



WRMarketplace

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The *WRMarketplace* is created exclusively for AALU members by experts at Greenberg Traurig and the AALU staff, led **by Jonathan M. Forster, Steven B. Lapidus, Martin Kalb, Richard A. Sirus, and Rebecca Manicone**. **WRMarketplace #17-30** was written by Greenberg Traurig **Shareholder Rebecca S. Manicone and Associate Jennifer M. Smith**.

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TOPIC: Case Study Series – Trust Decanting in Action: Breathing New Life into Old Trusts.

MARKET TREND: A trustee’s ability to decant an irrevocable trust can provide significant planning flexibility as a practical and economical solution to correct errors or address changing client concerns.

SYNOPSIS: Trust decanting allows a trustee to transfer assets from an existing irrevocable trust to a different irrevocable trust and may be used to address a wide array of issues, including correcting drafting errors, changing distributions standards or beneficiary powers of appointment, amending administrative provisions, and updating fiduciaries and their powers. As discussed in *WRMarketplace* Nos. 17-22 and 14-21, decanting has become increasingly popular in many states, with several of them implementing formal decanting statutes. To see why, the following case study demonstrates how decanting provides continued planning options for an old trust.

TAKE-AWAYS: In years past, irrevocable trust modifications primarily relied on costly and public judicial reformations or sales of assets from one trust to another (with associated administrative and valuation complexities). Now, with more states accepting and authorizing the process, trust decantings can be used to achieve the same modifications without the complications associated with sales and reformations. Decanting can make existing trusts more viable for use in future planning, which is likely of particular appeal for life insurance purposes, since the use of a pre-funded trust may

avoid the need to develop a separate premium funding arrangement for a trust-owned policy.

PRIOR REPORTS: 17-22; 14-21.

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CASE STUDY: TRUST DECANTING IN ACTION

Meet the Clients - The Joneses. The Joneses, Alan, age 50, and Becca, age 43, have been married for 20 years and have three children: Claire (age 18), David (age 16), and Fiona (age 4). Alan is a founder of FAM Co., a successful closely-held family business. A few years ago, before FAM Co.'s value took off, Alan made a gift of cash and some FAM Co. interests to an irrevocable dynasty trust, the Jones Family Trust ("**JF Trust**"), benefiting Becca and his descendants. Shortly thereafter, the JF Trust bought permanent life insurance coverage on Alan's life with a face amount of \$5 million. Now, the trust assets are worth over \$20 million. Alan's close friend is a trustee.

The JF Trust Agreement currently provides for a single "pot" benefiting Alan's descendants and Becca. After the passing of the survivor of Alan and Becca, this pot trust continues until Alan's youngest child attains age 25 and then breaks into a separate trust for each child. Each separate trust continues in further separate trusts for a child's descendants after the child's passing. A trust's primary beneficiary can act as a co-trustee of that trust at age 35 and as sole trustee at age 40. The trust provides for, but does not require, an independent trustee to serve. Successor trustees may be appointed by (1) Alan, then (2) Becca, then (3) the trust's primary beneficiary or beneficiaries, then (4) the attorney who originally drafted the trust agreement, or his firm.²

Client Concerns. As part of an overall review of their legacy and life insurance planning, Alan and Becca have recently engaged new legacy planning counsel and are looking at the ability to increase trust-owned life insurance coverage on Alan's life. There are concerns, however, with using the JF Trust. The ability of Alan and Becca's children to serve as sole trustees may limit the creditor protection and asset management guidance provided by the JF Trust, a particular concern given the trust's size. Also the significant age disparity between the couple's oldest and youngest child (14 years) raises the question of whether retaining the pot trust for such a long time will create disputes among the trustee and children, who will have widely-varying needs as they attain different phases of life at different times. Finally, the trustee successor provisions still tie the trust to Alan and Becca's prior attorney and his firm.

Solution – Decant to New Trust. Rather than create and fund a new trust to acquire additional life insurance, the advisors suggest the decanting of the existing trust assets to a new trust (“**New Trust**”),³ which provides for:

- **Separate Trusts for Children.** The New Trust agreement will immediately create a separate, equal trust for each child of Alan (Becca also will remain a beneficiary of each trust), which includes non-binding guidance to the trustee regarding distribution (e.g., primarily for education until a beneficiary turns 25, to purchase a house or start a business after completing school, to help with a beneficiary’s children, etc.). This separation allows the trustee to focus distributions on the specific circumstances of each child at a particular stage of life without worrying that such distributions will have an adverse or unfair impact on the other children.
- **Revised Trustee Succession Provisions.** The New Trust will revise the provisions for the appointment of successor trustees to eliminate the power of the prior attorney/law firm to name successors. Rather, the New Trust will provide that, if there is a vacancy in the office of trustee that is not filled within 30 days by any individual having the power appoint successor trustees under the trust, a court with jurisdiction over the trust will have the power to appoint a trustee at the request of any interested person.
- **Descendants as Co-Trustees Only.** To increase a trust’s creditor protection, the New Trust will provide that a primary beneficiary (e.g., a descendant) may only serve as a co-trustee, not sole trustee, of his or her trust. The beneficiary-trustee could be given sole authority to make distributions to himself or herself for health, education, maintenance, and support (i.e., under an ascertainable standard); however, for greater creditor protection, the New Trust would require the independent trustee’s consent to such decisions.⁴
- **An Independent Trustee at All Times.** The New Trust will require that an independent trustee be in office at all times for all trusts created under the agreement. The independent trustee can provide greater distribution flexibility, as it does not need to limit distribution decisions to those based on an ascertainable standard. Further, an independent trustee may increase the creditor protection provided by the trust. As a check and balance, Becca, followed by Alan’s descendants, can be given the power to remove and replace independent trustees of their trusts.
- **Appointment of Business/Investment Advisors.** To provide additional asset management guidance to the trustees (particularly descendants serving as co-trustees), the New Trust will appoint separate Business and Investment Advisors, who will provide guidance regarding the management of the trusts’ FAM Co. interests and other investments. The Business Advisor should be an employee, director, or another person familiar with the operation of FAM Co. and the family’s goals for the company. Again, as a check and balance, Becca, followed by Alan’s descendants, can be given the power to remove and replace these advisors.

Results. By decanting, the JF Trust is effectively revitalized so that its assets can be used to meet the Jones family's additional legacy and life insurance planning needs. Decanting updates the trust's fiduciary provisions, provides additional creditor protection and asset management guidance, and minimizes the potential for future conflicts, alleviating Alan and Becca's worries regarding the legacy management of a substantial trust. Further, the trustee, advisors, and clients are now comfortable using the trust to acquire the additional life insurance coverage, which eliminates concerns about using more assets to fund a new trust with additional premiums.

TAKE AWAYS

In years past, irrevocable trust modifications primarily relied on costly and public judicial reformations or sales of assets from one trust to another (with associated administrative and valuation complexities). Now, with more states accepting and authorizing the process, trust decantings can be used to achieve the same modifications without the complications associated with sales and reformations. Decanting can make existing trusts more viable for use in future planning, which is likely of particular appeal for life insurance purposes, since the use of a pre-funded trust may avoid the need to develop a separate premium funding arrangement for a trust-owned policy.

DISCLAIMER

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NOTES

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¹ Although increasingly popular, decanting is a relatively new and developing area of law. 25 states have adopted decanting statutes, while others rely on the trust instrument or common law to address the power to decant. Thus, the process varies significantly from state-to-state depending on the applicable legal and statutory requirements.

² Any successor trustee appointed may not be related or subordinate to the person appointing the trustee or to any beneficiary of the trust of which the trustee will serve.

³ As discussed in *WRMarketplace No. 17-22*, under the Uniform Trust Decanting Act and in states that have adopted this act (e.g., Colorado, New Mexico and Virginia), rather than decant to a trust newly created under a separate instrument, a trustee can simply modify or amend and restate the original trust, which simplifies the process and eliminates the down-stream administrative needs of re-titling or transferring assets to a second trust or obtaining a separate tax identification number for the second trust (if a new trust).

⁴ See *WRMarketplace No. 16-39* for a discussion of how a trust's creditor protection may be impacted if a beneficiary who serves as a trustee of his or her trust holds certain distribution powers.