

## Construction, Merger and Decanting

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## Construction, Merger and Decanting

- Why change the document?
  - Mistake, lengthen term, add Grantor Trust provisions, remove grantor trust provisions, better spendthrift language, etc
  - How do you do that?

## Construction, Merger and Decanting

- Construction / Reformation
  - Cost, time, multiple representation of generations
- Merger with another trust
  - Similar Trust – If substantially later creation, then issue of perpetuities beginning date
- Decanting
  - Perhaps the best of all worlds

## Construction, Merger and Decanting

- Focus Upon Decanting
  - Origin in Common Law, but virtually all statutes have grown out of NY decanting statutes
  - Concept is that if principal may be paid for any purpose, then one of purposes can be for trustee to create new trust
  - Declaration of Trust – New Provisions, Declared by the Trustee

## Construction, Merger and Decanting

- Alaska and Delaware revisions – that can decant even if the power of distribution is on an ascertainable standard, and even if no distributions would currently be appropriate under that HEMS standard.
- This is in contrast to NY law, and almost all original decanting statutes, which require complete discretion as to payment
  - No decanting if distribution of principal only allowed for HEMS
- But the “decanted trust” must have same distribution standard as “decanting trust.”

## Construction, Merger and Decanting

- Under modern decanting statutes, there is an express authorization to decant even if under an ascertainable standard like HEMS
- And in the best, additional provisions that decanting is authorized, whether or not a current distribution would be authorized under HEMS standard

## Construction, Merger and Decanting

- Under some statutes, there is an additional requirement that the decanting not place any beneficiary or trustee in a worse tax provision than they were before decanting
- This seems to me to be an issue, what is a worse position?
  - If changing from a complex trust to a grantor trust, is that a worse tax position for the grantor?

## Decanting Issues – Who Can Decant?

- Is Decanting Authorized Under State Law?
  - Statutory authorization – See Tables in Materials
  - Common Law Authorization
  - Authorized in Document

## Decanting Issues – Who Can Decant?

- State Law Authorization
  - Increasing Resistance to State Law Passage
  - List of States in Table attached to materials
  - Also, in Rev. Proc 2011-3, IRS has said it will not rule upon Decanting
  - Alaska and Arizona focus for this discussion

## Decanting Issues – Who Can Decant?

- Document Authorization
  - In Interactive Legal, we routinely ask a question about whether Trustee may create trusts
  - Only exercisable by an Independent Trustee

## Decanting Issues – Who Can Decant?

- Is the trust subject to decanting
  - Decanting is based upon ability of Trustee to distribute
  - If no power for Trustee to distribute, no ability to decant
  - What about distributions upon health, maintenance, support and education?

## Decanting Issues – Who Can Decant?

- Tax Issues in Decanting
  - Gift Tax Issues – Have beneficiaries made a gift?
  - Generation Skipping Tax Issues – Is either the grandfathering for pre-86 trusts, or the zero inclusion ration for post 86 trusts, applicable to the new trust?
  - Income Tax Issues

## Decanting Issues – Rule Against Perpetuities Issues

- Delaware Tax Trap – Sec 2041(a)(3)
- Changing the Measuring Lives, versus changing the Measuring Date for Lives in Being
- Careful drafting can result in major gains for clients

## Decanting Issues – Mechanics of Decanting

- Power of decanting is in the nature of a special power of appointment
- Exercised through a writing, exercising a special power of appointment held by the Trustee
- Could combine exercise with new Trust Agreement, or separate the two

## Decanting Issues – Mechanics of Decanting

- New Trust Agreement
  - Issues of distribution standard must be the same, or no less restrictive
  - Limitations on Beneficiaries
  - Granting of special powers of appointment
  - Extending Trust Term

## Decanting Issues – Mechanics of Decanting

- New Trust Agreement
  - Typically new agreement is a Declaration of Trust (by Trustee) not a Trust Agreement
  - Probably have to tie back to original trust with respect to RAP date

## Construction, Merger and Decanting – No State Decanting Statute

- STUDY ON MOVING TRUSTS TO ALASKA
- Alaska statutes provide mechanism to have Alaska laws apply to non-Alaska trust
  - Appointment of Alaska person as Trustee or Co-Trustee
  - Declaration that principal place of administration is Alaska
  - Duties of Alaska Trustee, records in Alaska, assets in Alaska
  -

## Construction, Merger and Decanting – No State Decanting Statute

- STUDY ON MOVING TRUSTS TO ALASKA
- Once those prerequisites are met, trustee can register the trust as an Alaska trust
- Once registered as an Alaska trust, Alaska decanting statutes apply

## Construction, Merger and Decanting – No State Decanting Statute

– STUDY ON MOVING TRUSTS TO ALASKA

– With the application of Alaska statutes, can decant to trust containing desired provisions

- Does not need to be Alaska Trust

## Construction, Merger and Decanting – Summary

- Very Powerful Tool to extend trusts, correct errors, provide flexibility
- State Law applicability, or move trust to appropriate jurisdiction
- More attractive in trusts which are not grandfathered for GST purposes