

# Wine Not? California's New Decanting Act

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## Introduction

- What is decanting?
- Why decant?



# Decants versus Modifications



- Probate Code § 15403: Modification When Settlor is Deceased
  - All beneficiaries must consent.
  - Petition must be filed.
  - Court must determine, in its discretion, the reason for modifying under the circumstances outweighs the interest in accomplishing a material purpose of the trust.

## Decants versus Modifications Cont'd



- Probate Code § 15404: Modification When Settlor is Alive
  - No Petition required if the settlor *and* all beneficiaries consent.
  - If any beneficiary does not consent, the other beneficiaries may file a Petition, with the settlor's consent. Court may grant the Petition if the interests of the non-consenting beneficiary are not substantially impaired.
- Probate Code §§ 19501 et seq.: Decanting Act
  - Court approval not required.
  - Beneficiary and settlor approval not required.
  - Different legal standard in Court proceedings.

# History of Decanting

- More than half of the states have decanting statutes.
- Uniform Trust Decanting Act (UTDA)
- AB 1855
- SB 909



## Probate Code § 19505: Applicability to California Administered Trusts or Trusts Governed by California Law

- Applies to trusts created before, on, or after January 1, 2019 that:
  - Have their principal place of administration in California, or
  - Provide they are governed by California law for a) administration, or b) construction of trust terms, or c) determining the meaning or effect of terms of the trust.



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## **Probate Code §§ 19503, 19515, 19521, 19529: Scope of the Decanting Law**

- Applies to irrevocable trusts, or trusts revocable by the settlor only with the consent of the trustee or an adverse party.
- Does not apply to trusts held solely for charitable purposes. However, can apply to trusts with charitable interests.
- Does not limit the power of a trustee to distribute or appoint property in further trust or modify a trust.

## **Probate Code §§ 19503, 19515, 19521, 19529: Scope of the Decanting Law – Cont'd**

- Does not affect the settlor's ability to provide in a trust instrument for the distribution of trust property or appointment in further trust of property or for modification.
- Does not limit the trustee's ability to file a petition for instructions or approval under Probate Code § 17200, or a petition for modification under Probate Code § 15400.
- The decanting power may be exercised whether or not the trustee would have made, or could have been compelled to make, a discretionary distribution of principal at the time of the exercise.



## Probate Code §§ 19503, 19515, 19521, 19529: Scope of the Decanting Law – Cont'd

- Trustee cannot exercise decanting power to the extent the first trust expressly prohibits its exercise.
  - *However, a general prohibition of the amendment or revocation of a first trust, a spendthrift clause, or a clause restraining the voluntary or involuntary transfer of a beneficiary's interest does not preclude exercising the decanting power.*

## Probate Code §§ 19503, 19515, 19521, 19529: Scope of the Decanting Law – Cont'd

- Trustee's exercise of the decanting power is subject to any restriction in the first trust *expressly* applying to the decanting power.

## Probate Code § 19502: Common Defined Terms

- Authorized Fiduciary
- Beneficiary
- Decanting Power
- Qualified Beneficiary



## Probate Code § 19512: Decanting Under Limited Distributive Discretion



- “Limited distributive discretion” means a discretionary power of distribution that is limited to an ascertainable standard or a reasonably definite standard.
- The second trust or trusts, must grant each beneficiary of the first trust beneficial interests which are substantially similar to the beneficial interests of the beneficiary in the first trust.

## Probate Code § 19512: Decanting Under Limited Distributive Discretion – “Substantially Similar”

- “Substantially similar” means no material change (the distribution provisions cannot be more restrictive or more expansive) in a beneficiary’s beneficial interests, except:
  - The second trust may be created or administered under the law of any jurisdiction;
  - The beneficiary is under a legal disability or the trustee reasonably believes the beneficiary is incapacitated, and the distribution is made as permitted under this code; or
  - 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.

## Probate Code § 19512: Decanting Under Limited Distributive Discretion - Examples

First trust permits distributions for health, education, maintenance, and support. Second trust permits distribution for education and maintenance only. This is considered a material change and the beneficiary's interest in the second trust are not considered "substantially similar."



## Probate Code § 19512: Decanting Under Limited Distributive Discretion - Examples

- First trust permits distributions for education but does not define education. Second trust defines education to include “private or public primary, secondary, college, graduate, and post graduate study, as well as trade school or vocational training.” This change is considered to be “substantially similar” and not a material change.



## Probate Code § 19512: Decanting Under Limited Distributive Discretion - Examples

First trust requires that the trust principal be distributed outright to the beneficiary at age 35. The second trust gives the beneficiary the right to withdraw all or any portion of the trust principal, starting at age 35. This change is considered to be “substantially similar” and not a material change.





## Probate Code § 19512: Decanting Under Limited Distributive Discretion - Examples

First trust requires that the trust principal be distributed outright to the beneficiary at age 35. The second trust requires that the trust principal be distributed outright to the beneficiary at age 40. This is considered a material change and the beneficiary's interest in the second trust is not considered "substantially similar."



## Probate Code § 19512: Decanting Under Limited Distributive Discretion - Examples

First trust is a pot trust for the benefit of A, B, and C. The trustee has discretion to make principal distributions for the benefit of A, B, and C, subject to a HEMS standard and without a requirement to make equal distributions to the three beneficiaries. Three separate second trusts are created – one for the benefit of A, subject to a HEMS standard, one for the benefit of B, subject to the HEMS standard, and one for the benefit of C, subject to the HEMS standard.



## **Probate Code § 19512: Decanting Under Limited Distributive Discretion – Other Non-Material Changes**

- Fiduciary's administrative powers;
- Fiduciary investment powers; and
- Changes in a fiduciary.

## **Probate Code § 19511: Decanting Under 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.

# Probate Code § 19511: Decanting Under Expanded Distributive Discretion - Examples

Eliminate (but not add) one or more current beneficiaries

“Current beneficiary” means a beneficiary that on the date of the beneficiary’s qualification, the beneficiary is a distributee or permissible distributee of income or principal OR a holder of a presently exercisable general power of appointment.



## Probate Code § 19511: Decanting Under Expanded Distributive Discretion - Examples

Make a current beneficiary a presumptive remainder beneficiary or a successor beneficiary.

- First trust – principal and income distributions to Mom, in the trustee’s absolute discretion, for Mom’s life. At Mom’s death, distributions to Mom’s kids, by right of representation.
- Second trust – principal and income distributions to Mom’s kids, upon the death of Mom’s kids, distributions to Mom.

# Probate Code § 19511: Decanting Under Expanded Distributive Discretion - Examples

- Eliminate (but not add) one or more presumptive remainder and successor beneficiaries.
- Make a presumptive remainder beneficiary a successor beneficiary, or vice versa.
- Alter or eliminate rights that are not vested interests.
- Change the standard for distributions.
- Add or eliminate a spendthrift provision.
- Extend the duration of a trust (subject to § 19520).
- Change the jurisdiction of the trust and the law governing the administration of the trust (subject to § 19514(e)).
- Eliminate, modify or add powers of appointment.
- Change the trustee or trustee succession provisions.
- Change the powers of the trustee.
- Change administrative provisions of the trust.
- Add investment advisors, trust protectors or other fiduciaries.
- Divide a trust into more than one trust.
- Consolidate trusts.

## Probate Code § 19513: Decanting for a Beneficiary with a Disability

- If the first trust has a beneficiary with a disability, the trustee, as defined in the Decanting Act as a “special needs fiduciary,” may decant under expanded distributive discretion even if the trustee would otherwise be subject to limited distributive discretion.
- If decanting under “limited distributive discretion,” the second trust must grant each beneficiary (other than the beneficiary with a disability) of the first trust beneficial interests in the second trusts which are substantially similar to the beneficiary’s beneficial interests in the first trust.



## **Probate Code § 19513: Decanting with a Special Needs Beneficiary – Examples**

First trust was created by Grandma and provides for all income to be distributed to grandson at age 21 and provides that the trustee may distribute principal for health, education, maintenance, and support. Grandson has the right to withdraw the trust principal at age 30 and has a testamentary general power of appointment. Upon Grandson's death, any unappointed property is distributed to Grandma's descendants by right of representation. Grandson is 25 and disabled. The trustee may decant to a second trust that provides for distributions to Grandson in the trustee's absolute discretion and upon Grandson's death, the trust property is distributed to Grandma's descendants by right of representation.

## Probate Code § 19513: Decanting with a Special Needs Beneficiary – Examples

- Same facts as first example but Grandson is 31. The trustee may decant to a second trust with the same terms as in the first example.
- Same facts as above but the trustee has no discretion to distribute principal. The trustee may still decant to a second trust with the same terms as in the first example. Here, the trustee is considered a “special needs fiduciary.”

## **Probate Code § 19513: Decanting with a Special Needs Beneficiary – Examples**

Trust was created for the sole purposes of providing for the health care needs of the settlor's grandchildren. The trustee may not decant to a second trust to pay for the support of a settlor's grandchild with special needs.

## **Probate Code § 19513: Decanting with a Special Needs Beneficiary – Examples**

First trust was created by Grandma and requires that income be distributed to Grandchildren and permits principal distributions for the Grandchildren's health, education, maintenance, and support. One of the Grandchildren has special needs. The trustee may distribute part of the principal to a second trust for the sole benefit of the Grandchild with special needs and distribute the remaining principal to a second trust with the same terms as the first trust solely for the benefit of the non-special needs Grandchildren. Upon the death of the special needs Grandchild, his or her trust must be distributed to the second trust for the benefit of the other Grandchildren.

## Probate Code § 19519: Tax Limitations of Decanting

If the first trust:

- was created for a “tax benefit;”
- expressly indicates or is clearly drafted to enable the trust to qualify for the tax benefit; and
- actually qualified for the tax benefit.

the Decanting Act prohibits the second trust from including or omitting a term that, if included in or omitted from the first trust, would prevent qualification for the tax benefit.

## **Probate Code § 19519: Tax Limitations of Decanting – Marital Trusts**

- If a first trust contains property that qualified, or would have qualified for a marital deduction (federal or state), the second trust shall not include or omit any term that would have prevented the transfer from qualifying for or would have reduced the amount of the marital deduction.
- If a QTIP election was made for the first trust, the second trust may not contain provisions that would disqualify the trust for QTIP treatment and such qualification must be under the same section of the IRC that resulted in the marital deduction.

## **Probate Code § 19519: Tax Limitations of Decanting – Charitable Deduction**

If a first trust contains property that qualified, or would have qualified for a charitable deduction for purposes of the income, gift, or estate tax (federal or state), the second trust shall not include or omit any term that would have prevented the transfer from qualifying for or would have reduced the amount of the charitable deduction.

## **Probate Code § 19519: Tax Limitations of Decanting – Gift Tax Exclusion**

If the first trust contains property that qualified or would have qualified for the exclusion from gift tax, the second trust shall not include or omit a term that, if included in or omitted from the first trust would have prevented the transfer from qualifying under gift tax exclusion.



## **Probate Code § 19519: Tax Limitations of Decanting – Qualified Subchapter-S Trusts**

If the property of the first trust includes shares of stock in an S-corporation and the first trust is a permitted shareholder or if the first trust is a qualified subchapter-S trust, the second trust shall not include or omit a term that prevents the second trust from qualifying as a permitted shareholder or a qualified subchapter-S trust.

## **Probate Code § 19519: Tax Limitations of Decanting – GST Trusts**

If the first trust contains property that qualified or would have qualified for a zero inclusion ratio for purposes of the GST tax, the second trust shall not include or omit a term that, if included in or omitted from the first trust instrument, would have prevented the transfer to the first trust from qualifying for a zero inclusion ratio.

# Probate Code § 19519: Tax Limitations of Decanting – Grantor Trusts

If the first trust is a grantor trust under IRC § 672(f)(2)(A),  
the second trust must be a grantor trust under IRC § 672(f)(2)(A).

If the first trust is a grantor trust under IRC § § 671, 673 - 677, or 679,  
the second trust may be a non-grantor trust.

If the first trust and second trust are grantor trusts, and  
the first trust grants the settlor or another person the power to turn off grantor trust status but the second trust does not,  
the trustee may not exercise the decanting power, if the settlor objects to the decanting.

If the first trust is a non-grantor trust,  
the second trust may be a grantor trust if:

- (i) the settlor has the power to turn off grantor trust treatment in the second trust; or
- (ii) the first and second trusts contain a provision granting the settlor or another person a power to turn off grantor trust status.

## Probate Code § 19504: Trustees are Bound by Their Fiduciary Duties

- Trustees must act in accordance with their fiduciary duties, including in accordance with the purpose of the trust.
- The purpose of decanting is not to disregard the settlor's intent, but to modify the trust to better effectuate the settlor's probable intent if the settlor had anticipated the circumstances at the time of the decanting.
- Trustees have no actual or implied duty to decant, or to inform the beneficiaries of the decanting power.
- Unless the first trust provides otherwise, the terms of the first trust are deemed to include the decanting power.

## Probate Code § 19507: Notice of the Proposed Decanting Exercise

- Trustee may exercise the decanting power without the consent of any person and without court approval.
- BUT, before exercising the decanting power, the trustee SHALL give notice of the intended decanting exercise not later than 60 days before the exercise.

# Probate Code § 19507: Notice of the Proposed Decanting Exercise Cont'd

- Who must receive notice of the intended decanting exercise?
  - Settlor
  - “Qualified Beneficiaries”
  - Holders of presently exercisable powers of appointment
  - Persons who currently have the right to remove or replace the trustee
  - Each trustee of the first trust
  - Each proposed trustee of the second trust
  - Attorney General where charitable interests are involved

## Probate Code § 19507: Notice of the Proposed Decanting Exercise Cont'd

- Qualified beneficiaries who are minors, and unborn/unascertained persons:
  - Notice must be provided to a guardian ad litem.
  - If there is no guardian ad litem, the trustee shall seek the appointment of a guardian ad litem.
  - The Court may appoint a guardian ad litem for purposes of this section, where the only matter before the Court is that appointment.

## Probate Code § 19507: Notice of the Proposed Decanting Exercise Cont'd

- Persons who are substantially unable to manage their financial resources or resist fraud and undue influence:
  - If the trustee knows, or has reason to know, that a person entitled to notice is substantially unable to manage his or her financial resources or resist fraud or undue influence, the trustee shall give notice to that person, as well as to the individual appointed to act on behalf of that person, i.e., an attorney-in-fact under a power of attorney.
  - If no such individual is appointed to act, the trustee shall seek the appointment of such individual.
  - The Court may appoint a guardian ad litem for purposes of this section, where the only matter before the Court is that appointment.



## **Probate Code § 19508: Notice on Agents or Representatives of Incapacitated Persons**

- Notice to a person with authority to represent and bind another person has the same effect as notice given directly to the person represented.
- Consent or waiver by a person with authority to represent and bind another person is binding on the person represented, unless the person represented objects to the representation before the consent or waiver becomes effective.
- Settlor may not represent or bind a beneficiary.

## **Probate Code § 19507(g): Contents of Written Notice of the Proposed Decanting Exercise**

- Must include a description of the manner in which the trustee intends to exercise the decanting power.
- Must include the trustee's reason for the decanting.
- Must include an explanation of the differences between the first trust and second trust or trusts.
- Must include the proposed effective date for the exercise of the decanting power.

## Probate Code § 19507(g): Contents of Written Notice of the Proposed Decanting Exercise Cont'd

- Must include a copy of the first trust.
- Must include a copy of the second trust.
- Must include the following warning, in a separate paragraph, in not less than 10 point bold font:

**“If you do not bring a court action to contest the proposed trust decanting (the proposed changes to the trust) within 59 days of this notice, you will lose your right to contest the decanting.”**

## **Probate Code § 19510: Written Exercise of the Decanting Power**

- Upon expiration of the notice period, the trustee shall exercise the decanting power in a signed writing.
- The signed writing shall identify the first trust and second trust or trusts, and state the property of the first trust being distributed to each second trust, and the property that remains in the first trust, if any.

## Probate Code § 19514: Decanting with Charitable Trusts

- If a first trust contains a determinable charitable interest, the Attorney General has the rights of a qualified beneficiary and may represent and bind the charitable interest.
  - If under a split interest trust (e.g., Charitable Lead Annuity Trust or Charitable Remainder Trust), the trustee does not have discretion to distribute principal to a current beneficiary, there is no authorized fiduciary and thus no ability to decant.

## Probate Code § 19514: Decanting with Charitable Trusts Cont'd

If a first trust contains a charitable interest, the second trust or trusts may not do any of the following:

- Diminish the charitable interest;
- Diminish the interest of an identified charitable organization that holds the charitable interest;
- Alter any charitable purpose stated in the first trust instrument; or
- Alter any condition or restriction related to the charitable interest.

## Probate Code § 19514: Decanting with Charitable Trusts Cont'd

- If a first trust contains a determinable charitable interest, the second trust or trusts that include a charitable interest shall be administered under California law unless any of the below occur.
  - The Attorney General, after receiving notice under Section 19507, fails to object in a signed writing delivered to the authorized fiduciary within the notice period.
  - The Attorney General consents in a signed writing to the second trust or trusts being administered under the law of another jurisdiction.
  - The court approves the exercise of the decanting power.

## Probate Code § 19507(i): Is Written Notice Enough to Protect the Trustee?

- Despite receiving notice and allowing the notice period to expire, or despite waiving notice, a person may still file a petition asserting the exercise of the decanting power is ineffective because:
  - The exercise did not comply with this part.
  - The exercise was an abuse of the trustee's discretion.
  - The exercise was a breach of the trustee's fiduciary duties.
  - Probate Code § 19522 applies.



## Probate Code § 19509: Decanting Petitions

- Persons with standing are trustees, and anyone entitled to notice.
- Burden of proof is on the trustee to establish:
  - Notice was given under Probate Code § 19507, and
  - He/she may exercise the decanting power.

## Probate Code § 19509: Decanting Petitions Cont'd

- Petitions may be brought to:
  - Instruct the trustee whether a proposed exercise is permitted and consistent with his or her fiduciary duties.
  - Appoint a special fiduciary and authorize the special fiduciary to determine whether the decanting power should be exercised, and to exercise the decanting power.
  - Approve an exercise of the decanting power.

## Probate Code § 19509: Decanting Petitions Cont'd

- Determine that a proposed or attempted exercise is ineffective a) under Probate Code § 19522, or b) because it would be or was an abuse of discretion or a breach of fiduciary duty.
- Determine the extent to which Probate Code § 19522 applies to a prior exercise of the decanting power.
- Provide instructions to the trustee regarding the application of Probate Code § 19522 to a prior exercise.
- Order other relief to carry out the purposes of this part.

## Probate Code § 19525: Who is the Settlor?

- A settlor of the first trust is deemed to be the settlor of the second trust.
- However, in determining the settlor's intent with respect to a second trust, the Court may consider the intent of the settlor of the first trust, the intent of the settlor of the second trust, and the intent of any other authorized fiduciary.

# Probate Code § 19516: Increasing Fiduciary Compensation

- First trust specifies the trustee's compensation:
  - Trustee cannot exercise the decanting power to increase his or her compensation unless a) all beneficiaries of the second trust consent to the increase in a signed writing, or 2) the increase is approved by the Court.
- First trust does not specify the trustee's compensation:
  - Trustee cannot exercise the decanting power to increase his or her compensation above the compensation permitted under the Probate Code unless a) all beneficiaries of the second trust consent to the increase in a signed writing, or b) the increase is approved by the Court.

## Probate Code § 19516: Increasing Fiduciary Compensation Cont'd

- A change in the trustee's compensation which is incidental to other changes made by the exercise of the decanting power is not an increase in the trustee's compensation. An incidental change includes, but is not limited to:
  - An increase in compensation because the second trust lasts longer than the first trust.
  - An increase in compensation because the second trust has a greater value than the first trust.

## Probate Code § 19518: Removal or Replacement of Fiduciaries

- Trustee cannot exercise the decanting power to modify a provision in the trust granting another person the power to remove or replace the trustee unless:
  - The person holding the power consents to the modification in a signed writing and the modification applies only to that person, or

## Probate Code § 19518: Removal or Replacement of Fiduciaries

- The person holding the power and the beneficiaries of the second trust consent in a signed writing, and the modification grants substantially similar power to another person, or
- The Court approves the modification and the modification grants a substantially similar power to another person.



## Probate Code § 19517: Liability and Indemnification

- The second trust cannot relieve the trustee from liability for breach of trust to a greater extent than the first trust.
- The second trust may 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.
- The second trust may not reduce the trustee's liability in the aggregate, but may reallocate fiduciary powers among fiduciaries.

## Probate Code § 19520: Duration of Second Trust

- Second trust may have a duration that is the same as, or different from, the first trust.
- To the extent property of the second trust is attributable to property of the first trust, the property of the second trust is subject to any rules governing maximum perpetuity, accumulation, or suspension of the power of alienation that apply to property of the first trust.

## Probate Code § 19522: Savings Statute

- If the second trust does not comply with this part because a particular provision in the second trust is not permitted, such provision is void, but the remaining provisions of the second trust are effective.
- If the second trust does not comply with this part because a provision required by this part is missing, such missing provision is deemed to be included in the second trust to the extent necessary.
- If the trustee determines either of these provisions apply, the trustee shall take corrective action consistent with his or her fiduciary duties.

## Probate Code § 19523: Animal Trusts

- With respect to animal trusts, a protector is a person appointed to enforce the trust on behalf of the animal, or appointed by the Court for that purpose. The protector has the rights of a beneficiary.
- Animal trusts can be decanted if the protector consents in writing to the exercise.

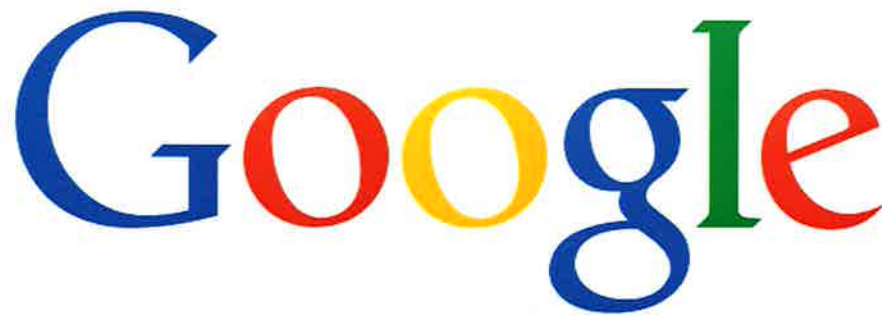
## Probate Code § 19526: Later Discovered Trust Property

- If the decanting exercise was intended to distribute all of the principal of the first trust to one or more second trusts:
  - Later discovered property is part of the trust estate of the second trust or trusts.
- If the decanting exercise was intended to distribute less than all of the principal of the first trust to one or more second trusts:
  - Later discovered property belonging to the first trust remains part of the first trust estate.
- Trustee may provide in the exercise of the decanting power, or by the terms of the second trust, for the disposition of later-discovered property.

## Probate Code § 19527: Debts

- Debts, liabilities, and obligations enforceable against the assets of the first trust are enforceable to the same extent against the assets of the second trust.

## A Great Resource



- Search: “Uniform Trust Decanting Act”
- On the Uniform Law Commission decanting page, download the PDF titled: “Final Act”
- You want the PDF with the comments

# The End



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