

Fixing “Broken” Estate Plans

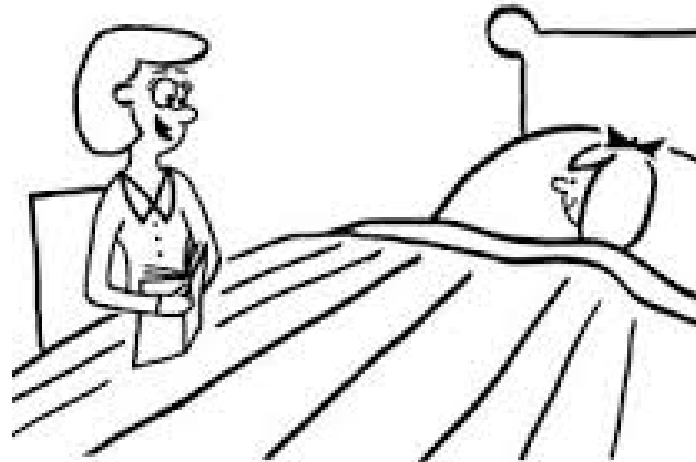
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Stu's Views

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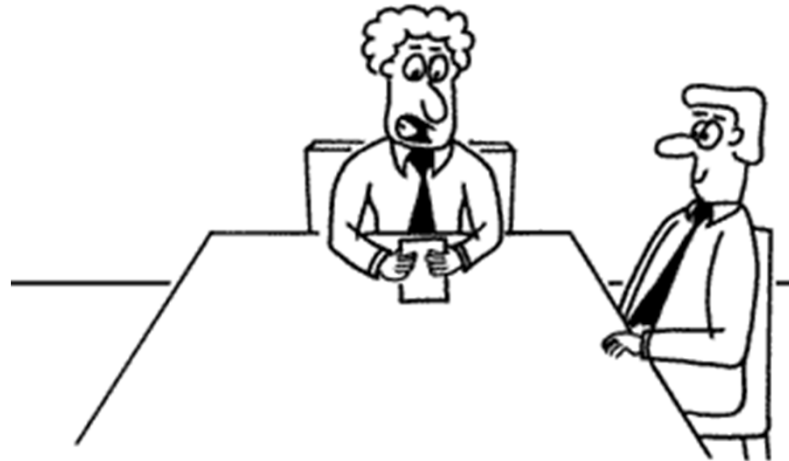
Estate Lawyer
Moms



Then the dragon ate the prince, but
his trust lived happily ever after.



Reading
the Will



"To my loyal estate planning attorney, I leave my children a complicated series of trusts that will generate huge legal fees."

Overview

- Reasons to Modify an Estate Plan
- Ways to Fix a Broken Estate Plan
 - Statutory judicial modification
 - Statutory nonjudicial modification
 - Document terms
 - Common law or other powers
- Two Underutilized Tools
 - Nonjudicial settlement agreements
 - Common law decanting

Reasons to Modify an Estate Plan

Reasons to Modify an Estate Plan

Mistakes, Ambiguities, Administration

- Correct a drafting error
- Modernize trust provisions
- Change trust situs and/or governing law
- Divide or merge trusts
- Reduce administrative costs
- Add corporate trustee's administrative provisions
- Trustees and successor trustees

Reasons to Modify an Estate Plan

Beneficiary related reasons

- Grant or limit a power of appointment
- Limit a beneficiary's right to receive information
- Eliminate a beneficiary
- Change a pot trust to separate shares
- Special needs trust for a remainder beneficiary
- Protect trust property from beneficiary's creditors, divorce, addiction

Reasons to Modify an Estate Plan

Tax reasons

- Settlor has unused estate and GST tax exemptions
- Change from grantor trust to non-grantor trust (or vice versa)
- Have beneficiary be taxed as owner of the trust
- Move to a jurisdiction that has lower state income tax and/or no state estate tax
- Use grantor's or beneficiary's GST tax exemption

How to Fix a Broken Estate Plan

How to Fix A Broken Estate Plan

Trusts: Statutory judicial modification

- Modification or termination of irrevocable trusts by consent if settlor not living (75-7-411(2))
- Unanticipated circumstances or inability to administer trust effectively (75-7-412)
- Cy pres (charitable trusts) (75-7-413)
- Modify, terminate, or replace trustee of uneconomic trusts (75-7-414(2))
- Reformation to correct mistakes (75-7-415)
- Modification to achieve settlor's tax objectives (75-7-416)

How to Fix A Broken Estate Plan

Trusts: Statutory nonjudicial modification

- Nonjudicial settlement agreements (75-7-110)
- Modification or termination of irrevocable trusts by consent if settlor living (75-7-411(1))
- Terminate uneconomic trusts (75-7-414(1))
- Combination and division of trusts (75-7-417)
- Revocation or amendment of revocable trusts (75-7-605)
- Decanting (no Utah statute)

How to Fix A Broken Estate Plan

Trusts: Document terms

- Power to revoke or amend
- Power of appointment
- Trust protector powers
- Trustee succession, removal, and appointment
- Combine, divide, and decant trusts
- Change trust situs and governing law
- Sell trust assets
- Disclaimers
- Trustee power to delay distributions
- Turn grantor trust powers on or off

How to Fix A Broken Estate Plan

Trusts: Common law or other powers

- UCA § 75-7-106: “The common law of trusts and principles of equity supplement this chapter, except to the extent modified by this chapter or laws of this state.”
- Decanting (Utah)
- Disclaimers

How to Fix A Broken Estate Plan

Wills: Statutory nonjudicial modification

- Revocation by writing or by act (75-2-507)
- Private agreements among successors (75-3-912)
- Spousal elective share (75-2-202)
- Premarital will (75-2-301)
- Omitted children (75-2-302)

How to Fix A Broken Estate Plan

Wills: Statutory judicial modification

- Will contest (75-3-402)
- Will construction (75-3-408)
- Venue for estate proceedings (75-3-201)
- Partition for purpose of distribution (75-3-911)

Wills: Other powers

- Disclaimers
- Asset sales

Underutilized Tools

- Nonjudicial Settlement Agreements
- Decanting

Nonjudicial Settlement Agreements

Uniform Trust Code comment:

While the Uniform Trust Code recognizes that a court may intervene in the administration of a trust ..., resolution of disputes by nonjudicial means is encouraged. This section facilitates the making of such agreements by giving them the same effect as if approved by the court.

Nonjudicial Settlement Agreement

75-7-110. Nonjudicial settlement agreements.

(1) 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.

(2) Except as otherwise provided in Subsection (3), interested persons may enter into a binding nonjudicial settlement agreement with respect to any matter involving a trust.

(3) 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 chapter or other applicable law.

Nonjudicial Settlement Agreement

75-7-110. Nonjudicial settlement agreements (cont.)

(4) Matters that may be resolved by a nonjudicial settlement agreement include:

- (a) the interpretation or construction of the terms of the trust;
- (b) the approval of a trustee's report or accounting;
- (c) direction to a trustee to refrain from performing a particular act or the grant to a trustee of any necessary or desirable power;
- (d) the resignation or appointment of a trustee and the determination of a trustee's compensation;
- (e) transfer of a trust's principal place of administration; and
- (f) liability of a trustee for an action relating to the trust.

(5) Any interested person may request the court to approve a nonjudicial settlement agreement, to determine whether the representation as provided in Part 3, Representation, was adequate, and to determine whether the agreement contains terms and conditions the court could have properly approved.

Nonjudicial Settlement Agreement

“Interested persons”

- Statute:

(1) 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.

- UTC comment:

Because of the great variety of matters to which a nonjudicial settlement may be applied, this section does not attempt to precisely define the “interested persons” whose consent is required to obtain a binding settlement.

- “Interested persons” depends on the matter
- Representation statutes under 75-7-301 et. seq. apply to bind certain classes of beneficiaries

Nonjudicial Settlement Agreement

“Interested persons”: Examples

- Modify noncharitable irrevocable trust if settlor not living: all of the beneficiaries
- Terminate uneconomic trusts: qualified beneficiaries and trustee
- UTC comment: “the consent of the trustee would ordinarily be required to obtain a binding settlement with respect to matters involving a trustee's administration, such as approval of a trustee's report or resignation.”

Nonjudicial Settlement Agreement

What can be modified?

- Statute

(2) Except as otherwise provided in Subsection (3), interested persons may enter into a binding nonjudicial settlement agreement with respect to any matter involving a trust.

(3) 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 chapter or other applicable law.

- “Material purpose” is not defined by the UTC or Utah statute, nor addressed in the UTC comments
- In general, the “material purpose” is the settlor’s intent in creating the trust

Nonjudicial Settlement Agreement

What can be modified?

- How to determine “material purpose”
 - If the settlor is living, the settlor may be able to clarify the purpose and sign the agreement to indicate the agreement doesn't violate the material purpose.
 - If settlor is not living, look to the provisions of the trust to determine settlor's intent
 - Practitioner note: document material purposes for trusts in files and working papers, especially if the settlor feels strongly about the purpose and the purpose is unique.

Nonjudicial Settlement Agreement

What can be modified?

- “Material purpose” examples:
 - Outright distributions to all children except spendthrift or irresponsible child
 - Trust for education of grandchildren and further descendants
 - Trust delays outright distribution to descendants until age 65 to provide for retirement “nest egg”
- “A spendthrift provision in the terms of the trust is not presumed to be a material purpose of the trust.” 75-7-411(3)

Nonjudicial Settlement Agreement

What can be modified?

- Subsection (4) includes a list of six matters that an agreement may address:
 - the interpretation or construction of the terms of the trust;
 - the approval of a trustee's report or accounting;
 - direction to a trustee to refrain from performing a particular act or the grant to a trustee of any necessary or desirable power;
 - the resignation or appointment of a trustee and the determination of a trustee's compensation;
 - transfer of a trust's principal place of administration; and
 - liability of a trustee for an action relating to the trust.
- UTC comment: "Subsection ([4]) is a nonexclusive list of matters to which a nonjudicial settlement may pertain."

Decanting

- Definitions
 - To pour (wine or other liquid) gently so as not to disturb the sediment
 - To pour (a liquid) from one container to another
- Practical application
 - Trustee transfers trust assets from one trust into a second trust with more favorable terms
 - Authority granted under the trust terms, state statute, or common law

Decanting

Statutory decanting

- 26 states have decanting statutes
- Utah doesn't have a decanting statute
- Neighboring states with decanting statute: Alaska, Arizona, Colorado, Nevada, South Dakota, Washington, Wyoming
- Decanting provisions not part of the UTC
- Uniform Trust Decanting Act: adopted in 5 states; introduced in 2 states

Decanting

Decanting under common law

- Cases argue that decanting is included in the trustee's broad discretionary power under common law.
- Cases:
 - *Phipps v. Palm Beach Trust Company*, 196 So. 299 (Fla. 1949)
 - *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)
 - *Morse v. Kraft*, 466 Mass. 92 (2013)
- These cases permitted the trustee to decant to a new trust through the exercise of a broad discretionary distribution power.

Decanting

Decanting authority under Restatements

- The Restatement (Second) of Property: Donative Transfers §§ 11.1, 19.4 states that unless the trust provides otherwise, the trustee's discretionary power to distribute trust property is akin to a power of appointment which includes the power to:
 - Make distributions in trust for permissible beneficiaries and
 - Create new powers of appointment over trust assets in favor of permissible appointees of the original power.
- The Restatement (Third) of Property (Wills and Other Donative Transfers) § 17.1 similarly supports this concept but does not treat the power to invade as a special power of appointment because the fiduciary obligations of a trustee.

Summary

- There are many tools available to fix a “broken” estate plan
- Some tools are more useful than others
- Use the tools wisely

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