Exs.* 10–11.

[899] *See* Worksheet 9.

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## 8. Status as a Self-Settled Trust

In 2016, an intermediate appellate court in New York held that a special needs trust created by the exercise of a decanting power was not self-settled for the following reasons: [900]

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[900] *Matter of Kroll v. N.Y. Dep't of Health*, 143 A.D.3d 716, 720 (N.Y. App. Div. 2016) (citations omitted).

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Inasmuch as the principal of the original trust was not the grandson's asset at the time that it was decanted into the new supplemental needs trust, it cannot be said the grandson “created” the new trust. As the grandson was not the “creator” of the new trust, a payback provision was not required.

Similarly, in 2017, the Supreme Court of Connecticut concluded that a trust created via the exercise of a decanting power was not self-settled because: [901]

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[901] *Ferri v. Powell-Ferri*, 165 A.3d 1137, 1148 (Conn. 2017).

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In light of the trial court's finding that Ferri took no active role in planning, funding, or creating the 2011 trust, we can find no authority for the proposition that it should be considered self-settled.

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## J. Power to Adjust and Total-Return Unitrust Statutes

### 1. Introduction

For generations, lawyers drafted trusts that direct the trustee to distribute the income (e.g., interest and dividends) to a beneficiary for a specified period of time, normally the life of that beneficiary. Often, the trustee of such a trust has a discretionary power (which usually requires it to assess the current beneficiary's needs) to distribute principal to that beneficiary. At the current beneficiary's death, the remaining principal (which usually includes capital gains incurred during the trust's administration) will go to, or continue in trust for, a beneficiary or group of beneficiaries.

Traditionally, trustees invested trust assets to produce enough income to meet the current beneficiary's needs. At one extreme, a trustee might invest all trust assets in stocks that pay no dividends and thereby generate no current income. At the other extreme, a trustee might invest all trust assets in junk bonds and thereby generate substantial interest income. Trustees understand that these extremes might accomplish income goals but create unacceptable investment risk. Further, neither extreme is in keeping with the trustee's fiduciary duty to income and remainder beneficiaries alike. A trustee's task is rendered more difficult by its obligation to preserve or grow principal for the remainder beneficiaries as well as to produce income for the current beneficiary. Consequently, trustees select a mix of investments to provide satisfactory income flow and an opportunity for principal growth. In so doing, trustees risk displeasing both groups.

Since the 1980s, all states have replaced the prudent-person rule with the prudent-investor rule for assessing a trustee's investment performance. Under the latter standard, the trustee's performance is measured on the whole portfolio rather than on the asset-by-asset basis of the prudent-person rule. The prudent-investor rule compels trustees to invest trust assets for total return. Here, the goal is to maximize the sum of income and growth irrespective of income yield, which requires a heavier emphasis on stocks and a lighter emphasis on fixed-income investments than in the past.

### 2. The Problem

Current beneficiaries of irrevocable trusts have seen their distributions decrease for two reasons. First, trustees have been investing more heavily in equities, and equities normally provide less current income than fixed-income investments. Second, the interest provided by fixed-income investments and the dividends provided by stocks have been falling. Indeed, some widely held stocks pay no dividend at all. This situation has been particularly pronounced for beneficiaries of income-only trusts such as traditional marital-deduction trusts with no discretion to distribute principal to the surviving spouse. Such trusts are particularly common in the case of second marriages where the decedent was survived by children of the first marriage. The pressure to increase distributions is more than that posed by the ability of a surviving spouse to require the trustee of a marital-deduction trust to make trust assets productive. Often, a beneficiary will demand a monthly or quarterly “allowance” of a size that currently available income yields cannot match.

As a result of this trend, current beneficiaries more frequently “demand” that trustees increase their distributions.

## 3. Statutory Changes

To solve the problems raised by declining income yields, the desire of trustees to invest for total return, and the need to balance the interests of current beneficiaries and remainder beneficiaries, states are changing the statutory definition of income. They are considering two types of statutory changes. [902]

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[902] *See* Candland, Murphy & Farnsworth, *Intricacies of the Uniform Principal and Income Act — Part 3*, 44 Est. Plan. 3 (July 2017); Cohen & Smith, *A Trustee's Guide to the Uniform Principal and Income Act*, 153 Tr. & Est. 49 (May 2014).

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The first approach is to amend the state's principal and income act to give trustees the power to adjust income to principal or principal to income if the trustee is managing the trust's investments under the prudent-investor rule, the trust describes the amount that may or must be distributed as "income," and, after application of the provisions of the governing instrument and the statutory rules governing income and principal, the trustee is unable to administer a trust impartially between the current and remainder beneficiaries. [903]

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[903] *See Whittier Tr. Co. v. Getty* (*In re Orpheus Tr.)*, 179 P.3d 562 (Nev. 2008) (trustee may exercise power to adjust retroactively in circumstances). *See also* Sager, *Litigation and the Total Return Trust*, 35 ACTEC J. 206 (Winter 2009); Levitan & Castleman, *There Will Be Litigation*, 147 Tr. & Est. 56 (Dec. 2008); Medlin, *Limitations on the Trustee's Power to Adjust*, 42 Real Prop., Prob. & Tr. J. 717 (Winter 2008).

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The second approach is to revise state law to permit a trustee to pay a percentage of the value of the trust (i.e., a unitrust amount) rather than the fiduciary accounting income to the current beneficiary.

Worksheet 10, below, shows that, as of September 2018, 48 states and the District of Columbia have enacted some form of the power to adjust. Although most of them enacted the power to adjust as part of the rest of the 1997 Uniform Principal and Income Act ("UPAIA"), Iowa does not include the power to adjust in its version of the UPAIA and three states — Georgia, Louisiana, and Rhode Island — have enacted the power to adjust but not the rest of the UPAIA. [904]

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[904] The text of the UPAIA is available at www.uniformlaws.org/shared/docs/principal%20and%20income/rupia00.pdf. To determine which jurisdictions have enacted the UPAIA, go to www.uniformlaws.org/LegislativeFactSheet.aspx?title=Principal and Income Act (2000).

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Worksheet 10, below, also shows that, as of September 2018, 36 states have enacted statutes that permit a trustee of an income trust to convert it to a unitrust, so that, after the conversion, the amount of "income" that must or may be distributed to the current beneficiary or beneficiaries will be defined as a percentage of the total assets of the trust. Because there is no model statute, each jurisdiction must draft its own law.

As shown in Worksheet 10, below, 34 states have enacted both the power to adjust and a unitrust-conversion statute, so that a trustee may choose either to follow the traditional income and principal rules (in which case it has the power to make adjustments between income and principal) or to convert the trust to a unitrust.

Attorneys are drafting new trusts that provide for the distribution of a unitrust amount to the current beneficiary. Because regulations under § 643 specify that such distributions will be respected for federal tax purposes only if they are allowed by state statutes, 27 state statutes now contemplate that trusts will be drafted in this manner. (See Worksheet 10, below.)

## 4. Federal Tax Safe Harbors

On January 2, 2004, the IRS issued regulations under § 643 ("the § 643 regulations") to redefine income for various purposes under federal tax law, including the definitions of income and distributable net income ("DNI"), qualification for the marital deduction, and modifications of grandfathered GST tax trusts. [905]

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[905] T.D. 9102, 69 Fed. Reg. 12 (Jan. 2, 2004) (finalizing REG-106513-00, 66 Fed. Reg. 10,396 (Feb. 15, 2001)).

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The § 643 regulations provide the following safe harbor for a state unitrust conversion statute: [906]

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[906] *Id.*

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For example, a state statute providing that income is a unitrust amount of no less than 3% and no more than 5% of the fair market value of the trust assets, whether determined annually or averaged on a multiple year basis, is a reasonable apportionment of the total return of the trust.

They provide the following safe harbor for state power-to-adjust statutes: [907]

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[907] *Id.*

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Similarly, a state statute that permits the trustee to make adjustments between income and principal to fulfill the trustee's duty of impartiality between the income and remainder beneficiaries is generally a reasonable apportionment of the total return of the trust. Generally, these adjustments are permitted by state statutes when the trustee invests and manages the trust assets under the state's prudent investor standard, the trust describes the amount that may or must be distributed to a beneficiary by referring to the trust's income, and the trustee after applying the state statutory rules regarding the allocation of receipts and disbursements to income and principal, is unable to administer the trust impartially.

The regulations continue by providing the following helpful rules: [908]

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[908] *Id.*

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Allocations pursuant to methods prescribed by such state statutes for apportioning the total return of a trust between income and principal will be respected regardless of whether the trust provides that the income must be distributed to one or more beneficiaries or may be accumulated in whole or in part, and regardless of which alternate permitted method is actually used, provided the trust complies with all requirements of the state statute for switching methods. A switch between methods of determining trust income authorized by state statute will not constitute a recognition event for purposes of section 1001 and will not result in a taxable gift from the trust's grantor or any of the trust's beneficiaries.

Finally, they give the following warnings for actions that do not fall within the unitrust or "power to adjust" safe harbor: [909]

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[909] *Id.*

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A switch to a method not specifically authorized by state statute, but valid under state law (including a switch via judicial decision or a binding non-judicial settlement) may constitute a recognition event to the trust or its beneficiaries for purposes of section 1001 and may result in taxable gifts from the trust's grantor and beneficiaries, based on the relevant facts and circumstances.

## 5. Observations

The § 643 regulations allay many concerns regarding the federal income tax, GST tax, and gift tax consequences of the exercise of the power to adjust and the conversion of income trusts into unitrusts under state statutes that satisfy their safe harbors. Accordingly, the exercise of the power to adjust over a Grandfathered Dynasty Trust [910] or the conversion of such a trust into a unitrust [911] under a qualifying statute will not result in loss of grandfathered status, a taxable gift, or a taxable exchange.

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[910] Reg. § 26.2601-1(b)(4)(i)(E) *Ex.* 12. *See, e.g.*, PLR 201129013–PLR 201129015, PLR 201128011–PLR 201128015, PLR 200901030.

[911] Reg. § 26.2601-1(b)(4)(i)(E) *Ex.* 11. *See, e.g.*, PLR 201825007, PLR 201528029, PLR 201527032, PLR 201516028, PLR 201320009, PLR 201104003, PLR 201025030.

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Because the regulations give no such assurance for the exercise of the power to adjust or a unitrust conversion under a nonqualifying statute or without statutory authority, clients should create new trusts in and move existing trusts to states that have statutes that fall within both safe harbors. Pennsylvania's power to adjust might not satisfy the safe harbor because it does not require the trustee to invest under the prudent-investor rule. [912] Similarly, the unitrust conversion statutes of Maine, Maryland, New Hampshire, and Pennsylvania might not qualify because they permit percentages outside the 3%–5% range. [913] Nonetheless, the IRS did not express concern about possible deviation from that range in rulings that involved such a statute. [914]

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[912] Mezzullo, *Final Regulations on the Definition of Fiduciary Income*, 19 Prob. & Prop. 26, 28 (Mar./Apr. 2005).

[913] Mezzulio*, Final Regulations on the Definition of Fiduciary Income,* 19 Prob. & Prop. 26, 31 (May/Apr. 2005).

[914] *See, e.g.*, PLR 201025030, PLR 200818019, PLR 200818015, PLR 200818008, PLR 200812018–PLR 200812020, PLR 200810019–PLR 200810022, PLR 200809023–PLR 200809027, PLR 200801011–PLR 200801036, PLR 200752026–PLR 200752028, PLR 200609003.

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Sometimes, it will be appropriate to convert a trust (e.g., a qualified subchapter S trust) into a 3% unitrust; other times, it will be appropriate to convert a trust (e.g., a marital-deduction trust) into a 5% unitrust. Hence, trusts should be created in or moved to states where the entire 3%–5% range is readily available.

The § 643 regulations contain no examples that illustrate the inclusion in or exclusion from DNI of capital gains incurred in connection with the exercise of the power to adjust that falls within their safe harbor, and some commentators are concerned that the inclusion of capital gains in DNI in these circumstances is problematic. [915] Consequently, clients might consider creating trusts in or moving them to states that specifically authorize such inclusion. [916] This might be desirable, for example, if the trustee can distribute taxable gains to offset taxable losses that the beneficiary has in a personal portfolio.

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[915] Blattmachr & Gans, *The Final 'Income' Regulations: Their Meaning and Importance*, 103 Tax Notes 891, 914 (May 17, 2004).

[916] *See, e.g.*, Del. Code Ann. tit. 12, § 3325(30).

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## 6. Delaware's Experience

In 2001, Delaware enacted the first total-return unitrust-conversion statute. [917] When the statute is available, the trustee may convert an income trust to a total-return unitrust with or without court approval. The trustee may select a unitrust percentage of not less than 3% nor more than 5%; decide how to account for and value illiquid assets; select the number of prior periods, if any, to use in calculating the unitrust percentage; and determine whether the current beneficiary or the trust will pay income taxes attributable to capital gains incurred to make unitrust distributions. Under the Delaware statute, the trustee is not liable if it makes the "wrong" decision.

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[917] Del. Code Ann. tit. 12, § 61-106.

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In 2004, Delaware amended its total-return unitrust-conversion statute to take account of three years of experience with the statute and the above § 643 regulations that the IRS issued early that year. The 2004 amendments also added a provision to Delaware law that recognizes newly created total-return unitrusts. [918]

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[918] Del. Code Ann. tit. 12, § 61-107.

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Delaware enacted the power to adjust in 2005. [919] In 2009, the power to adjust [920] was moved into Delaware's version of the UPAIA. [921]

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[919] Del. Code Ann. tit. 12, § 6113.

[920] Del. Code Ann. tit. 12, § 61-104.

[921] Del. Code Ann. tit. 12, § 61-101–§ 61- 605.

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## K. Court System

### 1. Introduction

A client should establish a trust in a state where judges will render the "right" decision if the trust ends up in court. Worksheet 11, below, summarizes a 2017 U.S. Chamber of Commerce study that rated the liability systems of the states that should be helpful in assessing this factor.

A Delaware court will not become involved in the administration of a trust unless an interested party seeks relief. When judicial involvement in a contested matter is needed (e.g., when the proper interpretation of the governing instrument is uncertain or a fiduciary is believed to be acting in breach of duty), prompt and efficient relief is available in the Delaware Court of Chancery and, if necessary, the Delaware Supreme Court. [922]

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[922] *See* Holland & Skeel, *Deciding Cases Without Controversy*, 5 Del. L. Rev. 115, 118–128 (2002).

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The Chancellor and Vice Chancellors of the Delaware Court of Chancery and the Justices of the Delaware Supreme Court (the courts that handle corporate as well as fiduciary matters in Delaware) are not elected. Instead, the Delaware Constitution requires that they be appointed by the Governor with the consent of a majority of the members of the Senate and that all Delaware judges come as equally as possible from the two major political parties. [923]

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[923] Del. Const. art. IV, § 3.

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### 2. Administrative Costs

Clients should establish trusts in states that will not burden trusts with unnecessary administrative costs. Thus, by making an informed designation of the law to govern matters of administration of the trust, the client may avoid periodic court accounting requirements, statutory fee schedules for trustees, and other undesirable features that would apply if the trust were created in the Home State.

For example, in Delaware, unless required by the governing instrument or ordered by the court, trustees are not required to file an inventory or reports with the Court of Chancery for an inter vivos trust (regardless of when the trust was created) [924] or for a testamentary trust established under the Will of a decedent who dies after July 31, 2005. [925] In Delaware, there is little reason to have judicial accountings because they do not have res judicata effect other than for matters to which exceptions have been taken and that have been determined by the court. [926] Although the Supreme Court of Delaware held in 1972 that a trustee that files a judicial accounting simply to obtain exculpation may have to pay the cost of the

accounting itself, [927] the Delaware Court of Chancery held in 2009 that a trustee may pay its accounting costs from a trust if the governing instrument contains appropriate language. [928] Moreover, there now is a nonjudicial mechanism for the prompt settlement of accounts of trustees leaving office. [929]

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[924] Del. Code Ann. tit. 12, § 3522.

[925] Del. Code Ann. tit. 12, § 3524(a)(2).

[926] Del. Court of Chancery Rule 129.

[927] *In re Helena S. Corcoran Trusts*, 282 A.2d 653 (Del. Ch. 1971), *aff'd sub nom. Bankers Tr. Co. v. Duffy*, 295 A.2d 725 (Del. 1972).

[928] *Merrill Lynch Tr. Co., FSB v. Campbell*, 2009 BL 217734, 2009 WL 2913893, at *11, at *13 (Del. Ch. Sept. 2, 2009).

[929] *See* Del. Code Ann. tit. 12, § 3585(a)(2).

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### 3. Recourse to Highest Court

Following the U.S. Supreme Court's decision in *Commissioner v. Estate of Bosch*, [930] the IRS generally is bound in a tax controversy only if a matter is adjudicated by a state's highest court. Massachusetts law gives the Supreme Judicial Court original jurisdiction in such disputes. [931]

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[930] 387 U.S. 456 (1967).

[931] Mass. Gen. L. ch. 215, § 6.

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### 4. Availability of Declaratory Judgment

Whereas courts in many states refuse to consider petitions for declaratory judgment, courts in other states welcome them. [932]

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[932] *See* IV.D.3.b.(7), above.

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## L. Surviving Spouses' Right of Election

All common-law states, except Georgia, allow a surviving spouse to take an elective share of the deceased spouse's assets if the deceased spouse does not provide adequately for the survivor. For good and bad reasons, individuals sometimes ask whether they may defeat their spouses' elective-share rights by creating revocable or irrevocable trusts in other jurisdictions. [933]

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[933] *See Restatement (Second) of Conflict of Laws* § 265 (1971). *See also* Cunningham, *Michigan's Elective Share: An Epic Failure*, 94 U. Det. Mercy L. Rev. 273 (Spring 2017); Vallario, *The Elective Share Has No Friends: Creditors Trump Spouse in the Battle Over the Revocable Trust*, 45 Cap. U.L. Rev. 333 (Spring 2017); Scroggin, *Limit Unwanted Spousal Asset Rights in Estate Plans*, 43 Est. Plan. 30 (Apr. 2016); Begleiter, *Grim Fairy Tales: Studies of Wicked Stepmothers, Poisoned Apples, and the Elective Share*, 78 Alb. L. Rev. 521 (2015). *See generally* Shapo, Bogert & Bogert, The Law of Trusts and Trustees § 211 at 90–139 (3d ed. 2007); Tanouye, Surviving Spouse's Rights to Share in Deceased *Spouse's* Estate (July 2018), www.actec.org/assets/1/6/Surviving_Spouse's_Rights_to_Share_in_Deceased_Spouse's_Estate.pdf. For detailed coverage of this subject, see 841 T.M., *Spouse's Elective Share*. For a case in which a pretermitted surviving spouse sought unsuccessfully to reach the assets of her deceased husband's revocable trust, see *In re Trust Under Deed of David P. Kulig Dated January 12, 2001*, 175 A.3d 222, 238 (Pa. 2017). *See also* Sager & Terebelo, *Trust Under Deed of Kulig*, LISI Est. Plan. Newsl. #2675 (Oct. 30, 2018), www.leimbergservices.com.

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As mentioned above, the comments to § 270 of the *Restatement (Second) of Conflict of Laws* suggest that the designation of a law to govern an inter vivos trust might be disregarded if it would frustrate a surviving spouse's elective-share rights. For various reasons, such a public policy, if it ever existed, probably is not as strong as it once was. [934] Nevertheless, the *Restatement*, the Scott treatise, and the Bogert treatise all indicate that there should be such an exception. [935] According to the Scott treatise: [936]

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[934] Domsky, *Till Death Do Us Part ... After That, My Dear, You're on Your Own: A Practitioner's Guide to Disinheriting a Spouse in Illinois*, 29 S. Ill. U.L.J. 207 (Winter 2005).

[935] *Restatement (Second) of Conflict of Laws* § 270 cmts. b, e (1971); 7 *Scott and Ascher on Trusts* § 45.4.2.4 at 3254–3260; *Bogert on Trusts* § 301 at 113–114.

[936] 7 *Scott and Ascher on Trusts* § 45.4.2.4 at 3255 (footnotes omitted).

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If ... there is a statute in the settlor's domicil that gives the settlor's surviving spouse an elective share of the trust property, it would appear that for this purpose the settlor's domicil, rather than the place of administration, would have the most significant relationship with the trust. Because the purpose of the statute is to protect the decedent's surviving spouse, decedent should not be able to avoid this policy

simply by creating a trust to be administered in another state in which there is no, or less, protection for the surviving spouse.

But, three pertinent cases go the other way. [937]

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[937] *Johnson v. La Grange State Bank*, 383 N.E.2d 185 (Ill. 1978); *Rose v. St. Louis Union Tr. Co.*, 253 N.E.2d 417 (Ill. 1969); *Nat'l Shawmut Bank v. Cumming*, 91 N.E.2d 337 (Mass. 1950). *See* CCA 201416007 (marital deduction not allowable to extent elective share was to be satisfied with assets of foreign trust).

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Hence, in *National Shawmut Bank v. Cumming*, [938] the Supreme Judicial Court of Massachusetts applied Massachusetts rather than Vermont law to deny a Vermont widow's attempt to satisfy the elective rights granted her by Vermont law.

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[938] 91 N.E.2d 337 (Mass. 1950).

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A commentator discusses the other two pertinent cases as follows: [939]

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[939] Danforth, *Estate Planning Implications of Surviving Spouse's Elective Share Rights*, 22 Tax Mgmt. Est., Gifts & Tr. J. 235, 242 (Nov. 11, 1997) (footnotes omitted). *See* Domsky, *Till Death Do Us Part ... After That, My Dear, You're on Your Own: A Practitioner's Guide to Disinheriting a Spouse in Illinois*, 29 S. Ill. U.L.J. 207, 225–230 (Winter 2005).

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The courts of at least one other jurisdiction — Illinois — have embraced the principle articulated in *Shawmut Bank* that the law of the situs of a trust should control with respect to elective share issues. In the first Illinois case to address this issue, *Rose v. St. Louis Union Trust Co.*, an Illinois decedent established an irrevocable trust with a Missouri corporation as trustee. The trust was administered in Missouri, and the trust instrument specified the application of Missouri law to its administration. Under these circumstances, the court ruled that the validity of the trust with respect to the surviving spouse's elective share rights would be determined under Missouri law, which it further determined precluded the spouse from having any rights to the trust property.

In *Johnson v. La Grange State Bank*, the Supreme Court of Illinois extended its ruling in *Rose* to assets held in a revocable trust. As described earlier in this article, shortly before her death the decedent in *Johnson* established a revocable trust in Illinois, naming herself as trustee and La Grange State Bank, an Illinois trust company, as successor trustee. She then moved to Florida and lived there at her death. The decedent's husband brought an action in an Illinois court to set aside the revocable trust insofar as it deprived him of his elective share rights under Florida law. The Supreme Court of Illinois ruled that the trust assets were not subject to the surviving spouse's elective share claim. In reaching its decision, the court made the following comment on the relevance of Illinois law:‘As our appellate court properly noted, the trust was created in this State, the corpus has remained here, the [surviving spouse] was domiciled here at the time of the decedent's death, and the principal defendants are located in this State.’

Based on these factors, the court applied Illinois law and determined that the trust assets were not subject to the spouse's claim.

The Maryland Court of Appeal's 2008 *Karsenty v. Schoukroun* [940] decision might illustrate a weakening of the strong public policy against defeating surviving spouses' elective-share rights. There, the surviving spouse attempted to reach the assets in the deceased spouse's inter vivos trust. The court summarized its views as follows: [941]

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[940] 959 A.2d 1147 (Md. 2008).

[941] *Id.* at 1172–1173 (citations omitted). *See* 755 ILCS 25/1 (regarding illusory inter vivos transfers).

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[W]hen a surviving spouse seeks to invalidate the non-probate disposition of an asset, a scrutinizing court must focus on the nature of the underlying inter vivos transfer. If it was "complete and bona fide" or done in "good faith" (both phrases meaning the same thing in this context), the court must respect the estate planning arrangements of the decedent and may not invalidate the transaction; however if it was "a mere device or contrivance," "a mere fiction," "a sham," or "colorable" (each also sharing the same meaning in this context), the court shall invalidate the underlying transaction as to the surviving spouse. In order to answer this question, a court must consider whether the decedent truly intended that the inter vivos transfer divest her or him of ownership in form, but not in substance. Stated in more practical language, the question for a court to decide is whether the decedent intended that the transfer change nothing, except how the property is directed at the decedent's death. Notwithstanding our previous references to "fraud" on marital rights, because we ultimately are not concerned with whether a decedent intended to deprive her or his surviving spouse of property, we emphasize today that it is more helpful for a court to think of a sham transfer in this context as an unlawful frustration of the surviving spouse's statutory share.

The court then enumerated factors for Maryland courts to consider in future cases [942] and remanded the case to the trial court for further proceedings. [943]

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[942] *Id.* at 1173–1180.

[943] *Id.* at 1180.

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The surviving spouse of a Delaware decedent never has been able to reach trust assets by electing against the Will, [944] and Delaware law does not defer to the law of a decedent's domicile to determine a surviving spouse's elective-share rights. Rather, it is governed by the law of the situs of the property. [945]

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[944] Del. Code Ann. tit. 12, § 901(a), § 908(b). *See Machulski v. Boudart*, 2008 BL 72398, 2008 WL 836065, at *2, (Del. Super. Ct. Mar. 28, 2008) ("A transfer of the house into a trust, even two months before the decedent's death, would have removed it from his 'contributing estate', regardless of whether it removed it from his elective estate").

[945] Del. Code Ann. tit. 12, § 901(b).

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Hence, by creating a revocable or irrevocable trusts elsewhere, trustors might be able to defeat their spouses' elective-share rights.

The IRS shocked the estate-planning world when it issued Rev. Proc. 2005-24, which required spouses of trustors of certain post-June 27, 2005, inter vivos CRTs to waive rights to reach such trusts by electing against the Will. Under § 2-205 of the UPC, a surviving spouse may reach the assets of an inter vivos CRT created during marriage to the deceased spouse (but not while the deceased spouse was unmarried or was married to a prior spouse) by electing against the Will. [946] Section 2-205 is in effect in at least 14 states — Alaska, Colorado, Hawaii, Kansas, Maine, Minnesota, Montana, Nebraska, New Jersey, North Dakota, South Dakota, Utah, Virginia, and West Virginia. [947] Although the IRS deferred the effective date of the revenue procedure in 2006, [948] it alerted taxpayers as recently as 2014 that it has not forgotten the issue by requesting comments on procedures to ensure that elective rights do not affect assets for which a charitable deduction was taken on the creation of a CRT. [949] A client therefore should consider choosing a jurisdiction for a CRT where it will be immune from a spouse's election so that the trust's assets will be protected in case the IRS issues similar restrictions in the future or in case a surviving spouse actually elects against the Will.

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[946] UPC § 2-205 (amended 2010).

[947] *See* Alaska Stat. § 13.12.205; Colo. Rev. Stat. § 15-11-205; Haw. Rev. Stat. § 560:2-205; Kan. Stat. Ann. § 59-6a205; Me. Rev. Stat. Ann. tit. 18-A, § 2-202; Minn. Stat. § 524.2-205; Mont. Code Ann. § 72-2-222; Neb. Rev. Stat. § 30-2314; N.J. Rev. Stat. § 3B:8-3; N.D. Cent. Code § 30.1-05-02; S.D. Codified Laws A§ 29A-2-205; Utah Code Ann. § 75-2-206; Va. Code Ann. § 64.2-308.6; W. Va. Code § 42-3-2.

[948] Notice 2006-15.

[949] 2014 Tax Notes Today 67-32 (Apr. 8, 2014).

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## M. Life Insurance Trusts

### 1. Introduction

As with many undertakings, corporate fiduciaries must acquaint themselves with any monitoring duties that might be imposed by federal and state regulatory agencies with respect to life insurance policies. Subject to that caveat, trustees must take account of three concerns specific to an irrevocable life-insurance trust ("ILIT"), as discussed below.

### 2. Insurable Interest of Trustee

In 2005, a federal district court in Virginia held that an insurer could rescind an insurance policy owned by an ILIT following the insured's death because the applicant made misrepresentations on the application and because, under Maryland law, the trustee lacked an insurable interest in the insured's life. [950] Even though the Fourth Circuit affirmed the district court's holding on the first ground only and vacated its holding on the insurable-interest ground, [951] trustors should create ILITs in the following states (e.g., Alaska, Delaware, Florida, Georgia, Maine, Maryland, Minnesota, Nevada, Oklahoma, South Dakota, Utah, Virginia, or Washington) [952] where a trustee clearly has an insurable interest in the insured's life, regardless of the identity of the beneficiaries. The Uniform Laws Commission formed a committee to draft a uniform statute to address this issue, which it finalized in the summer of 2010. [953] Trustors may establish ILITs in the following states that have adopted this provision — Colorado, Kansas, Kentucky, Michigan, New Mexico, North Carolina, North Dakota, West Virginia, and Wyoming. [954]

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[950] *Chawla v. Transamerica Occidental Life Ins. Co.*, 2005 BL 6754, 2005 WL 405405 (E.D. Va. Feb. 3, 2005) *aff'd in part and vac'd in part*, 440 F.3d 639 (4th Cir. 2006).

[951] *Chawla v. Transamerica Occidental Life Ins. Co.*, 440 F.3d 639 (4th Cir. 2006).

[952] *See* Alaska Stat. § 21.42.020; Del. Code Ann. tit. 18, § 2704(c)(5); Fla. Stat. § 627.404(2)(b)(5); Ga. Code Ann. § 33-24-3(c); Me. Rev. Stat. Ann. tit. 24-A, § 2404; Md. Code Ann., Ins. § 12-201(b)(6); Minn. Stat. Ann. § 60A.0783 (Sub.2)(d); Nev. Rev. Stat. § 687B.040(2); 36 Okla. Stat. § 3604(c)(4); S.D. Codified Laws § 58-10-4(6); Utah Code Ann. § 31A-21-104(1)(b), § 31A-21-104(3); Va. Code Ann. § 38.2-301(B)(5); Wash. Rev. Code § 48.18.030(3)(c).

[953] To view the Insurable Interest Amendments to the Uniform Trust Code, go to https://uniformlaws.org/. To identify the states that have enacted the amendments, go to https://my.uniformlaws.org/committees/community-home?CommunityKey=23e21d77-30a6-4321-87d6-5c341bc0086a.

[954] *See* Colo. Rev. Stat. § 15-5-114; Kan. Stat. Ann. § 58a-113; Ky. Rev. Stat. § 386B.1-120; Mich. Comp. Laws § 700-7114; N.M. Stat. Ann. § 46A-1-113; N.C. Gen. Stat. § 36C-1-114; N.D. Cent. Code § 59-09-13; W. Va. Stat. § 44D-1-113; Wyo. Stat. § 4-10-112.

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The enforceability of stranger-originated life insurance ("STOLI") policies has been controversial in recent years. [955] The Supreme Court of Delaware addressed the issue in 2011 holding that the lack of an insurable interest voids the policy. [956]

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[955] *See* Zaritsky, *STOLI Cases Continue to Yield Inconsistent Results*, LISI Est. Plan. Newsl. #2534 (Apr. 14, 2017), www.leimbergservices.com; Leimberg, *Wells Fargo v. Pruco: Florida Supreme Court Rules Incontestability Clause Applies Regardless of Misrepresentations and Even Absent Good Faith Purchase of Policy*, LISI Est. Plan. Newsl. #2460 (Oct. 6, 2016), www.leimbergservices.com; Beers, *Trends and Developments in Investor-Owned Life Insurance*, 37 Tax Mgmt. Est., Gifts & Tr. J. 325 (Nov. 8, 2012).

[956] *PHL Variable Ins. Co. v. Price Dawe 2006 Ins. Tr., ex rel. Christiana Bank and Tr. Co.*, 28 A.3d 1059, 1068 (Del. 2011). *See* Covey & Hastings, *Life Insurance Trust; Stranger Originated Life Insurance (SOLI); Delaware Law*, Prac. Drafting 10604–10611 (Oct. 2011); Leimberg, *PHL Variable Insurance Company v. Dawe: Delaware Supreme Court Holds Lack of Insurable Interest Voids Policy Ab Initio*, LISI Est. Plan. Newsl. #1872 (Sept. 26, 2011), www.leimbergservices.com.

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## 3. Trust Design

The applicable law should relieve a trustee from liability for a life-insurance policy held in a trust. In this regard, a Delaware Statute does so provided that the insured is notified of such limitation of the trustee's responsibilities in the governing instrument or in a separate writing. [957] An ILIT may also be designed as a directed trust.

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[957] Del. Code Ann. tit. 12, § 3302(d). *See Paradee v. Paradee*, 2010 BL 316939, 2010 WL 3959604, at *15 (Del. Ch. Oct. 5, 2010). *See also* Klotz, *Fixing the Imploding Irrevocable Life Insurance Trust*, 155 Tr. & Est. 32 (June 2016); Klein, *Issues and Conflicts Associated With Trust-Owned Life Insurance: Managing Policies and Fulfilling Fiduciary Obligations*, 57 Tax Mgmt. Memo. 223 (May 30, 2016); Flotron & Whitelaw, *A Comprehensive Perspective on the Four UPIA-TOLI Cases, Plus One That Includes the UTC, and Their Astounding Implications for ILIT Trustees (Part 2)*, LISI Est. Plan. Newsl. #2438 (July 20, 2016), www.leimbergservices.com.

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State statutes regarding the acquisition and management of life insurance policies are listed at the end of Worksheet 6.

Like many others, the author's institution — Wilmington Trust Company — accepts appointment as trustee of an ILIT when combined with other business but generally declines appointment as trustee of a stand-alone ILIT. Instead, it is suggested that trustors appoint individual trustees until policies mature.

## 4. Premium Tax

Effective as of 2016, Delaware assesses the lowest premium tax in the country on large private-placement policies in ILITs: 0% on net premiums over $100,000. [958] Alaska [959] and South Dakota [960] also assess particularly low premium taxes for large policies.

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[958] Del. Code Ann. tit. 18, § 702(c)(3).

[959] Alaska Stat. § 21.09.210(m)(2).

[960] S.D. Codified Laws § 10-44-2(1)(a).

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## N. Noncharitable Purpose Trusts

At common law, a trust created for a noncharitable purpose (e.g., to care for pets living at a decedent's death) was invalid because no one could enforce the trust. [961] As shown in Worksheet 12, below, several state statutes authorize noncharitable purpose trusts to last for 21 years, some state statutes permit such trusts to last for a longer period, and others allow them to be perpetual. It should be noted, however, that a state cannot make perpetual noncharitable purpose trusts available simply by saying that the common-law rule against perpetuities does not apply to such trusts. Professor Hirsch explains: [962]

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[961] *See* Ausness, *Non-Charitable Purpose Trusts: Past, Present, and Future*, 51 Real Prop., Tr. & Est. L.J. 321 (Fall 2016); Bove & Mattson, *The Purpose Trust: Drafting Becomes a Work of Art*, 43 Est. Plan. 26 (Oct. 2016); Hirsch, *Delaware Unifies the Law of Charitable and Noncharitable Purpose Trusts*, 36 Est. Plan. 13 (Nov. 2009); Hirsch, *Bequests for Purposes: A Unified Theory*, 56 Wash. & Lee L. Rev. 33 (Winter 1999); Hirsch, *Trusts for Purposes: Policy, Ambiguity, and Anomaly in the Uniform Laws*, 26 Fla. St. U.L. Rev. 913 (Summer 1999).

[962] Hirsch, *Delaware Unifies the Law of Charitable and Noncharitable Purpose Trusts*, 36 Est. Plan. 13, 18–19 (Nov. 2009) (footnotes omitted; emphasis in original). *See* Ausness, *Noncharitable Purpose Trusts: Past, Present, and Future*, 51 Real Prop., Tr. & Est. L.J. 321 (Fall 2016); Hirsch, *Trusts for Purposes: Policy, Ambiguity, and Anomaly in the Uniform Laws*, 26 Fla. St. U.L. Rev. 913 (Summer 1999).

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Delaware is not the only state vying for trust business. In fact, its current legislative initiative appears a reaction to its competitors, six of whom have also sought to elbow their way into the noncharitable purpose trust market. Statutes in Wyoming (dating to 2003), Idaho (dating to 2005), Maine (dating to 2005), New Hampshire (as amended in 2006), North Dakota (dating to 2007), and South Dakota (as amended in 2008), likewise set no limit on the duration of a noncharitable purpose trust. Yet all these other statutes are vulnerable to litigation on this score, for none of them affirmatively authorizes perpetual noncharitable purpose trusts. Legislators simply *omitted* express durational limitations, while also, in most of these states, repealing “the rule against perpetuities.”

The respective drafters apparently assumed that perpetual noncharitable purpose trusts become effective once the rule against perpetuities disappears. That assumption is erroneous: The rule against perpetuities applies only to remote *contingencies*, which a noncharitable purpose trust need not contain. Technically speaking, these trusts are subject to a second, unnamed common-law rule, limiting the *duration* of a noncharitable purpose trust to “the period” of the rule against perpetuities. Whether a court would construe the repealing statutes so strictly remains uncertain, but they leave sufficient ambiguity as to invite litigation. In comparison, Delaware's repealing statute applies more assuredly to “the common-law rule against perpetuities, [and] *any common-law rule limiting the duration of noncharitable purpose trusts*.” In addition, among these states, only Delaware extends the cy pres doctrine to its potentially protracted noncharitable purpose trusts.

To the author's knowledge, Delaware (2008), South Dakota (2011), and Wyoming (2013), which allow perpetual noncharitable-purpose trusts, and Washington, which allows 150-year trusts for animals, [963] are

the only states that have made this change.

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[963] Wash. Rev. Code § 11.98.130, § 11.118.005–§ 11.118.110.

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One of these uses of this vehicle is to maintain a family vacation property once the members of the senior generation have died. An appellate court in Michigan confronted the deficiencies of the use of traditional trusts in the 2015 *Trupp v. Naughton* case. In that case, the court terminated a trust created for this purpose because "the purpose could not be met where none of the parties could follow the terms of the trust." [964]

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[964] *Trupp*, 2015 WL 3389414, at *2.

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The tax attributes of purpose trusts will vary from case to case. In this regard, the IRS announced in 2015 that a Florida gun trust constituted a "trust" for federal tax purposes. [965]

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[965] IRS Info. Ltr. 2015-0039 (Nov. 9, 2015), https://www.irs.gov/pub/irs-wd/15-0039.pdf.

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A perpetual noncharitable-purpose trust might be used to:
• Maintain a family's vacation compound; [966]

• Purchase stock in the family company from family members who wish to sell;

• Publish manuscripts that were unpublished at an author's death; or

• Maintain a collection of antique automobiles.

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[966] *See Trupp v. Naughton*, 2015 BL 451352, at *3 (Mich. Ct. App. May 26, 2015) (trust holding vacation cottage terminated where "none of the parties could follow the terms of the trust").

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Estates, Gifts and Trusts Portfolios
Trusts
Portfolio 867-2nd: Choosing a Domestic Jurisdiction for a Long-Term Trust
Detailed Analysis
VI. Ethical and Practical Concerns When Creating a Dynasty Trust in a Trust State

## A. Background

If an attorney and a client conclude that the client should create a trust under the law of a state in which the attorney is not licensed to practice law, the attorney must determine how to implement the trust without engaging in the unauthorized practice of law or committing any other ethical violation, committing malpractice, or losing the client. [967]

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[967] *See* Peter J. Walsh, *Multijurisdictional Practice of Law Issues in Estate Planning*, 40 Est. Plan. 23 (June 2013).

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## B. Ethical Principles

Although each state has its own rules that govern conduct by attorneys admitted to practice in the state, the ABA *Model Rules of Professional Conduct* ("Model Rules") [968] are the basis of the rules in effect in all 50 states and the District of Columbia. [969] California has its own rules. Two Model Rules are of particular concern. First, Rule 5.5 of the Model Rules provides in pertinent part as follows: [970]

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[968] Model Rules of Prof'l Conduct (2002). For additional discussion of the Model Rules, see 801 T.M., *Ethical Rules for Estate Planning Lawyers—Conflicts, Confidentiality, and Other Issues*.

[969] A list of the states that have adopted the Model Rules is available at www.americanbar.org/groups/professional_responsibility/publications/model_rules_of_professional_conduct/alpha_list_state_adopting_model_rules/. Effective November 1, 2018, California was the final state to adopt a version of the Model Rules.

[970] Model Rules of Prof'l Conduct R. 5.5 (2002).

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(a) A lawyer shall not practice law in a jurisdiction in violation of the regulation of the legal profession in that jurisdiction, or assist another in doing so.

(b) A lawyer who is not admitted to practice in this jurisdiction shall not:

(1) except as authorized by these Rules or other law, establish an office or other systematic and continuous presence in this jurisdiction for the practice of law; or

(2) hold out to the public or otherwise represent that the lawyer is admitted to practice law in this jurisdiction.

(c) A lawyer admitted in another U.S. jurisdiction, and not disbarred or suspended from practice in any jurisdiction, may provide legal services on a temporary basis in this jurisdiction that:

(1) are undertaken in association with a lawyer who is admitted to practice in this jurisdiction and who actively participates in the matter; ...

(4) are not within paragraph (c)(2) or (c)(3) [that relate to judicial and alternative-dispute-resolution proceedings] and arise out of or are reasonably related to the lawyer's practice in a jurisdiction in which the lawyer is admitted to practice.

Second, Model Rule 1.1 provides as follows: [971]

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[971] Model Rules of Prof'l Conduct R. 1.1 (2002).

A lawyer shall provide competent representation to a client. Competent representation requires the legal knowledge, skill, thoroughness and preparation reasonably necessary for the representation.

Neither the commentaries to the Model Rules nor the 2016 ACTEC commentaries [972] on them specifically address the subject.

[972] ACTEC Commentaries on the Model Rules of Prof'l Conduct (5th ed. 2016).

## C. Malpractice Concerns

Each state has its peculiarities. For example, whereas the residuary clause in a Will exercises the testator's general powers of appointment in New York, [973] it does not in Connecticut. [974] Similarly, because the exercise of a nongeneral power of appointment over a Delaware trust begins a new perpetuities period in certain circumstances, [975] attorneys must make sure that clients' exercises of such powers will not inadvertently subject the trust to federal estate or gift tax pursuant to the Delaware tax trap. [976] Nevertheless, the malpractice risks of creating trusts in another state may be minimized through research, experience, and/or the involvement of local counsel.

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[973] N.Y. Est. Powers & Trusts Law § 10-6.1(a)(4). *See Estate of Greve v. Commissioner*, T.C. Memo. 2004-91.

[974] *Matter of Chappell*, 883 N.Y.S.2d 857, 863 (N.Y. Sur. Ct. N.Y. Cty. 2009).

[975] Del. Code Ann. tit. 25, § 501–§ 505.

[976] § 2041(a)(3), § 2514(d). *See* II.F.3., above.

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## D. Practical Considerations

While some attorneys from various parts of the country draft Delaware estate planning documents regularly without engaging Delaware counsel, others draft such documents but insist that they be approved by local counsel prior to execution. In the author's experience, Delaware counsel always is sensitive to the existing attorney-client relationship.

Estates, Gifts and Trusts Portfolios
Trusts
Portfolio 867-2nd: Choosing a Domestic Jurisdiction for a Long-Term Trust
Detailed Analysis
VII. Moving a Dynasty Trust to a More Favorable State

## A. Introduction

### 1. Background

From time to time, the beneficiaries of a trust might explore replacing a trustee or the beneficiaries and trustees of a trust might investigate whether they may change the law that governs the trust's validity, construction, or administration or the place where it is administered. The remainder of this section gives reasons why beneficiaries might want to change a trust's trustee, governing law, or situs; identifies potential roadblocks to such a change; and offers some comments. The balance of this section focuses on how changing governing law or trust situs might benefit a trust and its beneficiaries.

### 2. Reasons to Move a Trust

In descending order of frequency, the most common reasons why beneficiaries explore moving a trust are: [977]

• to address dissatisfaction with the current corporate trustee (whether or not a purported breach of trust is involved);

• to escape state income tax on the trust's accumulated ordinary income and capital gains;

• to improve the trust's investment performance (e.g., because a new trustee will provide better investment results or because a change of governing law will enable a cotrustee or adviser to direct investments);

• to reduce fees and administrative costs (including accounting costs);

• to consolidate trusts at a single location;

• to amend the terms of the trust;

• to convert an income trust into a total-return unitrust;

• to obtain more effective creditor protection for beneficiaries;

• to extend the trust's duration;

• to avoid burdensome state regulatory requirements (usually on charitable trusts);

• to take advantage of a virtual representation statute in order to avoid the appointment of a guardian or trustee ad litem to represent unknown or minor beneficiaries in a court proceeding;

• to use a statute that offers more grounds for removing a trustee; and/or

• to qualify for diversity jurisdiction so that a dispute may be litigated in federal district court.

[977] This list and the next list are based on comments made by Carol A. Johnston, Richard W. Nenno, Joshua S. Rubenstein, and W. Donald Sparks, II, at *The Nuts and Bolts of Changing the Situs of a Trust*, 40 U. Miami Inst. on Est. Plan. Special Sess. 3-B (Jan. 12, 2006).

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## 3. Roadblocks to Moving a Trust

In descending order of frequency, the most common roadblocks to moving a trust are:
• lack of agreement among the beneficiaries;

• lack of appropriate language in the governing instrument;

• court intervention (e.g., refusal of a court to permit the move or excessive cost of a court proceeding);

• fee issues (e.g., principal termination fee for current trustee; excessive fees of new trustee);

• uncooperative trustees;

• accounting requirements and liability issues (e.g., releases and indemnifications);

• choice-of-law issues;

• conflict-of-interest issues;

• involvement of guardian or trustee ad litem who objects to the move; and/or

• inability to terminate all ties to the original jurisdiction.

## 4. Comments

Although beneficiaries might have valid reasons to move a trust, one or more of the above roadblocks might make it impossible or impracticable to make the change. Accordingly, it is essential in the creation of a new trust to select the right trustees, situs, and governing law and to include appropriate language in case a change is needed in the future.

## B. What Law Applies?

### 1. Restatement Approach — Introduction

Moving the situs or place of administration of a trust from one state to another will not automatically result in a change in the law that applies. [978] In 2013, however, the Supreme Court of Delaware, relying on the *Restatement (Second) of Conflict of Laws*, [979] held that if the governing instrument provides that the validity, construction, and administration of a trust will be governed by the law of a specific state, then moving the trust to Delaware will change the law that governs matters of administration (but not of validity or construction) to that of Delaware unless the testator or trustor intended the designation of the original state's law to be "permanent." [980] Thus, if the governing instrument contains no such permanent designation, then moving the trust is worth exploring.

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[978] *See* 7 *Scott and Ascher on Trusts* § 45.5.3.2 at 3302–3303.

[979] *See Restatement (Second) of Conflict of Laws* § 267–§ 282 (Am. Law Inst. 1971).

[980] *In re Peierls Family Inter Vivos Tr.*, 77 A.3d 249, 259 (Del. 2013).

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Under the *Restatement (Second) of Conflict of Laws*, the determination of what state's law is used to resolve an issue that arises in the administration of a trust is a function of whether the trust holds movables or land; whether the trust was created by Will or inter vivos; and whether the issue implicates the validity or construction of a trust provision, the administration of the trust, or restraints on the alienation of beneficiaries' interests. [981] It also is relevant whether the governing instrument designates the law of a particular state on the matter. [982]

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[981] *See* III.B., above.

[982] *See* III.B., above.

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### 2. Restatement Approach — Trust of Movables — Law Designated

#### a. Trust Under Will

#### (1) Validity

The validity of a provision of a trust of movables created by Will (e.g., whether the provision violates the rule against perpetuities or the rule against accumulations) is determined by the law designated by the

testator provided that:
• The designated state has a substantial relation to the trust; and

• The provision does not offend a strong public policy of the testator's domicile. [983]

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[983] *Restatement (Second) of Conflict of Laws* § 269(b) (Am. Law Inst. 1971).

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The beneficiaries and trustee might want to change the law that governs a trust's validity to get a longer perpetuities period or to escape a state where the rule against accumulations is in effect. As noted previously, these issues should not raise considerations of strong public policy. [984] A state has a substantial relation to a trust if it is the state in which the trust is to be administered, the place of business or domicile of the trustee at the testator's death, the testator's domicile at that time, or the domicile of the beneficiaries. [985] If the Will designates a particular Trust State to govern questions of validity, subsequent events (e.g., a change of trustee) probably will have no bearing on that choice. But, if the Will provides that questions of validity are to be resolved by the law of the state where the trust is administered from time to time, a change of trustee or place of administration should result in a change of governing law.

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[984] *Restatement (Second) of Conflict of Laws* § 269 cmt. i (Am. Law Inst. 1971).

[985] *Restatement (Second) of Conflict of Laws* § 269 cmt. f (Am. Law Inst. 1971).

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### (2) Administration

The administration of a provision of a trust of movables created by Will is determined by the law designated by the testator. [986] The beneficiaries and trustee might want to change the law that governs a trust's administration to get a better directed trust statute, a better unitrust-conversion or power-to-adjust law, or a statute to modify or terminate the trust. If the Will designates a particular Trust State to govern questions of administration, subsequent events (e.g., a change of trustee) might have no bearing on that choice. But, Delaware attorneys have found that, when trusts are moved to Delaware, a court order sometimes changes the law that governs administration (but not validity or construction) to Delaware because that is where the trust will be administered. Also, if the Will provides that questions of administration are to be resolved by the law of the state where the trust is administered from time to time, a change of trustee or place of administration should result in a change of governing law as well.

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[986] *Restatement (Second) of Conflict of Laws* § 271(a) (Am. Law Inst. 1971).

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### (3) Construction

The law that governs the construction of a provision of a trust of movables created by Will is the law designated in the Will. [987]

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[987] *Restatement (Second) of Conflict of Laws* § 268(1) (Am. Law Inst. 1971).

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### (4) Restraints on Alienation

The law that governs the ability of creditors to reach a beneficiary's interest in a trust of movables created by Will is the law of the state in which the testator has fixed the administration of the trust. [988]

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[988] *Restatement (Second) of Conflict of Laws* § 273(a) (Am. Law Inst. 1971). *See id.* cmt. b.

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## b. Trust Created Inter Vivos

### (1) Validity

The validity of a provision of a trust of movables created inter vivos (e.g., whether the provision violates the rule against perpetuities or the rule against accumulations) is determined by the law designated by the trustor provided that:
• The designated state has a substantial relation to the trust; and

• The provision does not offend 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. [989]

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[989] *Restatement* § 270(a).

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The beneficiaries and trustee of a trust might want to explore moving a trust to get a longer perpetuities period or to avoid the rule against accumulations. A state has a substantial relation to a trust when it is the state, if any, which the trustor designated as that in which the trust is to be administered, the place of business or domicile of the trustee at the time of the creation of the trust, the location of the trust assets at that time, the domicile of the trustor at that time, or the domicile of the beneficiaries. [990]

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[990] *Restatement* § 270 cmt. b.

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### (2) Administration

The administration of a provision of a trust of movables created inter vivos is determined by the law designated by the trustor. [991] The beneficiaries and trustee of such a trust might want to investigate changing the law that governs questions of administration to get a better directed trust statute. If the trust specifies that issues of administration are to be governed by the law of a particular state, changing the

situs of the trust or the trustee might not result in a change of governing law, but Delaware practitioners have found that court decrees relating to the move of trusts to Delaware sometimes contain a change of law governing administration. If the trust says that questions of administration will be resolved by the law of the state where the trust is administered from time to time, then the governing law will change upon the change of situs.

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[991] *Restatement* § 272(a).

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### (3) Construction

The law that governs the construction of a provision of a trust of movables created inter vivos is that designated in the governing instrument. [992]

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[992] *Restatement* § 268(1).

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### (4) Restraints on Alienation

Whether a creditor may reach a beneficiary's interest in an inter vivos trust of movables is determined under the law of the state in which the trustor has manifested an intention that the trust be administered. [993]

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[993] *Restatement* § 273(b). *See id.* cmt. c. *See also Bowne of Phoenix, Inc. v. Bank One Arizona, NA*, 1996 WL 694116, at *2 (Ariz. Ct. App. Dec. 5, 1996) (Arizona not Pennsylvania law governed ability of creditors to reach beneficiary's interest because Pennsylvania court had transferred situs to Arizona).

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## 3. Restatement Approach — Trust of Movables — Law Not Designated

### a. Trust Under Will

### (1) Validity

Regarding the determination of the law that will be used to resolve a question of validity under a trust of movables created by Will when no governing law is designated, § 269(b) of the *Restatement* provides in pertinent part: [994]

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[994] *Restatement (Second) of Conflict of Laws* § 269(b) (1971).

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The validity of a trust of interests in movables created by will is determined 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 ...by the local law of the state of the testator's domicil at death, except that the local law of the state where the trust is to be administered will be applied if application of this law is necessary to sustain the validity of the trust.

A comment to § 269 further develops the above rule as follows: [995]

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[995] *Restatement* § 269 cmt. g (cross-references omitted).

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When the testator does not designate a state whose local law is to govern the validity of the trust, or when the designation will not be given effect, the trust will be upheld if it is valid under either the local law of the state of the testator's domicil at death or the local law of the state where the trust is to be administered, provided that this would not be contrary to the strong public policy of the state of the testator's domicil at death.

If a testator by will creates a trust to be administered in a state other than that of his domicil, the trust will not be invalid as in violation of the rule against perpetuities, if it would be valid either under the local law of the state of his domicil or under the local law of the state of the place of administration. This is true also as to a rule against accumulations. It is true also where by the local law of one or the other of these states trusts are not permitted. In these situations, there is no such strong policy of the state of the domicil as to preclude upholding the trust if valid under the local law of the state of administration....

If the testator has not manifested an intention that the trust should be administered in a particular state, and has not designated a state whose local law is to govern the validity of the trust, the validity of the trust will be governed by the local law of the state of the testator's domicil.

### (2) Administration

Section 271(b) of the *Restatement (Second) of Conflict of Laws* provides in pertinent part that: [996]

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[996] *Restatement* § 271(b). *See id.* cmt. d.

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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 ... if there is no such designation, by the local law of the state of the testator's domicil at death, unless the trust is to be administered in some other state, in which case the local law of the latter state will govern.

A comment under *Restatement* § 271 describes whether or not the law governing administration will change as follows: [997]

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[997] *Restatement* § 271(b) cmt. g.

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When the court has authorized a change in the place of administration to another state, the question arises whether thereafter the administration of the trust is governed by the local law of the other state. It will be so governed if this is in accordance with the intention of the testator, express or implied. Thus, the testator may expressly provide for a change in the place of administration. So also, the change of the place of administration may be authorized by implication, such as when the will contains a power to appoint a new trustee and the new trustee appointed is domiciled or does business in another state. Where the court authorizes a change in the place of administration because of a change of domicil of the beneficiaries or of the trustee, the court may direct that the trust be administered thereafter in accordance with the local law of the other state. In such cases the trust will be administered in accordance with the local law of the new state of administration.

On the other hand, there will be no change in the law governing the administration of the trust if this would be contrary to the intention of the testator, such as when he has expressly or by implication provided in the will that the administration of the trust should be governed by the local law of the state of his domicil at death, even though the place of administration should subsequently be changed.

### (3) Construction

Section 268(2) of the *Restatement* provides that: [998]

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[998] *Restatement* § 268(2). *See id.* cmt. c.

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(2) In the absence of such a designation, the instrument is construed

(a) as to matters pertaining to administration, in accordance with the rules of construction of the state whose local law governs the administration of the trust, and

(b) as to matters not pertaining to administration, in accordance with the rules of construction of the state which the testator or settlor would probably have desired to be applicable.

The law that governs questions of administration is discussed in VII.B.3.a.(2), above. [999] Rules of construction relate to the disposition of the trust property. [1000] For testamentary trusts, a comment under *Restatement* § 268 provides that: [1001]

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[999] *See Restatement* § 268 cmt. d.

[1000] *See Restatement* § 268 cmt. e.

[1001] *Restatement* § 268 cmt. f.

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As to the rules of construction which relate to the disposition of the trust property rather than to the administration of the trust, the will is ordinarily construed in the case of movables in accordance with the rules of construction of the state of the testator's domicil, even though the trust is to be administered in some other state.

Although ordinarily the courts will apply the rule of construction of the testator's domicil at death, it will not

do so if the testator is found to have intended that the rule of construction of some other state should be applicable. Although when a trust is created by will, the will is ordinarily construed in accordance with the rules of the state of the testator's domicil at death, the fact that he executed the will when domiciled in another state is usually sufficient to show that he presumably intended that the will should be construed in accordance with the rules of that state. So also, the fact that he executed the will in a state other than that of his domicil at the time when he executed it and at the time of his death may show an intention that the will should be construed in accordance with the rules of that state.

### (4) Restraints on Alienation

If a testator has not manifested an intention that a trust of movables created by Will is to be administered in a particular state, whether a creditor may reach a beneficiary's interest in such a trust is determined by the law of the testator's domicile. [1002]

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[1002] *Restatement* § 273(a).

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## b. Trust Created Inter Vivos

### (1) Validity

Section 270(b) of the *Restatement* provides in relevant part:

An inter vivos trust of interests in movables is valid if valid ...under the local law of the state with which, as to the matter at issue, the trust has its most significant relationship under the principles stated in § 6.

A comment amplifies the general rule as follows: [1003]

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[1003] *Restatement* § 270(b) cmt. c.

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When the settlor does not designate a state whose local law is to govern the validity of the trust, or when the designation will not be given effect because the state has no substantial relation to the trust, the trust will be valid if valid under the local law of the state with which, as to the matter at issue, the trust has its most significant relationship under the principles stated in § 6.

Of the states having relationships with the trust, much the most important insofar as the validity of the trust is concerned is the state, if any, where the settlor manifested an intention that the trust should be administered.

If the settlor has not manifested an intention that the trust should be administered in a particular state, the trust will be upheld if valid under the local law of the state which, as to the matter at issue, has the most significant relationship to the trust under the principles stated in § 6.

Another comment emphasizes the importance of carrying out the trustor's intent as follows: [1004]

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[1004] *Restatement* § 270 cmt. d.

One factor which the courts consider in determining the state of the applicable law is whether application of a particular law would result in sustaining the validity of the trust. It is improbable that the settlor intended to execute an instrument wholly or partially invalid. Some indication of his intention, if any, as to which law should govern the validity of the trust may be provided by the circumstance that under the local law of one state closely connected with the trust, the trust or a particular trust provision would be invalid, whereas under the local law of another state also closely connected with the trust there would be no such invalidity....

The rule of this Section is applicable to questions of substantial validity, such as those involved in the rule against perpetuities or a rule against accumulations or a rule precluding the creation of a charitable trust or of any trust. As to these matters the trust will be upheld if the settlor has manifested an intention that it should be administered in a particular state, and if under the local law of that state the trust would be valid, even though the settlor was domiciled in a state in which it would be invalid... . On the other hand, the trust will also be upheld if valid under the local law of the settlor's domicil, even though it would be invalid under the local law of the place of administration. The settlor could have designated the state of the applicable law and it is to be inferred even though he made no such designation that he would intend to make applicable the local law of a state under which the trust would be valid.

### (2) Administration

Section 272 of the *Restatement* provides in relevant part that:

(b) if there is no such designation, by the local law of the state to which the administration of the trust is most substantially related.

A comment under § 272 elaborates as follows: [1005]

[1005] *Restatement* § 272 cmt. d.

When the settlor does not designate a state whose local law is to govern the administration of the trust, its administration will be governed by the local law of the state to which the administration is most substantially related.

Of the states having relationships with the administration of the trust, much the most important is the state, if any, where the settlor manifested an intention that the trust should be administered. If the settlor has manifested an intention that the trust should be administered in a particular state, the local law of that state will be held to be the law governing the administration of the trust, unless it appears that the settlor desired to have some other law applied... ..

If the settlor has not manifested an intention that the trust should be administered in a particular state, and has not designated the law to control the administration of the trust, the administration of the trust will be determined by the local law of the state to which the administration is most substantially related... ..

Those factors are analyzed in IV.D.3.b., above.

Another comment under § 272 discusses whether the law governing administration changes upon a

change of the place of administration as follows: [1006]

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[1006] *Restatement* § 272 cmt. e.

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When an inter vivos trust has not become subject to the control of a particular court, a question arises as to the effect of a change in the place of administration of the trust. If the actual place of administration is changed, either because the trustee acquires a place of business or domicil in another state, or if in the exercise of a power of appointment a trustee is appointed whose place of business or domicil is in another state, the question arises whether thereafter the administration of the trust is governed by the local law of the other state. This depends upon the terms of the trust, express or implied. Such a change of the applicable law may be expressly authorized by the terms of the trust, or it may be authorized by implication, such as when the trust instrument contains a power to appoint a trustee in another named state. A simple power to appoint a successor trustee may be construed to include a power to appoint a trust company or individual in another state. In such cases, the law governing the administration of the trust thereafter is the local law of the other state and not the local law of the state of original administration.

On the other hand, the terms of the trust may show the testator's intention that the trust is always to be administered under the local law of the original state. In such a case the mere fact that the trustee acquires a domicil in another state or that by the exercise of a power of appointment a successor trustee is appointed who is domiciled in another state does not result in a change of the law applicable to the administration of the trust.

When an inter vivos trust has become subject to the continuing jurisdiction of a court to which it is thereafter accountable, it becomes necessary to obtain the permission of that court to terminate such accountability. The question arises when the court is thereafter asked to appoint a successor trustee, or when the trustee acquires a place of business or domicil in another state, or when by the exercise of a power of appointment a trustee is appointed whose place of business or domicil is in another state. The same rules are applicable as are applicable in the case of a testamentary trustee.

### (3) Construction

*Restatement* § 268(2) covers trusts of movables created inter vivos as well as by Will. [1007] Regarding inter vivos trusts, one of § 268's comments provides: [1008]

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[1007] *Restatement* § 268(2).

[1008] *Restatement* § 268(2) cmt. g.

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The domicil of the settlor of an inter vivos trust is of less importance than it is in the case of a trust created by will. Where an inter vivos trust is to be administered in a state other than that of the settlor's domicil, the cases are not altogether clear whether the applicable rules of construction as to matters not relating to administration are those of the settlor's domicil or those of the place of administration. All that can be said with assurance is that the courts attempt to apply the rules which the settlor would probably have desired to be applicable. In a number of cases the courts have applied the rules of construction of the place of administration in the case of an inter vivos trust, although they would presumably have applied the rules

of construction of the state of the testator's domicil in the case of a testamentary trust. If the settlor engages a lawyer at his domicil to draw the trust instrument, it may be that he intends to apply the rules of construction of his domicil, although he names as trustee a trust company of another state. On the other hand, if the instrument is drawn by a lawyer of the state in which the trust company does business, it may well be that the settlor intends to apply the rules of construction of the state where the trust company does business....

If the settlor of an inter vivos trust has not manifested an intention that the trust should be administered in a particular state, the applicability of rules of construction will be determined by those contacts which for the matter at issue have the most significant relationship to the trust....

Those factors are discussed in IV.D.3.b., above.

A comment under § 268 provides that: [1009]

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[1009] *Restatement* § 268(2) cmt. h (cross-reference omitted).

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The question of the allocation of receipts and expenditures to principal or income presents a different problem. If a testator creates a trust to be administered in a state other than that of his domicil, the question is whether the allocation, as for instance of extraordinary dividends, is to be determined by the local law of his domicil or the local law of the place of administration. This could conceivably be treated as a question of administration and governed by the local law of the place of administration. On the other hand, it can be treated as a question of the distribution of the trust property and governed by the local law of the testator's domicil. For the purposes of the choice of the applicable law, it is generally held that it is a question of construction and that the local law of the testator's domicil is applicable.

### (4) Restraints on Alienation

If a trustor has not manifested an intent that an inter vivos trust of movables is to be administered in a particular state, whether a creditor may reach a beneficiary's interest in such a trust is determined “by the local law of the state to which the administration of the trust is most substantially related.” [1010] Those factors are discussed in IV.D.3.b., above.

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[1010] *Restatement (Second) of Conflict of Laws* § 273(b) (1971).

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## 4. Restatement Approach — Trust of Movables — Delaware's Experience

Delaware courts have looked to a number of factors in determining what governing law should apply in interpreting or administering trusts. These factors include the location of the trustee, the place where the trust assets are held, any governing law provisions set forth in the trust instrument, the domicile of the testator (in the case of a testamentary trust) or the domicile of the trustor (in the case of an inter vivos trust), and the location of the beneficiaries of the trust. [1011] In Delaware cases that involve inter vivos trusts, in the absence of an explicit governing law provision, the courts have tended to emphasize the location of the trustee and the location of the administration of the trust as the most significant factors in determining the nexus for the application of the appropriate governing law. [1012]

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[1011] *See Lewis v. Hanson*, 128 A.2d 819, 826 (Del. 1957), *aff'd sub. nom. Hanson v. Denckla*, 357 U.S. 235 (1958).

[1012] *See id.* at 826.

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## 5. Restatement Approach — Trust of Movables — Summary

The Scott treatise describes the impact of the move of a trust on the law that governs various aspects of its operation as follows: [1013]

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[1013] 7 *Scott and Ascher on Trusts* § 45.5.3.2 at 3306 (footnotes omitted). *See Restatement (Second) of Conflict of Laws* § 272 cmt. e (1971).

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Even when a change in the place of administration is authorized, any resulting change in the applicable law ordinarily pertains only to matters of administration. Thus, the law of the new place of administration ordinarily applies, for example, to the trustee's compensation, trust investments, and the trustee's powers and duties. In contrast, a change in the place of administration ordinarily has no effect on the law that applies to the disposition of the trust property. Thus a change in the place of administration does not ordinarily affect the determination of who the trust beneficiaries are or the allocation of receipts and expenses between income and principal. Presumably, as to these matters, the settlor did not intend that the applicable law would change merely because there was a change in the place of administration.

## 6. Restatement Approach — Trust of Land

The law that is used to resolve questions of construction of a trust of land created by Will or inter vivos is the law designated by the testator or trustor in the governing instrument. [1014] Otherwise, questions of construction, validity, administration, and restraints on alienation involving such a trust are determined using the law that would be applied by the courts of the situs. [1015]

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[1014] *Restatement (Second) of Conflict of Laws* § 277(1) (Am. Law Inst. 1971).

[1015] *Restatement (Second) of Conflict of Laws* § 277(2), § 278, § 279, § 280 (Am. Law Inst. 1971).

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## 7. UTC Approach

Unlike the *Restatement*, the UTC does not distinguish between trusts of movables and trusts of land or between trusts created by Will or inter vivos. UTC § 107(1) provides that the meaning and effect (probably comparable to the *Restatement's* "construction") of the terms of a trust are determined by the law of the jurisdiction designated by 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. [1016] Section 107(2) provides that, in the absence of an effective designation, the meaning and effect of the trust is determined under the law of the jurisdiction having the most significant relationship to the matter at issue. [1017] The UTC stipulates that the law of the state that has the most significant relationship to the

trust's creation should govern the “dispositive provisions” (probably comparable to the *Restatement's* “validity”) [1018] and that the law of the trust's principal place of administration should control administrative matters. [1019] The UTC does not cover the determination of which state's law should govern the ability of creditors to reach trust interests.

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[1016] UTC § 107(1) (amended 2018). The text of the UTC and the jurisdictions that have enacted the it may be viewed at, https://my.uniformlaws.org/committees/community-home?CommunityKey=193ff839-7955-4846-8f3c-ce74ac23938d.

[1017] UTC. § 107(2) (amended 2018).

[1018] UTC § 107 cmt. (amended 2018).

[1019] *Id.*

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Those factors are analyzed in IV.D.3.b., above.

## C. Effecting the Move

The transfer of a trust's situs or place of administration from one state to another might be accomplished through an express provision in the trust instrument, a pertinent statute, or a court petition. If the governing instrument provides for the removal and replacement of the trustee without the necessity for court proceedings, the nomination of a trustee in the more favorable state might be sufficient in itself to accomplish the transfer of the situs. Similarly, the governing instrument might confer powers of appointment that may be exercised by the beneficiaries in a way that will accomplish the transfer of situs without court intervention. Frequently, however, the governing instrument is silent on the issues of removal, resignation, and replacement or does not contain powers of appointment. In such a case, the beneficiaries must either obtain the trustee's agreement to resign or convince the local probate court to remove the trustee. In this connection, California has had a procedure for transferring a trust to another jurisdiction since 1991. [1020] In addition, UPC § 7-305, [1021] which is or will be in effect in at least four states, [1022] provides as follows:

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[1020] Cal. Prob. Code § 17400–§ 17405. *See* 7 *Scott and Ascher on Trusts* § 45.5.3.1 at 3301–3302 n.28.

[1021] UPC § 7-305 (amended 2010).

[1022] *See, e.g.*, Alaska Stat. § 13.36.090; Colo. Rev. Stat. § 15-16-305; Haw. Rev. Stat. § 560:7-305; Idaho Code § 15-7-305.

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A trustee is under a continuing duty to administer the trust at a place appropriate to the purposes of the trust and to its sound, efficient management. If the principal place of administration becomes inappropriate for any reason, the Court may enter any order furthering efficient administration and the interests of beneficiaries, including, if appropriate, release of registration, removal of the trustee and appointment of a trustee in another state. Trust provisions relating to the place of administration and to changes in the place of administration or of trustee control unless compliance would be contrary to efficient administration or the purposes of the trust. Views of adult beneficiaries shall be given weight in determining the suitability of the trustee and the place of administration.

Whereas the Supreme Court of Nebraska refused to replace a corporate trustee pursuant to the Nebraska version of § 7-305 in a 1982 case, [1023] the Supreme Court of Alaska replaced the corporate trustee and transferred the situs of the trust out of Alaska in a 2004 case, [1024] and a Michigan intermediate appellate court replaced the corporate trustee and transferred the trust's situs from Michigan to Georgia in an unpublished 2008 case. [1025]

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[1023] *In re Zoellner Tr.*, 325 N.W.2d 138 (Neb. 1982).

[1024] *Marshall v. First Nat'l Bank Alaska*, 97 P.3d 830 (Alaska 2004).

[1025] *In re Wege Trust.*, 2008 WL 2439904 (Mich. Ct. App. June 17, 2008).

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Similarly, § 108(b) of the UTC, [1026] which is the law (in identical or substantially the same form) in 26 states, [1027] specifies that:

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[1026] UTC § 108(b) (amended 2018).

[1027] *See* Worksheet 15.

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(b) A trustee is under a continuing duty to administer the trust at a place appropriate to its purposes, its administration, and the interests of the beneficiaries.

Even in the seven states that have enacted § 108 without adopting a version of subsection (b), [1028] the provision might be helpful in replacing trustees and transferring trusts. For example, Pennsylvania practitioners have told the author that they have used that commonwealth's version of § 108 [1029] to transfer trusts to Delaware to eliminate Pennsylvania income tax.

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[1028] *See* Worksheet 15. *See also In re Stanley A. Seneker Tr.*, 2015 BL 51771, 2015 WL 847129, at *3 (Mich. Ct. App. Feb. 26, 2015) (principal place of administration was in Florida not in Michigan).

[1029] *See* 20 Pa. Cons. Stat. § 7708.

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In order to move a trust in conjunction with the resignation or removal of a trustee, the beneficiaries or the trustee must file a petition (often accompanied by an accounting) in the local probate court. In many instances, it also is necessary to file a petition in a court in the new state seeking the court's approval of the transfer of situs and acceptance of jurisdiction over the trust prior to the proceeding in the local probate court. Thus, the local court knows of the new trustee's willingness to serve and the new court's acceptance of jurisdiction upon the local court's approval of transfer.

For trusts of movables created by Will, a comment under *Restatement* § 271 provides that: [1030]

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[1030] *Restatement (Second) of Conflict of Laws* § 271 cmt. g (1971).

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[A] testamentary trustee may be required by statute to qualify as trustee in the court of the testator's domicil having jurisdiction over the testator's estate, when the trust is to be administered in that state. The trustee is then accountable to that court. Thereafter, however, the question may arise whether the administration of the trust may be changed to another state. In such a case, in contrast to the usual situation that prevails in the case of an inter vivos trust, it is necessary to obtain the permission of the court for a change in the place of administration. Since the trustee is accountable to the court, it is necessary to obtain the permission of the court to terminate the accountability of the trustee to it.

The court should permit a change in the place of administration and a termination of the trustee's accountability to it if this would be in accordance with the testator's intention, either express or implied. Such a change may be expressly authorized in the will. It may be authorized by implication, such as when the will contains a power to appoint a new trustee in another state, or simply a power to appoint a new trustee if this is construed to include the power to appoint a trustee in another state.

The court may permit a change in the place of administration and a termination of the trustee's accountability to it even though such change was not expressly or impliedly authorized by the testator. The court may authorize such a change when this would be in the best interests of the beneficiaries, as, for example, when the beneficiaries have become domiciled in another state or when the trustee has become domiciled in another state.

The court may refuse to permit a change in the place of administration and termination of the trustee's accountability to it, unless the trustee qualifies as trustee in a court of the state in which the trust is to be thereafter administered.

For trusts of movables created inter vivos, a comment under *Restatement* § 272 provides that: [1031]

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[1031] *Restatement* § 272 cmt. e.

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When an inter vivos trust has become subject to the continuing jurisdiction of a court to which it is thereafter accountable, it becomes necessary to obtain the permission of that court to terminate such accountability. The question arises when the court is thereafter asked to appoint a successor trustee, or when the trustee acquires a place of business or domicil in another state, or when by the exercise of a power of appointment a trustee is appointed whose place of business or domicil is in another state. The same rules are applicable as are applicable in the case of a testamentary trustee.

The means by which the trust is moved might have a bearing on which of the more favorable state's benefits can be made available. Thus, in one case, it might be possible to gain perpetual duration, no state fiduciary income taxation, avoidance of accounting requirements, effective spendthrift protection, a favorable total-return unitrust law, reduction in administrative costs, and a direction investment adviser. In another case, however, it might not be possible to obtain one or more of these benefits.

Generally, courts have permitted the transfer of a trust when no contrary intent is expressed in the trust instrument and when the administration of the trust will be facilitated and the interests of the beneficiaries will be promoted. [1032]Trustees and beneficiaries should not assume, though, that courts will automatically grant petitions to transfer situs. For example, courts have denied such petitions when the accomplishment of the stated objective — the elimination of New York fiduciary income tax — did not require the change. [1033]

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[1032] *See Estate of Gladys T. Perkin*, N.Y.L.J., June 9, 2010, at 33, Col. 2 (N.Y. Surr. Ct. N.Y. Cty. 2010); *Estate of McComas*, 630 N.Y.S.2d 895 (N.Y. Sur. Ct. N.Y. Cty. 1995). *Matter of Matthiessen,* 87 N.Y.S.2d 787, 794–95 (N.Y. Sup. Ct. N.Y. Cty. 1949).

[1033] *See In re Bush*, 774 N.Y.S.2d 298 (Sur. Ct. N.Y. Cty. 2003); *In re Estate of Rockefeller*, 773 N.Y.S.2d 529 (Sur. Ct. 2003). *See also In re Harold J. Allen Tr. No. Three v. Brook*, 728 N.W.2d 60 (Iowa Ct. App. 2006) (request to change situs denied); *Matter of Hudson.*, 286 N.Y.S.2d 327, 330 (App. Div., 1968), *aff'd*, 245 N.E.2d 405 (N.Y. 1969) (same).

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Some states facilitate the application of their laws to the administration of trusts moved from other states. For example, a Delaware statute provides that Delaware law governs the administration of a trust unless the governing instrument or a court order provides otherwise. [1034]

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[1034] Del. Code Ann. tit. 12, § 3332(b).

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## D. Moving to Carry Out Clients' Objectives or to Facilitate Amendment or Termination of a Trust

As discussed in V.C., above, states vary on the degree to which they will honor a client's wishes. Thus, if a trustee is concerned that the client's objectives might be thwarted in the current state, the trustee might investigate the possibility of moving the trust. But, the trustee and the beneficiaries might want to amend or terminate a trust, in which case they should explore moving the trust to a state where this can be accomplished readily.

## E. Moving to Create a Perpetual Trust

A provocative question is whether a trust created in a state that does not countenance perpetual trusts may be moved to another state and become a perpetual trust. As discussed in V.D., above, the determination of how long a trust may last is a matter of validity, and the law that governs such matters rarely changes upon the move of a trust. The author is aware of one instance, however, in which the trust instrument expressed the client's intent that the trust be perpetual and encouraged the trustee to consider moving the trust to achieve this objective.

The task of converting a trust into a perpetual trust should be easier if the trust confers powers of appointment. Thus, based on Delaware cases decided in the 1940s, it might be possible to turn a trust into a perpetual trust if the trust was written with sufficient flexibility and if it confers a nongeneral power of appointment on a beneficiary. [1035] Consequently, beneficiaries who possess nongeneral powers of appointment over irrevocable trusts that are governed by the common-law rule against perpetuities or the USRAP should, under certain circumstances, be able to move the trusts to states that allow perpetual trusts so that they may exercise their powers to make it possible for the trusts to last forever.

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[1035] *See Wilmington Tr. Co. v. Wilmington Tr. Co.*, 24 A.2d 309 (Del. 1942); *Wilmington Tr. Co. v. Sloane*, 54 A.2d 544 (Del. Ch. 1947).

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As discussed in II.F.2., above, attorneys must be mindful of the potential adverse federal transfer-tax consequences of lengthening trusts.

## F. Moving to Save State Income Tax

### 1. Introduction

Trustees should review the trusts that they administer to identify all trusts that are paying state income tax. With the assistance of counsel, they should determine whether tax can be reduced or eliminated. If tax has been paid erroneously, trustees should request refunds for open years. If trustees discover that tax can be escaped, they should consider filing “final” returns in the year before the occurrence of major transactions (e.g., the sale of a large block of low-basis stock). At the same time, trustees and advising attorneys must make sure that steps taken to eliminate one state's tax won't subject trusts to tax elsewhere.

Taking action, such as by moving the trust, might make it possible for the trust to stop paying a state-level income tax. If a state assesses a tax if the trustee is located or resides in that state or if the trust is administered there, then moving the trust should terminate liability for the tax.

### 2. Trust Created by Will of Resident

If the original state imposes its tax on a testamentary trust if the testator lived there at death, whether or not tax will continue to apply raises complex constitutional issues that were discussed in V.E., above. The constitutional issues involve the question of whether the state statute that created the basis on which the income tax is imposed violates various federal and state constitutional mandates (including the Commerce Clause and the Due Process Clause of the U.S. Constitution) and therefore can be safely ignored in the absence of any continuing nexus between the trust and the original state.

As discussed in V.E.4., above, New York, New Jersey, and other states offer clear guidance on how to escape tax. To escape tax in these states or to improve prospects for avoiding tax in states where the rules are not as clear, the trustee might explore transferring the trust's situs to another state, which might be accomplished by a provision in the governing instrument or by a state statute or court proceeding. Wisconsin recognizes that a change of situs will end a testamentary trust's liability for tax. [1036]

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[1036] *See* instructions to 2017 Wis. Form 2 at 1.

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### 3. Inter Vivos Trust Created by Resident

To determine whether a state's income tax on an inter vivos trust created by a resident can be escaped, the trustee and attorney should go through a process comparable to that described in V.F.2., above.

### 4. Trust Administered in State

Here, it might be possible to escape tax simply by changing the place where the trust is administered, with or without court involvement.

## 5. Resident Trustee

In states that tax on this basis, it should be possible to escape tax simply by replacing the resident fiduciaries with nonresident fiduciaries.

## 6. Resident Beneficiary

Short of having the beneficiary move, it is difficult if not impossible to prevent a resident beneficiary from being taxed on current distributions. Nonetheless, the attorney and trustee should make sure that tax is not paid unnecessarily or prematurely on accumulated income and capital gains.

## 7. Recommendation

Trustees no longer can ignore this issue. This is because courts are beginning to recognize the state income taxation of trusts as an important factor when considering petitions to relocate trusts. [1037]

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[1037] *See, e.g.*, *Beardmore v. JPMorgan Chase Bank, N.A.*, 2017 BL 104708, 2017 WL 1193190, at *6 (Ky. Ct. App. Mar. 31, 2017) ("The move to Delaware would provide a significant aggregate tax savings over those years"); *In re McKinney*, 67 A.3d 824, 833 (Pa. 2013) (factors relevant to whether a trustee best serves the interests of the beneficiaries include the "location of trustee as it affects trust income tax"); *Davis v. U.S. Bank Nat'l Ass'n*, 243 S.W.3d 425, 430 (Mo. Ct. App. 2008) ("Changing the domicile of the Trust to Delaware would avoid out of state income tax being paid on Trust income").

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## G. Moving to Provide More Investment Flexibility

A state's explicit recognition of directed trusts may, by itself, be a sufficient reason to move a trust. This feature might be particularly attractive to trustees and beneficiaries of trusts that hold closely held business interests, lack diversification of investments, or invest in assets (e.g., limited partnerships) that were traditionally viewed as inappropriate because of the trustee's deemed delegation of its investment responsibility.

## H. Moving to Provide Greater Protection from Creditor Claims

As discussed in V.H., above, some states provide more protection than other states against creditor claims for the beneficiaries of third-party trusts, and, as discussed in V.I., above, some states offer protection from creditor claims for the trustor-beneficiary of self-settled trusts. Given that trustees have a fundamental duty to use reasonable care to protect trust assets from unnecessary exposure to risk of loss [1038] and to ensure that trusts are administered in appropriate jurisdictions, [1039] trustees of certain third-party and self-settled trusts might have an obligation to explore moving them to more protective jurisdictions. [1040]

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[1038] *Restatement (Second) of Trusts* § 176 (Am. Law Inst. 1959). Accord UTC § 809 (amended 2018). *Restatement (Third) of Trusts* § 76(2)(b) (Am. Law Inst. 2007).

[1039] *See* VII.C., above.

[1040] *See Matter of Heller*, 613 N.Y.S.2d 809 (N.Y. Sur. Ct. N.Y. Cty. 1994) (trustee petitioned court to divide trust to protect cash and securities from potential liability from realty).

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## I. Moving to Use the Power to Adjust or to Convert to a Total-Return Unitrust

It might be desirable to move a trust to take advantage of a state's power to adjust and total-return unitrust conversion statutes, particularly because there is greater assurance of the tax consequences of action taken pursuant to such a statute than there is for action that is taken without statutory authority. [1041] Several states' unitrust-conversion statutes [1042] and a few states' power to adjust statutes [1043] provide that conversion of a trust to a total-return unitrust or the exercise of the power to adjust is a matter of trust administration and that the statute is available to trusts administered in that state under that state's law. Thus, if moving a trust changes the law that governs its administration, the trust will be able to take advantage of such a statute. Nevertheless, changing the situs of a trust will not automatically change the law that governs its administration. Consequently, absent an applicable statute in the new jurisdiction or specific language in the court order or the trust instrument stating that the law governing the administration of the trust will be that of the new situs, the governing law of the original state might still apply.

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[1041] *See* Reg. § 1.643(b)-1.

[1042] *See, e.g.*, Colo. Rev. Stat § 15-1-404.5(13); Del. Code Ann. tit. 12, § 61-106(l); Fla. Stat. § 738.1041(9); 760 ILCS 5/5.3(1); Iowa Code Ann. § 637.613; N.M. Stat. Ann. § 46-3A-113(B); S.D. Codified Laws § 55-15-12; Va. Code Ann. § 64.2-1003(J).

[1043] *See, e.g.*, Del. Code Ann. tit. 12, § 61-104(g).

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## J. Moving to Avoid Accounting Requirements and Administrative Costs

Moving a trust might avoid the court-accounting requirements that may exist in the original state. If the trust to be moved is an inter vivos trust, then it should be possible to avoid future court accountings. Even if the trust to be moved is a testamentary trust for which judicial accountings are required, it might be possible to avoid court accountings if the governing instrument contains language waiving the requirement. For example, Delaware courts have demonstrated some flexibility in interpreting governing instruments to avoid the necessity for judicial intervention.

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## K. Federal Transfer Tax Consequences of Moving

The attorney should confirm that moving a trust will not produce adverse federal transfer-tax consequences. Hence, unless or until the GST tax is repealed, great care should be taken in moving a Grandfathered Dynasty Trust because the IRS takes the position that a trust will lose its grandfathered status if it is moved to lengthen its duration: [1044]

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[1044] Reg. § 26.2601-1(b)(4)(i)(E) *Ex.* 4. *See, e.g.*, PLR 201518002–PLR 201518005, PLR 201422011.

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If . . . as a result of the change in situs, State Y law governed such that the time for vesting was extended beyond the period prescribed under the terms of the original trust instrument, the trust would not retain exempt status.

Moving a trust to a state that has a longer perpetuities period than that of the original state will not lengthen a trust's duration if the trust instrument specifies that the trust must terminate on a particular date (e.g., at the end of the USRAP period or the common law perpetuities period). A Delaware statute provides that the duration of a trust will not change merely because it is moved to Delaware. [1045] In addition, a beneficiary of a Grandfathered Dynasty Trust may not exercise a nongeneral power of appointment to create a perpetual trust and preserve the trust's grandfathered status. [1046] The IRS takes the position that moving a Grandfathered Dynasty Trust to escape state income tax [1047] or to utilize (or to avoid) another state's total return unitrust–conversion law [1048] or statutory power to adjust [1049] will not cost the trust its grandfathered status.

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[1045] Del. Code Ann. tit. 12, § 3332(a).

[1046] Reg. § 26.2601-1(b)(1)(v)(B)(2).

[1047] Reg. § 26.2601-1(b)(4)(i)(D)(2).

[1048] Reg. § 26.2601-1(b)(4)(i)(E) *Ex.* 11.

[1049] Reg. § 26.2601-1(b)(4)(i)(E) *Ex.* 12.

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There is no regulatory guidance on the GST tax consequences of modifications of Exempt Dynasty Trusts, but the IRS has approved changes of trust situs for Exempt Dynasty Trusts that would have been allowed for Grandfathered Dynasty Trusts, [1050] some of which involved change of situs where neither jurisdiction had a rule against perpetuities for trusts. [1051]

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[1050] *See. e.g.*, PLR 201518002–PLR 201518005, PLR 201210001–PLR 201210002, PLR 201208031, PLR 201208006, PLR 200841027, PLR 200840024, PLR 200839025–PLR 200839027, PLR 200817009, PLR 200743028, PLR 200714016.

[1051] *See* PLR 200841027, PLR 200840024, PLR 200839025–PLR 200839027.

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The author is often asked whether a Grandfathered Dynasty Trust or an Exempt Dynasty Trust might be moved to Delaware from a state that does not permit perpetual trusts if the governing instrument expresses the intent that the trust be perpetual. This should be possible under the language quoted above.

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## A. Introduction

Section 2663 provides in relevant part: [1052]

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[1052] § 2663(2).

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The secretary shall prescribe such regulations as may be necessary or appropriate to carry out the purposes of this chapter ... including —

(2) regulations (consistent with the principles of chapters 11 and 12 ... providing for the application of this chapter ... in the case of transferors who are nonresidents not citizens of the United States ....

Pursuant to the above directive, the Treasury Department issued regulations providing that a generation-skipping transfer is subject to GST tax only if the transfer also is or was subject to gift or estate tax. [1053] This creates planning options that are discussed below. Certain citizens of U.S. possessions are treated as nonresident aliens (NRA) for these purposes. [1054]

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[1053] Reg. § 26.2663-2(b).

[1054] *See* § 2208–§ 2209. *See also* PLR 200848014 (U.S. citizen/Puerto Rico resident considered NRA for estate-tax purposes).

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## B. Gift and Estate Tax Rules

Whereas every U.S. citizen or resident must potentially pay gift tax on lifetime transfers of every kind of property wherever it is located, [1055] an NRA is only taxable on lifetime transfers of property situated in the United States, [1056] which does not include intangible property even if it is situated in this country. [1057] Thus, although an NRA might be taxed on gifts of real property and tangible personal property located in the United States, an NRA may make gifts of stocks, bonds, notes, and other obligations without having to file a gift tax return. For these purposes, cash is treated as tangible personal property. [1058]

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[1055] § 2501(a)(1).

[1056] § 2511(a).

[1057] § 2501(a)(2). *See* PLR 201032021 (NRA's transfer of shares of stock in holding company to or for U.S. beneficiaries not subject to gift tax).

[1058] Rev. Rul. 55-143. *See* PLR 200748008, PLR 200748011–PLR 200748013, PLR 200748016, PLR 200340015, PLR 8138103, PLR 7737063.

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The rules are different for estate-tax purposes. All property situated in the United States is included in the gross estate of an NRA, [1059] and there is no parallel to the gift-tax exemption of intangible property. Thus, if an NRA dies owning shares of stock in a U.S. company, then the stock is subject to federal estate tax unless the decedent resided in a country with which the United States has an estate-tax treaty and the treaty exempts the U.S. stock. [1060]

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[1059] § 2103.

[1060] *See Estate of Charania v. Commissioner*, 133 T.C. 122 (2009), *aff'd in part, rev'd in part on other grounds sub nom. Estate of Charania v. Shulman*, 608 F.3d 67 (1st Cir. 2010) (NRA's stock in U.S. Corporation — Citigroup — is situated in U.S. and subject to federal estate tax). *See also* CCA 201020009 (gift tax paid by NRA within three years of death not includible in gross estate). *See also* Hoke, *Foreign Banks Wary of Liability for Unpaid Taxes*, 149 Tax Notes 888 (Nov. 16, 2015).

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This anomaly in the treatment of intangible property situated in the United States permits NRAs to give away their stock in U.S. companies during lifetime free of gift tax but not to bequeath the stock at their death free of estate tax. The planning opportunities for NRAs who have U.S. beneficiaries and who wish to fund dynasty trusts with U.S.-situs intangible property are obvious. If the trust is funded with assets other than real estate or tangible personal property located in the United States, no gift tax return is required and no gift tax is due. [1061]

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[1061] *See* CCA 201432022 (filing requirement for foreign trust converting to domestic trust and vice versa). *See also* Maggi, Scheidlinger & Shenkman, *Coming to America: Part II*, 150 Tr. & Est. 16 (Sept. 2017); Jonathan A. Mintz, *Estate Planning Gets More Complex for Non-U.S. Citizens*, 44 Est. Plan. 33 (July 2017); Patrick J. McCormick, *Key Estate Planning Concepts for International Clients*, 44 Est. Plan. 18 (June 2017); John R. Strohmeyer, *Estate and Gift Taxation of Nonresidents*, 30 Prob. & Prop. 50 (Nov./Dec. 2016); Meltzer, Schwartz & Weissbart, *International Estate Planning for the Domestic Lawyer*, 43 Est. Plan. 13 (Apr. 2016).

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## C. GST Tax Rules

Given that the GST tax applies to a transfer of property by an NRA only if the transfer is subject to gift or estate tax, [1062] there is no GST tax on a gift of intangible property (e.g., U.S. stocks, bonds, notes, or other obligations) to a dynasty trust for the benefit of an NRA's U.S. children and grandchildren because such gift is exempt from gift tax. If the same NRA donor bequeaths the same assets to the dynasty trust on death, however, then the transfer will be subject to the GST tax because the transfer will be subject to estate tax. Again, this anomaly gives rise to an opportunity for NRAs to create inter vivos dynasty trusts of unlimited amount — the GST exemption need not be applied — for the benefit of their children and grandchildren who are U.S. citizens or residents without suffering any gift-tax or GST-tax consequences.

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[1062] § 2663(2); Reg. § 26.2663-2. *See, e.g.*, PLR 201311004, PLR 201250001.

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## D. Location of Property

Even though the tax laws provide several examples of property situated within the United States [1063] and of property situated without the United States, [1064] it still often is difficult to determine with certainty where property will be deemed to be located for estate-tax purposes. For example, certain types of property — such as deposits with U.S. banks and savings and loan associations and life insurance proceeds paid by (and amounts left at interest with) U.S. insurance companies — are clearly situated within the United States and yet are deemed to have a situs outside the United States. [1065] For an NRA who wishes to create a U.S. dynasty trust to take advantage of the favorable gift-tax and GST-tax rules applicable to such a transfer, the difficult question of where property has its situs generally will be avoided if neither real estate nor tangible personal property located in the United States will be used to fund the trust. Clearly, an NRA may create a perpetual dynasty trust of unlimited amount with intangible property free of gift and GST tax.

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[1063] § 2104.

[1064] § 2105.

[1065] § 2103–§ 2105. *See* CCA 201003013 (Canadian decedent's registered retirement savings plan is includible in gross estate); PLR 200842013 (proceeds of certain annuity contracts not situated in U.S.); PLR 200752016 (portfolio debt obligations not situated in U.S.).

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## E. United States as Trust Situs

In 2017, a commentator observed that the United States once was not an attractive trust jurisdiction for NRAs but that this is no longer true. [1066] His reasons included the following:
• The United States offers investment opportunities, legal protections, and political stability;

• This country's tax laws provide a clear distinction between domestic and foreign trusts (for income-tax purposes, a foreign trust is taxed as an NRA, with adjustments);

• The United States is not on many other countries' black lists;

• For the time being, this country offers more confidentiality than the many other countries that are subject to the Organization for Economic Cooperation and Development's Common Reporting Standard;

• States, particularly Delaware, offer more flexibility than offshore jurisdictions via revocable trusts, directed trusts, perpetual trusts, and asset-protection trusts;

• Funding a revocable trust with a corporate trustee here during life provides a smoother transition from a foreign trust to a domestic trust at death than does a decanting from a foreign trust;

• Domestic trusts are not subject to penalty provisions that apply to foreign trusts. [1067]

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[1066] Aballi, *The Pros and Cons of U.S. Trusts for Foreign Persons — The Movement Onshore*, 42 Tax Mgmt. Est., Gifts & Tr. J. 79, 80–81 (Mar. 9, 2017). *See* Angkatavanich, Fischer, Bowman & Vergara, *Foreign Affairs: A Primer on International Tax and Estate Planning (Part 2)*, 42 Tax Mgmt. Est., Gifts & Tr. J. 247 (Sept. 14, 2017); Angkatavanich, Fischer, Bowman & Vergara, *Foreign Affairs: A Primer on International Tax and Estate Planning (Part 1)*, 42 Tax Mgmt. Est., Gifts & Tr. J. 187 (July 13, 2017); Ward, *Planning for the Use of the U.S. as a Financial Haven: Part Two*, 9 Daily Tax Rep. J-1 (Jan. 13, 2017); Ward, *Planning for the Use of the U.S. as a Financial Haven: Part One*, 6 Daily Tax Rep. J-1 (Jan. 10, 2017); Kosnitzky, *U.S. Gains Favor as Trust Jurisdiction for Nonresidents*, 43 Est. Plan. 27, 29 (Sept. 2016); Smith, *Careful Pre-Immigration Planning Can Save Significant Taxes*, 34 Est. Plan. 30, 33 (Feb. 2007); Whitaker, *The U.S. May Be a Good Trust Jurisdiction for Foreign Persons*, 33 Est. Plan. 36 (Feb. 2006).

[1067] Gopman, Harris, Els & D'Alessandro, *Foreign Trusts: It's All Fun and Games Until Someone Gets Caught,* 43 Tax Mgmt. Est., Gifts & Tr. J. 311 (Nov. 18, 2018); Aballi, *The Pros and Cons of U.S. Trusts for Foreign Persons — The Movement Onshore*, 42 Tax Mgmt. Est., Gifts & Tr. J. 79, 79–88 (Mar. 9, 2017).

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NRAs sometimes create U.S. trusts by having the U.S. trustee sign a declaration of trust rather than by entering into a trust agreement with the trustee. Some states recognize the declaration approach. [1068]

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[1068] *See, e.g.*, Del. Code Ann. tit. 12, § 3545.

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For these reasons, NRAs should consider the United States in choosing a jurisdiction for their trusts, whether or not they have family members in this country.

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B-1601 Worksheet 16 Generation-Skipping Trust Agreement.

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## Worksheet 1 Exempt Dynasty Trust Illustrations*

**Value of Property in:**

| | 25 Years | 25 Years | 50 Years | 50 Years |
|---|---|---|---|---|
| Annual After Tax Growth | GST Exempt Dynasty Trust | No Trust or Nonexempt Trust | GST Exempt Dynasty Trust | No Trust or Nonexempt Trust |
| 3% | $2,093,778 | $1,256,267 | $4,383,906 | $1,578,206 |
| 4% | 2,665,836 | 1,599,502 | 7,106,683 | 2,558,406 |
| 5% | 3,386,355 | 2,031,813 | 11,467,400 | 4,128,264 |
| 6% | 4,291,871 | 2,575,123 | 18,420,154 | 6,631,257 |
| 7% | 5,427,433 | 3,256,460 | 29,457,025 | 10,604,529 |
| 8% | 6,848,475 | 4,109,085 | 46,901,613 | 16,884,581 |
| 9% | 8,623,081 | 5,173,848 | 74,357,520 | 26,768,707 |
| 10% | 10,834,706 | 6,500,824 | 117,390,853 | 42,260,707 |

**Value of Property in:**

| | 75 Years | 75 Years | 100 Years | 100 Years |
|---|---|---|---|---|
| Annual After Tax Growth | GST Exempt Dynasty Trust | No Trust or Nonexempt Trust | GST Exempt Dynasty Trust | No Trust or Nonexempt Trust |
| 3% | $9,178,926 | $1,982,648 | $19,218,632 | $2,490,735 |
| 4% | 18,945,255 | 4,092,175 | 50,504,948 | 6,545,441 |
| 5% | 38,832,686 | 8,387,860 | 131,501,258 | 17,042,563 |
| 6% | 79,056,921 | 17,076,299 | 339,302,084 | 43,973,560 |
| 7% | 159,876,019 | 34,533,220 | 867,716,326 | 112,456,036 |
| 8% | 321,204,530 | 69,380,178 | 2,199,761,256 | 285,089,059 |
| 9% | 641,190,893 | 138,497,233 | 5,529,040,792 | 716,563,687 |
| 10% | 1,271,895,371 | 274,729,402 | 13,780,612, | 1,785,967,369 |

| | | | | |
|---|---|---|---|---|
| | | | 340 | |

*Note:* Computations assume $1 million initial gift, no distributions, and 40% tax imposed on assets owned outright or held in Nonexempt Dynasty Trust every 25 years.

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## Worksheet 2 Charitable Lead Unitrust Illustrations*

Duration of Trust

| Annual Payout Rate to Charity | 20 Years | 40 Years | 60 Years | 80 Years | 99 Years |
|---|---|---|---|---|---|
| 3% | $1,833,916 | $3,362,893 | $6,165,912 | $11,304,033 | $20,102,926 |
| 4% | 2,253,810 | 5,078,926 | 11,443,480 | 25,779,840 | 55,756,899 |
| 5% | 2,776,389 | 7,706,950 | 21,389,459 | 59,354,226 | 156,470,035 |
| 6% | 3,426,922 | 11,741,223 | 40,218,790 | 137,741,046 | 443,458,980 |
| 7% | 4,240,288 | 17,957,589 | 76,184,671 | 322,788,896 | |
| 8% | 5,257,595 | 27,634,233 | 145,222,189 | 762,776,506 | |

*Note*: Chart shows the amount that can be placed in a charitable lead unitrust with the indicated annual payout rate to charity (with payments made annually) and the indicated term to produce a $1 million taxable gift, using a 1.8% § 7520 rate and assuming 6% annual growth.

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## Worksheet 3 State Uniform Trust Code Statutes*

**(As of September 2018)**

| State with Uniform Trust Code (33) | | |
|---|---|---|
| **State** | **Citation** | **Effective Date** |
| Alabama | Ala. Code § § 19-3B-101–19-3B-1305 | 2007 |
| Arizona | Ariz. Rev. Stat. Ann. § § 14-10101–14-11102 | 2009 |
| Arkansas | Ark. Code Ann. § § 28-73-101–28-73-1106 | 2005 |
| Colorado | Colo. Rev. Stat. § § 15-5-101–15-5-1404 | 2019 |
| District of Columbia | D.C. Code Ann. § 19-1301.01–19-1311.03 | 2004 |
| Florida | Fla. Stat. § § 736.0101–736.1303 | 2007 |
| Kansas | Kan. Stat. Ann. § § 58a-101–58a-1107 | 2003 |
| Kentucky | Ky. Rev. Stat. Ann. § § 386B.1-010–386B.1-11-050 | 2014 |
| Maine | Me. Rev. Stat. Ann. tit. 18-B, § § 101–1104 | 2005 |
| Maryland | Md. Code Ann., Est. & Trusts § § 14.5-5-101–14.5-1006 | 2015 |
| Massachusetts | Mass. Gen. L. ch. 203E, § § 101–1013 | 2012 |
| Michigan | Mich. Comp. Laws § § 700.7101–700.7913 | 2010 |
| Minnesota | Minn. Stat. § § 501C.0101–501C.1304 | 2016 |
| Mississippi | Miss. Code Ann.§ § 91-8-101–91-8-1206 | 2014 |
| Missouri | Mo. Ann. Stat. § § 456.1-101–456.11-1106 | 2005 |
| Montana | Mont. Code Ann. § § 72-38-101–72-38-1111 | 2013 |
| Nebraska | Neb. Rev. Stat. § § 30-3801–30-38,110 | 2005 |
| New Hampshire | N.H. Rev. Stat. Ann. § § 564-B:1-101–564-B:12-1210 | 2004 |
| New Jersey | N.J. Rev. Stat. § § 3B:1-1–3B:31-84 | 2016 |
| New Mexico | N.M. Stat. Ann. § § 46A-1-101–46A-11-1105 | 2007 |
| North Carolina | N.C. Gen. Stat. § § 36C-1-101–36C-11-1106 | 2006 |
| North Dakota | N.D. Cent. Code § § 59-09-01–59-19-02 | 2007 |
| Ohio | Ohio Rev. Code Ann. § § 5801.01–5811.03 | 2007 |
| Oregon | Or. Rev. Stat. § § 130.001–130.910 | 2006 |
| Pennsylvania | 20 Pa. Cons. Stat. § § 7701–7790.3 | 2006 |
| South Carolina | S.C. Code Ann. § § 62-7-101–62-7-1106 | 2006 |
| Tennessee | Tenn. Code Ann. § § 35-15-101–35-15-1206 | 2004 |
| Utah | Utah Code Ann. § § 75-7-10–75-7-1201 | 2004 |
| Vermont | Vt. Stat. Ann. tit. 14A, § § 101–1204 | 2009 |
| Virginia | Va. Code Ann. § § 64.2-700–64.2-808 | 2006 |
| West Virginia | W. Va. Code § § 44D-1-101–44D-11-1105 | 2011 |
| Wisconsin | Wis. Stat. § § 701.0101–701.1205 | 2014 |
| Wyoming | Wyo. Stat. § § 4-10-101–4-10-1103 | 2003 |

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| States Without Uniform Trust Code (18) | | |
|---|---|---|
| **State** | | |
| Alaska | | |
| California | | |
| Connecticut | | |
| Delaware | | |
| Georgia | | |
| Hawaii | | |
| Idaho | | |
| Illinois | | |
| Indiana | | |
| Iowa | | |
| Louisiana | | |
| Nevada | | |
| New York | | |
| Oklahoma | | |
| Rhode Island | | |
| Rhode Island | | |
| South Dakota Texas | | |
| South Dakota | | |
| Texas | | |
| Washington | | |

*Note:* The text of the Uniform Trust Code ("UTC") is available at www.uniformlaws.org/shared/docs/trust_code/UTC_Final_2018may17.pdf. To determine which states have enacted the UTC, go to www.uniformlaws.org/LegislativeFactSheet.aspx?title=Trust Code.

## Worksheet 4 State Perpetuities Statutes*

**(As of September 2018)**

| State | Citation | Year |
|---|---|---|
| **Permits Perpetual Trusts (24)** | | |
| Alaska | Alaska Stat. § § 34.27.051, 34.27.100 | 2000 |
| Arkansas[2] | Ark. Code Ann. § 18-3-104(8) | 2017 |
| Delaware | Del Code Ann. tit. 25, § 503 (trusts of personal property only) | 1995[1] |
| District of Columbia | D.C. Code Ann. § 19-904(a)(10) | 2001 |
| Hawaii | Haw. Rev. Stat. § § 525-4(6) (trusts under Permitted Transfers in Trust Act only) | 2010 |
| Idaho | Idaho Code § § 55-111, 55-111A | 1957 |
| Illinois | 765 ILCS § § 305/3(a-5), 305/4(a)(8) | 1998 |
| Kentucky | Ky. Rev. Stat. Ann. § § 381.224, 381.226 | 2010 |
| Maine | Me. Rev. Stat. Ann. tit. 33, § 114(7) | 1999 |
| Maryland | Md. Code Ann., Est. & Trusts § 11-102(b)(5) | 1998 |
| Michigan | Mich. Comp. Laws § § 554.91–554.94 (trusts of personal property only) | 2008 |
| Missouri | Mo. Ann. Stat. § 456.025(1) | 2001 |
| Nebraska | Neb. Rev. Stat. § 76-2005(9) | 2002 |
| New Hampshire | N.H. Rev. Stat. Ann. § § 547:3-k, 564-B:4-402A, 564:24 | 2004 |
| New Jersey | N.J. Rev. Stat. § § 46:2F-9–46:2F-10 | 1999 |
| North Carolina[2] | N.C. Gen. Stat. § 41-23(h) | 2007 |
| Ohio | Ohio Rev. Code Ann. § 2131.09(B) | 1999 |
| Oklahoma[2] | Okla. Stat. Ann. tit. 60, § 175.47(A) | 2015 |
| Pennsylvania | 20 Pa. Cons. Stat. § 6107.1(b)(1) | 2007 |
| Rhode Island | R.I. Gen. Laws § 34-11-38 | 1999 |
| South Dakota | S.D. Codified Laws Ann. § § 43-5-1, 43-5-8 | 1983 |
| Virginia | Va. Code Ann. § 55-12.4(A)(8), (B) (trusts of personal property only) | 2000 |
| Wisconsin | Wis. Stat. § 700.16(1)(a) | — |
| | | |
| **Permits Very Long Trusts (11)** | | |
| Alabama (360 years) | Ala. Code § 35-4A-5(9) | 2012 |
| Arizona[2] (500 years) | Ariz. Rev. Stat. Ann. § 14-2901(A) | 2009 |
| Colorado (1,000 years) | Colo. Rev. Stat. § 15-11-1102.5(1)(b) | 2001 |
| Florida (360 years) | Fla. Stat. § 689.225(2)(f) | 2001 |
| Georgia (360 years) | Ga. Code Ann. § 44-6-201(a) | 2018 |
| Mississippi (360 | Miss. Code Ann. § 89-25-9(h)(iii) (trusts of personal property | 2015 |

| | | |
|---|---|---|
| years) | only) | |
| Nevada[2] (365 years) | Nev. Rev. Stat. § 111.1031(1)(b) | 1999 |
| Tennessee[2] (360 years) | Tenn. Code Ann. § 66-1-202(f) | 2007 |
| Utah (1,000 years) | Utah Code Ann. § 75-2-1203(1) | 2003 |
| Washington (150 years) | Wash. Rev. Code § 11.98.130 | 2001 |
| Wyoming[2] (1,000 years) | Wyo. Stat. § 34-1-139(b)(ii) | 2003 |
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|---|---|---|
| **Flows USRAP (13)** | | |
| California | Cal. Prob. Code § 21205 | 1992 |
| Connecticut | Conn. Gen. Stat. § 45a-491 | 1989 |
| Hawaii | Haw. Rev. Stat. § 525-1 (except trusts under Permitted Transfers in Trust Act) | 1992 |
| Indiana | Ind. Code Ann. § 32-17-8-3 | 1991 |
| Kansas | Kan. Stat. Ann. § 59-3401 | 1992 |
| Massachusetts | Mass. Gen. L. ch. 190B, § 2-901 | 1989 |
| Minnesota | Minn. Stat. § § 501A.01, 501C.1202 | 1992 |
| Montana[2] | Mont. Code Ann. § 72-2-1002 | 1989 |
| New Mexico | N.M. Stat. Ann. § 45-2-901 | 1992 |
| North Dakota | N.D. Cent. Code § 47-02-27.1 (except business trusts) | 1991 |
| Oregon | Or. Rev. Stat. § 105.950 | 1990 |
| South Carolina | S.C. Code Ann. § 27-6-20 | 1987 |
| West Virginia | W. Va. Code § 36-1A-1 | 1992 |
| | | |
| **Follows Common-Law Rule Against Perpetuities (4)** | | |
| Iowa | Iowa Code Ann. § 558.68 | |
| New York | N.Y. Est. Powers & Trusts Law § 9-1.1 | |
| Texas[2] | Tex. Prop. Code Ann. § 112.036 | |
| Vermont | Vt. Stat. Ann. tit. 27, § § 501–503 | |
| | | |
| **Requires Trust to Terminate at Death of Last Member of Class of Specified Relations of Trustor and/or Trustor's Current, Former, or Predeceased Spouse** | | |
| Louisiana | La. Rev. Stat. Ann. § 9:1981 | 2001 |

*Note*: The text of the Uniform Statutory Rule Against Perpetuities ("USRAP") is available at www.unifromlaws.org/shared/docs/statutory%20rule%20against%20perpetuities/USRAPA_2011_Final%Act_2014sep11.pdf. To determine which states have enacted the USRAP, go to www.uniformlaws.org/LegislativeFactSheet.aspx?title=Statutory Rule Against Perpetuities.

[1] Delaware has permitted the creation of perpetual trusts through the successive exercise of nongeneral

powers of appointment since 1933 (38 Del. Laws 198, § 1).

[2] State's constitution contains prohibition of perpetuities.

Estates, Gifts and Trusts Portfolios
Trusts
Portfolio 867-2nd: Choosing a Domestic Jurisdiction for a Long-Term Trust
Working Papers

## Worksheet 5 Bases of State Income Taxation of Nongrantor Trusts*

**(Revised 2/15/18)**

| State | Citations | Top 2017 Rate | Trust Created by Will of Resident | Inter Vivos Trust Created by Resident | Trust Administered in State | Trust With Resident Trustee | Trust With Resident Beneficiary | Tax Dept. Website |
|---|---|---|---|---|---|---|---|---|
| Alabama | Ala. Code § § 40-18-1(33), 40-18-5(l)(c); instructions to 2017 Ala. Form 41 at 1, 2. | 5.00% on inc. over $3,000 | ✓ [1] | ✓ [1] | | | | revenue.alabama.gov |
| Alaska | No income tax imposed on trusts. | | | | | | | www.dor.alaska.gov |
| Arizona | Ariz. Rev. Stat. § § 43-1011(5)(a), 43-1301(5), 43-1311(B); instructions to 2017 Ariz. Form 141AZ at 1, 20. | 4.54% on inc. over $155,159 | | | | ✓ | | www.azdor.gov |
| Arkansas | Ark. Code Ann. § § 26-51-201(a)(9), (10), 26-51-203(a); instructions to 2017 Ark. AR1002 at 1; 2017 Ark. Indexed Tax Brackets Chart. | 6.9% inc. on or over $82,601 | ✓ [2] | ✓ [2] | | | | www.dfa.arkansas.gov |
| California | Cal. Rev. & Tax. Code § § 17041(a)(1), 17043(a), 17742(a); Cal. Const. Art. XIII, § 36(f)(2); instructions to 2017 Cal. Form 541 at 4, 9, 10. | 13.3% on inc. over $1 million | | | | ✓ | ✓ | www.ftb.ca.gov |

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| Colorado | Colo. Rev. Stat. § § 39-22-103(10), 39-22-104(1.7); instructions to 2017 Colo. Form 105 at 3, 4; 2017 Colo. Form 105 at 1. | 4.63% | | | ✓ | | | www.colorado.gov/revenue |
| Connecticut | Conn. Gen. Stat. § § 12-700(a)(9), 12-701(a)(4)(C)–(D); Conn. Agencies Regs. § 12-701(a)(4)-1; instructions to 2017 Form CT-1041 at 6; 2017 Form CT-1041 at 3. | 6.99% | ✓ | ✓ [3] | | | | www.ct.gov/drs |

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| State | Citations | Top 2017 Rate | Trust Created by Will of Resident | Inter Vivos Trust Created by Resident | Trust Administered in State | Trust With Resident Trustee | Trust With Resident Beneficiary | Tax Dept. Website |
|---|---|---|---|---|---|---|---|---|
| Delaware | 30 Del. Code Ann. tit. 30, § § 1102(a)(14), 1601(8); 2017 Del. Form 400-I at 1, 2; 2017 Del. Form 400 at 2. | 6.6% on inc. over $60,000 | ✓ [4] | ✓ [4] | | ✓ [4] | | www.revenue.delaware.gov |
| District of Columbia | D.C. Code Ann. § § 47-1806.03(a)(10), 47-1809.01, 47-1809.02; instructions to 2017 D.C. Form D-41 at 6, 7. | 8.95% on inc. over $1,000,000 | ✓ | ✓ | | | | otr.cfo.dc.gov |
| Florida | No income tax imposed on trusts; Florida intangible property tax repealed for 2007 and later years. | | | | | | | floridarevenue.com |
| Georgia | Ga. Code Ann. § § 48-7-20(b)(1), (d), 48-7-22; Ga. Comp. R. & Regs. r. 560-7-3-.07(1); | 6.0% on inc. over $7,000 | | | | | ✓ [5] | dor.georgia.gov |

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | instructions to 2017 Ga. Form 501 at 6. | | | | | | | |
| Hawaii | Haw. Rev. Stat. § § 235-1, 235-4.5, 235-51(d); Haw. Admin. Rules § 18-235-1.17; instructions to 2017 Haw. Form N-40 at 1, 13. | 8.25% on inc. over $40,000 | | | ✓ [4] | ✓ [4] | | tax.hawaii.gov |
| Idaho | Idaho Code § § 63-3015(2), 63-3024(a); Idaho Admin. Code Regs. 35.01.01.035.01, 35.01.01.075.03(e); instructions to 2017 Idaho Form 66 at 1, 10. | 7.40% on inc. over $10,905 | ✓ [6] | ✓ [6] | ✓ [6] | ✓ [6] | | www.tax.idaho.gov |
| Illinois | 35 ILCS 5/201(a), (b)(5.3), (c), (d), 5/1501(a)(20)(C)–(D); Ill. Admin. Code tit. 86, § 100.3020(a)(3)–(4); instructions to 2017 Form IL-1041 at 4, 10; 2017 Form IL-1041 at 2, 3. | 5.85% | ✓ | ✓ | | | | www.tax.illinois.gov |
| Indiana | Ind. Code Ann. § § 6-3-1-12(d), 6-3-1-14, 6-3-2-1(a)(3); Ind. Admin. Code tit. 45, r. 3.1-1-21(d); instructions to 2017 Ind. Form IT-41 at 1, 3; 2017 Ind. Form IT-41 at 1. | 3.23% | | | ✓ | | | www.in.gov/dor |
| Iowa | Iowa Code Ann. § 422.5(1)(i), (6); Iowa Admin. Code r. 701-89.3(1)–(2); instructions to 2017 Iowa Form IA 1041 at 1; 2017 Iowa Form IA 1041 at 2. | 8.98% on inc. over $70,785 | ✓ [6] | ✓ [6] | ✓ [6] | ✓ [6] | | tax.iowa.gov |
| Kansas | Kan. Stat. Ann. § § 79-32,109(d), 79-32,110(a)(2)(E), (d); instructions to 2017 Kan. Form K-41 at 2; 2017 Kan. Form K-41 at | 5.2% on inc. over $30,000 | | | ✓ | | | www.ksrevenue.org |

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | 4. | | | | | | | |
| Kentucky | Ky. Rev. Stat. Ann. § § 141.020(2)(b)(6), 141.030(1); 103 Ky. Admin. Regs. 19:010; instructions to 2017 Ky. Form 741 at 1, 2. | 6.0% on inc. over $75,000 | | | | ✓ | | revenue.ky.gov |
| Louisiana | La. Rev. Stat. Ann. § § 47:300.1(3), 47:300.10(3); instructions to 2017 La. Form IT-541 at 1. | 6.0% on inc. over $50,000 | ✓ | | ✓ [7] | | | www.revenue.louisiana.gov |
| Maine | Me. Rev. Stat. Ann. tit. 36, § § 5102(4)(B)–(C), 5111(1-E), 5403; instructions to 2017 Form 1041ME at 1, 2. | 7.15% on inc. over $50,000 | ✓ | ✓ | | | | www.maine.gov/revenue |
| Maryland | Md. Code Ann., Tax–Gen. § § 10-101(k)(1)(iii), 10-105(a)(1), 10-106(a)(1)(iii); instructions to 2017 Md. Form 504 at 1, 5, 6. | 5.75% (plus county tax between 1.25% and 3.20%) on inc. over $250,000 | ✓ | ✓ | ✓ | | | www.marylandtaxes.com |
| Massachusetts | Mass. Gen. L. ch. 62, § § 4, 10(c); Mass Regs. Code tit. 830, § 62.10.1(1); instructions to 2017 Mass. Form 2 at 1, 3, 22; 2017 Mass. Form 2 at 2. | 5.1% (12.0% for short-term gains and gains on sales of collectibles) | ✓ [4] | ✓ [4, 8] | | | | www.mass.gov/dor |
| Michigan | Mich. Comp. Laws § § 206.16, 206.18(1)(c), 206.51(1)(b); instructions to 2017 MI-1041 at 2; 2017 MI-1041 at 1. | 4.25% | ✓ | ✓ [9] | | | | www.michigan.gov/taxes |
| Minnesota | Minn. Stat. § § 290.01 Subd. 7b, 290.06 Subd. 2c, | 9.85% on inc. over | ✓ [10] | ✓ [10] | ✓ [11] | | | www.revenue.state.mn.us |

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | Subd. 2d; instructions to 2017 Minn. Form M2 at 1, 14. | $130,760 | | | | | | |
| Mississippi | Miss. Code Ann. § 27-7-5(1)(b); instructions to 2017 Miss. Form 81-110 at 3, 11. | 5.0% on inc. over $10,000 | | | ✓ | | | www.dor.ms.gov |
| Missouri | Mo. Ann. Stat. § § 143.011, 143.061; 143.331(2)–(3); instructions to 2017 Form MO-1041 at 4, 10. | 6.00% on inc. over $9,072 | ✓ [12] | ✓ [12] | | | | dor.mo.gov |
| Montana | Mont. Code Ann. § § 72-38-103(14), 15-30-2103; instructions to 2017 Mont. Form FID-3 at 2, 12, 1516; 2017 Mont. Form FID-3 at 2. | 6.9% on inc. over $17,600 | ✓ [12] | ✓ [12] | ✓ | ✓ | ✓ | revenue.mt.gov |
| Nebraska | Neb. Rev. Stat. § § 77-2714.01(6)(b)–(c), 77-2715.03(2), (3), 77-2717(1)(a); Neb. Admin. Code tit. 316, Ch. 23, REG-23-001; instructions to 2017 Neb. Form 1041N at 7, 8. | 6.84% on inc. over $15,580 | ✓ | ✓ | | | | www.revenue.nebraska.gov |
| Nevada | No income tax imposed on trusts. | | | | | | | tax.nv.gov |
| New Hampshire | No income tax imposed on trusts. | | | | | | | www.revenue.nh.gov |
| New Jersey | N.J. Rev. Stat.§ § 54A:1-2(o)(2)–(3), 54A:2-1(b)(5); instructions to 2017 Form NJ-1041 at 1, 24. | 8.97% on inc. over $500,000 | ✓ [13] | ✓ [13] | | | | www.state.nj.us/treasury/taxation |
| New Mexico | N.M. Stat. Ann. § § 7-2-2(I), (S), 7-2-7(C); instructions to 2017 N.M. Form F1D-1 at 2, 5. | 4.9% on inc. over $16,000 | | | ✓ | ✓ | | www.tax.newmexico.gov |
| New York State | N.Y. Tax Law § § 601(c)(1)(A), 605(b)(3); 20 NYCRR § 105.23; instructions to 2017 | 8.82% on inc. over $1,077,550 | ✓ [13] | ✓ [13] | | | | www.tax.ny.gov |

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|---|---|---|---|---|---|---|---|---|
| | N.Y. Form IT-205 at 2, 10. | | | | | | | |
| New York City | N.Y. Tax Law § § 1304(a)(3), 1304-B, 1305; Admin. Code City of N.Y. § § 11-1701, 11-1704.1, 11-1705; instructions to 2017 N.Y. Form IT-205 at 16, 17. | 3.876% on inc. over $50,000 | ✓ [13] | ✓ [13] | | | | www.tax.ny.gov |
| North Carolina | N.C. Gen. Stat. § § 105-153.7(a), 105-160.2; instructions to 2017 N.C. Form D-407 at 1; 2017 N.C. Form D-407 at 1. | 5.499% | | | | | ✓ | www.ncdor.gov |
| North Dakota | N.D. Cent. Code § § 57-38-07, 57-38-30.3(1)(e), (g); N.D. Admin. Code § 81-03-02.1-04(2); instructions to 2017 N.D. Form 38 at 2; 2017 N.D. Form 38 at 2. | 2.90% on inc. over $12,400 | | | ✓ | ✓ | ✓ | www.nd.gov/tax |
| Ohio | Ohio Rev. Code Ann. § § 5747.01(I)(3), 5747.02(A)(3), (D); instructions to 2017 Ohio Form IT 1041 at 4, 12. | 4.997% on inc. over $213,350 | ✓ | ✓ [4] | | | | www.tax.ohio.gov |
| Oklahoma | Okla. Stat. tit. 68, § § 2353(6) 2355(C)(1)(f), (G), 2355.1A; Okla. Admin. Code § 710:50-23-1(c); instructions to 2017 Okla. Form 513 at 2, 14. | 5.0% on inc. over $8,700 | ✓ | ✓ | | | | www.tax.ok.gov |
| Oregon | Or. Rev. Stat. § § 316.037, 316.282(1)(d); Or. Admin. R. 150-316.0400(3); instructions to 2017 Or. Form 41 at 3; 2017 Or. Form 41 at 3. | 9.9% on inc. over $125,000 | | | ✓ | ✓ | | www.oregon.gov/dor |

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|---|---|---|---|---|---|---|---|---|
| Pennsylvania | 72 P.S. § § 7301(s), 7302; 61 Pa. Code § 101.1; instructions to 2017 Form PA-41 at 4; 2017 Form PA-41 at 1. | 3.07% | ✓ [14] | ✓ [14] | | | | www.revenue.pa.gov |
| Rhode Island | R.I. Gen. Laws § § 44-30-2.6(c)(3)(A)(II), (E), 44-30-5(c)(2)–(4); R.I. Admin. Code 60-1-154:1; instructions to 2017 Form RI-1041 at 1-1; 2017 RI-1041 Tax Rate Schedules at 1. | 5.99% on inc. over $7,800 | ✓ [4] | ✓ [4] | | | | www.tax.ri.gov |
| South Carolina | S.C. Code Ann. § § 12-6-30(5), 12-6-510(A), 12-6-520; instructions to 2017 Form SC1041 at 1, 3. | 7.0% on inc. over $14,670 | | | ✓ | | | dor.sc.gov |
| South Dakota | No income tax imposed on trusts. | | | | | | | dor.sd.gov |
| Tennessee | Tenn. Code Ann. § § 67-2-102, 67-2-110(a); instructions to 2017 Tenn. Form INC. 250 at 1, 3, 4. | 4.0% (interest and dividends only) | | | | | ✓ | www.tn.gov/revenue |
| Texas | No income tax imposed on trusts. | | | | | | | www.comptroller.texas.gov/taxes |
| Utah | Utah Code Ann. § § 59-10-104(2)(b), 59-10-201(1), 75-7-103(1)(i)(ii)–(iii); instructions to 2017 UT Form TC-41 at 3, 6; 2017 UT Form TC-41 at 1. | 5.0% | ✓ [15] | | ✓ [15, 16] | | | www.tax.utah.gov |
| Vermont | Vt. Stat. Ann. tit. 32, § § 5811(11)(B), 5822(a)(5), (6), (b)(2); instructions to 2017 Vt. Form FIT-161 at 2; 2017 Vt. Form FIT-161 at | 8.95% on inc. over $12,450 | ✓ | ✓ | | | | www.tax.vt.gov |

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | 2. | | | | | | | |
| Virginia | Va. Code Ann. § § 58.1-302, 58.1-320, 58.1-360; 23 Va. Admin. Code § 10-115-10; instructions to 2017 Va. Form 770 at 1, 8. | 5.75% on inc. over $17,000 | ✓ | ✓ | ✓ | ✓ | | www.tax.virginia.gov |
| Washington | No income tax imposed on trusts. | | | | | | | dor.wa.gov |
| West Virginia | W. Va. Code § § 11-21-4e(a), 11-21-7(c); W. Va. Code St. Rs. § 110-21-4, 110-21-7.3; instructions to 2017 W. Va. Form IT-141 at 1, 5. | 6.5% on inc. over $60,000 | ✓ | ✓ | | | | www.tax.wv.gov |
| Wisconsin | Wis. Stat. § § 71.06(1q), (2e)(b), 71.125(1), 71.14(2), (3), (3m); instructions to 2017 Wis. Form 2 at 1, 19. | 7.65% on inc. over $247,350 | ✓ | ✓ [17] | ✓ [18] | | | www.revenue.wi.gov |
| Wyoming | No income tax imposed on trusts. | | | | | | | revenue.wyo.gov |

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[1] Provided that trust has resident fiduciary or current beneficiary.

[2] Provided that trust has resident trustee.

[3] Provided that trust has resident noncontingent beneficiary.

[4] Provided that trust has resident beneficiary.

[5] Tax also applies if trustee receives income from business done in state or manages funds or property located in state.

[6] Provided that other requirements are met.

[7] Unless trust designates governing law other than Louisiana.

[8] Provided that trust has Massachusetts trustee.

[9] Unless trustees, beneficiaries, and administration are outside Michigan.

[10] Post-1995 trusts only.

[11] Pre-1996 trusts only.

[12] Provided that trust has resident income beneficiary during or on last day of year.

[13] Unless trustees and trust assets are outside state and no source income; trustee should file informational return.

[14] Unless settlor is no longer resident or is deceased and trust lacks sufficient contact with Pennsylvania to establish nexus.

[15] Post-2003 irrevocable resident nongrantor trust having Utah corporate trustee may deduct all nonsource income but must file Utah return if must file federal return.

[16] Testamentary trust created by non-Utah resident; inter vivos trust created by Utah or non-Utah resident.

[17] Trust created or first administered in Wisconsin after October 28, 1999, only.

[18] Irrevocable inter vivos trust administered in Wisconsin before October 29, 1999, only.

## Worksheet 6 State Prudent-Investor Rule Statutes*

**(As of September 2018)**

| State | Citation | Year[1] |
|---|---|---|
| **Has Stand-Alone Prudent-Investor Rule (7)** | | |
| Delaware[2] | Del. Code Ann. tit. 12, § 3302 | 1986 |
| Florida | Fla. Stat. § § 518.11–518.112, 736.0901 | 1993 |
| Georgia | Ga. Code Ann. § § 53-12-340–53-12-345 | 1988 |
| Kentucky | Ky. Rev. Stat. Ann. § § 286.3-277, 386B.9-010 | 1996 |
| Louisiana | La. Rev. Stat. Ann. § 9:2127 | 2001 |
| New York | N.Y. Est. Powers & Trusts Law § 11-2.3 | 1995 |
| Pennsylvania | 20 Pa. Cons. Stat. § § 7201–7214 | 1999 |
| | | |

| Follows 1994 Uniform Prudent Investor Act (44) | | Year Adopted Stand Alone Prudent-Investor Rule[1] | Year Adopted UPIA[1] |
|---|---|---|---|
| Alabama | Ala. Code § § 19-3B-901–19-3B-906 | 1989 | 2007 |
| Alaska | Alaska Stat. § § 13.36.225–13.36.290 | | 1998 |
| Arizona | Ariz. Rev. Stat. Ann. § § 14-10901–14-10909 | | 1996 |
| Arkansas | Ark. Code Ann. § § 28-73-901–28-73-908 | | 1997 |
| California | Cal. Prob. Code § § 16045–16054 | 1987 | 1996 |
| Colorado | Colo. Rev. Stat. § § 15-1.1-101–15-1.1-115 | | 1995 |
| Connecticut | Conn. Gen. Stat. § § 45a-541–45a-541l | | 1997 |
| District of Columbia | D.C. Code Ann. § § 19-1309.01–19-1309.06 | | 2004 |
| Hawaii | Haw. Rev. Stat. § § 554C-1–554C-12 | | 1997 |
| Idaho | Idaho Code § § 68-501–68-514 | | 1997 |
| Illinois | 760 ILCS 5/5–5/5.1 | | 1992 |
| Indiana | Ind. Code Ann. § § 30-4-3.5-1–30-4-3.5-13 | | 1999 |
| Iowa | Iowa Code Ann. § § 633A.4301–633A.4309 | 1991 | 2000 |
| Kansas | Kan. Stat. Ann. § § 58-24a01–58-24a14, 58a-901 | 1993 | 2000 |

| | | | |
|---|---|---|---|
| Maine | Me. Rev. Stat. Ann. tit. 18-B, § § 901–908 | | 1997 |
| Maryland | Md. Code Ann., Est. & Trusts § 15-114 | 1994 | |
| Massachusetts | Mass. Gen. L. ch. 203C, § § 1–11 | | 1999 |
| Michigan | Mich. Comp. Laws § § 700.1501–700.1512 | | 2000 |
| Minnesota | Minn. Stat. § 501C.0901 | 1986 | 1997 |
| Mississippi | Miss. Code Ann. § § 91-9-601–91-9-627, 91-8-901 | | 2006 |
| Missouri | Mo. Ann. Stat. § § 469.900–469.913 | | 1996 |
| Montana | Mont. Code Ann. § § 72-38-901–72-38-906 | 1989 | 2003 |
| Nebraska | Neb. Rev. Stat. § § 30-3883–30-3889 | | 1997 |
| Nevada | Nev. Rev. Stat. § § 164.705–164.775 | 1989 | 2003 |
| New Hampshire | N.H. Rev. Stat. Ann. § § 564-B:9-901–564-B:9-907 | 1999 | 2004 |
| New Jersey | N.J. Rev. Stat. § § 3B:20-11.1–3B:20-11.12 | | 1997 |
| New Mexico | N.M. Stat. Ann. § § 45-7-601–45-7-612 | | 1995 |
| North Carolina | N.C. Gen. Stat. § § 36C-9-901–36C-9-907 | | 2000 |
| North Dakota | N.D. Cent. Code § § 59-17-01–59-17-06 | | 1997 |
| Ohio | Ohio Rev. Code Ann. § § 5809.01–5809.08 | | 1999 |
| Oklahoma | Okla. Stat. Ann. tit. 60, § § 175.60–175.72 | | 1995 |
| Oregon | Or. Rev. Stat. § § 130.750–130.775 | | 1995 |
| Rhode Island | R.I. Gen. Laws § § 18-15-1–18-15-13 | | 1996 |
| South Carolina | S.C. Code Ann. § 62-7-933 | 1990 | 2001 |
| South Dakota | S.D. Codified Laws Ann. § § 55-5-6–55-5-16 | 1995 | |

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| **Follows 1994 Uniform Prudent Investor Act (Cont'd)** | | **Year Adopted Stand Alone Prudent-Investor Rule**[1] | **Year Adopted UPIA**[1] |
|---|---|---|---|
| Tennessee | Tenn. Code Ann. § § 35-14-101–35-14-114, 35-15-901 | 1989 | 2002 |
| Texas | Tex. Prop. Code Ann. § § 117.001–117.012 | 1991 | 2004 |
| Utah | Utah Code Ann. § § 75-7-901–75-7-907 | | 1995 |
| Vermont | Vt. Stat. Ann. tit. 14A, § § 901–906 | | 1998 |

| | | | |
|---|---|---|---|
| Virginia | Va. Code Ann. § § 64.2-780–64.2-791 | 1992 | 2000 |
| Washington | Wash. Rev. Code § 11.100.020 | 1985 | |
| West Virginia | W. Va. Code § § 44-6C-1–44-6C-15, 44D-9-901 | | 1996 |
| Wisconsin | Wis. Stat. § § 881.01, 701.0901 | | 2004 |
| Wyoming | Wyo. Stat. § § 4-10-901–4-10-913 | | 1999 |

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[1] Information based on Schanzenbach & Sitkoff, "*Did Reform of Prudent Trust Investment Laws Change Trust Portfolio Allocation*?," 50 J. Law & Econ. 681, 708 (Nov. 2007).

[2] Specifically allows trustee to pursue sustainable or socially responsible investment strategies.

**Has Special Rules for Acquisition and Administration of Life Insurance Policies**

| State | Citation | Year |
|---|---|---|
| Alabama | Ala. Code § 19-3B-818 | 2006 |
| Alaska | Alaska Stat. § 13.36.273 | 2013 |
| Arizona | Ariz. Rev. Stat. § 14-10908 | 2009 |
| Colorado | Colo. Rev. Stat. § 15-5-1301 | 2013 |
| Delaware | Del. Code Ann. tit. 12, § 3302(d) | 2003 |
| Florida | Fla. Stat. § 736.0902 | 2010 |
| Maryland | Md. Code Ann., Est. & Trusts § 15-116 | 1997 |
| North Carolina | N.C. Gen. Stat. § 36C-9-903.1 | 2007 |
| North Dakota | N.D. Cent. Code § 26.1-33-44 | 2001 |
| Ohio | Ohio Rev. Code Ann. § 5809.031 | 2012 |
| Pennsylvania | 20 Pa. Cons. Stat. § 7208 | 1999 |
| South Carolina | S.C. Code Ann. § 62-7-933(J)(1) | 2006 |
| South Dakota | S.D. Codified Laws § 55-5-17 | 2010 |
| Tennessee | Tenn. Code Ann. § 35-14-105(c)(1) | 2002 |
| Virginia | Va. Code Ann. § 64.2-782(G) | 2012 |
| Wisconsin | Wis. Stat. § 701.0903 | 2014 |
| Wyoming | Wyo. Stat. § 4-10-902(g) | 2005 |

*Note*: The text of the Uniform Prudent Investor Act ("UPIA") is available at www.uniformlaws.org/shared/docs/prudent%20investor/upia_final_94.pdf. To determine which states have enacted the UPIA, go to www.uniformlaws.org/LegislativeFactSheet.aspx?title=Prudent Investor Act.

Estates, Gifts and Trusts Portfolios
Trusts
Portfolio 867-2nd: Choosing a Domestic Jurisdiction for a Long-Term Trust
Working Papers

## Worksheet 7 State Directed Trust Statutes*

**(As of September 2018)**

| State | Citation | Effective Date |
|---|---|---|
| **Follows § 808(b) of Uniform Trust Code and § 75 of Third Restatement of Trusts (20)—directed trustee liable if direction is [manifestly] contrary to terms of trust or trustee knows direction is [serious] breach of fiduciary duty of directing person** | | |
| Alabama | Ala. Code § 19-3B-808(b) | 1/1/07 |
| Arkansas | Ark. Code Ann. § 28-73-808(b) | 9/1/05 |
| District of Columbia | D.C. Code Ann. § 19-1308.08(b) | 3/10/04 |
| Florida (if directing person is not cotrustee) | Fla. Stat. § 736.0808(2) | 7/1/07 |
| Kansas | Kan. Stat. Ann. § 58a-808(b) | 1/1/03 |
| Kentucky | Ky. Rev. Stat. Ann. § 386B.8-080(2) | 7/15/14 |
| Maine | Me. Rev. Stat. Ann. tit. 18-B, § 808(2) | 7/1/05 |
| Maryland | Md. Code Ann., Est. & Trusts § 14.5-808(b)(1)(ii)(1)–(2) | 1/1/15 |
| Massachusetts | Mass. Gen. L. ch. 203E, § 808(b) | 7/8/12 |
| Michigan | Mich. Comp. Laws § 700.7809(4) | 4/1/10 |
| Montana | Mont. Code Ann. § 72-38-808(2) | 10/1/13 |
| Nebraska | Neb. Rev. Stat. § 30-3873(b) | 1/1/05 |
| New Jersey | N.J. Rev. Stat. § 3B:31-61(b) | 7/17/16 |
| North Dakota | N.D. Cent.Code § 59-16-08(2) | 8/1/07 |
| Oregon | Or. Rev. Stat. § § 130.685(2), 130.735(2) | 1/1/06 |
| Pennsylvania | 20 Pa. Cons. Stat. § 7778(b) | 11/6/06 |
| South Carolina | S.C. Code Ann. § 62-7-808(b) | 5/23/05 |
| Texas (charitable trusts only) | Tex. Prop. Code Ann. § 114.003(b) | 1/1/06 |
| Vermont | Vt. Stat. Ann. tit. 14A, § 808(b) | 7/1/09 |
| Virginia (unless § 64.2-770(E) applies) | Va. Code Ann. § 64.2-770(B) | 7/1/06 |
| West Virginia | W. Va. Code § 44D-8-808(b) | 6/10/11 |
| *Note*: Might not apply if directing person is cotrustee. | | |
| | | |
| **Has Protective Statute (30)—directed trustee liable for deficient execution of direction, for willful misconduct, or not at all** | | |
| Alaska (cotrustee or advisor) | Alaska Stat. § § 13.36.072(c), 13.36.375(c) | 9/9/13 |
| Arizona (settlor, cotrustee, beneficiary, or third party; bad faith or reckless indifference) | Ariz. Rev. Stat. Ann. § 14-10808(B) | 1/1/09 |
| Colorado (willful misconduct) | Colo. Rev. Stat. § 15-16-807 | 8/6/14 |
| Delaware (wilful misconduct; statute codified long-standing practice (see | Del. Code Ann. tit. 12, § § 3313, 3301(g), 3317, 3313A; Del. Code Ann. tit. 1, § | 7/3/86 |

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|---|---|---|
| *Lewis v. Hanson*, 128 A.2d 819 (Del. 1957); statute upheld in *Duemler v. Wilmington Trust Co.*, 2004 BL 31983, 2004 WL 5383927 (Del. Ch. 2004)) | 302(15) | |
| Florida (if directing person is cotrustee; willful misconduct) | Fla. Stat. § 736.0703(9) | 7/1/08 |
| Georgia[1] (settlor, advisory or investment committee, other person (including cotrustee); investment decisions only; bad faith or reckless indifference) | Ga. Code Ann. § 53-12-303 | 7/1/10 |
| Idaho | Idaho Code § § 15-7-501(2), (5), 15-1-201(34) | 7/1/99 |
| Illinois (willful misconduct) | 760 ILCS 5/16.3(f)(1), 5/16.7 | 1/1/13 |
| Indiana (if terms expressly direct trustee to rely or relieve trustee from liability for relying on directions) | Ind. Code Ann. § § 30-4-3-9(a), 30-4-1-2(12), 30-2-14-9 | 9/2/71 |

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| State | Citation | Effective Date |
|---|---|---|
| Kentucky (corporate trustees, investment decisions, authorized directions only) | Ky. Rev. Stat. Ann. § 286.3-275 | 7/15/96 |
| Louisiana | La. Rev. Stat. Ann. § 9:2114.1 | 8/1/15 |
| Maryland (willful misconduct; unclear when overrides § 14.5-808(b)) | Md. Code Ann., Est. & Trusts § § 14.5-808(c), 14.5-103(p) | 1/1/15 |
| Minnesota (willful misconduct) | Minn. Stat. § § 501C.0808, subd. 6,501C.0103(j) | 1/1/16 |
| Mississippi (trustee, trust advisor, or trust protector) | Miss. Code Ann. § § 91-8-808(b), 91-8-710, 91-8-1204–91-8-1205 | 7/1/14 |
| Missouri | Mo. Ann. Stat. § 456.8-808(2), (8) | 8/28/12 |
| Nevada | Nev. Rev. Stat. § 163.5549 | 10/1/09 |
| New Hampshire (trustee, trust advisor, or trust protector) | N.H. Rev. Stat. Ann. § § 564-B:8-808(b), 564-B:1-103(9), (23), (24), (27), 564-B:7-711, 564-B:12-1204–564-B:12-1205 | 9/9/08 |
| New Jersey (investment decisions only; willful misconduct or gross negligence; unclear when overrides NJSA § 3B:31-61(b)) | N.J. Rev. Stat. § 3B:31-62(b) | 7/17/16 |
| New Mexico[1] | 2018 N.M. Laws 63 (willful misconduct) | 1/1/19 |
| North Carolina (cotrustee or other power holder; intentional misconduct if directed by power holder) | N.C. Gen. Stat. § § 36C-7-703(g1), 36C-8A-4 | 6/11/12 |
| North Dakota (willful misconduct) | N.D. Cent. Code § 59-16.2-07(3)(a) | 3/21/17 |
| Ohio (grantor, advisory or investment committee, or other person (including | Ohio Rev. Code Ann. § § 5808.08(B), 5815.25(B)–(C) | 1/1/07 |

| | | |
|---|---|---|
| fiduciary)) | | |
| Oklahoma (trust, advisory or investment committee, or other person (including cotrustee); investment decisions only; negligent execution) | Okla. Stat. Ann. tit. 60, § 175.19 | 2/19/68 |
| South Dakota | S.D. Codified Laws § 55-1B-2 | 3/19/97 |
| Tennessee | Tenn. Code Ann. § § 35-15-710, 35-15-808(b), (e), 35-15-1201(a), 35-15-1204–35-15-1205 | 7/1/13 |
| Texas (noncharitable trusts only; wilful misconduct) | Tex. Prop. Code Ann. § 114.0031 | 6/19/15 |
| Utah (investment decisions only; willful misconduct or gross negligence) | Utah Code Ann. § § 75-7-906(4), 75-1-201(35) | 7/1/04 |
| Virginia (willful misconduct or gross negligence; if statute is incorporated into trust by settlor or nonjudicial settlement agreement) | Va. Code Ann. § 64.2-770(E) | 10/1/12 |
| Washington (statutory trust advisor; directed trustee must act with good faith and honest judgment) | Wash. Rev. Code § 11.98A.100 | 7/24/15 |
| Wisconsin (willful misconduct) | Wis. Stat. § § 701.0808, 701.0103(7) | 7/1/14 |
| Wyoming | Wyo. Stat. § § 4-10-808(b), 4-10-715, 4-10-717, 4-10-103(a)(vi), (xii), (xxii), (xxiii), (xxviii) | 7/1/07 |
| *Note*: Unless otherwise indicated, statute does/might not apply if one trustee (not advisor, protector, etc.) holds power to direct another trustee. | | |
| | | |
| **Has Other Statute (2)** | | |
| Indiana (unless § 30-4-3-9(a) applies; directed trustee liable if direction violates terms of trust or fiduciary duty of directing person) | Ind. Code Ann. § § 30-4-3-9(b), 30-4-1-2(11), 30-2-14-9 | 9/2/71 |
| Iowa (unless trustee knows attempted exercise violates terms of trust or knows powerholder is incompetent) | Iowa Code Ann. § § 633A.4207(2), 633A.1102(11) | 7/1/00 |
| | | |
| **Has Protector Statute (16)** | | |
| Alaska | Alaska Stat. § 13.36.370 | 10/8/03 |
| Arizona | Ariz. Rev. Stat. § 14-10818 | 1/1/09 |
| Delaware | Del. Code Ann. tit. 12, § 3313 | 8/1/08 |
| Idaho | Idaho Code § 15-7-501 | 7/1/99 |
| Illinois | 760 ILCS 5/16.3, 5/16.7 | 1/1/13 |
| Michigan | Mich. Comp. Laws § 700.7809 | 6/18/09 |
| Mississippi | Miss. Code Ann. § § 91-8-1201–91-8-1206 | 7/1/14 |
| Missouri | Mo. Ann. Stat. § 456.8-808 | 8/28/12 |
| Nevada | Nev. Rev. Stat. § § 163.5536, 163.5547, 163.5553, 163.5555 | 10/1/09 |
| New Hampshire | N.H. Rev. Stat. Ann. § § 564-B:12-1201564-B:12-1206 | 9/9/08 |
| North Carolina | N.C. Gen. Stat. § § 36C-8A-1–36C-8A-11 | 6/11/12 |
| South Dakota | S.D. Codified Laws § § | 3/19/97 |

| | | |
|---|---|---|
| | 55-1B-1–55-1B-11 | |
| Tennessee | Tenn. Code Ann. § § 35-15-1201–35-15-1206 | 7/1/13 |
| Vermont | Vt. Stat. Ann. tit. 14A, § § 1101–1105 | 7/1/09 |
| Wisconsin | Wis. Stat. § 701.0818 | 7/1/14 |
| Wyoming | Wyo. Stat. § § 4-10-710–4-10-718 | 7/1/03 |
| | | |
| **Has No Statute (5)** | | |
| California | | |
| Connecticut | | |
| Hawaii | | |
| New York | | |
| Rhode Island | | |

*Note*: The text of the Uniform Directed Trust Act ("UDTA") is available at www.uniformlaws.org/LegislativeFactSheet.aspx?title=Directed Trust Act. To determine which states have enacted the UDTA, go to www.uniformlaws.org/shared/docs/divided%20trusteeship/UDTA_Final_2017nov3.pdf

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[1] Has enacted the Uniform Directed Trust Act.

## Worksheet 8 State Third-Party Trust Statutes*

**(As of September 2018)**

| State | Spendthrift Trust | Discretionary Trust |
|---|---|---|
| Alabama | Ala. Code § § 19-3B-502–19-3B-503 | Ala. Code § § 19-3B-504, 19-3B-814(a) |
| Alaska | Alaska Stat. § 34.40.110 | Alaska Stat. § 34.40.113 |
| Arizona | Ariz. Rev. Stat. Ann. § § 14-10502–14-10503 | Ariz. Rev. Stat. Ann. § § 14-10504, 14-10814(A) |
| Arkansas | Ark. Code Ann. § 28-73-502 | Ark. Code Ann. § § 28-73-504, 28-73-814(a) |
| California | Cal. Prob. Code § § 15300–15301, 15303, 15305–15309 | Cal. Prob. Code § § 15303, 15305–15308, 16080–16082 |
| Colorado | | |
| Connecticut | | |
| Delaware | Del. Code Ann. tit. 12, § 3536 | Del. Code Ann. tit. 12, § § 3315, 3536 |
| District of Columbia | D.C. Code Ann. § § 19-1305.02–19-1305.03 | D.C. Code Ann. § 19-1308.14(a) |
| Florida | Fla. Stat. § § 736.0502–736.0503 | Fla. Stat. § § 736.0504, 736.0814(1) |
| Georgia | Ga. Code Ann. § 53-12-80 | Ga. Code Ann. § § 53-12-81, 53-12-260 |
| Hawaii | | |
| Idaho | Idaho Code § 15-7-502 | |
| Illinois | 735 ILCS 5/2-1403 | 735 ILCS 5/2-1403 |
| Indiana | Ind. Code Ann. § 30-4-3-2 | Ind. Code Ann. § § 30-4-2.1-14, 30-4-2.1-14.5 |
| Iowa | Iowa Code Ann. § 633A.2302 | Iowa Code Ann. § § 633A.2305–633A.2306 |
| Kansas | Kan. Stat. Ann. § 58a-502 | Kan. Stat. Ann. § § 58a-502, 58a-814 |
| Kentucky | Ky. Rev. Stat. Ann. § 386B.5-020 | Ky. Rev. Stat. Ann. § § 386B.5-030, 386B.8-140(1) |
| Louisiana | La. Rev. Stat. Ann. § § 9:2001–9:2007 | |
| Maine | Me. Rev. Stat. Ann. tit. 18-B, § § 502–503 | Me. Rev. Stat. Ann. tit. 18-B, § § 504, 814(1) |
| Maryland | Md. Code Ann., Est. & Trusts§ § 14.5-504–14.5-505 | Md. Code Ann., Est. & Trusts § § 14.5-203, 14.5-502 |
| Massachusetts | Mass. Gen. L. ch. 203E, § 502 | Mass. Gen. L. ch. 203E, § 814(a) |
| Michigan | Mich. Comp. Laws § § 700.7502, 700.7504 | Mich. Comp. Laws § § 700.7505, 700.7815(1) |
| Minnesota | Minn. Stat.§ 501C.0502 | Minn. Stat. § § 501C.0504, 501C.0814(a) |
| Mississippi | Miss. Code Ann. § § 91-9-501, 91-9-503, 91-9-505, 91-9-511 | Miss. Code Ann. § § 91-9-507, 91-9-511, 91-8-814(a)(b) |
| Missouri | Mo. Ann. Stat. § § 456.5-502–456.5-503 | Mo. Ann. Stat. § § 456.5-504, 456.8-814(1) |
| Montana | Mont. Code Ann. § 72-38-502 | Mont. Code Ann. § § 72-38-504, 72-38-814(1) |

| | | |
|---|---|---|
| Nebraska | Neb. Rev. Stat. § § 30-3847–30-3848 | Neb. Rev. Stat. § § 30-3849, 30-3879(a) |
| Nevada | Nev. Rev. Stat. § § 166.010–166.180 | Nev. Rev. Stat. § 166.110, 163.4185–163.419 |
| New Hampshire | N.H. Rev. Stat. Ann. § 564-B:5-502 | N.H. Rev. Stat. Ann. § § 564-B:5-504, 564-B:8-814(a)–(c) |
| New Jersey | N.J. Rev. Stat. § 3B:31-36 | N.J. Rev. Stat. § § 3B:31-38, 3B:31-68 |
| New Mexico | N.M. Stat. Ann. § § 46A-5-502–46A-5-503 | N.M. Stat. Ann. § § 46A-5-504, 46A-8-814(A) |
| New York | N.Y. Est. Powers & Trusts Law § 7-1.5 | |
| North Carolina | N.C. Gen. Stat. § § 36C-5-502–36C-5-503 | N.C. Gen. Stat. § § 36C-5-503–36C-5-504, 36C-8-814(a) |
| North Dakota | N.D. Cent. Code § § 59-13-02–59-13-03 | N.D. Cent. Code § § 59-13-04, 59-16-14(1) |
| Ohio | Ohio Rev. Code Ann. § § 5805.01–5805.02 | Ohio Rev. Code Ann. § § 5805.04, 5808.14(A) |
| Oklahoma | Okla. Stat. Ann. tit. 60, § 175.25 | Okla. Stat. Ann. tit. 60, § 175.25(F) |
| Oregon | Or. Rev. Stat. § § 130.305–130.310 | Or. Rev. Stat. § 130.715(1) |
| Pennsylvania | 20 Pa. Cons. Stat. § § 7742–7743 | 20 Pa. Cons. Stat. § § 7744, 7780.4 |
| Rhode Island | R.I. Gen. Laws § 18-9.1-1 | |
| South Carolina | S.C. Code Ann. § § 62-7-502–62-7-503 | S.C. Code Ann. § § 62-7-504, 62-7-814(a) |
| South Dakota | S.D. Codified Laws § § 55-1-24–55-1-26, 55-1-34–55-1-35, 55-1-37, 55-1-41–55-1-42 | S.D. Codified Laws § § 55-1-24–55-1-26, 55-1-38, 55-1-39, 55-1-40, 55-1-43 |

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| | | |
|---|---|---|
| Tennessee | Tenn. Code Ann. § § 35-15-502–35-15-503 | Tenn. Code Ann. § § 35-15-504, 35-15-814(a) |
| Texas | Tex. Prop. Code Ann. § 112.035; Tex. Fam. Code Ann. § 154.005 | Tex. Fam. Code Ann. § 154.005 |
| Utah | Utah Code Ann. § § 75-7-502–75-7-503 | Utah Code Ann. § § 75-7-504, 75-7-812(1) |
| Vermont | Vt. Stat. Ann. tit. 14A, § § 502–503 | Vt. Stat. Ann. tit. 14A, § § 504, 814(a) |
| Virginia | Va. Code Ann. § § 64.2-743–64.2-745 | Va. Code Ann. § § 64.2-745, 64.2-746, 64.2-776(A) |
| Washington | Wash. Rev. Code § 6.32.250(2) | Wash. Rev. Code § 11.97.010 |
| West Virginia | W. Va. Code § § 44D-5-502–44D-5-503 | W. Va. Code § § 44D-5-504, 44D-8-814(a) |
| Wisconsin | Wis. Stat. § § 701.0502–701.0503 | Wis. Stat. § § 701.0504, 701.0814(1) |
| Wyoming | Wyo. Stat. § § 4-10-502–4-10-503, 4-10-505 | Wyo. Stat. § 4-10-504 |

## Worksheet 9 State Self-Settled Spendthrift Trust Statutes*

**(As of September 2018)**

| State | Citation | Effective Date |
|---|---|---|
| **Prohibits Trustor's Creditors From Reaching Trustor's Interest in or Assets of Self-Settled Spendthrift Trust in Certain Circumstances[1] (17)** | | |
| Alaska | Alaska Stat. § 34.40.110 | 1997 |
| Delaware | Del. Code Ann. tit. 12, § § 3536(c), 3570–3576 | 1997 |
| Hawaii | Haw. Rev. Stat. § § 554G-1–554G-11 | 2010 |
| Michigan | Mich. Comp. Laws § § 700.1041–700.1050 | 2017 |
| Mississippi | Miss. Code Ann. § § 91-9-701–91-9-723 | 2014 |
| Missouri | Mo. Ann. Stat. § 456.5-505(3) | 2005 |
| Nevada | Nev. Rev. Stat. § § 166.010–166.180 | 1999 |
| New Hampshire | N.H. Rev. Stat. Ann. § § 564-B:5-505A, 564-B:5-505B | 2009 |
| Ohio | Ohio Rev. Code Ann. § § 5816.01–5816.14 | 2013 |
| Oklahoma | Okla. Stat. Ann. tit. 31, § § 10–18 | 2005 |
| Rhode Island | R.I. Gen. Laws § § 18-9.2-1–18-9.2-7 | 1999 |
| South Dakota | S.D. Codified Laws Ann. § § 55-1-36, 55-16-1–55-16-17 | 2005 |
| Tennessee | Tenn. Code Ann. § § 35-15-505(a)(2), 35-16-101–35-16-112 | 2007 |
| Utah | Utah Code Ann. § 25-6-502 | 2003 |
| Virginia | Va. Code Ann. § § 64.2-747(A)(2), 64.2-745.1–64.2-745.2 | 2012 |
| West Virginia | W. Va. Code § § 44D-5-505, 44D-5-503a–44D-503C | 2016 |
| Wyoming | Wyo. Stat. § § 4-10-506(b), 4-10-510–4-10-523 | 2007 |
| | | |
| **Permits Trustor's Creditors to Reach Trustor's Interest in Self-Settled Spendthrift Trust (45)** | | |
| Alabama | Ala. Code § 19-3B-505(a)(2) | |
| Arizona | Ariz. Rev. Stat. § 14-10505(A)(2) | |
| Arkansas | Ark. Code Ann. § 28-73-505(a)(2) | |
| California | Cal. Prob. Code § 15304 | |
| Colorado | Colo. Rev. Stat. § 38-10-111 | |
| Delaware | Del. Code Ann. tit. 12, § 3536(c) | |
| District of Columbia | D.C. Code § 19-1305.05(a)(2) | |
| Florida | Fla. Stat. § 736.0505(1)(b) | |
| Georgia | Ga. Code. Ann. § 53-12-82(2) | |
| Idaho | Idaho Code § 15-7-502(4) | |
| Illinois | 735 ILCS 5/2-1403 | |
| Indiana | Ind. Code Ann. § 30-4-3-2(b) | |
| Iowa | Iowa Code Ann. § § 633A.2303–633A.2304 | |
| Kansas | Kan. Stat. Ann. § 58a-505(a)(2) | |
| Kentucky | Ky. Rev. Stat. Ann. § 386B.5-040(1)(b) | |
| Louisiana | La. Rev. Stat. Ann. § 9:2004 | |
| Maine | Me. Rev. Stat. Ann. tit. 18-B, § 505(1)(B) | |

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|---|---|---|
| Maryland | Md. Code Ann., Est. & Trusts § 14.5-508(A)(2) | |
| Massachusetts | Mass. Gen. L. ch. 203E, § 505(a)(2) | |
| Michigan | Mich. Comp. Laws § 700.7506(1)(c) | |
| Minnesota | Minn. Stat. § 501C.0505(2) | |
| Montana | Mont. Code Ann. § 72-38-505(1)(b) | |
| Nebraska | Neb. Rev. Stat. § 30-3850(a)(2) | |
| Nevada | Nev. Rev. Stat. § 166.015 | |
| New Hampshire | N.H. Rev. Stat. Ann. § 564-B:5-505A(2) | |
| New Jersey | N.J. Rev. Stat. § § 3B:31-39(a)(2), 3B:11-1(a) | |
| New Mexico | N.M. Stat. Ann. § 46A-5-505(A)(2) | |
| New York | N.Y. Est. Powers & Trusts Law § 7-3.1(a), N.Y. C.P.L.R. § 5205(c)(1) | |
| North Carolina | N.C. Gen. Stat. § 36C-5-505(a)(2) | |
| North Dakota | N.D. Cent. Code § 59-13-05(1) | |

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| | | |
|---|---|---|
| Ohio | Ohio Rev. Code Ann. § 5805.06(A)(2) | |
| Oklahoma | Okla. Stat. tit. 60, § 175.25(H) | |
| Oregon | Or. Rev. Stat. § 130.315(1)(b) | |
| Pennsylvania | 20 Pa. Cons. Stat. § 7745(2) | |
| South Carolina | S.C. Code Ann. § 62-7-505(a)(2) | |
| South Dakota | S.D. Codified Laws Ann. § 55-1-36 | |
| Tennessee | Tenn. Code Ann. § 35-15-505(a)(2) | |
| Texas | Tex. Prop. Code Ann. § 112.035(d) | |
| Utah | Utah Code Ann. § 75-7-505(2) | |
| Vermont | Vt. Stat. Ann. tit. 14A, § 505(a)(2) | |
| Virginia | Va. Code Ann. § 64.2-747(A)(2) | |
| Washington | Wash. Rev. Code § 19.36.020 | |
| West Virginia | W. Va. Code § 44D-5-505(a)(2) | |
| Wisconsin | Wis. Stat. § 701.0505(1)(b)(2) | |
| Wyoming | Wyo. Stat. § 4-10-506(b) | |
| | | |
| **Provides that Self-Settled Spendthrift Trust is Valid Even Though Trustor's Creditors May Reach Trustor's Interest (1)** | | |
| California | Cal. Prob. Code § 15304(a) | |
| **Provides That Self-Settled Spendthrift Trust is Void as to Creditor Claims (4)** | | |
| | | |
| Idaho | Idaho Code § 55-905 | |
| Illinois | 735 ILCS 5/2-1403 | |
| New York | N.Y. Est. Powers & Trusts Law § 7-3.1(a), N.Y. C.P.L.R. § 5205(c)(1) | |
| Washington | Wash. Rev. Code § 19.36.020 | |
| | | |
| **Has No Relevant Statute (1)** | | |
| Connecticut | | |

**Permit Lifetime Marital-Deduction and Other Trusts (16)**

| State | Citation | Year |
|---|---|---|
| Arizona | Ariz. Rev. Stat. § 14-10505(E) | 2009 |
| Arkansas | Ark. Code Ann. § 28-73-505(c)(1) | 2015 |
| Delaware | Del. Code Ann. tit. 12, § 3536(c)(1), (e) | 2009 |
| Florida | Fla. Stat. § 736.0505(3) | 2010 |
| Kentucky | Ky. Rev. Stat. Ann. § 386B.5-020(8) | 2014 |
| Maryland | Md. Code Ann., Est. & Trusts § 14.5-1003(a)(2) | 2015 |
| Michigan | Mich. Comp. Laws § 700.7506(b) | 2010 |
| New Hampshire | N.H. Rev. Stat. Ann. § 564-B:5-505A(c)(3)–(4) | 2014 |
| North Carolina | N.C. Gen. Stat. § 36C-5-505(c)(1) | 2011 |
| Oregon | Or. Rev. Stat. § 130.315(4) | 2013 |
| South Carolina | S.C. Code Ann. § 62-7-505(b)(2) | 2014 |
| Tennessee | Tenn. Code Ann. § 35-15-505(d) | 2010 |
| Texas | Tex. Prop. Code Ann. § 112.035(g)–(h) | 2013 |
| Virginia | Va. Code Ann. § 64.2-747(B)(3) | 2012 |
| Wyoming | Wyo. Stat. Ann. § 4-10-506(f) | 2011 |

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[1] For summaries of the statutes in this category, see Shaftel, *Eleventh Annual ACTEC Comparison of the Domestic Asset Protection Trust Statutes* (Aug. 2017), www.actec.org/assets/1/6/Shaftel-Comparison-of-the-Domestic-Asset-Protection-Trust-Statutes.pdf.

## Worksheet 10 State Power to Adjust and Unitrust Statutes*

**(As of September 2018)**

| State | Power to Adjust (49) | Protection for Trustee (40) | Unitrust Conversion Statute (36) | New Unitrust Statute (27) |
|---|---|---|---|---|
| Alabama | Ala. Code § 19-3A-104 | Ala. Code § 19-3A-104(f) | Ala. Code § 19-3A-106 | Ala. Code § 19-3A-105 |
| Alaska | Alaska Stat. § 13.38.210 | Alaska Stat. § 13.38.220 | Alaska Stat. § § 13.38.300–13.38.435 | Alaska Stat. § 13.38.420 |
| Arizona | Ariz. Rev. Stat. Ann. § 14-7403 | Ariz. Rev. Stat. Ann. § 14-7404(A) | Ariz. Rev. Stat. Ann. § 14-11014 | |
| Arkansas | Ark. Code Ann. § 28-70-104 A | | | |
| California | Cal. Prob. Code § 16336 | Cal. Prob. Code § § 16337–16338 | Cal. Prob. Code § § 16336.4–16336.8 | Cal. Prob. Code § 16328 |
| Colorado | Colo. Rev. Stat. § 15-1-404 | Colo. Rev. Stat. § 15-1-405 | Colo. Rev. Stat. § 15-1-404.5 | Colo. Rev. Stat. § 15-1-404.5(14) |
| Connecticut | Conn. Gen. Stat. § 45a-542c | | | |
| Delaware | Del. Code Ann. tit. 12, § 61-104 | Del. Code Ann. tit. 12, § 61-105 | Del. Code Ann. tit. 12, § 61-106 | Del. Code Ann. tit. 12, § 61-107 |
| District of Columbia | D.C. Code Ann. § 28-4801.04 | | | |
| Florida | Fla. Stat. § 738.104 | Fla. Stat. § 738.105 | Fla. Stat. § 738.1041 | Fla. Stat. § 738.1041(10) |
| Georgia | Ga. Code Ann. § 53-12-361 | Ga. Code Ann. § 53-12-363 | Ga. Code Ann. § 53-12-362 | Ga. Code Ann. § 53-12-364 |
| Hawaii | Haw. Rev. Stat. § 557A-104 | Haw. Rev. Stat. § § 557A-105–557A-106 | | |
| Idaho | Idaho Code § 68-10-104 | Idaho Code § 68-10-105 | | |
| Illinois | | | 760 ILCS5/5.3 | 760 ILCS 5/5.3(m) |
| Indiana | Ind. Code Ann. § 30-2-14-15 | Ind. Code Ann. § § 30-2-14-16–30-2-14-17 | Ind. Code Ann. § § 30-2-15-1–30-2-15-26 | |
| Iowa | | | Iowa Code Ann. § § 637.601–637.615 | |
| Kansas | Kan. Stat. Ann. § 58-9-104 | | Kan. Stat. Ann. § 58-9-105 | |
| Kentucky | Ky. Rev. Stat. Ann. § 386.454 | | Ky. Rev. Stat. Ann § § | Ky. Rev. Stat. Ann. § § 386.450(15), |

| | | | | |
|---|---|---|---|---|
| | | | 386.450(15), 386.454(2) | 386.454 |
| Louisiana | La. Rev. Stat. Ann. § 9:2158–2162 | La. Rev. Stat. Ann. § 9:2163 | La. Rev. Stat. Ann. § 9:2068 | |
| Maine | Me. Rev. Stat. Ann. tit. 18-C, § 7-404 | Me. Rev. Stat. Ann. tit. 18-C, § 7-406 | Me. Rev. Stat. Ann. tit. 18-C, § 7-405 | |
| Maryland | Md. Code Ann., Est. & Trusts § 15-502.2 | Md. Code Ann., Est. & Trusts § 15-502.3 | Md. Code Ann., Est. & Trusts § 15-502.1 | |
| Massachusetts | Mass. Gen. L. ch. 203D, § 4 | Mass. Gen. L. ch. 203D, § 5 | | |
| Michigan | Mich. Comp. Laws § 555.504 | Mich. Comp. Laws § 555.505 | | |
| Minnesota | Minn. Stat. § 501C.1112 | Minn. Stat. § 501C.1112, Subd. 7 | | |
| Mississippi | Miss. Code Ann. § 91-17-104 | Miss. Code Ann. § 91-17-105 | | |
| Missouri | Mo. Ann. Stat. § 469.405 | Mo. Ann. Stat. § 469.409 | Mo. Ann. Stat. § 469.411 | Mo. Ann. Stat. § 469.411(5)(1) |
| Montana | Mont. Code Ann. § 72-34-424 | Mont. Code Ann. § § 72-34-424(8), 72-34-425, 72-34-426 | | |
| Nebraska | Neb. Rev. Stat. § 30-3119 | Neb. Rev. Stat. § § 30-3120–30-3121 | Neb. Rev. Stat. § 30-3119.01 | |
| Nevada | Nev. Rev. Stat. § § 164.795, 164.725 | Nev. Rev. Stat. § 164.725 | Nev. Rev. Stat. § § 164.796–164.799, 164.700(3), 164.725 | |
| New Hampshire | N.H. Rev. Stat. Ann. § 564-C:1-104 | N.H. Rev. Stat. Ann. § § 564-C:1-104(h), 564-C:1-105 | N.H. Rev. Stat. Ann. § 564-C:1-106 | |
| New Jersey | N.J. Rev. Stat. § 3B:19B-4 | N.J. Rev. Stat. § 3B:19B-31 | | |
| New Mexico | N.M. Stat. Ann. § 46-3A-104 | | N.M. Stat. Ann. § § 46-3A-105–46-3A-113 | |
| New York | N.Y. Est. Powers & Trusts Law § 11-2.3(b)(5) | N.Y. Est. Powers & Trusts Law § 11-2.3-A | N.Y. Est. Powers & Trusts Law § 11-2.4 | N.Y. Est. Powers & Trusts Law § 11-2.4(e)(1)(A) |
| North Carolina | N.C. Gen. Stat. § 37A-1-104 | N.C. Gen. Stat. § 37A-1-105 | N.C. Gen. Stat. § § 37A-1-104.1–37A-1-104.9 | N.C. Gen. Stat. § § 37A-1-104.21–37A-1-104.26 |
| North Dakota | N.D. Cent. Code § 59-04.2-03 | N.D. Cent. Code § 59-04.2-03.1 | N.D. Cent. Code § § 59-16.3-0159-16.3-14 | N.D. Cent. Code § 59-16.3-01(8) |
| Ohio | Ohio Rev. Code Ann. § 5812.03 | Ohio Rev. Code Ann. § 5812.03(G) | | |
| Oklahoma | Okla. Stat. Ann. tit. 60, § 175.104 | | | |

| | | | | |
|---|---|---|---|---|
| Oregon | Or. Rev. Stat. § 129.215 | Or. Rev. Stat. § 129.220 | Or. Rev. Stat. § 129.225 | |
| Pennsylvania | 20 Pa. Cons. Stat. § 8104 20 | Pa. Cons. Stat. § 8106 | 20 Pa. Cons. Stat. § 8105 20 | Pa. Cons. Stat. § 8107 |
| Rhode Island | R.I. Gen. Laws § 18-4-28 | | R.I. Gen. Laws § 18-4-29 | R.I. Gen. Laws § 18-4-29(a) |
| South Carolina | S.C. Code Ann. § 62-7-904 | S.C. Code Ann. § 62-7-904A | S.C. Code Ann. § § 62-7-904B62-7-904I | S.C. Code Ann. § § 62-7-904B(3), 62-7-904I64-7-904P |
| South Dakota | S.D. Codified Laws § 55-13A-104 | S.D. Codified Laws § 55-13A-105 | S.D. Codified Laws § § 55-15-1–55-15-15 | S.D. Codified Laws § 55-15-1(7A) |
| Tennessee | Tenn. Code Ann. § 35-6-104 | Tenn. Code Ann. § § 35-6-104(g), 35-6-106 | Tenn. Code Ann. § 35-6-108 | Tenn. Code Ann. § 35-6-109 |
| Texas | Tex. Prop. Code Ann. § 116.005 | Tex. Prop. Code Ann. § 116.006 | | Tex. Prop. Code Ann. § 116.007 |
| Utah | Utah Code Ann. § 22-3-104 | Utah Code Ann. § § 22-3-105–22-3-107 | Utah Code Ann. § § 22-7-101–22-7-118 | Utah Code Ann. § 22-7-106 |
| Vermont | Vt. Stat. Ann. tit. 14, § 3324 | Vt. Stat. Ann. tit. 14, § 3325 | Vt. Stat. Ann. tit. 14A, § 907 | Vt. Stat. Ann. tit. 14A, § 908 |
| Virginia | Va. Code Ann. § 64.2-1002 | | Va. Code Ann. § 64.2-1003 | Va. Code Ann. § 64.2-1003 |
| Washington | Wash. Rev. Code § 11.104A.020 | Wash. Rev. Code § 11.104A.030 | Wash. Rev. Code § 11.104A.040 | Wash. Rev. Code § 11.104A.040(a)(2) |
| West Virginia | W. Va. Code § 44B-1-104 | W. Va. Code § 44B-1-105 | W. Va. Code § 44B-1-104a | W. Va. Code § 44B-1-104a(m) |
| Wisconsin | Wis. Stat. § 701.1104 | Wis. Stat. § § 701.1105, 701.1109 | Wis. Stat. § § 701.1106, 701.1109 | Wis. Stat. § 701.1107 |
| Wyoming | Wyo. Stat. Ann. § 2-3-804 | Wyo. Stat. Ann. § 2-3-832 | Wyo. Stat. Ann. § § 2-3-901–2-3-917 | Wyo. Stat. Ann. § § 2-3-906, 2-3-9082-3-909 |

*Note:* The text of the Uniform Principal and Income Act ("UPAIA") is available at www.uniformlaws.org/shared/docs/principal%20and%20income/rupia00.pdf. To determine which jurisdictions have enacted the UPAIA, go to www.uniformlaws.org/LegislativeFactSheet.aspx?title=Principal and Income Act (2000).

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## Worksheet 11 State Liability Systems Ranking*

**(As of September 2018)**

| State | Ranking | | States in Order of Ranking | Ranking | Score |
|---|---|---|---|---|---|
| Alabama | 43 | | South Dakota | 1 | 75.3 |
| Alaska | 6 | | Vermont | 2 | 75.2 |
| Arizona | 25 | | Idaho | 3 | 75.0 |
| Arkansas | 36 | | Minnesota | 4 | 74.2 |
| California | 47 | | New Hampshire | 5 | 73.9 |
| Colorado | 35 | | Alaska | 6 | 73.8 |
| Connecticut | 16 | | Nebraska | 7 | 73.5 |
| Delaware | 11 | | Wyoming | 8 | 73.3 |
| Florida | 46 | | Maine | 9 | 73.2 |
| Georgia | 40 | | Virginia | 10 | 72.8 |
| Hawaii | 23 | | Delaware | 11 | 72.8 |
| Idaho | 3 | | Utah | 12 | 72.8 |
| Illinois | 48 | | Iowa | 13 | 72.6 |
| Indiana | 15 | | Massachusetts | 14 | 72.1 |
| Iowa | 13 | | Indiana | 15 | 71.9 |
| Kansas | 18 | | Connecticut | 16 | 71.8 |
| Kentucky | 42 | | North Dakota | 17 | 71.5 |
| Louisiana | 50 | | Kansas | 18 | 71.5 |
| Maine | 9 | | Maryland | 19 | 70.8 |
| Maryland | 19 | | Wisconsin | 20 | 70.7 |
| Massachusetts | 14 | | Oregon | 21 | 70.4 |
| Michigan | 22 | | Michigan | 22 | 70.4 |
| Minnesota | 4 | | Hawaii | 23 | 70.0 |
| Mississippi | 44 | | Rhode Island | 24 | 69.9 |
| Missouri | 49 | | Arizona | 25 | 69.8 |
| Montana | 27 | | Ohio | 26 | 68.7 |
| Nebraska | 7 | | Montana | 27 | 68.7 |
| Nevada | 37 | | Washington | 28 | 68.4 |
| New Hampshire | 5 | | New York | 29 | 68.4 |
| New Jersey | 41 | | Tennessee | 30 | 68.3 |
| New Mexico | 32 | | Oklahoma | 31 | 68.3 |
| New York | 29 | | New Mexico | 32 | 68.2 |
| North Carolina | 33 | | North Carolina | 33 | 68.2 |
| North Dakota | 17 | | South Carolina | 34 | 67.7 |
| Ohio | 26 | | Colorado | 35 | 67.6 |
| Oklahoma | 31 | | Arkansas | 36 | 67.2 |
| Oregon | 21 | | Nevada | 37 | 66.6 |
| Pennsylvania | 38 | | Pennsylvania | 38 | 66.3 |

| | | | | | |
|---|---|---|---|---|---|
| Rhode Island | 24 | | Texas | 39 | 64.3 |

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| State | Ranking | | States in Order of Ranking | Ranking | Score |
|---|---|---|---|---|---|
| South Carolina | 34 | | Georgia | 40 | 64.1 |
| South Dakota | 1 | | New Jersey | 41 | 63.8 |
| Tennessee | 30 | | Kentucky | 42 | 61.7 |
| Texas | 39 | | Alabama | 43 | 61.1 |
| Utah | 12 | | Mississippi | 44 | 61.1 |
| Vermont | 2 | | West Virginia | 45 | 60.6 |
| Virginia | 10 | | Florida | 46 | 60.5 |
| Washington | 28 | | California | 47 | 60.0 |
| West Virginia | 45 | | Illinois | 48 | 59.1 |
| Wisconsin | 20 | | Missouri | 49 | 58.1 |
| Wyoming | 8 | | Louisiana | 50 | 56.6 |

*Note:* The data in the above table is taken from the 2017 Lawsuit Climate Survey: Ranking the States, dated September 12, 2017, conducted by Harris Poll, for the U.S. Chamber Institute for Legal Reform. The study was based on interviews with 1,321 in-house general counsel, senior litigators or attorneys, and other senior executives knowledgeable about litigation matters at public and private companies with annual revenues of at least $100 million from March 31, 2017–June 26, 2017, www.instituteforlegalreform.com/states.

## Worksheet 12 State Noncharitable Purpose Trust Statutes*

**(As of September 2018)**

| State | Citation |
|---|---|
| **Permits Perpetual Trusts (8)** | |
| Delaware[1] | Del. Code Ann. tit. 12, § § 3556, 3303(b), 3541; Del. Code Ann. tit. 25, § 503(a) |
| Idaho | Idaho Code § § 15-7-601, 55-111 |
| Kentucky[1] | Ky. Rev. Stat. Ann. § § 386B.4-090, 381.260, 381.224381.226 |
| Maine | Me. Rev. Stat. Ann. tit. 18-B, § 409; 33, § 101-A |
| New Hampshire | N.H. Rev. Stat. Ann. § § 564-B:4-409, 564-B:4-402A, 547:3-k, 564:24 |
| South Dakota[1] | S.D. Codified Laws § 55-1-20 |
| Wisconsin | Wis. Stat. § § 701.0409, 700.16 |
| | |
| **Permits Trusts of Limited Duration—Based on § 2-907(a) of Uniform Probate Code (6)** | |
| Alaska | Alaska Stat. § 13.12.907(a) (21 years) |
| Arizona[2] | Ariz. Rev. Stat. Ann. § 14-2907(A) (90 years) |
| Colorado | Colo. Rev. Stat. § 15-11-901(1) (21 years) |
| Iowa | Iowa Code Ann. § 633A.2105(1) (21 years) |
| Michigan | Mich. Comp. Laws § 700.2722(1) (21 years) |
| Montana[2] | Mont. Code Ann. § 72-2-1017(1) (21 years) |
| | |
| **Permits Trusts of Limited Duration—Based on § 409 of Uniform Trust Code (26)** | |
| Alabama | Ala. Code § 19-3B-409 (21 years) |
| Arizona | Ariz. Rev. Stat. Ann. § 14-10409 (90 years) |
| Arkansas | Ark. Code Ann. § 28-73-409 (21 years) |
| District of Columbia | D.C. Code Ann. § 19-1304.09 (21 years) |
| Florida | Fla. Stat. § § 736.0409, 736.04113 (21 years) |
| Kansas | Kan. Stat. Ann. § 58a-409 (21 years) |
| Maryland | Md. Code Ann., Est. & Trusts § 14.5-408 (21 years) |
| Massachusetts | Mass. Gen. L.ch. 203E, § 409 (USRAP Period—21 years after death of last individual living when trust became irrevocable, 90 years, or shorter of such periods) |
| Minnesota | Minn. Stat. § 501C.0409 (21 years) |
| Mississippi | Miss. Code Ann. § 91-8-409 (21 years) |
| Missouri | Mo. Ann. Stat. § 456.4-409 (21 years) |
| Montana[3] | Mont. Code Ann. § 72-38-409 (21 years) |
| Nebraska | Neb. Rev. Stat. § 30-3835 (21 years) |
| New Mexico | N.M. Stat. Ann. § 46A-4-409 (21 years) |
| North Carolina | N.C. Gen. Stat. § 36C-4-409 (21 years) |
| North Dakota | N.D. Cent. Code § § 59-12-09, 47-02-27.1, 47-02-27.4 (USRAP period—21 years after death of last individual living when |

| | |
|---|---|
| | trust became irrevocable, 90 years, or shorter of such periods) |
| Ohio | Ohio Rev. Code Ann. § 5804.09 (21 years) |
| Oregon | Or. Rev. Stat. § 130.190 (90 years) |
| Pennsylvania | 20 Pa. Cons. Stat. § 7739 (21 years) |
| South Carolina | S.C. Code Ann. § § 62-7-409, 27-6-20 (USRAP period—21 years after death of last individual living when trust became irrevocable, 90 years, or shorter of such periods) |
| Tennessee | Tenn. Code Ann. § 35-15-409 (90 years) |
| Utah | Utah Code Ann. § § 75-7-409, 75-2-1001(1) (21 years) |
| Vermont | Vt. Stat. Ann. tit. 14A, § 409 (21 years) |
| Virginia | Va. Code Ann. § 64.2-727 (21 years) |
| West Virginia | W. Va. Code § § 44D-44-409, 36-1A-1(a)(2) (USRAP Period—21 years after death of last individual living when trust became irrevocable or 90 years) |
| Wyoming[1] | Wyo. Stat. § § 4-10-410, 34-1-13834-1-139 (1,000 years) |
| | |

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| State | Citation |
|---|---|
| **Permits Trusts of Limited Duration—Other (4)** | |
| California | Cal. Prob. Code § § 15211, 15204 (21 Years) |
| Indiana | Ind. Code Ann. § 30-4-2-19 (21 years) |
| Nevada | Nev. Rev. Stat. § § 163.5505, 163.006 (365 years) |
| Washington | Wash. Rev. Code § § 11.98.015, 11.98.130 (150 years) |
| | |
| **Has No Relevant Statute (9)** | |
| Connecticut | |
| Georgia | |
| Hawaii | |
| Illinois | |
| Louisiana | |
| New York | |
| Oklahoma | |
| Rhode Island | |
| Texas | |

*Note*: This chart does not include citations to statutes that deal specifically with burial lots or animals.

[1] Has abolished or does not follow any common-law rule limiting the duration of noncharitable purpose trusts.

[2] Also has version of § 409 of Uniform Trust Code.

[3] Also has version of § 2-907(a) of Uniform Probate Code.

## Worksheet 13 State Decanting Statutes*

**(As of September 2018)**

| State | Citation | Year |
|---|---|---|
| Alabama[1] | Ala. Code § § 19-3D-1–19-3D-29 | 2019 |
| Alaska | Alaska Stat. § § 13.36.15713.36.159, 13.36.215 | 1998 |
| Arizona | Ariz. Rev. Stat. § 14-10819 | 2009 |
| California[1] | Cal. Prob. Code § § 19501–19530 | 2019 |
| Colorado[1] | Colo. Rev. Stat. § § 15-16-90115-16-931 | 2016 |
| Connecticut | Conn. Gen. Stat. § 45a-572 | 1976 |
| Delaware | Del. Code Ann. tit. 12, § 3528 | 2003 |
| Florida | Fla. Stat. § 736.04117 | 2007 |
| Georgia | Ga. Code Ann. § 53-12-62 | 2018 |
| Illinois | 760 ILCS 5/16.4 | 2013 |
| Indiana | Ind. Code Ann. § 30-4-3-36 | 2010 |
| Kentucky | Ky. Rev. Stat. Ann. § 386.175 | 2012 |
| Michigan | Mich. Comp. Laws § § 556.115a, 700.7103, 700.7820a | 2012 |
| Minnesota | Minn. Stat. Ann. § 502.851 | 2016 |
| Missouri | Mo. Ann. Stat. § 456.4-419 | 2011 |
| Nevada | Nev. Rev. Stat. § 163.556 | 2009 |
| New Hampshire | N.H. Rev. Stat. Ann. § 564-B:4-418 | 2008 |
| New Mexico[1] | N.M. Stat. Ann. § § 46-12-10146-12-129 | 2017 |
| New York | N.Y. Est. Powers & Trusts Law § 10-6.6 | 1992 |
| North Carolina[1] | N.C. Gen. Stat. § § 36C-8B-1–36C-8B-26 | 2017 |
| North Dakota | N.D. Cent. Code § § 59-16.1-0159-16.1-17 | 2017 |
| Ohio | Ohio Rev. Code Ann. § 5808.18 | 2012 |
| Rhode Island | R.I. Gen. Laws § 18-4-31 | 2012 |
| South Carolina | S.C. Code Ann. § 62-7-816A | 2014 |
| South Dakota | S.D. Codified Laws § § 55-2-1555-2-21 | 2007 |
| Tennessee | Tenn. Code Ann. § 35-15-816 | 2004 |
| Texas | Tex. Prop. Code § § 112.071112.087 | 2013 |
| Virginia[1] | Va. Code Ann. § § 64.2-779.164.2-779.25 | 2012 |
| Washington[1] | Wash. Rev. Code § § 11.107.010–11.107.080 | 2017 |
| Wisconsin | Wis. Stat. § 701.0418 | 2014 |
| Wyoming | Wyo. Stat. § 4-10-816(a)(xxviii) | |

*Note:* The text of the Uniform Trust Decanting Act ("UTDA") may be viewed at www.uniformlaws.org/shared/docs/trustdecanting/UTDA_Final%20Act_2018may17.pdf. To determine which jurisdictions have adopted the UDTA, go to www.uniformlaws.org/LegislativeFactSheet.aspx?title=Trust Decanting.

[1] Has enacted the Uniform Trust Decanting Act.

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## Worksheet 14 State Lifetime Validation of Trust and No-Contest Clause Statutes*

**(As of September 2018)**

**Lifetime Validation of Trust Statutes**

| State | Statute | |
|---|---|---|
| Alaska | Alaska Stat. § § 13.12.535–13.12.590 | |
| California | Cal. Prob. Code § 16061.8 | |
| Delaware | Del. Code Ann. tit. 12, § 3546 | |
| Nevada | Nev. Rev. Stat. § 164.021 | |
| New Hampshire | N.H. Rev. Stat. Ann. § 564-B:4-406 | |
| North Dakota | N.D. Cent. Code § § 59-10.1-01–59-10.1-05 | |
| South Dakota | S.D. Codified Laws § 55-4-57 | |
| Wyoming | Wyo. Stat. § 4-10-604 | |

**No-Contest Clause Statutes**

| State | Will | Trust |
|---|---|---|
| **Enforceable Without Exception** | | |
| Alaska | — | Alaska Stat. § 13.36.330 |
| Massachusetts | Mass. Gen. L. ch. 190B, § 2-517 | — |
| | | |
| **Enforceable With Exception** | | |
| Alaska | Alaska Stat. § 13.16.555 | — |
| Arizona | Ariz. Rev. Stat. Ann. § 14-2517 | — |
| California | Cal. Prob. Code § § 21310–21315 | Cal. Prob. Code § § 21310–21315 |
| Colorado | Colo. Rev. Stat. § 15-12-905, 15-11-517 | — |
| Delaware | Del. Code Ann. tit. 12, § 3329 | Del. Code Ann. tit. 12, § 3329 |
| Georgia | Ga. Code Ann. § 53-4-68 | Ga. Code Ann. § 53-12-22 |
| Hawaii | Haw. Rev. Stat. § § 560:3-905, 560:2-517 | Haw. Rev. Stat. § 560:3-905 |
| Idaho | Idaho Code § 15-3-905 | — |
| Maine | Me. Rev. Stat. Ann. tit. 18-C, § 3-905 | — |
| Maryland | Md. Code Ann., Est. & Trusts § 4-413 | — |
| Michigan | Mich. Comp Laws § § 700.2518, 700.3905 | Mich. Comp. Laws 700.7113 |
| Minnesota | Minn. Stat. § 524.2-517 | — |
| Mississippi | Miss. Code Ann. § 91-8-1014 | Miss. Code Ann. § § 91-8-1014, 91-8-103(31) |
| Missouri | Mo. Ann. Stat. § 474.395 | Mo. Ann. Stat. § 456.4-420, 456.1-103(29) |

| | | |
|---|---|---|
| Montana | Mont. Code Ann. § 72-2-537 | — |
| Nebraska | Neb. Rev. Stat. § 30-24,103 | — |
| Nevada | Nev. Rev. Stat. § 137.005 | Nev. Rev. Stat. § 163.00195 |
| New Hampshire | N.H. Rev. Stat. Ann. § 551:22 | N.H. Rev. Stat. Ann. § § 564-B:10-1014, 564-B:1-105 |
| New Jersey | N.J. Rev. Stat. § 3B:3-47 | — |
| New Mexico | N.M. Stat. Ann. § 45-2-517 | — |
| New York | N.Y. Est. Powers & Trusts Law § 3-3. 5 | — |
| North Dakota | N.D. Cent. Code § 30.1-20-05 | — |
| Oregon | Or. Rev. Stat. § 112.272 | Or. Rev. Stat. § 130.235 |
| Pennsylvania | 20 Pa. Cons. Stat. § 2521 20 | Pa. Cons. Stat. § 2521 |
| South Carolina | S.C. Code Ann. § 62-3-905 | S.C. Code Ann. § 62-7-605 |
| South Dakota | S.D. Codified Laws § § 29A-2-517, 29A-3-905 | S.D. Codified Laws § § 55-1-46–55-1-51 |

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| State | Will | Trust |
|---|---|---|
| **Enforceable Without Exception (cont'd)** | | |
| Tennessee | Tenn. Code Ann. § 35-15-1014 | Tenn. Code Ann. § § 35-15-1014, 35-15-103 (36) |
| Texas | Tex. Est. Code § 254.005 | Tex. Prop. Code § § 112.038, 111.0035 |
| Utah | Utah Code Ann. § § 75-3-905, 75-2-515 | — |
| Wisconsin | Wis. Stat. § 854.19 | — |
| | | |
| **Never Enforceable** | | |
| Florida | Fla. Stat. § § 732.517–732.518 | Fla. Stat. § § 736.0207, 736.1108 |
| Indiana | Ind. Code Ann. § 29-1-6-2 | Ind. Code Ann. § 30-4-2.1-3 |

## Worksheet 15 State Uniform Trust Code Successor Trustee Statutes*

**(As of September 2018**

| State | UTC § 107 | UTC § 108 | UTC § 111 | UTC § 202 | UTC § 411 |
|---|---|---|---|---|---|
| | **Governing Law** | **Principal Place of Administration** | **Nonjudicial Settlement Agreement** | **Jurisdiction Over Trustee and Beneficiary** | **Modification or Termination of Noncharitable Irrevocable Trust by Consent** |
| Alabama | Ala. Code § 19-3B-107 | Ala. Code § 19-3B-108 | Ala. Code § 19-3B-111 | Ala. Code § 19-3B-202 | Ala. Code § 19-3B-411 |
| Arizona | Ariz. Rev. Stat. Ann. § 14-10107 | Ariz. Rev. Stat. Ann. § 14-10108 | Ariz. Rev. Stat. Ann. § 14-10111 | Ariz. Rev. Stat. Ann. § 14-10202 | Ariz. Rev. Stat. Ann. § 14-10411 |
| Arkansas | Ark. Code Ann. § 28-73-107 | Ark. Code Ann. § 28-73-108 | Ark. Code Ann. § 28-73-111 | Ark. Code Ann. § 28-73-202 | Ark. Code Ann. § 28-73-411 |
| Colorado | Colo. Rev. Stat. § 15-5-107 | Colo. Rev. Stat. 15-5-108 | Colo. Rev. Stat. § 15-5-111 | Colo. Rev. Stat. § 15-5-202 | Colo. Rev. Stat. § 15-5-411 |
| District of Columbia | D.C. Code Ann. § 19-1301.07 | D.C. Code Ann. § 19-1301.08 | D.C. Code Ann. § 19-1301.11 | D.C. Code Ann. § 19-1302.02 | D.C. Code Ann. § 19-1304.11 |
| Florida | Fla. Stat. § 736.0107 | Fla. Stat. § 736.0108 | Fla. Stat. § 736.0111 | Fla. Stat. § 736.0202 | |
| Kansas | Kan. Stat. Ann. § 58a-107 | Kan. Stat. Ann. § 58a-108 | Kan. Stat. Ann. § 58a-111 | Kan. Stat. Ann. § 58a-202 | Kan. Stat. Ann. § 58a-411 |
| Kentucky | Ky. Rev. Stat. Ann. § 386B.1-050 | Ky. Rev. Stat. § 386B.1-060 | Ky. Rev. Stat. § 386B.1-090 | Ky. Rev. Stat. § 386B.2-020 | Ky. Rev. Stat. § 386B.4-110 |
| Maine | Me. Rev. Stat. Ann. tit. 18-B, § 107 | Me. Rev. Stat. Ann. tit. 18-B, § 108 | Me. Rev. Stat. Ann. tit. 18-B, § 111 | Me. Rev. Stat. Ann. tit. 18-B, § 202 | Me. Rev. Stat. Ann. tit. 18-B, § 411 |
| Maryland | Md. Code Ann., Est. & Trusts § 14.5-107 | Md. Code Ann., Est. & Trusts § 14.5-108 | Md. Code Ann., Est. & Trusts § 14.5-111 | Md. Code Ann. Est. & Trusts § 14.5-202 | Md. Code Ann., Est. & Trusts § 14.5-410 |
| Massachusetts | Mass. Gen. L. ch. 203E, § 107 | Mass. Gen. L. ch. 203E, § 108[1] | Mass. Gen. L. ch. 203E, | Mass. Gen. L. ch. 203E, § 202 | Mass. Gen. L. ch. 203E, § 411 |

| | | | | | |
|---|---|---|---|---|---|
| | (reserved) | | § 111 | | |
| Michigan | Mich. Comp. Laws § 700.7107 | Mich. Comp. Laws § 700.7108 | Mich. Comp. Laws § 700.7111 | Mich. Comp. Laws § 700.7202 | Mich. Comp. Laws § 700.7411 |
| Minnesota | Minn. Stat. § 501C.0107 | Minn. Stat. § 501C.0108 | Minn. Stat. § 501C.0111 | Minn. Stat. § 501C.0206 | Minn. Stat. § 501C.0411 |
| Mississippi | Miss. Code Ann. § 91-8-107 | Miss. Code Ann. § 91-8-108 | Miss. Code Ann. § 91-8-111 | Miss. Code Ann. § 91-8-202 | Miss. Code Ann. § 91-8-411 |
| Missouri | Mo. Ann. Stat. § 456.1-107 | Mo. Ann. Stat. § 456.1-1081 | Mo. Ann. Stat. § 456.1-111 | Mo. Ann. Stat. § 456.2-202 | Mo. Ann. Stat. § 456.4-411A |
| Montana | Mont. Code Ann. § 72-38-107 | Mont. Code Ann. § 72-38-108 | Mont. Code Ann. § 72-38-111 | Mont. Code Ann. § 72-38-203 | Mont. Code Ann. § 72-38-411 |

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| **State** | **UTC § 107** | **UTC § 108** | **UTC § 111** | **UTC § 202** | **UTC § 411** |
|---|---|---|---|---|---|
| | **Governing Law** | **Principal Place of Administration** | **Nonjudicial Settlement Agreement** | **Jurisdiction Over Trustee and Beneficiary** | **Modification or Termination of Noncharitable Irrevocable Trust by Consent** |
| Nebraska | Neb. Rev. Stat. § 30-3807 | Neb. Rev. Stat. § 30-3808 | Neb. Rev. Stat. § 30-3811 | Neb. Rev. Stat. § 30-3813 | Neb. Rev. Stat. § 30-3837 |
| New Hampshire | N.H. Rev. Stat. Ann. § 564-B:l-107 | N.H. Rev. Stat. Ann. § 564-B:l-108 | N.H. Rev. Stat. Ann. § 564-B:l-111 | N.H. Rev. Stat. Ann. § 564-B:2-202 | N.H. Rev. Stat. Ann. § 564-B:4-411 |
| New Jersey | N.J. Rev. Stat. § 3B:31-7 | N.J. Rev. Stat. § 3B:31-8 | N.J. Rev. Stat. § 3B:31-11 | | N.J. Rev. Stat. § 3B:31-27 |
| New Mexico | N.M. Stat. Ann. § 46A-1-107 | N.M. Stat. Ann. § 46A-1-108 | N.M. Stat. Ann. § 46A-1-111 | N.M. Stat. Ann. § 46A-2-202 | N.M. Stat. Ann. § 46A-4-411 |
| North Carolina | N.C. Gen. Stat. § 36C-1-107 | N.C. Gen. Stat. § 36C-1-1081 | N.C. Gen. Stat. § 36C-1-111 | N.C. Gen. Stat. § 36C-2-202 | N.C. Gen. Stat. § 36C-4-411 |
| North Dakota | N.D. Cent. Code § 59-09-07 | N.D. Cent. Code § 59-09-08 | N.D. Cent. Code § 59-09-11 | N.D. Cent. Code § 59-10-02 | N.D. Cent. Code § 59-12-11 |
| Ohio | Ohio Rev. Code Ann. § 5801.06 | Ohio Rev. Code Ann. § 5801.07 | Ohio Rev. Code Ann. § 5801.10 | Ohio Rev. Code Ann. § 5802.02 | Ohio Rev. Code Ann. § 5804.11 |
| Oregon | Or. Rev. Stat. § 130.030 | Or. Rev. Stat. § 130.022 | Or. Rev. Stat. § 130.045 | Or. Rev. Stat. § 130.055 | Or. Rev. Stat. § 130.200 |
| Pennsylvania | 20 Pa. Cons. Stat. § 7707 | 20 Pa. Cons. Stat. § 7708[1] | 20 Pa. Cons. Stat. § 7710.1 | 20 Pa. Cons. Stat. § 7712 20 | Pa. Cons. Stat. § 7740.1 |
| South | S.C. Code Ann. § | S.C. Code Ann. § | S.C. Code Ann. § | S.C. Code Ann. § | S.C. Code Ann. § |

| | | | | | |
|---|---|---|---|---|---|
| Carolina | 62-7-107 | 62-7-108 | 62-7-111 | 62-7-202 | 62-7-411 |
| Tennessee | Tenn. Code Ann. § 35-15-107 | Tenn. Code Ann. § 35-15-108 | Tenn. Code Ann. § 35-15-111 | Tenn. Code Ann. § 35-15-202 | Tenn. Code Ann. § 35-15-411 |
| Utah | Utah Code Ann. § 75-7-107 | Utah Code Ann. § 75-7-108 | Utah Code Ann. § 75-7-110 | Utah Code Ann. § 75-7-202 | Utah Code Ann. § 75-7-411 |
| Vermont | Vt. Stat. Ann. tit. 14A, § 107 | Vt. Stat. Ann. tit. 14A, § 108 | Vt. Stat. Ann. tit. 14A, § 111 | Vt. Stat. Ann. tit. 14A, § 202 | Vt. Stat. Ann. tit. 14A, § 411 |
| Virginia | Va. Code Ann. § 64.2-705 | Va. Code Ann. § 64.2-706[1] | Va. Code Ann. § 64.2-709 | Va. Code Ann. § 64.2-711 | Va. Code Ann. § 64.2-729 |
| West Virginia | W. Va. Code § 44D-1-107 | W. Va. Code § 44D-1-108[1] | W. Va. Code § 44D-1-111 | W. Va. Code § 44D-2-202 | W. Va. Code § 44D-4-411 |
| Wisconsin | Wis. Stat. § 701.0107 | Wis. Stat. § 701.0108[1] | Wis. Stat. § 701.0111 | Wis. Stat. § 701.0202 | Wis. Stat. § 701.0411 |
| Wyoming | Wyo. Stat. § 4-10-107 | Wyo. Stat. § 4-10-108 | Wyo. Stat. § 4-10-111 | Wyo. Stat. § 4-10-202 | Wyo. Stat. § 4-10-412 |

*Note*: The text of the Uniform Trust Code ("UTC") is available at www.uniformlaws.org/shared/docs/trust_code/UTC_Final_2018may17.pdf. To determine which states have enacted the UTC, go to www.uniformlaws.org/LegislativeFactSheet.aspx?title=Trust Code.

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[1] Does not have § 108(b) of Uniform Trust Code requiring trustee to administer trust in appropriate

Estates, Gifts and Trusts Portfolios
Trusts
Portfolio 867-2nd: Choosing a Domestic Jurisdiction for a Long-Term Trust
Working Papers

## Worksheet 16 Generation-Skipping Trust Agreement*

**(As of September 2018)**

**NOT A VALID TRUST AGREEMENT**
**SAMPLE GENERATION-SKIPPING TRUST AGREEMENT**

***[Intended to Use Trustor's GST Exemption*]**

THIS AGREEMENT, made this _____ day of _____, 20_____, between [TRUSTOR'S NAME], of _____ County, State of _____, hereafter called "Trustor," and WILMINGTON TRUST COMPANY, a Delaware trust company, hereafter called "Trustee," WITNESSETH:

WHEREAS, Trustor desires to establish a trust of the property described in the attached "Schedule" and other property which may be added from time to time, all of which is hereafter called the "trust fund"; and

WHEREAS, Trustee accepts such trust and agrees to administer it in accordance with the terms and conditions of this agreement;

NOW, THEREFORE, Trustor hereby gives Trustee the property described in "Schedule A," in trust, for the following purposes:

**SECTION 1: DISTRIBUTION.**

A. Until Death of Trustor. Until Trustor's death, Trustee shall hold the trust fund in further trust, and, subject to Subsection F of this Section 1, Trustee may, from time to time, distribute to such of Trustor's issue as shall be living from time to time all, some, or none of the net income and/or principal in such amounts and proportions (whether equally or unequally, and even to the exclusion of one or more beneficiaries) as Trustee, in its sole discretion, deems appropriate, after taking account of all other sources of funds available to them. Trustee shall accumulate any net income not so distributed and add it to principal at least annually, to be disposed of as a part of it. No such distribution shall be deemed to be an advancement, and no such distribution shall be made that would discharge anyone's legal obligation to support any of such issue.

B. On Death of Trustor. On Trustor's death, Trustee shall divide the assets then held hereunder into shares for Trustor's then living issue, per stirpes, and administer and distribute such shares according to the provisions of Subsection C of this Section 1.

C. Shares Held for Issue. Trustee shall hold each share set aside for an issue of Trustor in further trust for such issue, referred to hereafter in this Subsection C as the "beneficiary."

(1) During the Beneficiary's Life. During the beneficiary's life and subject to Subsection F of this Section 1, Trustee may, from time to time, distribute to the beneficiary and his or her issue all, some, or none of the net income and/or principal in such amounts and proportions (whether equally or unequally, and even to the exclusion of one or more beneficiaries) as Trustee, in its sole discretion, deems appropriate, after taking account of all other sources of funds available to them. Trustee shall accumulate

any net income not so distributed and add it to principal at least annually, to be disposed of as a part of it. No such distribution shall be deemed to be an advancement, and no such distribution shall be made that would discharge the beneficiary's legal obligation to support any of such issue.

(2) On the Death of the Beneficiary. On the death of the beneficiary, Trustee shall distribute so much of the beneficiary's share as is then held hereunder, free from this trust, to such of Trustor's issue (other than the beneficiary) and the spouses of such issue (including the beneficiary's spouse), in such manner and amounts, and on such terms, whether in trust or otherwise, as is effectively appointed by specific reference hereto in the last written instrument which the beneficiary executes and delivers to Trustee during his or her lifetime or, failing any such instrument, in his or her Will. However, the beneficiary may not appoint any more than an income interest to his or her spouse or to a spouse of any other issue of Trustor. Before the beneficiary exercises this nongeneral power of appointment, he or she should consider Section 2041(a)(3) of the Code and 25 Delaware Code Sections 501-505, as amended, or any corresponding Delaware statutes enacted after the date of this agreement.

On the death of the beneficiary, Trustee shall divide the balance of the beneficiary's share, to the extent not effectively appointed, into further shares for his or her then living issue, per stirpes, but if no such issue is then living, then for the then living issue, per stirpes, of the closest ascendant of the beneficiary who was an issue of Trustor and who has then living issue, but if no such issue is then living, then for Trustor's then living issue, per stirpes. Trustee shall hold each share set aside pursuant to the preceding sentence in further trust under the provisions of this Subsection C. Any share set aside for an issue of Trustor for whose benefit a share is then held in trust under the provisions of this Subsection C shall be distributed to the Trustee of such share, to be added to its principal and disposed of as a part of it.

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D. Perpetuities Savings Clause. Notwithstanding the foregoing provisions, unless sooner terminated in the manner previously provided, each trust held hereunder shall end in its entirety or with respect to certain of its assets on the date, if any, required by the Delaware rule against perpetuities. Thereupon, Trustee shall distribute the principal of such trust or such assets, as the case may be, free from trust, to the beneficiary for whom the trust was set aside.

E. Failure of Issue. If, at any time, Trustee holds any portion of the principal of the trust fund not disposed of effectively under the previous provisions, then, at such time, Trustee shall distribute such principal, free from trust, to such then living person or persons as are then determined to be Trustor's distributees by the application of the intestacy laws of the State of Delaware governing the distribution of intestate personal property then in effect, as though Trustor had died at that particular time, unmarried, intestate, a resident of the State of Delaware, and owning such property then so distributable.

F. Distribution Adviser. Trustee shall exercise its discretionary power to distribute income and/or principal to Trustor's issue pursuant to Subsection A or Subsection C of this Section 1 only on the written direction of the distribution adviser who shall be [*Person Not Trustor or Beneficiary*], so long as [*he/she*] is willing and able to act in such capacity.

If at any time there is no distribution adviser, Trustee may act in the matter as it deems appropriate.

The distribution adviser shall act in a fiduciary capacity and conform to the purposes of this agreement. Such adviser shall have no duty to inquire into or see to the performance by Trustee of its duties under this agreement.

The distribution adviser shall receive no compensation and shall not be reimbursed for expenses incurred while acting as such adviser.

**SECTION 2: MINORITY OR OTHER INCAPACITY.**

If any property is otherwise required to be distributed to a beneficiary who has not attained age twenty-five (25) or is, in Trustee's opinion, unable to manage funds due to illness or infirmity, Trustee may:

A. Distribute such property to such beneficiary himself or herself; or

B. Apply such property for the benefit of such beneficiary; or

C. Hold the property not so distributed or applied in a separate trust hereunder for the benefit of such beneficiary and distribute or apply the net income and principal thereof as provided in Subsections A and B hereof. Trustee shall distribute the property in such trust to such beneficiary upon his or her attaining age twenty-five (25) or upon the termination of his or her incapacity (as the case may be). If the beneficiary dies prior to such distribution, Trustee shall distribute the property to such beneficiary's estate.

**SECTION 3: MERGER WITH SIMILAR TRUSTS.**

If, at any time, a trust is set aside for any person or persons under the terms of this agreement that is substantially the same as any other trust established for that person or persons, Trustee may, in its sole discretion, merge the trust created hereunder with the other trust for such person or persons, and the two trusts shall thereafter be held, administered, and distributed as one. However, Trustee shall not combine any trust having an inclusion ratio, as defined in Section 2642 of the Code (hereafter “inclusion ratio”), of other than zero (0) with a trust having an inclusion ratio of zero (0).

**SECTION 4: ALTERNATIVE METHODS OF DISTRIBUTION.**

Trustee may take any reasonable steps to disburse funds to or for a beneficiary, including: (i) distribution, either by hand or mail, to the beneficiary or the guardian of the person or property (whether the guardian is formally appointed or a natural guardian); (ii) distribution to a custodian for the beneficiary under the Uniform Transfers to Minors Act (or similar statute) of any state; (iii) deposit to the account of the beneficiary in any federally insured depository; (iv) direct application for the benefit of the beneficiary; or (v) distribution to a new or existing trust for the beneficiary.

**SECTION 5: SPENDTHRIFT PROVISION.**

A beneficiary may not alienate or in any other manner assign or transfer his or her interest in any trust hereunder, and no one (including a spouse or former spouse) may attach or otherwise reach any interest of any beneficiary hereunder to satisfy a claim against that beneficiary, whether the claim is legal or equitable in origin. The provisions of this Section shall not limit or otherwise affect any power of appointment conferred upon a beneficiary or the right of a beneficiary to disclaim or release any interest created hereunder.

**SECTION 6: TRUSTEE'S POWERS.**

In addition to those powers granted by law, Trustee is specifically authorized and empowered, in its sole discretion, but subject to the provisions of Sections 7 and 10:

A. To sell at public or private sale, exchange for like or unlike property, convey, lease for terms longer or shorter than the trust, and otherwise dispose of any or all property held hereunder, for such price and upon such terms and credits as it deems proper.

B. To invest in any kind of property, real, personal, or mixed, regardless of the laws governing

investments by fiduciaries, without any duty to diversify investments.

C. Unless otherwise directed by the investment adviser named in Section 7 hereof, to execute securities transactions, without necessity of providing written confirmation thereof to such adviser at the time of settlement, and to execute securities transactions through any brokerage service, whether discount or full service, including M& T Securities, at its normal rates of compensation, without diminution of compensation otherwise payable to Trustee, even if Wilmington Trust Company is serving as Trustee.

D. To vote directly or by proxy at any election or stockholders' meeting any shares of stock, including stock of M& T Bank Corporation, even if Wilmington Trust Company is serving as Trustee.

E. To participate in any plan or proceeding, including any voting trust plan for liquidating, protecting, or enforcing any interest in any property, or for reorganizing, consolidating, merging, or adjusting the finances of any corporation issuing any such interest; to accept in lieu thereof any new or substituted stocks, bonds, notes, or securities, whether of the same or a different kind or class, or with different priorities, rights, or privileges; to pay any assessment or any expense incident thereto; and to do any other act or thing that it deems necessary or advisable in connection therewith.

F. To deposit, or arrange for the deposit of, securities at Depository Trust Company (DTC) and/or at any other securities depository or clearing corporation.

G. To make any division or distribution in cash or in kind or partly in cash and partly in kind; to make reasonable valuations of the property so divided or distributed; and to elect to recognize taxable gain or loss resulting from a distribution. Trustee may consider the income tax basis of the property then available for division or distribution, as well as the circumstances of the beneficiaries, and need not make division or distribution on a pro rata, asset-by-asset basis. Trustee shall not adjust the interest of any beneficiary as a result of any action taken or forborne under the provisions of this Subsection G.

H. To make loans, against adequate collateral, to the Personal Representative of the estate of any beneficiary and/or to purchase any property belonging to his or her estate.

I. To borrow money, extend loans, pledge assets, and provide guarantees for any purpose connected with the protection, preservation, or improvement of the trust estate whenever in its judgment advisable, and as security to pledge any real or personal property forming a part of the trust estate upon such terms and conditions as it may deem advisable.

J. To bring or defend litigation, participate in arbitration or mediation, compromise or settle any claim in favor of or against any trust hereunder, and to execute all agreements, deeds, and releases necessary or proper in connection therewith. However, Trustee need not institute or defend any suit or proceeding unless its expenses, including counsel fees and costs, are available in the trust fund or are advanced or guaranteed in an amount and in a manner reasonably satisfactory to it. Trustee shall incur no liability to anyone for any action taken or not taken pursuant to the preceding sentence.

K. To retain attorneys-at-law, accountants, investment counsel, agents, and other advisers and to pay all compensation and other costs associated therewith from the trust without diminution of compensation otherwise payable to Trustee.

L. To pay the taxes and expenses of maintaining, repairing, improving, and insuring any real property held hereunder.

M. Except as otherwise provided, to determine whether receipts and disbursements, including its commissions, are allocable or chargeable to income or principal.

N. To renounce, in whole or in part, any property or interest in property that may become payable to

any trust hereunder, except to the extent that the distribution of such property resulting from such renunciation is fundamentally inconsistent with the provisions of this agreement.

O. To divide any trust hereunder into separate trusts if the purposes for which the trust was created are better served thereby.

P. To take such actions as are necessary to cause gains from the sale or exchange of trust assets (as determined for federal income-tax purposes) to be taxed for federal income-tax purposes as part of a distribution of principal to a beneficiary.

Q. To invest in any closely held company, limited liability company, or partnership, or in any successor entity, and to purchase additional interests in any such entity, even though, as a result, such trust is invested largely or entirely in such entity.

R. To settle its accounts judicially or nonjudicially at any time and from time to time and to pay all of its counsel, accountant, or other professional fees and costs associated therewith from the trust without diminution of compensation otherwise payable to Trustee.

S. To invest in, retain, or otherwise deal in any securities managed, issued, underwritten, or distributed by Trustee or by any of its affiliates, any participation in any investment company registered under the Investment Company Act of 1940, any investment fund exempt from registration under the Investment Company Act of 1940, for which Trustee or its affiliates is an adviser or agent, and any other "affiliated investment" within the meaning of 12 Delaware Code Section 3312, as amended, or any corresponding Delaware statute enacted after the date of this agreement, and is authorized to otherwise deal with or transact business with any of its affiliates, notwithstanding the fact that such trustee or affiliate may receive separate fees, commissions, or other costs directly from such security, fund, "affiliated investment," dealing, or transaction.

**SECTION 7: INVESTMENT ADVISER.**

During any period in which an investment adviser is serving and notwithstanding any other provision hereunder, the investment adviser shall:

A. Serve in a fiduciary capacity and hold and exercise the full powers to manage the investments of the Trust. Trustee shall exercise such powers only upon the investment adviser's written directions and shall be required to exercise such powers if so directed, including, but not limited to, all investment powers granted under Subsections (2) through (5), and Subsections (7) through (14) of 12 Delaware Code Section 3325, as amended, or any corresponding Delaware statute enacted after the date of this agreement, all powers described as an "investment decision" in 12 Delaware Code Section 3313(d), as amended, or any corresponding Delaware statute enacted after the date of this agreement, and all the powers in Subsections A, B, D, E, I, Q, and S of Section 6 with respect to each trust hereunder; provided that: (i) Trustee shall sell any M& T Bank Corporation stock held by it hereunder unless specifically directed to do otherwise by such adviser; (ii) the purchase, sale, and voting of M& T Bank Corporation stock shall be solely on the direction of the investment adviser; (iii) Trustee shall manage and invest the otherwise uninvested cash in each such trust in its sole discretion; and (iv) notwithstanding the foregoing, during an emergency or based upon exigent circumstances, where the Trustee reasonably believes based upon its actual knowledge that its inaction would be "wilful misconduct" within the meaning of 12 Delaware Code Section 3313(b), as amended, or any corresponding Delaware statute enacted after the date of this agreement, then the Trustee is hereby authorized and empowered to take such action regarding the investment management of such trust as it, in its sole discretion, shall deem to be for the best interest of the beneficiaries of such trust. The power set forth in (iv) above is solely intended to give the Trustee the ability to act should such action become essential to the trust fund, but does not impose a duty upon the Trustee to monitor or warn an interested party concerning the investments of the trust fund nor does this power create a duty of the Trustee to take such action.

B. The initial investment adviser shall be [*Name of Adviser*]. The investment adviser may resign as investment adviser of any trust hereunder by written notice delivered to the Trustee and the adult beneficiaries who may then receive income or principal. Until Trustor's death, a majority of the Trustor's then living issue who have attained age twenty-five (25) may remove the investment adviser and a successor investment adviser may be a person, if any, chosen from time to time by a majority of Trustor's then living issue who have attained age twenty-five (25) as shall be able to act. After Trustor's death, the investment adviser of each trust hereunder shall be the beneficiary for whom the trust was set aside, provided that he or she has attained age twenty-five (25). If such beneficiary has not attained age twenty-five (25) or is unwilling or unable to serve, the investment adviser of such trust shall be the person, if any, chosen from time to time by a majority of Trustor's then living issue who have attained age twenty-five (25) as shall be able to act, until such beneficiary attains age twenty-five (25) or is no longer unwilling or unable to act, at which time such beneficiary shall become the investment adviser of such trust. To qualify, any person appointed investment adviser of a trust hereunder shall deliver a written instrument to Trustee indicating acceptance and agreement that all powers conferred upon such adviser will be exercised in a fiduciary capacity for the exclusive interest of the beneficiaries.

C. With regard to trust assets over which the investment adviser holds the power to direct Trustee and in addition to the investment adviser's other duties herein, the investment adviser shall have the duty (i) to confirm to Trustee, in writing, the value of trust assets, whether publicly traded or nonpublicly traded assets, at least annually and upon request by Trustee, (ii) to direct Trustee with respect to making any representation, warranty, or covenant required to be made in order to maintain any investment, (iii) to direct and instruct Trustee on future actions, if any, to be taken with respect to such representations, warrantees, and covenants, (iv) to manage or participate in the management of any entity owned by the trust, to the extent such entity's governing instruments or applicable law require the owners to manage the same, and (v) to direct Trustee to sign agreements and any other documentation required in connection with the purchase of any investment and the maintenance of any such investment. With regard to the investment adviser's exercise of the foregoing powers, all such directions to the Trustee shall be in writing, delivered in such manner as the Trustee may specify from time to time by written notice to investment adviser. Further, the Trustee shall have no obligation to investigate or confirm the authenticity of directions it receives or the authority of the person or persons conveying them, and the Trustee shall be exonerated from any and all liability in relying on any such direction from a person purporting to be the investment adviser without further inquiry by the Trustee. Notwithstanding the foregoing, Trustee has no duty to monitor whether the investment adviser is abiding by its duty to provide valuation of publicly traded or nonpublicly traded assets and shall not be liable for failing to request a valuation or for the investment adviser's failure to give Trustee a valuation.

D. Whenever, pursuant to the terms of this Agreement, Trustee acts at the direction of any investment adviser regarding the exercise of the Trustee's powers as to any particular matter, or whenever Trustee takes no action except at the direction of any investment adviser, then notwithstanding any other provision hereunder, (i) as provided in 12 Delaware Code Section 3313(b), as amended, or any corresponding Delaware statute enacted after the date of this agreement, Trustee shall not be liable for any loss resulting from such acts or inaction except in cases of wilful misconduct proven by clear and convincing evidence, and (ii) to the extent any such action or inaction concerns a matter outside the scope of 12 Delaware Code Section 3313(b), as amended, or any corresponding Delaware statute enacted after the date of this agreement, in accordance with 12 Delaware Code Section 3303, as amended, or any corresponding Delaware statute enacted after the date of this agreement, Trustee shall have no liability hereunder except for Trustee's own wilful misconduct proven by clear and convincing evidence. The Trustee shall be under no obligation to review the trust assets, make any investment recommendations with respect to trust assets, solicit any direction from the investment adviser, value the assets if they are nonpublicly traded, or insure trust assets. As provided in 12 Delaware Code Section 3313(e), as amended, or any corresponding Delaware statute enacted after the date of this agreement, Trustee shall have no duty to monitor the conduct of the investment adviser, provide advice to the investment adviser, consult with the investment adviser, or communicate with or warn or apprise any

beneficiary or third party concerning instances in which the Trustee would or might have exercised the Trustee's own discretion in a manner different from the manner directed by the investment adviser.

E. The investment adviser may direct the Trustee to employ the professional services of accountants, investment management professionals, attorneys, tax advisers, and such other advisers ("Agent") as the investment adviser determines necessary to fulfill the duties of managing the investments of the trust. The investment adviser shall be solely responsible for the oversight, supervision, and monitoring of such Agent and shall notify the Trustee in writing of the employment of such Agent. The Trustee shall have no obligation to investigate or confirm the authenticity of directions it receives or the authority of the Agent conveying any such directions, and the Trustee shall be exonerated from any and all liability in relying on any such direction from a person purporting to be an Agent of the investment adviser without further inquiry by the Trustee until such time as the Trustee is notified in writing of the termination of such Agent's employment. The fees associated with the retention of an Agent by the investment adviser shall not diminish the compensation otherwise payable to the Trustee.

F. The investment adviser need not inquire into Trustee's performance of its duties and shall not be held liable for any loss whatsoever to any trust hereunder, unless it results from actions taken in bad faith. The investment adviser shall serve without compensation but may be reimbursed for out of pocket expenses, including investment counsel fees.

**SECTION 8: ADDITIONS TO THE TRUST FUND.**

With the consent of Trustee, any person may add property to any trust hereunder, and such property shall thereafter be held by Trustee as a part thereof. However, no property shall be added to a trust if such addition would cause the inclusion ratio of such trust to become other than zero (0). Instead, such property shall be held as a separate trust with terms identical to those of the trust to which the property would have been added.

**SECTION 9: TRUST IRREVOCABLE.**

This trust shall be irrevocable and not subject to amendment by Trustor or any other person. However, if, after the effective date of this agreement, any future requirements imposed by the Code or any regulations promulgated thereunder would cause the intended generation-skipping-transfer-tax-exempt status of any trust hereunder to be lost because of the failure of such trust to terminate immediately prior to the expiration of the period of the common-law rule against perpetuities or any specified term of years designated by the Code or the regulations promulgated thereunder, or because of any other reason, Trustee shall have the power to amend this agreement in any manner necessary for the sole purpose of complying with the requirements imposed by the Code or the regulations promulgated thereunder so that the intended generation-skipping-transfer-tax-exempt status of such trust is preserved. Trustee may rely upon the advice of counsel in taking any action pursuant to the authority given to Trustee, and Trustee shall be without liability therefor.

**SECTION 10: GRANTOR TRUST.**

A. Substitution of Trust Property. Trustor expressly reserves the right to substitute other property for that property then held by Trustee, provided that the investment adviser confirms in a writing filed with the Trustee that the property so substituted shall be of equal value to the property so replaced. The right granted in this Section is a personal right of Trustor and is not to be considered exercisable in a fiduciary capacity. Trustor has the right to relinquish this power of substitution and may do so by giving Trustee thirty (30) days written notice.

B. Discretionary Tax Reimbursement. Trustee, in Trustee's sole discretion, may reimburse Trustor for any income taxes payable on income of the trust fund.

**SECTION 11: NON-ACCRUAL OF INCOME.**

Any statute or rule of law to the contrary notwithstanding, any income accrued or on hand and not actually distributed to a beneficiary upon the termination of his or her interest shall be treated as though it had, in fact, accrued thereafter.

Any income accrued upon shares of stock or interest-bearing property when delivered to Trustee shall be treated as though such income had, in fact, accrued after such delivery.

**SECTION 12: THIRD PARTIES NOT OBLIGED TO FOLLOW FUNDS.**

No person or corporation dealing with Trustee shall be obliged to see to the application of money paid or property delivered to Trustee, to inquire into the propriety of Trustee's exercise of its powers, or to determine the existence of any fact upon which Trustee's power to perform any act hereunder may be conditioned.

**SECTION 13: TRUSTEE'S COMPENSATION.**

Unless otherwise agreed upon in writing between Trustee and Trustor (or, after Trustor's death or incapacity, by the investment adviser, or, if none, by a majority of the current beneficiaries of any trust created under this trust agreement who are over the age of twenty-five [25] years), Trustee shall receive compensation for its services hereunder from time to time in accordance with the current rates then charged by it for trusts of similar size and character. If Trustee renders any extraordinary services, it may receive additional compensation therefor.

**SECTION 14: RESIGNATION AND REMOVAL OF TRUSTEE.**

Trustee may resign as Trustee of any trust hereunder by written notice delivered to the adult beneficiaries to whom Trustee then may distribute income and principal, and Trustee may be removed by written notice delivered to Trustee signed by a majority of such beneficiaries who have attained age thirty (30). In either case, another bank or trust company, which is not related or subordinate to such beneficiaries within the meaning of Section 672(c) of the Code, shall be appointed successor Trustee by written notice signed by a majority of such beneficiaries who have attained age twenty-one (21).

Unless objections are filed as provided below, Trustee shall deliver the assets held in such trust to the successor Trustee. If a successor Trustee is not appointed in the above manner, Trustee may petition the Delaware Court of Chancery to appoint a successor Trustee.

Upon giving notice of resignation or upon receiving notice of removal, Trustee shall deliver a statement of its activities to the date of such notice for which it has not reported to the person or persons to whom Trustee gave notice of resignation or who were authorized to remove Trustee. Such person or persons shall have sixty (60) days from receipt of such statement to file with Trustee any objections to its actions as Trustee. If no such objections are filed, Trustee shall be without any further liability or responsibility to any past, or future beneficiaries.

No successor Trustee shall be required to examine into the acts of its predecessor Trustee, and each successor Trustee shall have responsibility only with respect to the property actually delivered to it by its predecessor Trustee.

Notwithstanding the foregoing provisions of this Section, Trustee may, but shall not be required to, prepare and file accountings for a trust hereunder with the Delaware Court of Chancery. Further, prior to delivering all the property of a trust hereunder to a successor trustee or to making any partial or complete distribution of the trust estate, Trustee may require an approval of the trust's accounting either by a release and discharge by the beneficiary or beneficiaries of the trust or by the Delaware Court of

Chancery. All of Trustee's fees and expenses (including reasonable counsel fees, accountant, or other professionals fees) attributable to any accounting and/or approval shall be paid by the trust.

**SECTION 15: MERGER OF CORPORATE TRUSTEE.**

Any corporation resulting from any merger, conversion, reorganization, or consolidation to which any corporation acting as Trustee hereunder shall be a party, or any corporation to which shall be transferred all or substantially all of any such corporation's trust business, shall be the successor of such corporation as Trustee hereunder, without the execution or filing of any instrument or the performance of any further act and shall have the same powers, authorities, and discretions as though originally named in this agreement; provided, however, that in the case of any corporation that is acting as a Trustee hereunder, the provisions of this Section shall apply only if the resulting or transferee corporation is domiciled in the same jurisdiction as the corporation that was acting as Trustee.

**SECTION 16: TRUST SITUS.**

This agreement creates a Delaware trust, and all matters pertaining to the validity, construction, and application of this agreement; to the administration of the trusts created by it; and to the effectiveness of restraints on alienation of beneficiaries' interests hereunder shall be governed by Delaware law. The Delaware Court of Chancery shall have exclusive jurisdiction over any action brought with respect to any trust hereunder.

**SECTION 17: ADOPTED PERSONS AND PERSONS BORN OUT OF WEDLOCK.**

For all purposes of this agreement, with regard to adopted persons, only a person adopted while under age twenty-one (21) shall be deemed to be a child and an issue of the adopting person and an issue of the ascendants of the adopting person, and, furthermore, the children and issue of a person so adopted shall be deemed to be issue of the adopting person and his or her ascendants. A person born out of wedlock shall not be deemed to be a child or an issue of his or her parent or an issue of the ascendants of his or her parent unless such child is acknowledged in writing by such parent.

**SECTION 18: DEEMED INCAPACITY OF TRUSTOR, TRUSTEE, OR ADVISER.**

An individual Trustor, Trustee, or adviser shall be deemed to be incapacitated: (i) during any period that such individual is legally incompetent as determined by a court of competent jurisdiction; (ii) during any period that a conservator or guardian for such individual has been appointed, based upon his or her incapacity; (iii) during any period when two (2) physicians licensed to practice medicine certify in writing to Trustee (if Trustor's capacity is at issue), to Trustor or the adviser (if a Trustee's capacity is at issue), or to Trustor and Trustee (if an adviser's capacity is at issue), that in the opinion of such physicians, such individual, as a result of illness, age, or other cause, no longer has the capacity to act prudently or effectively in financial affairs; or (iv) thirty (30) days after Trustee or any trust beneficiary requests such Trustor, Trustee, or adviser, as applicable, to provide a certificate from a physician licensed to practice medicine that, in the opinion of such physician, such individual has the capacity to act prudently or effectively in financial affairs if such Trustor, Trustee, or adviser, as applicable, fails to provide such certification within such period.

**SECTION 19: ILLIQUID ASSETS.**

To the extent that any of the creditors of Trustor, or any other beneficiary of a trust hereunder, asserts a claim that it is entitled, through the exercise of the judicial process or otherwise, to reach the assets of the trust in satisfaction of its claim, Trustee shall have no obligation to defend the trust or its assets against any such claim or to initiate or intervene in any litigation, arbitration proceeding, or mediation proceeding for the purpose of resisting any such claim, unless Trustee is reasonably satisfied that it will be fully indemnified from the assets of the trust for all of its liabilities and expenses (including professional fees

and expenses of counsel, accountants, and expert witnesses) arising from or attributable to Trustee's participation therein. If Trustee reasonably determines that the readily marketable assets of the trust are, or have become, insufficient for such purposes, Trustee may request that the Trustor or beneficiary provide Trustee with comparable indemnity, supported with such security as may be satisfactory to Trustee in its sole discretion, and in the absence of such additional indemnity or security, Trustee may refuse to participate in any such proceeding or may withdraw from an ongoing proceeding, even if such refusal or withdrawal may result in the granting or awarding of relief against the trust (including a distribution of trust assets in satisfaction of a claim). Trustee shall incur no liability to anyone whomsoever in connection with any such refusal or withdrawal pursuant to this Section 19.

**SECTION 20: DEFINITIONS.**

A. "Issue" of a person means all the lineal descendants of that person of all generations.

B. "Code" means the Internal Revenue Code of 1986, as amended, or any corresponding federal tax statute enacted after the date of this agreement. A reference to a specific section of the Code refers not only to that section but also to any corresponding provision of any federal tax statute enacted after the date of this agreement, as in effect on the date of application.

C. Use of any gender in this agreement includes the masculine, feminine, and neuter genders as appropriate. Use of the singular number includes the plural and vice versa unless the context clearly requires otherwise.

D. In applying any provision of this agreement which refers to a person's issue, "per stirpes," the children of that person are the heads of their respective stocks of issue, whether or not any child is then living.

E. "Personal Representative" means the executor or administrator of a decedent's estate and shall include all persons serving in such capacity from time to time.

F. Use of the verb "shall" in this agreement indicates a mandatory direction, and use of the verb "may" indicates authorization to take action.

G. Captions, headings, and sub-headings, as used herein, are for convenience only and have no legal or dispositive effect.

IN WITNESS WHEREOF, [*TRUSTOR'S NAME*], Trustor, has set [*his/her*] Hand and Seal the _____ day of _____, 20_____, and WILMINGTON TRUST COMPANY, Trustee, has caused this agreement to be signed in its name by one of its Vice Presidents and its corporate seal to be affixed by one of its Assistant Secretaries the _____ day of _____, 20_____, all done in duplicate as of the date of execution by Trustor, which date shall be the effective date of this instrument.

WITNESS:

_____ _____ [SEAL]

[*TRUSTOR'S NAME*], Trustor

WILMINGTON TRUST COMPANY

By _____

Vice President

Attest _____

Assistant Secretary

WITNESS:

_____ By _____

Investment Adviser

WITNESS:

_____ By _____

Distribution Adviser

"SCHEDULE A"

Consisting of One Page

of

Generation-Skipping Trust Agreement

Dated _____

Between

[*TRUSTOR'S NAME*]

and

WILMINGTON TRUST COMPANY

* * *

CASH in the amount of One Dollar ($1.00)

* * *

STATE OF _____ )

) SS.

COUNTY OF _____ )

The foregoing instrument was acknowledged before me this _____ day of _____, 20____, by [*TRUSTOR'S NAME*[.

_____

Notary Public

STATE OF DELAWARE )

) SS.

COUNTY OF NEW CASTLE )

The foregoing instrument was acknowledged before me this ____ day of _____, 20____, by _____, a Vice President of WILMINGTON TRUST COMPANY, a Delaware corporation, on behalf of the corporation.

_____

Notary Public