

**WHAT YOU CAN LEARN FROM THE UNIFORM TRUST DECANTING ACT  
EVEN IF YOUR STATE DOESN'T HAVE DECANTING**

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*for presentation at  
Tulsa Estate Planning Forum  
Tulsa, Oklahoma*

Monday, November 14, 2016

**I. Why Should You Care About Decanting Even If Your State Doesn't Have a Decanting Statute?**

**A. Increasing Need for Flexibility in Trusts**

1. *Need for Flexibility.* There is a need for mechanisms to modify the terms of irrevocable trusts to address changes in beneficiary circumstances (e.g., a beneficiary with special needs), changes in trust law (e.g., the ability to have divided fiduciary roles), changes in the financial and investment worlds (e.g., the introduction of the prudent investor rule and growing interest in socially responsible investments), changes in tax law (e.g., the rollercoaster of changing estate tax laws over the past 15 years) and other changes (such as changes in who might be an appropriate trustee).
2. *Drafted-In Flexibility.* Trusts can be drafted to build in flexibility through trustee discretion, powers of appointment and trust protector provisions. Clients may find it difficult, however, to identify appropriate persons to act as trust protectors and to create effective provisions for naming successors. While trusts can include “built in” decanting provisions, drafting such provisions from scratch is complicated and costly. In any event, most trusts do not have effective decanting or trust protector provisions.
3. *Judicial Modifications.* Some flexibility is provided by judicial modifications. The Uniform Trust Code expanded the circumstances in which judicial modification is available. Judicial modifications, however, can be expensive and invasive of privacy.
4. *Non-Judicial Modifications by Settlement Agreement.* At least 33 states now allow the trustee and beneficiaries to make certain modifications to

trusts without court involvement through nonjudicial settlement agreements, but the usefulness of these statutes is limited because (1) they may not permit changes to dispositive provisions; (2) using these statutes may result in adverse tax consequences; (3) sometimes consent cannot be obtained on behalf of minor, unborn, or incapacitated beneficiaries; and (4) not all of the required beneficiaries may be willing to consent.

## B. Decanting

1. *What is Decanting?* Decanting is a process by which a trustee may modify the terms of an irrevocable trust without going to court and usually without beneficiary consent, although certain beneficiary rights are protected. Originally, decanting involved “pouring” the assets of the first trust into a separate trust, but now decanting doesn’t necessarily require a second new trust. Decanting filters out trust provisions no longer useful in accomplishing trust purposes, such as outdated investment provisions. Decanting aerates a trust by permitting new provisions that help accomplish the broad purposes of the trust.
2. *Common Law Decanting.* While decanting may be permitted in some situations under common law in some states, in many states it is unclear whether common law decanting is permitted, and if it is, the circumstances in which it is permitted and the parameters within which it may be exercised. See Prefatory Note to Uniform Trust Decanting Act.

## C. Decanting Statutes

1. *Generally.* These statutes represent one of several recent innovations in trust law that seek to make trusts more flexible so that the settlor’s material purposes can best be carried out under current circumstances. A decanting statute provides flexibility by statutorily expanding discretion already granted to the trustee to permit the trustee to modify the trust either directly or by distributing its assets to another trust. While some trusts expressly grant the trustee or another person a power to modify or decant the trust, a statutory provision can better describe the power granted, impose limits on the power to protect the beneficiaries and the settlor’s intent, protect against inadvertent tax consequences, provide procedural rules for exercising the power and provide for appropriate remedies.
2. *Half the States.* Twenty-five states have decanting statutes. See attached table. Summaries of the state decanting statutes can be found at <http://www.sidley.com/experience/state-decanting-statutes>.
3. *Decanting Distinguished from Other Modification Methods.* Decanting is distinct from judicial modification because decanting does not require court approval. Decanting is also distinct from modifications by

nonjudicial settlement agreements because beneficiary consent is not required. Because decanting does not require beneficiary consent or court approval, adverse tax consequences may be avoided when making certain modifications.

4. *Uses of Decanting.* Some of the uses for decanting include:
  - a. Administrative Change
  - b. Change Investment Limitations, Authorize Acquiring or Retaining an Asset or Permit Lack of Diversification
  - c. Define (and Limit) Beneficiary Rights to Information
  - d. Change Governing Law
  - e. Trustee Change
  - f. Provide for Advisors, Trust Protectors or Directed Trustees
  - g. Divide a Trust
  - h. Consolidate Trusts
  - i. Correct Scrivener's Error or Ambiguity
  - j. Add or Remove Spendthrift Provisions
  - k. Create a Supplemental Needs Trust
  - l. Limit a Beneficiary's Rights, or Eliminate a Beneficiary
  - m. Add a Beneficiary (with a Power of Appointment)
  - n. Convert Non-Grantor Trust to Grantor Trust
  - o. Convert Grantor Trust to Non-Grantor Trust

#### **D. Evaluating Decanting Statutes**

1. *The Race to the Bottom.* Some states have adopted decanting statutes of easy virtue to attract trusts to change jurisdictions. One commentator, from one of these states, evaluates decanting statutes largely on the basis of the extent to which they allow the trustee to do whatever it wants.
2. *Toxic Decanting Statutes.* If under an applicable decanting statute the trustee has the power to modify the trust in a manner that causes it not to qualify for an intended tax benefit, such as the marital deduction or gift tax

annual exclusion, the trust arguably does not qualify for the tax benefit from its inception, even if it is never decanted.

3. *Tax Integrity Test.* Does the decanting statute protect the integrity of the tax system, or does it permit tax shenanigans?
  4. *Veil of Ignorance.* A decanting statute should be evaluated from a veil of ignorance. If you don't know whether you represent a trustee contemplating a decanting, or one of the beneficiaries advocating for a decanting, or one of the beneficiaries whose interests may be affected adversely by a decanting, which decanting statute would you want?
- E. **Being an Ostrich is Dangerous.** Even if you believe decanting is an abomination, the head in the sand approach doesn't work any longer.
1. *Migrating Trusts.* Trusts are moving from states that don't permit decanting to states that do. States are trying to attract trusts by the ability to decant.
  2. *Voluntary Migration.* Whether or not your state has a decanting statute, you need to know about decanting if you are considering moving a trust to another state to decant it or for other reasons. There are states that have decanting statutes so permissive that the mere existence of the statute may cause tax issues.
  3. *Should Your State Allow Decanting?* You need to be informed to help decide if your state should have a decanting statute and, if so, what changes should be permitted and where limits should be drawn.
- F. **Drafting in Light of Decanting.** Because it is so easy to move a trust to a state with a decanting statute, and because there are states with toxic decanting statutes, whether or not your state has a decanting statute you may wish to thoughtfully address decanting in your trust documents. A trust can prohibit decanting that modifies certain provisions the settlor would never want changed. Special trust provisions may be needed to protect trusts that qualify for special tax treatment from decanting statutes that permit changes that would threaten the tax status, particularly in states with overly permissive decanting statutes.

## II. Uniform Trust Decanting Act

- A. **Uniform Law Commission.** The Uniform Law Commission ("ULC") is a non-profit organization that drafts model state legislation on topics for which uniformity is desirable.
- B. **Uniform Acts.** Uniform Acts are drafted by committees of volunteer attorney commissioners, reporters with subject matter expertise and observers from different interested organizations, such as the American Bar Association. Meetings are open to all interest groups.

- C. **Uniform Trust Decanting Act.** The UTDA was approved at the ULC annual meeting in the summer of 2015 after two years of work. Stan Kent, a ULC commissioner from Colorado, chaired the Committee. Susan Bart served as the reporter. Mark Ramsey from Oklahoma served on the Committee. Representatives from the ABA, the American College of Trust and Estate Counsel, corporate fiduciaries, elder law organizations and state attorney generals participated. The UTDA has been approved by the American Bar Association.

### III. Why Should You Care About the Uniform Act?

- A. **It May be Coming Soon.** Two states, New Mexico and Colorado, have passed the UTDA. Other states are considering the UTDA, including West Virginia, Pennsylvania, Illinois and Washington.
- B. **Balanced Approach.** The UTDA is a balanced approach, balancing the settlor's intent and preservation of beneficial interests with the need for flexibility. The UTDA is also drafted with the hope it will provide the basis for reasonable tax rules for decanting.
- C. **Tax Guidance.** The existing statutes vary wildly. We do not, for the most part, have guidance on the tax effects of decanting. The UTDA contains extensive provisions to prevent a decanting, or the decanting power itself, from disqualifying a trust for a tax benefit, such as the marital or charitable deduction. We hope that the IRS, in issuing guidance on the tax impact of decanting, will find that this "middle way" provides sufficient restrictions to avoid adverse tax consequences.
- D. **Need for Uniformity.** The Prefatory Note to the UTDA explains the need for uniformity:

*Need for Uniformity.* Trusts may be governed by the laws of different states for purposes of validity, meaning and effect, and administration. The place of administration of a trust may move from state to state. It often may be difficult to determine the state in which a trust is administered if a trust has co-trustees domiciled in different states or has a corporate trustee that performs different trust functions in different states. As a result it may sometimes be unclear whether a particular state's decanting statute applies to a trust and sometimes more than one state's decanting statute may apply to a trust. A uniform statute can eliminate conflicts between different state statutes. It can also protect a trustee who decants under one state's statute when more than one state's statute might apply and protect a trustee who reasonably relies on a prior decanting.

- E. **Innovative Provisions.** There are innovative provisions in the UTDA that states with pre-existing statutes may borrow, even if they do not immediately convert to the UTDA.

- F. **Incorporation into Trusts.** The UTDA provides language you may want to incorporate into your trusts to permit “decanting,” especially if your state does not permit decanting.
- G. **Comments.** The UTDA, like all Uniform Acts, has comments that provide helpful explanations of the provision and examples.
- H. **ULC Support.** The ULC provides support to states considering the UTDA.

#### IV. **What Does the Uniform Act Permit?**

##### A. **What Trusts Can Be Decanted?**

1. Only irrevocable trusts.
2. A trust cannot be decanted if its terms prohibit decanting.
3. Trust terms prohibiting amendment, stating that a trust is irrevocable or imposing spendthrift provisions do not prohibit decanting.
4. Wholly charitable trusts cannot be decanted.

B. **Fiduciary Duty.** The UTDA makes clear that the power to decant is a fiduciary power that must be exercised in accordance with fiduciary duties. A trustee must administer a trust in good faith, in accordance with its terms (subject to the decanting power) and purposes, and in the interests of the beneficiaries. An exercise of decanting power must be in accordance with the purposes of the first trust. The purpose of decanting is not to disregard the settlor’s intent but to modify the trust to better effectuate the settlor’s broader purposes or the settlor’s probable intent if the settlor had anticipated the circumstances at the time of decanting. See Section V.

C. **Extent of Decanting Authority Depends on Extent of Discretion Granted to Trustee.** Under the UTDA, the extent of the decanting authority depends upon the extent of the discretion granted to the trustee to distribute principal. Where the trustee has limited distributive discretion (e.g., an ascertainable standard), generally the decanting can modify administrative, but not dispositive, trust provisions. Where the trustee has expanded distributive discretion (e.g., “best interests,” “welfare” or no standard), the decanting may modify dispositive provisions subject to restrictions to protect “vested rights” and to protect qualification for tax benefits.

D. **Notice.** As a discretionary power, the decanting power may be exercised without consent or approval of the beneficiaries or the court, except in the case of a few specific modifications that may benefit the trustee personally. Nonetheless, qualified beneficiaries and certain other interested parties are entitled to notice and may petition the court if they believe the authorized fiduciary has breached its fiduciary duty. Further, the authorized fiduciary, another fiduciary, a beneficiary

or the settlor may petition the court for instructions, approval of an exercise of decanting power, a determination that the authorized fiduciary breached its fiduciary duties or a determination that the attempted decanting is invalid.

## V. **Fiduciary Duties**

### A. **Fiduciary Duties When Decanting**

1. The exercise of a trustee's power to decant is subject to all of the fiduciary duties that otherwise govern the trustee's administration of the trust whether imposed by the trust instrument or by governing law.
2. The UTDA provides: "In exercising the decanting power, an authorized fiduciary shall act in accordance with its fiduciary duties, including the duty to act in accordance with the purposes of the first trust." UTDA § 4(a).

### B. **Duty to Consider Purposes of Trust**

1. Note that the UTDA clearly directs the trustee to consider the purposes of the first trust. The UTDA comments state:

An exercise of the decanting power must be in accordance with the purposes of the first trust. The purpose of decanting is not to disregard the settlor's intent but to modify the trust to better effectuate the settlor's broader purposes or the settlor's probable intent if the settlor had anticipated the circumstances in place at the time of the decanting. The settlor's purposes generally include efficient administration of the trust. The settlor's purposes may also include achieving certain tax objectives or generally minimizing overall tax liabilities. The settlor's purposes often include avoiding fruitless, needless dissipation of the trust assets should a beneficiary develop dependencies such as substance abuse or gambling, have creditor problems, or otherwise be unfit to prudently manage assets that might be distributed from the trust.

2. The UTDA balances fidelity to the literal terms of the first trust with the potential advantages from decanting by providing: "Except as otherwise provided in a first-trust instrument, for purposes of this [act] . . . , the terms of the first trust are deemed to include the decanting power." UTDA § 4(c). The comments to Section 4(c) explain:

The exercise of the decanting power need not be in accord with the literal terms of the first-trust instrument because decanting by definition is a modification of the terms of the first trust. Therefore subsection 4(c) provides that the terms of the first trust shall be deemed to include the decanting power for purposes of determining the fiduciary duties of the authorized fiduciary.

Nonetheless, the other terms of the first trust may provide insight into the purposes of the first trust and the settlor's probable intent under current circumstances.

- C. **Duty of Impartiality.** The trustee has a duty of impartiality in exercising the decanting power, just like the trustee has a duty of impartiality in making discretionary distributions. The comments to Section 4 of the UTDA explain:

The duty to act impartially does not mean that the trustee must treat the beneficiaries equally. Rather the trustee must treat the beneficiaries equitably in light of the purposes and terms of the trust.

- D. **Duty of Loyalty.** In exercising a decanting power the trustee cannot place the trustee's own interests over those of the beneficiaries. For example, a trustee may breach its fiduciary duties if the trustee decants to permit self-dealing. Some statutes contain specific provisions restricting a trustee's ability to decant in a manner that might benefit the trustee as a fiduciary, for example, by allowing for increased trustee fees.

1. *Trustee Compensation.* The UTDA generally prohibits a trustee from decanting to increase its compensation unless the qualified beneficiaries consent or the court approves the increase.
2. *Trustee Liability.* The UTDA generally does not permit a trustee to decant to grant itself greater protection from liability.
3. *UTDA Exception for Claims Payable from First Trust.* Section 17(b) of the UTDA permits a second-trust instrument to provide for indemnification of the trustee of the first trust for any liability or claim that would have been payable from the first trust if the decanting power had not been exercised. Subsection (b) recognizes that the trustee of the first trust may be unwilling to distribute the assets of the first trust to the second trust unless the trustee is indemnified for any liability or claim that may become payable from the first trust after its assets are distributed.
4. *UTDA Exception for Directed Trusts.* Section 17(d) of the UTDA provides that "a second-trust instrument may divide and reallocate fiduciary powers among fiduciaries, including one or more trustees, distribution advisors, investment advisors, trust protectors, or other persons, and relieve a fiduciary from liability for an act or failure to act of another fiduciary as permitted by law of this state other than this [act]." The second-trust instrument, however, may not reduce fiduciary liability in the aggregate. UTDA § 17(c).

- E. **Ability to Remove Trustee.** The UTDA does not permit a trustee to decant to eliminate a trustee remover. Such a provision may be modified provided a substantially similar removal power is granted to someone else and the current

remover and the qualified beneficiaries of the second trust consent, or the court approves the modification. UTDA § 18.

- F. **No Creation of Duty to Decant.** The UTDA provides: “This [act] does not create or imply a duty to exercise the decanting power or to inform beneficiaries about the applicability of this [act].” The comments to the UTDA note that while the UTDA does not impose a duty to decant, there may be circumstances where trust law imposes a duty on the trustee to seek a deviation and a decanting is one way to accomplish such a deviation. The comments to Section 4 of the UTDA explain:

The Reporter’s Note to Comment e to subsection 66(2) of the Restatement Third of Trusts notes that the situations that might result in a duty to seek a deviation if the trustee has actual knowledge of the circumstances include extraordinary needs of the life beneficiary or irresponsibility of a potential distributee. See Illustration 2 in the Comments on subsection 66(1) of the Restatement Third of Trusts and the last paragraph of the Reporter’s Note to Comment b to Section 66 of the Restatement Third of Trusts. In the Reporter’s Notes to Comment b of Section 66 of the Restatement Third of Trusts, the Reporter notes that there may be a duty to seek deviation when there would be substantial distributions to beneficiaries who are legally competent to manage funds but practically at serious risk of squandering those distributions due, for example, to substance addiction or gambling. Although the Uniform Trust Decanting Act does not impose a duty to decant, an exercise of the decanting power would usually be an appropriate exercise of the authorized fiduciary’s discretion in such circumstances. See also Restatement Third of Trusts § 87.

Where the trustee has a duty to seek a deviation and the appropriate deviation could be achieved by an exercise of the decanting power, the trustee could fulfill such duty by an exercise of the decanting power rather than seeking a judicial deviation.

## VI. **Innovations in the Uniform Trust Decanting Act**

- A. **Restatements Permitted.** The UTDA makes clear that the second trust may be a restatement of the first trust, thus eliminating the need in many cases to create an entirely new trust, assign assets and terminate the first trust. “The decanting power” means the power of an authorized fiduciary under the UTDA to distribute property of a first trust to one or more second trusts *or to modify the terms of the first trust*. Section 2(10).
- B. **Reasonable Reliance.** The UTDA permits a trustee to reasonably rely on a prior decanting under the law of the enacting state or a different state, even if a decanting done under the law of another state does not comply with all of the requirements of the state’s uniform decanting statute.

- C. **Savings Provision.** The UTDA provides a remedy for an imperfect attempted decanting, to avoid the uncertainty that would exist if an attempted decanting is later discovered to have failed to comply fully with the UTDA. The UTDA essentially reads out of the second-trust instrument any impermissible provision and reads into the second-trust instrument any required provision. This gives fiduciaries exercising decanting power greater comfort that their intent will be implemented and not subject to challenge for an inadvertent misstep or technicality.
- D. **Protection of Charitable Interest.** The UTDA also addresses in detail the extent to which charitable interests may be modified by decanting. The UTDA does not permit decanting of wholly charitable trusts. If the first trust contains a charitable interest, the second trust cannot diminish the charitable interest or change the charitable purpose. To ensure that these protections are respected, the Attorney General must receive notice of any decanting of a trust with a charitable interest. Further, the UTDA prohibits changing the governing law of trusts containing determinable charitable interests without court approval if the Attorney General objects. The UTDA also prohibits modifying trust terms in a manner that would be inconsistent with any charitable deduction that may have been claimed.
- E. **Special Needs Trusts.** When a trust has a beneficiary with a disability, it may not be in the beneficiary's interest to make mandatory distributions to the beneficiary. Further, it may be in the beneficiary's interest to restructure the trust as a special needs trust so that the trust does not adversely affect the beneficiary's qualification for governmental benefits. This carries out the settlor's probable intent if the settlor had known of the beneficiary's disability. The UTDA permits a trust to be decanted to modify the interest of the beneficiary with a disability even if the trustee does not have expanded distributive discretion.
- F. **Tax Restrictions.** The UTDA contains extensive provisions to prevent a decanting, or the decanting power itself, from disqualifying a trust for a tax benefit, such as the marital or charitable deduction. The UTDA addresses tax issues seldom addressed in other statutes including grantor trust status, subchapter S qualifications and qualified retirement benefits.
- G. **Restrictions on Self-Interested Decantings.** The UTDA contains provisions that expressly prohibit or restrict modifications are in the self-interest of the authorized fiduciary.
- H. **Who is the Settlor?** The UTDA clarifies who is treated as the settlor of the second trust for different purposes.
- I. **Role of the Court.** The UTDA also delineates the role of the court in greater detail than in existing state statutes. While decanting generally does not require court approval, the authorized fiduciary may wish to seek instructions or approval from the court to confirm that the decanting is not an abuse of discretion. A fiduciary may also wish to seek court instructions as to the effect of a prior

decanting, particularly if the prior decanting may be in some way flawed. The UTDA permits the court to appoint a special fiduciary to exercise the decanting power in appropriate cases.

- J. **Animal Trusts.** The UTDA permits decanting of animal trusts if there is a protector named for the animal who consents. The UTDA protects animal trusts from decantings that might reduce the interests of the animal.

VII. **Decanting Prohibitions.** Decanting may *not* be used to:

- Eliminate a determinable charitable interest.
- Increase a trustee's compensation without consent of the qualified beneficiaries or court approval.
- Remove a person who has the power to remove the trustee.
- Violate a rule governing the maximum perpetuity period.
- Disqualify a trust for an intended tax benefit.

VIII. **Protection of Settlor Intent and Beneficiaries**

- A. **Fiduciary Duties.** The trustee must consider the purposes of the first trust and thus respect the settlor's broader purposes. Further, the trustee's fiduciary duties to the beneficiaries protects the beneficiaries.
- B. **Decanting Powers Related to Degree of Discretion.** The UTDA only permits decanting to change dispositive provisions where the settlor granted the trustee broad discretion.
- C. **Specific Protections of Beneficial Interests.** The UTDA prohibits certain changes even when the trustee has expanded distributive discretion. Beneficiaries may not be added and vested interests may not be eliminated.
- D. **Notice to Beneficiaries and Settlor.** Under the UTDA, a trustee must provide notice of a proposed decanting to all interested parties 60 days in advance of the decanting distribution.
- E. **Court Intervention.** Any interested party may ask a court to intervene and determine whether the decanting is permissible and consistent with the trustee's fiduciary duties.

IX. **Decanting Power Under Expanded Distributive Discretion**

- A. **Expanded Distributive Discretion.** "Expanded distributive discretion" means a discretionary power of distribution that is not limited to an ascertainable standard or a reasonably definite standard. UTDA § 2(11).

1. *Ascertainable Standard.* “Ascertainable standard” means a standard relating to an individual’s health, education, support, or maintenance within the meaning of Internal Revenue Code (“Code”) Section 2041(b)(1)(A) or Code Section 2514(c)(1). UTDA § 2(2).
  2. *Reasonably Definite Standard.* “Reasonably definite standard” means a clearly measurable standard under which a holder of a power of distribution is legally accountable within the meaning of Code Section 674(b)(5)(A).
- B. Decanting Power.** An authorized fiduciary that has expanded distributive discretion over the principal of a first trust for the benefit of one or more current beneficiaries may exercise the decanting power over the principal of the first trust.
1. *Authorized Fiduciary.* “Authorized fiduciary” means a trustee or other fiduciary, other than a settlor, that has discretion to distribute or direct a trustee to distribute part or all of the principal of the first trust to one or more current beneficiaries. UTDA § 2(3).
    - a. An authorized fiduciary must have the ability to make distributions currently.
    - b. A distribution director could be the authorized fiduciary.
  2. *Authority Over Principal.* The distributive discretion must be over principal.
- C. Restrictions**
1. *No Acceleration of Remainder Interests.* A second trust may not include as a current beneficiary a person who is not a current beneficiary of the first trust. UTDA § 11(c)(1).
  2. *No New Beneficiaries.* The second trust may not contain new beneficiaries. A second trust may not (1) include as a current beneficiary a person who is not a current beneficiary of the first trust, or (2) include as a presumptive remainder beneficiary or successor beneficiary a person who is not a current beneficiary, presumptive remainder beneficiary, or successor beneficiary of the first trust. UTDA § 11(c). See UTDA § 11(a) for definitions of “presumptive remainder beneficiary” and “successor beneficiary.”
  3. *Vested Interests.* A second trust may not reduce or eliminate a vested interest. UTDA § 11(c)(3). Vested interests include:
    - a. *Noncontingent Mandatory Distribution Right.* UTDA § 11(a)(3)(A). “Noncontingent” means: (A) not subject to the exercise of discretion or the occurrence of a specified event that is

not certain to occur; and (B) no person has discretion to distribute the property subject to the interest to any person other than the beneficiary or the beneficiary's estate. Section 2(16). A noncontingent mandatory distribution right means, for example, a right to withdraw at age 30 if the beneficiary has attained age 30, assuming the trustee does not have discretion to distribute the trust assets to anyone other than the beneficiary.

- b. *Current, Noncontingent Right to Income, Annuity or Unitrust Amount.* UTDA § 11(a)(3)(B) and (C). For example this means a right to receive income that is already in "pay status." It does not include a right to receive income starting at age 30 when the beneficiary has not yet attained age 30.
- c. *Presently Exercisable General Power of Appointment.* UTDA § 11(a)(3)(D).
- d. *Vested Remainder Interest.* A right to receive an ascertainable part of the trust property on the trust's termination that is not subject to the exercise of discretion or to the occurrence of a specified event that is not certain to occur. UTDA § 11(a)(3)(E).

4. *Powers of Appointment.* UTDA § 11(d).

- a. If the authorized fiduciary has expanded distributive discretion, a second trust may:
  - (i) retain a power of appointment granted in the first trust;
  - (ii) omit a power of appointment granted in the first trust, other than a presently exercisable general power of appointment;
  - (iii) create or modify a power of appointment if the powerholder is a current beneficiary of the first trust and the authorized fiduciary has expanded distributive discretion to distribute principal to the beneficiary;
  - (iv) create or modify a power of appointment if the powerholder is a presumptive remainder beneficiary or successor beneficiary of the first trust, but the exercise of the power may take effect only after the powerholder becomes, or would have become if then living, a current beneficiary.
- b. The power of appointment may be general or nongeneral. The class of permissible appointees in favor of which the power may be exercised may be broader than or different from the beneficiaries of the first trust. UTDA § 11(e).

5. *Change of Jurisdiction.* The second trust may be a trust created or administered under the law of any jurisdiction. UTDA § 11(d)(5).

X. **Decanting Power Under Limited Distributive Discretion**

- A. **Decanting Power.** An authorized fiduciary that has limited distributive discretion over the principal of the first trust for benefit of one or more current beneficiaries may exercise the decanting power over the principal of the first trust. UTDA § 12(b).
- B. **Restriction.** The second trust must grant each beneficiary of the first trust beneficial interests in the second trust which are substantially similar to the beneficial interests of the beneficiary in the first trust. UTDA § 12(c).
- C. **Distributions for “the benefit of.”** A power to make a distribution under a second trust for the benefit of a beneficiary who is an individual is substantially similar to a power under the first trust to make a distribution directly to the beneficiary. A distribution is for the benefit of a beneficiary if (1) the distribution is applied for the benefit of the beneficiary; (2) the beneficiary is under a legal disability or the trustee reasonably believes the beneficiary is incapacitated, and the distribution is made as permitted under the state’s trust code; or (3) the distribution is made as permitted under the terms of the first-trust instrument and the second-trust instrument for the benefit of the beneficiary.
- D. **Change of Jurisdiction.** The second trust may be a trust created or administered under the law of any jurisdiction. UTDA § 12(e).

- XI. **Reasonable Reliance.** When a decanting power is exercised, the trustee must act in accordance with its fiduciary duties. When a trustee does not exercise the power to decant, the state statutes generally protect the trustee in not exercising the power to decant. Similarly, the UTDA provides that it “does not create or imply a duty to exercise the decanting power or to inform beneficiaries about the applicability of” the UTDA. UTDA § 4(b). But what if the trustee accepts a trust that appears to have been previously decanted? How does the trustee determine whether those prior decanting were valid and what are the terms of the trust?

- A. **Which State’s Decanting Statute Applied?** When trusts have changed jurisdictions, it may be difficult to determine what law governs the administration of the trust. When trusts have multiple trustees, or a trustee conducts different trust functions in different places, it may be difficult to determine where the trust is administered. Thus it may be difficult in some cases to confirm with certainty which state statute applied to a prior attempted decanting. In some instances more than one state’s decanting statute may apply, creating further uncertainty if the prior attempted decanting did not comply with all of the potentially applicable statutes.
- B. **Technical Violations.** Uncertainty may also be created when an attempted decanting substantially, but not completely, complied with the statute. For

example, what if notice was not given to a person required to receive notice, or no evidence can be found confirming that notice was given? When someone receives notice on behalf of a minor or incapacitated person, there may be uncertainty about whether the notice requirement was met, for example if the rules for representation are unclear or require that the notice recipient not have a “conflict of interest.”

- C. **Substantive Violations.** A prior attempted decanting may purport to modify terms in a manner that does not, or arguably does not, comply with the statute. If there is a substantive violation is the entire decanting void, or is it only void in part?
  - D. **Reasonable Reliance.** Section 6 of the UTDA provides: “A trustee or other person that reasonably relies on the validity of a distribution of part or all of the property of a trust to another trust, or a modification of a trust, under this [act], law of this state other than this [act], or the law of another jurisdiction is not liable to any person for any action or failure to act as a result of the reliance.”
  - E. **Not a Validation Provision.** The UTDA does not validate all prior attempted decantings. Even if a trustee may reasonably rely on a prior decanting, a beneficiary may still have the right to challenge the decanting as invalid.
  - F. **Fixing Old Decantings.** Potentially a new trustee for a trust may wish to use a decanting power or a nonjudicial settlement agreement to confirm the validity of prior attempted decanting and the current terms of the trust. In some cases a court action may be necessary.
- XII. **Savings Provision.** The UTDA provides a remedy for an imperfect attempted decanting, to avoid the uncertainty that would exist if an attempted decanting is later discovered to have failed to fully comply with the UTDA.
- A. **Read Out.** UTDA Section 22(a)(1) provides: “A provision in the second-trust instrument which is not permitted under this [act] is void to the extent necessary to comply with this [act].” The UTDA essentially reads out of the second-trust instrument any impermissible provision. For example, if the second trust attempted to give the trustee a spray power over a QTIP trust, the spray provision would be ineffective.
  - B. **Read In.** UTDA Section 22(a)(2) provides: “A provision required by this [act] to be in the second-trust instrument which is not contained in the instrument is deemed to be included in the instrument to the extent necessary to comply with this [act].” This provision essentially reads into the second-trust instrument any required provision. For example, if the second trust failed to include the appropriate rule against perpetuities provision, the provision would be read into the document.
  - C. **Remedial Action.** If a trustee or other fiduciary of a second trust discovers that Section 22 applies to a prior exercise of the decanting power, the fiduciary shall

take such appropriate corrective action as is consistent with the fiduciary's duties. This corrective action may include informing the beneficiaries of the impact of Section 22, taking remedial action for distributions that were or were not made in error, and possibly seeking court guidance on the action to be taken.

- D. **Notice Forgiveness.** What if, years after an attempted decanting, someone argues that the trustee did not comply with the notice requirements because someone did not receive notice? Perhaps the trustee did not properly identify all of the qualified beneficiaries or fiduciaries, or failed to realize the Attorney General should have received notice, or sent a notice to the wrong address. The UTDA anticipates this by providing that an "exercise of the decanting power in not ineffective because of the failure to give notice to one or more persons . . . if the authorized fiduciary acted with reasonable care to comply with" the notice provisions. UTDA § 7(d).

### XIII. Protection of Charitable Interests

- A. **No Decanting of Wholly Charitable Trusts.** The UTDA does not permit decanting of wholly charitable trusts. UTDA § 3(b).

- B. **Split Interest Trusts.** While a split interest trust such as a charitable remainder trust or a charitable lead trust is not a wholly charitable trust, in almost all cases the trustee of such a trust would not have discretion to distribute principal to a current beneficiary and therefore there would be no authorized fiduciary (see UTDA § 2(3)) who would have authority to exercise the decanting power under Section 11 or Section 12.

#### C. Protection of Charitable Interests

1. *Charitable Interest.* "Charitable Interest" means the type of interest that makes, or if it were held by a named charity would make, the charity a qualified beneficiary. UTDA § 2(5). It does not include remote, contingent charitable interests. Thus in most cases the fact that charity is named as the failsafe beneficiary will not involve the charity or the Attorney General in the decanting.

2. *Restrictions.*

- a. If the first trust contains a charitable interest, the second trust cannot diminish the charitable interest. UTDA § 14(c)(1).
- b. If the first trust contains a charitable interest that names a specific charity, the second trust cannot change the charity to a different one. UTDA § 14(c)(2).
- c. If the first trust sets forth a particular charitable purpose, the second trust cannot change the charitable purpose. UTDA § 14(c)(3).

- d. If the first trust imposes certain conditions or restrictions on the charitable gift, the second trust cannot change the conditions or restrictions. UTDA § 14(c)(4).

**D. Notice to Attorney General**

1. *Notice.* If a first trust contains a determinable charitable interest, the Attorney General has the rights of a qualified beneficiary, including the right to notice and to bring a court action. UTDA § 14(b).
2. *Determinable Charitable Interest.* “Determinable charitable interests” include only mandatory interests and do not include discretionary interests. Section 14(a)(1). The term only includes unconditional interests that are not subject to any contingency other than a contingency that the charity be in existence and qualified as a charity for tax purposes. UTDA § 14(a)(2).

- E. Changing Trust Jurisdiction.** If the decanting changes the jurisdiction of a trust containing a determinable charitable interest, the Attorney General may block the decanting by objecting, even without petitioning the court. UTDA § 14(e). This prevents end runs around the protections for charitable interests.

**XIV. Special Needs Trusts**

- A. **Exception to Normal Rules for Beneficiary with a Disability.** When a trust has a beneficiary with a disability, the special needs fiduciary may decant the trust as if the fiduciary had expanded distributive discretion if (1) a second trust is a special needs trust that benefits the beneficiary with a disability, and (2) the special needs fiduciary determines that exercise of the decanting power will further the purposes of the first trust. UTDA § 13(b). The special needs fiduciary need not have any discretion over income or principal to decant under Section 13.
- B. **Beneficiary With a Disability.** “Beneficiary with a disability” means a beneficiary of the first trust who the special needs fiduciary believes may qualify for governmental benefits based on disability, whether or not the beneficiary currently receives those benefits or is an individual who has been adjudicated incompetent. UTDA § 13(a)(1).
- C. **Special Needs Trust.** “Special needs trust” means a trust the trustee believes would not be considered a resource for purposes of determining whether the beneficiary with a disability is eligible for governmental benefits.
- D. **Protection of Interests of Other Beneficiaries.** Except as affected by any change to the interests of the beneficiary with a disability, the second trusts, in the aggregate, must grant each other beneficiary of the first trust beneficial interests in the second trusts which are substantially similar to the beneficiary’s beneficial interests in the first trust. UTDA § 13(c)(3). Thus the presence of a beneficiary with a disability does not give the fiduciary free rein to alter the interests of other

beneficiaries, although those interests may be affected as a result of providing for the beneficiary with a disability.

XV. **Tax Restrictions.** The UTDA contains extensive provisions to prevent a decanting, or the decanting power itself, from disqualifying a trust for a tax benefit. The UTDA addresses tax issues seldom addressed in other statutes including grantor trust status, subchapter S qualifications and qualified retirement benefits.

A. **Marital Deduction.** UTDA § 19(b)(1).

B. **Charitable Deduction.** UTDA § 19(b)(2).

C. **Gift Tax Annual Exclusion.** UTDA § 19(b)(3).

D. **S Corporation Trusts.** UTDA § 19(b)(4).

1. If the first trust includes stock in an S corporation and the first trust is a permitted S corporation stock shareholder, the second trust must be a permitted shareholder.

2. If the first trust includes stock in an S corporation and the first trust is a QSST, the second trust must be a QSST. If the authorized fiduciary had the power to modify a trust intended to qualify as a QSST to a trust that did not so qualify, the trust would not be a QSST from its inception. In order for a trust to qualify as a QSST, (a) the terms of the trust must require that during the life of the current income beneficiary there shall be only one income beneficiary and (b) all of the income must be distributed to such beneficiary. Code § 1361(d)(3). Thus it may be important that a trust intended to qualify as a QSST not be permitted to be decanted into a trust that would not qualify as a QSST. If the first trust owns S corporation stock and qualifies as an S corporation shareholder because it is a QSST, Section 19(b)(4) requires that the second trust also be a QSST. If the first trust is a QSST, it is not sufficient that the second trust qualify to hold S corporation stock under another provision of the Code.

E. **GST “Annual Exclusion.”** UTDA § 19(b)(5).

F. **Qualified Benefits Property.** UTDA § 19(b)(6). Under the rules in Code Section 401(a)(9), only trusts with certain provisions and restrictions permit the life expectancy of the beneficiary to be used to determine required minimum distributions. If a trustee could decant to a trust that would not meet these requirements, then arguably the old trust would not qualify from the inception to use the life expectancy of the beneficiary.

G. **Foreign Grantor Trusts.** UTDA § 19(b)(7).

H. **Catchall.** A second-trust instrument may not include or omit a term that, if included in or omitted from the first-trust instrument, would have prevented

qualification for a tax benefit if (1) the first-trust instrument expressly indicates an intent to qualify for the benefit or the first-trust instrument clearly is designed to enable the first trust to qualify for the benefit; and (2) the transfer of property held by the first trust or the first trust qualified, or but for provisions of the UTDA other than Section 19, would have qualified for the tax benefit. UTDA § 19(b)(8).

## I. Grantor Trusts

1. *Turning Off.* Decanting can turn off grantor trust status. UTDA § 19(b)(A). The authorized trustee, however, would still have to consider the trustee's fiduciary duties in deciding whether to turn off the grantor trust status. Thus in general it is better to use other methods to turn off grantor trust status, but decanting may provide relief when other methods are not available.
2. *Turning On.* Decanting can convert a trust that is not a grantor trust for income tax purposes to a trust that is a grantor trust, but subject to special rules to protect the settlor. Special rules are needed because the authorized fiduciary does not ordinarily have any fiduciary duty to consider the settlor's interests, and grantor trust status may often be in the interests of the beneficiaries. The authorized fiduciary should consider the purposes of the trust in contemplating a decanting, and thus may often conclude that because the settlor did not choose to make the trust a grantor trust, such a conversion is not consistent with the purposes of the trust. If the authorized fiduciary nonetheless intends to decant to make a trust a grantor trust, the UTDA gives the settlor notice of the proposed decanting and the right to block the decanting by objection during the notice period if the second trust does not give the settlor the power to turn off the grantor trust status. UTDA § 19(b)(10)(B). The UTDA also gives the settlor the right to block a decanting of a grantor trust that would take away the settlor's power to turn off the grantor trust status. UTDA § 19(b)(10)(A).

XVI. **Restrictions on Self-Interested Decantings.** The UTDA contains provisions that expressly prohibit or restrict decantings that may be in the self-interest of the authorized fiduciary.

### A. Change in Compensation

1. If a first-trust instrument specifies an authorized fiduciary's compensation, the fiduciary may not exercise the decanting power to increase the fiduciary's compensation beyond the specified compensation unless (1) all qualified beneficiaries of the second trust consent to the increase in a signed record; or (2) the increase is approved by the court. UTDA § 16(a).
2. If a first-trust instrument does not specify an authorized fiduciary's compensation, the fiduciary may not exercise the decanting power to

increase the fiduciary's compensation above the compensation permitted by other law of the state unless (1) all qualified beneficiaries of the second trust consent to the increase in a signed record; or (2) the increase is approved by the court. UTDA § 16(b).

**B. Relief from Liability and Indemnification**

1. *Expanding Exculpation Prohibited.* With important exceptions, a second-trust instrument may not relieve an authorized fiduciary from liability for breach of trust to a greater extent than the first-trust instrument. UTDA § 17(a).
2. *Carry Over of Claims.* The second trust may indemnify the fiduciaries of the first trust from any liability or claim that would have been payable from the first trust. UTDA § 17(b).
3. *Divided Trustee Powers.* A second-trust instrument may divide and reallocate fiduciary powers among fiduciaries, including one or more trustees, distribution advisors, investment advisors, trust protectors, or other persons, and relieve a fiduciary from liability for an act or failure to act of another fiduciary as permitted by a directed trust statute. UTDA § 17(d).

- C. Removal or Replacement of Authorized Fiduciary.** An authorized fiduciary may not exercise the decanting power to modify a provision in the first-trust instrument granting another person power to remove or replace the fiduciary unless: (1) the person holding the power consents to the modification in a signed record and the modification applies only to the person; (2) the person holding the power and the qualified beneficiaries of the second trust consent to the modification in a signed record and the modification grants a substantially similar power to another person; or (3) the court approves the modification and the modification grants a substantially similar power to another person. UTDA § 18.

**XVII. Who is the Settlor?** It is important to know who is the settlor of the second trust for various purposes. Is it the nominal grantor of the second trust? Where the second trust is created for purposes of the decanting, or the second trust is a “restatement” of the first trust, the nominal grantor may be the trustee.

- A. Tax Purposes.** The settlor or grantor for tax purposes is the person who contributed the property. The UTDA confirms this by providing that “a settlor of a first trust is deemed to be the settlor of the second trust with respect to the portion of the principal of the first trust subject to the exercise of the decanting power.” UTDA § 25(a). Where the second trust was a pre-existing trust whose settlor was different than the settlor of the first trust, after the decanting the second trust may have two settlors.

- B. Purposes of Trust Administration Actions.** Various provisions of trust law may require the consent of the settlor for certain actions (e.g. trust modification under

Section 411 of the Uniform Trust Code), or may limit the ability of the settlor to take certain actions (e.g. representing a beneficiary), or may need to identify the settlor for other purposes (e.g. determining an insurance interest). The UTDA clarifies who is the settlor for such purposes by providing that “a settlor of a first trust is deemed to be the settlor of the second trust with respect to the portion of the principal of the first trust subject to the exercise of the decanting power.” UTDA § 25(a).

- C. **Determining Settlor Intent.** Who should be considered the settlor for purposes of determining settlor intent when construing a provision of the trust after the decanting? If the decanting distributed assets into a pre-existing trust, probably for the most part the original settlor of the pre-existing trust, although it may be relevant what the authorized fiduciary believed the terms of the second trust to be. If the authorized fiduciary created a new trust for purposes of the decanting, probably the intent of the authorized fiduciary is most relevant. If the authorized fiduciary essentially modified certain provisions of the first trust, but left other provisions of the first trust intact, perhaps the intent of the authorized fiduciary matters for the new provisions, but the intent of the original settlor of the first trust for other provisions. The UTDA recognizes that this is an issue and provides: “In determining settlor intent with respect to a second trust, the intent of a settlor of the first trust, the intent of a settlor of the second trust, and the intent of the authorized fiduciary may be considered.” UTDA § 25(b).

XVIII. **Role of the Court.** The UTDA delineates the role of the court in greater detail than in existing state statutes. While decanting generally does not require court approval, the court plays an important supporting role.

- A. **Special Fiduciary.** The court may appoint a special fiduciary to exercise the decanting power in appropriate cases. UTDA § 9(a)(2). The special fiduciary only has the decanting power that such person would have if acting as authorized fiduciary, and is subject to the same restrictions. The appointment of a special fiduciary may be helpful where the acting fiduciary’s distributive powers are limited because the fiduciary is a beneficiary, but the trust instrument grants disinterested fiduciaries expanded distributive discretion. The appointment of a special fiduciary may also be helpful where the authorized fiduciary is reluctant to decant, but does not necessarily oppose the decanting.
- B. **Approval of Changes to Compensation or Removal Powers.** The court’s approval may be required to increase the authorized fiduciary’s compensation or to modify the provisions regarding the removal or replacement of the authorized fiduciary. UTDA § 9(b).
- C. **Who May Petition Court.** A wide array of interested persons may petition the court, including the authorized fiduciary, any other fiduciary, the settlor, a beneficiary and, with respect to a charitable interest, the Attorney General and any other person that has standing to enforce the charitable interest. UTDA § 9(a).

D. **Subjects of Petition.** The court may:

1. *Instruct.* Provide instructions to the authorized fiduciary regarding whether a proposed exercise of the decanting power is permitted under the UTDA and consistent with the fiduciary duties of the authorized fiduciary.
2. *Appoint Special Fiduciary.* Appoint a special fiduciary and authorize the special fiduciary to determine whether the decanting power should be exercised under the UTDA and to exercise the decanting power.
3. *Approve.* Approve an exercise of the decanting power.
4. *Declare Attempted Decanting Ineffective.* Determine that a proposed or attempted exercise of the decanting power is ineffective because (1) after applying UTDA § 22, the proposed or attempted exercise does not or did not comply with the UTDA or (2) the proposed or attempted exercise would be or was an abuse of the fiduciary's discretion or a breach of fiduciary duty.
5. *Apply Remedial Provisions.* Determine the extent to which UTDA § 22 applies to a prior exercise of the decanting power or provide instructions to the trustee regarding the application of UTDA § 22 to a prior exercise of the decanting power.
6. *Other Relief.* Order other appropriate relief to carry out the purposes of the UTDA.

XIX. **Animal Trusts**

A. **Decanting Issues.** A trust for a nonhuman animal may be drafted so that the trust names a human beneficiary or may be drafted in a manner so that the trust has no human beneficiary. "Pet trust" statutes in many states and under the Uniform Trust Code validate trusts for nonhuman animals even if no human beneficiary is named.

1. If no human beneficiary is named, decanting statutes may not apply to the trust because there is no recognized beneficiary. Yet there may be reasons to decant such trusts, for example to change the identity of the caretaker. Or perhaps Fluffy is aging and no longer enjoying the penthouse in New York and would prefer a beach side cottage in Hawaii.
2. If a human beneficiary is named, decanting statutes may permit changes to the trust provisions that would reduce or eliminate the benefits for the animal in a manner not intended by the settlor.

B. **Decanting Permitted.** The UTDA permits the decanting of an animal trust that has a protector for the animal if the protector consents. A protector is a person appointed in the trust or by the court to enforce the trust on behalf of the animal.

UTDA § 23(b). In addition to having the power to consent or not consent to the decanting, the protector has all of the rights of a qualified beneficiary, including the right to petition the court. If no protector is named in the trust, the court could appoint a special fido-uciary to represent the animal.

- C. **Animal Protected.** The UTDA provides that if an animal trust is decanted, the second trust “must provide that the trust property may be applied only to its intended purposed for the period the first trust benefitted the animal.” UTDA § 23(d). Thus the decanting cannot divert some or all of the trust property away from the animal. Nor can the decanting shorten the time during which the animal benefits from the trust. Note that these provisions apply even if there is a human beneficiary and the trust is being decanted under UTDA § 11 or UTDA § 12.

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