

A DELAWARE TRUST LAW PRIMER

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I. STATE INCOME AND TRANSFER TAXATION

A. Introduction

Delaware has a personal income tax,¹ which applies to resident individuals,² nonresident individuals,³ resident estates,⁴ nonresident estates,⁵ resident trusts,⁶ and nonresident trusts.⁷ In 2015, the top rate is 6.60% on taxable income over \$60,000.⁸

Delaware's estate tax⁹ was reinstated in 2009,¹⁰ made permanent early in 2013,¹¹ and amended later that year.¹² It applies to resident estates¹³ and to nonresident estates.¹⁴ In 2015, the exemption amount is \$5,430,000.¹⁵ Rates range from 0% on the first \$40,000 of the Delaware taxable estate to 16.0% on the excess of the Delaware taxable estate over \$10,040,000.¹⁶ Portability of a deceased spouse's unused applicable credit amount¹⁷ and a qualified-terminable-interest-property

¹ 30 Del. C. § 1101, *et seq.* Tax forms and reference materials are [available at www.revenue.delaware.gov](http://www.revenue.delaware.gov).

² 30 Del. C. § 1105.

³ 30 Del. C. § 1121.

⁴ 30 Del. C. §§ 1631, 1635.

⁵ 30 Del. C. §§ 1631, 1639.

⁶ 30 Del. C. §§ 1631, 1635.

⁷ 30 Del. C. §§ 1631, 1639.

⁸ 30 Del. C. § 1102(a)(14).

⁹ 30 Del. C. §§ 1501–1507

¹⁰ 77 Del. Laws 85, § 1 (2009).

¹¹ 79 Del. Laws 11, § 1 (2013).

¹² 79 Del. Laws 162, § 1 (2013).

¹³ 30 Del. C. § 1502(c). The resident return may be viewed at www.revenue.delaware.gov/services/current_pit/TY14_900re.pdf (last visited Oct. 14, 2015).

¹⁴ 30 Del. C. § 1504. The nonresident return also may be viewed at www.revenue.delaware.gov/services/current_pit/TY14_900nre.pdf (last visited Oct. 14, 2015).

¹⁵ See 30 Del. C. § 1501(3)(c); Rev. Proc. 2014-61 § 3.33, 2014-47 IRB 860, 867 (Nov. 17, 2014).

¹⁶ 30 Del. C. § 1502(c).

¹⁷ See 30 Del. C. § 1501(3)(c); Internal Revenue Code (“IRC”) § 2010(c).

(“QTIP”) election independent of any federal election are available.¹⁸ The return and the tax are due nine months after the date of death.¹⁹

Delaware’s gift tax was repealed on January 1, 1998,²⁰ and its inheritance tax was repealed on January 1, 1999.²¹ Delaware never has imposed a generation-skipping transfer (“GST”) tax.

B. Personal Income Tax—Individuals

1. General Rule

a. Introduction

Delaware defines “resident individual” as follows:²²

A resident individual of this State means an individual:

- (1) Who is domiciled in this State to the extent of the period of such domicile; . . . ;
or
- (2) Who maintains a place of abode in this State and spends in the aggregate more than 183 days of the taxable year in this State.

A “nonresident individual” is an individual “who is not a resident individual of this State.”²³

b. Domiciliaries

As shown above, a domiciliary of Delaware is taxed as a resident individual so long as he or she remains a domiciliary. The tax return instructions define “domicile” in the following manner:²⁴

¹⁸ 30 Del. C. § 1501(4)(d).

¹⁹ 30 Del. C. § 1505(b), (c).

²⁰ 71 Del. Laws 130, § 1 (1997).

²¹ 71 Del. Laws 353, § 10 (1998).

²² 30 Del. C. § 1103. See instructions to 2014 Del. Form 200-01 at 2; instructions to 2014 Del. Form 200-02 NR at 2. The resident return may be viewed at www.revenue.delaware.gov/services/current_pit/TY14_booklet_res.pdf (last visited Oct. 14, 2015); the nonresident return may be viewed at www.revenue.delaware.gov/services/current_pit/TY14_booklet_nr.pdf (last visited Oct. 14, 2015).

²³ 30 Del. C. § 1104.

²⁴ Instructions to 2014 Del. Form 200-01 at 2. See instructions to 2014 Del. Form 200-02 NR at 2.

A domicile is the place an individual intends to be his permanent home. An individual can have only one domicile. A domicile, once established, continues until the individual moves to a new location and exhibits a bona fide intention of making it his or her permanent home.

c. Nondomiciliaries

An individual who maintains a permanent place of abode in Delaware may be taxed as a resident individual even though domiciled elsewhere.²⁵ Thus, a nondomiciliary is taxed as a resident individual if he or she:

- Maintains a place of abode in Delaware; and
- Spends more than 183 days in the state during the taxable year.²⁶

Conversely, a nondomiciliary is not taxed as a resident individual if he or she:

- Does not maintain a place of abode in Delaware (even if he or she spends more than 183 days in the state during the taxable year); or
- Spends less than 184 days in Delaware during the taxable year (even if he or she has a place of abode in the state).²⁷

The term “place of abode” is not defined.

2. Specific Situations

a. Introduction

The tax law and the tax return instructions describe four specific situations in which individuals will not be treated as residents.

b. Individuals Living Abroad

²⁵ 30 Del. C. § 1103.

²⁶ 30 Del. C. § 1103.

²⁷ See 30 Del. C. § 1103.

A Delaware statute offers the following guidance for individuals living overseas:²⁸

[A]n individual who is present in a foreign country or countries for at least 495 full days in any consecutive 18-month period, and during such period of 18 consecutive months is not present in this State for more than 45 days, and does not maintain a permanent place of abode in this State at which the individual's spouse, children or parents are present for more than 45 days, and is not an employee of the United States, its agencies or instrumentalities (including members of the Armed Forces) shall not be considered a resident of this State during such period . . .

c. Students

The tax return instructions provide the following guidelines for students:²⁹

Full-time students with a legal residence in another state remain legal residents of that state unless they exhibit intentions to make Delaware their permanent residence.

d. Members of the Armed Forces and Their Spouses

The tax return instructions give rules for members of the armed forces³⁰ and for their spouses.³¹

e. Decedent's Final Return

The tax return instructions provide that the executor, administrator, or other person responsible for the property of a decedent should file the decedent's final return.³²

²⁸ 30 Del. C. § 1103(1). See instructions to 2014 Del. Form 200-01 at 2; instructions to 2014 Del. Form 200-02 NR at 2.

²⁹ Instructions to 2014 Del. Form 200-01 at 2. See instructions to 2014 Del. Form 200-02 NR at 2.

³⁰ See instructions to 2014 Del. Form 200-01 at 4; instructions to 2014 Del. Form 200-02 NR at 4.

³¹ See instructions to 2014 Del. Form 200-01 at 4; instructions to 2014 Del. Form 200-02 NR at 4.

³² Instructions to 2014 Del. Form 200-01 at 2; instructions to 2014 Del. Form 200-02 NR at 2. See instructions to 2014 Del. Form 200-01 at 12; instructions to 2014 Del. Form 200-02 NR at 9.

3. Cases, Regulations, and Rulings

Delaware has no pertinent caselaw,³³ regulations, or rulings.

4. Guidance for Becoming or Ceasing to Be Resident/Domiciliary

Except as noted above, Delaware gives no guidance on how an individual becomes or stops being a resident or domiciliary for personal-income-tax purposes.

C. Personal Income Tax—Estates

1. General Rule

A statute defines “resident estate” as follows:³⁴

“Resident estate” means the estate of a decedent who at death was domiciled in this state.

A “nonresident estate” is “an estate that is not a resident estate.”³⁵

Note that Delaware only taxes estates of domiciliaries as residents. Estates of nondomiciliaries who had a place of abode in Delaware and spent more than 183 days in the state during the tax year are not so treated.

2. Cases, Regulations, and Rulings

Delaware has no relevant caselaw, regulations, or rulings.

D. Personal Income Tax—Trusts

1. General Rule

Delaware defines “resident trust” as follows:³⁶

“Resident trust” means a trust:

³³ See McGinnes v. State Farm Mut. Auto Ins. Co., 2013 Del. Super Lexis 414 at 8–9 (Del. Super. 2013) (quoting statute in nontax case); Williamson v. Std. Fire Ins. Co., 2005 Del. Super. Lexis 281 at 13 (Del. Super. 2005) (same); Capano v. Dir. of Revenue, 2002 Del. Super. Lexis 183 at 12 (Del. Super. 2002) (paraphrasing but not applying statute in tax case).

³⁴ 30 Del. C. § 1601(7). See 2014 Del. Form 400-I at 2. The form may be viewed at www.revenue.delaware.gov/services/current_pit/TY14_400i.pdf (last visited Oct. 14, 2015).

³⁵ 30 Del. C. § 1601(4). See 2014 Del. Form 400-I at 2.

³⁶ 30 Del. C. § 1601(8). See 2014 Del. Form 400-I at 2.

- a. Created by the will of a decedent who at death was domiciled in this State;
- b. Created by, or consisting of property of, a person domiciled in this State; or
- c. With respect to which the conditions of 1 of the following paragraphs are met during more than 1/2 of any taxable year:
 1. The trust has only 1 trustee who or which is:
 - A. A resident individual of this State, or
 - B. A corporation, partnership or other entity having an office for the conduct of trust business in this State;
 2. The trust has more than 1 trustee, and 1 of such trustees is a corporation, partnership or other entity having an office for the conduct of trust business in this State; or
 3. The trust has more than 1 trustee, all of whom are individuals and 1/2 or more of whom are resident individuals of this State.

A “nonresident trust” is a “trust that is not a resident trust of this State.”³⁷

Note that taxation under (a) and (b) above is based on domicile, whereas taxation under (c) above turns on whether an individual is a resident. Hence, a trust might be treated as a resident trust even if an individual trustee is domiciled elsewhere.

2. Nonresident Beneficiary Deduction

Delaware allows resident trusts to deduct taxable income set aside for future distribution to nonresidents as follows:³⁸

A resident . . . trust shall be allowed a deduction against the taxable income otherwise computed under Chapter 11 of this title for any taxable year for the amount of its federal taxable income, as

³⁷ 30 Del. C. § 1601(5). See 2014 Del. Form 400-I at 2.

³⁸ 30 Del. C. § 1636(a).

modified by § 1106 of this title which is, under the terms of the governing instrument, set aside for future distribution to nonresident beneficiaries.

Delaware determines the residency of all unknown or unascertained beneficiaries based on the residences of relevant existing beneficiaries on the last day of the tax year.³⁹ The combination of Delaware’s small population (about 900,000 according to the 2010 census) and this favorable rule for determining the residences of future beneficiaries means that few trusts created by nonresidents pay Delaware income tax. If this deduction covers all taxable income, which often is the case, the trustee does not have to file a return.⁴⁰

3. Cases, Regulations, and Rulings

Delaware has no pertinent caselaw, regulations, or rulings.⁴¹

E. Estate Tax

1. General Rule

The Delaware estate tax applies to “the transfer of the property of every decedent who was a resident of this State at the time of death”⁴² and to “the transfer of the estate of every decedent who, at the time of death, was a nonresident of this State and owned real or tangible personal property situated in this State” that was subject to federal estate tax.⁴³ The terms “resident estate” and “nonresident estate” are not defined. I understand that the decedent’s domicile is determinative.

2. Cases, Regulations, and Rulings

Delaware has no relevant caselaw, regulations, or rulings.

II. MODIFICATION OF TRUSTS

A. Peierls Decisions

1. Introduction

³⁹ 30 Del. C. § 1636(b).

⁴⁰ 30 Del. C. § 1605(b)(1)(a).

⁴¹ See In re Trust Under Agreement of Christopher L. Ward, 2001 Del. Ch. Lexis 158 at 4–5 (Del. Ch. 2001) (“solely for [state income] tax reasons, the situs of the trusts was being transferred to New Jersey”).

⁴² 30 Del. C. § 1502(a).

⁴³ 30 Del. C. § 1504(a).

On October 4, 2013, the Supreme Court of Delaware issued the following three decisions involving Peierls family trusts:

- In re Ethel F. Peierls Charitable Lead Unitrust (“Peierls I”⁴⁴)
- In re Peierls Family Inter Vivos Trusts (“Peierls II”⁴⁵)
- In re Peierls Family Testamentary Trusts (“Peierls III”⁴⁶)

Among other things, Peierls III confirmed that Delaware courts follow the Second Restatement of Conflict of Laws (“Restatement”) on whether a Delaware court has and should exercise jurisdiction in a matter involving a trust⁴⁷ and Peierls II confirmed that Delaware courts consult the Restatement to determine when Delaware law applies.⁴⁸

2. Whether a Delaware Court Has and Should Exercise Jurisdiction

In Peierls III, the Supreme Court of Delaware had to decide whether Delaware courts had and should exercise jurisdiction over seven testamentary trusts created by members of the Peierls family. After noting that these questions should be resolved under Restatement § 267,⁴⁹ it found that Delaware courts did possess jurisdiction⁵⁰ for the following reason:⁵¹

[A]ll interested parties consented to the Court of Chancery’s jurisdiction: Trustees Brian and Jeffrey filed the Petitions in the Court of Chancery; the beneficiaries provided written consents to the court’s jurisdiction; Northern Trust is a Delaware entity; and Bank of America (corporate successor to U.S. Trust Co.), though not subjecting itself to jurisdiction, filed written acknowledgment of its removal as corporate trustee. Having obtained jurisdiction over the trustees, the Court of Chancery

⁴⁴ In re Ethel F. Peierls Charitable Lead Unitrust, 77 A.3d 232 (Del. 2013) (Peierls I).

⁴⁵ In re Peierls Family Inter Vivos Trusts, 77 A.3d 249 (Del. 2013) (Peierls II).

⁴⁶ In re Peierls Family Testamentary Trusts, 77 A.3d 223 (Del. 2013) (Peierls III)

⁴⁷ Peierls III, 77 A.3d 223, 227 (“In cases such as these where a trust maintains contacts with multiple states, we prefer to consult the Restatement (Second) of Conflict of Laws to resolve the issue of jurisdiction.”).

⁴⁸ Peierls II, 77 A.3d 249, 255 (“When confronted with a choice-of-law issue, Delaware courts adhere to the Restatement (Second) of Conflict of Laws.”).

⁴⁹ Restatement (Second) of Conflict of Laws § 267 (1971).

⁵⁰ Peierls III, 77 A.3d 223, 227.

⁵¹ Peierls III, 77 A.3d 223, 228 (footnote omitted).

had jurisdiction to adjudicate issues of administration of the Trusts under the Restatement.

The court then turned to the question of whether Delaware courts should exercise jurisdiction in the circumstances. It first observed:⁵²

Distinct from whether the Court of Chancery had jurisdiction to evaluate the Petitions is the issue of whether the Vice Chancellor should have exercised jurisdiction to do so. This question is largely one of which court has primary supervision over the Trusts. One indication that a particular court has primary supervision over the administration of a trust is if the trustee is required to render regular accountings in the court in which he has qualified. If the court in which the trustee has qualified does not exercise active control over the administration of the trust, then the court of the place of administration may exercise primary supervision. A court having primary supervisory power has and will exercise jurisdiction as to all questions which may arise in the administration of a trust.

Referring to comment e under § 267,⁵³ the court continued:⁵⁴

The Restatement further recognizes the need to “promote comity and respect for other states’ laws”:

A court of a state other than that of the testator’s domicile or that in which the trust is to be administered will not exercise jurisdiction if to do so would be an undue interference with the supervision of the trust by the court which has primary supervision. Whether there is such interference depends on the relief sought. Thus, if a court acquires jurisdiction over the trustee it may entertain a suit to compel him to redress a breach of trust, even though the trustee has qualified as trustee in a court of another state or the administration of the trust is in another state. It may compel the trustee to render an

⁵² Peierls III, 77 A.3d 223, 228 (internal quotation marks and footnotes omitted).

⁵³ Restatement (Second) of Conflict of Laws § 267 cmt. e (1971).

⁵⁴ Peierls III, 77 A.3d 223, 228 (footnotes omitted; emphasis in original).

accounting or it may even remove the trustee. On the other hand, it will ordinarily decline to deal with questions of construction or validity or administration of the trust, leaving these matters to be dealt with by the court of primary supervision. Thus, it will not ordinarily give instructions to the trustee as to his powers and duties.

3. Whether Delaware Law Applies

In Peierls II, the Supreme Court of Delaware confirmed that Delaware courts should look to the Restatement to resolve conflict-of-laws issues in trust matters.⁵⁵ It first considered the applicability of the following Delaware statute:⁵⁶

Except as otherwise expressly provided by the terms of a governing instrument or by court order, the laws of this State shall govern the administration of a trust while the trust is administered in this State.

The court found that the statute was inapplicable for the following reason:⁵⁷

Notably, the statute imposes a precondition upon its application—namely that the trust “[be] administered” in Delaware. The Petitions in part seek orders approving the resignation of the current trustees—resignations that are conditioned on judicial approval—and the appointment of a successor trustee, whose acceptance is also conditioned on judicial approval. Because the current trustees have not actually resigned and the successor trustee has not yet assumed its role, the Trusts are not yet “in Delaware” for purposes of deciding whether to permit a transfer of administration and a change in the law of administration. Accordingly, Section 3332(b) is not yet applicable. We, therefore, must look to our conflict-of-laws jurisprudence to determine whether

⁵⁵ Peierls II, 77 A.3d 249, 255.

⁵⁶ 12 Del. C. § 3332(b) (emphasis added).

⁵⁷ Peierls II, 77 A.3d 249, 256.

a Delaware court can exercise jurisdiction over and approve the Peierls' Petitions.

The court then turned to identifying issues that constitute matters of administration under the Restatement.⁵⁸ It said:⁵⁹

Section 272 of the Restatement specifically addresses which state's law governs the administration of inter vivos trusts. Section 272's Comment a directs us to Section 271's Comment a (which discusses testamentary trusts) to determine what matters are administrative in nature. Administrative matters are those matters which relate to the management of the trust, including a trustee's powers, the liabilities a trustee may incur for breach of trust, what constitutes a proper investment, a trustee's compensation and indemnity rights, a trust's terminability, and, importantly, a trustee's removal and successor trustees' appointment.

The court continued:⁶⁰

We note that the Peierls' Petitions seek to change the existing trustees; declare that Delaware is the Trusts' situs and that Delaware law governs administrative matters; modify the Trusts' provisions to allow for particular management changes under the Delaware trust statutes; and accept jurisdiction over the Trusts. All of these are administrative matters. Accordingly, we must determine which state's law governs the Trusts' administrative provisions to determine whether the Vice Chancellor properly denied the Petitions.

Regarding whether the law that governs the administration of a trust changes upon the change of trustee, the court said:⁶¹

A trust instrument may expressly authorize a change in the law governing administration of the

⁵⁸ Peierls II, 77 A.3d 249, 256.

⁵⁹ Peierls II, 77 A.3d 249, 256 (footnotes and internal quotation marks omitted).

⁶⁰ Peierls II, 77 A.3d 249, 256–57.

⁶¹ Peierls II, 77 A.3d 249, 259 (footnotes and internal quotation marks omitted; emphasis added).

trust. The trust instrument may also implicitly authorize the change, such as when the trust instrument contains a power to appoint a trustee in another named state. As the Restatement notes, even a simple power to appoint a successor trustee may be construed to include a power to appoint a trust company or individual in another state. Whether the trust instrument expressly or implicitly authorizes a change in the trust's administrative governing law, the law governing the administration of the trust thereafter is the local law of the other state and not the local law of the state of original administration. That rule applies even when the trust instrument contains a choice-of-law provision. Therefore, when a settlor does not intend his choice of governing law to be permanent and the trust instrument includes a power to appoint a successor trustee, the law governing the administration of the trust may be changed.

4. Implications

For present purposes, the three Peierls decisions have the following two implications. First, a Delaware trustee must actually be in office for a Delaware court to adjudicate a trust matter. Second, unless the governing instrument specifies that the law of another state applies in all circumstances, Delaware law will govern the administration of a trust once a Delaware corporate trustee is in place. This means that a Delaware directed trust, "silent trust," unitrust, or other arrangement might become available.

B. Current Methods for Modifying Trusts

Absent a mechanism in the governing instrument, Delaware attorneys consider four ways of modifying trusts to add a direction investment adviser or to make other changes. In order of preference, they are by merger, by decanting, by a nonjudicial settlement agreement, or by a consent-petition proceeding in the Court of Chancery. Each is described briefly below. Before embarking on a modification, the attorney must consider its federal transfer-tax implications, particularly under the federal GST tax.⁶²

C. Merger

⁶² See Reg. § 26.2601-1(b)(4)(i); Internal Revenue Service ("IRS") Notice 2011-101.

The default powers given to Delaware trustees include authority to:⁶³

Declare one or more new trusts for the purpose of merging all, or a portion, of an existing trust or trusts with and into the new trust or trusts and to merge any 2 or more trusts, including statutory trusts and foreign statutory trusts as defined in § 3801 of this title, whether or not created by the same trustor and whether or not funded prior to the merger, to be held and administered as a single trust if such a merger would not result in a material change in the beneficial interests of the trust beneficiaries, or any of them, in the trust

Thus, if a direction investment adviser is desired, the trustor might execute a new trust having identical dispositive provisions to the original trust but incorporating the adviser clause. The trustee might then merge the old trust into the new trust.

D. Decanting

Delaware's decanting statute, which originally was enacted in 2003, generally provides:⁶⁴

(a) Unless the terms of the instrument expressly provide otherwise, a trustee who has authority (whether acting at such trustee's discretion or at the direction or with the consent of an adviser), under the terms of a testamentary instrument or irrevocable inter vivos trust agreement (including a trust that, by its terms, is revocable but was created by a settlor who presently lacks the capacity to revoke the trust), to invade the principal or income or both of a trust (the "first trust") to make distributions to, or for the benefit of, 1 or more proper objects of the exercise of the power, may instead exercise such authority (whether acting at such trustee's discretion or at the direction or with the consent of an adviser, as the case may be) by appointing all or part of such principal or income or both as is subject to the power in favor of a trustee of a trust (the "second trust") under an instrument other than that under which the power to invade is

⁶³ 12 Del. C. § 3325(29), as amended by 80 Del. Laws 153, § 3 (2015).

⁶⁴ 12 Del. C. § 3528(a), as amended by 80 Del. Laws 153, § 4 (2015).

created or under the same instrument, provided, however, that, except as otherwise provided in this subsection (a):

- (1) The exercise of such authority is in favor of a second trust having only beneficiaries who are proper objects of the exercise of the power except that the governing instrument of the second trust may provide that, at a time or upon an event specified in the governing instrument, the remaining trust assets shall thereafter be held for the benefit of the beneficiaries of the first trust upon terms and conditions concerning the nature and extent of each such beneficiary's interest that are substantially identical to the first trust's terms and conditions concerning such beneficial interests;
- (2) In the case of any trust, contributions to which have been treated as gifts qualifying for the exclusion from gift tax described in § 2503(b) (26 U.S.C. § 2503(b)) of the Internal Revenue Code of 1986 (26 U.S.C. § 1 et seq.) (hereinafter referred to in this section as the "I.R.C."), by reason of the application of I.R.C. § 2503(c) (26 U.S.C. § 2503(c)), the governing instrument for the second trust shall provide that the beneficiary's remainder interest shall vest and become distributable no later than the date upon which such interest would have vested and become distributable under the terms of the governing instrument for the first trust;
- (3) The exercise of such authority does not reduce any income or unitrust interest of any beneficiary of a trust for which a marital deduction has been taken for federal tax purposes under I.R.C. § 2056 or § 2523 (26 U.S.C. § 2056 or § 2523) or for state tax purposes under any comparable provision of applicable state law; and
- (4) The exercise of such authority does not apply to trust property subject to a

presently exercisable power of withdrawal held by a trust beneficiary who is the only trust beneficiary to whom, or for the benefit of whom, the trustee has authority to make distributions.

Notwithstanding the foregoing provisions of this subsection (a), the governing instrument for the second trust may grant a power of appointment (including a power to appoint trust property to the powerholder, the powerholder's creditors, the powerholder's estate, the creditors of the powerholder's estate or any other person, whether or not such person is a trust beneficiary) to 1 or more of the trust beneficiaries who are proper objects of the exercise of the power in the first trust. The exercise of a trustee's authority granted under this subsection (a) shall in all respects comply with any standard that limits the trustee's authority to make distributions from the first trust but may be exercised whether or not the trustee would have been permitted to exercise the power to make a current outright distribution of all of the trust assets in compliance with any such standard. For purposes of this subsection (a), an open class of beneficiaries identified in the governing instrument for the first trust (such as, but not limited to, a class comprised of the descendants of a person who is living or who has living descendants) is a proper object of the exercise of a power to make distributions and the exercise of such a power in favor of a second trust having only beneficiaries, including unborn future beneficiaries, who are among the members of the open class satisfies the requirement of paragraph (a)(1) of this section even if, pursuant to the terms of the governing instrument for the second trust, the class remains, or might remain, open beyond the time when the class would have closed pursuant to the terms of the governing instrument for the first trust; provided, however, that the governing instrument for the second trust shall not permit distributions to or among members of the open class sooner than when or in excess of the amounts permitted by the governing instrument for the first trust. A trustee's power, pursuant to this subsection (a), to appoint principal in favor of

the trustee of a second trust shall include the power to create the second trust.

The statute sets out the manner in which a decanting power is to be exercised,⁶⁵ specifies that the exercise of a decanting power is to be considered to be the exercise of a nongeneral power of appointment,⁶⁶ and establishes other rules.⁶⁷

Through the use of a decanting power, a trustee may modernize the administrative provisions of a trust being administered in Delaware.

E. Nonjudicial Settlement Agreements

Delaware's nonjudicial settlement agreement statute, which took effect in 2013 and is closely based on § 111 of the Uniform Trust Code ("UTC"),⁶⁸ provides in general:⁶⁹

(b) Except as otherwise provided in subsection (c) of this section, interested persons may enter into a binding nonjudicial settlement agreement with respect to any matter involving a trust (other than a trust described in § 3541 of this title).

The term "interested persons" means all persons whose consent would be required for a settlement agreement to be approved by the Court of Chancery⁷⁰ and currently is defined as follows:⁷¹

(a) For purposes of this section, with respect to any proposed nonjudicial settlement agreement regarding a trust, the term "interested persons" means all whose interest in the trust would be affected by the proposed nonjudicial settlement agreement, which may include, but shall not be limited to:

- (1) trustees and other fiduciaries;

⁶⁵ 12 Del. C. § 3528(b).

⁶⁶ 12 Del. C. § 3528(c).

⁶⁷ 12 Del. C. § 3528(d)–(f).

⁶⁸ UTC § 111 (2005).

⁶⁹ 12 Del. C. § 3338(b).

⁷⁰ Del. Ch. Ct. R. 101(a)(7).

⁷¹ 12 Del. C. § 3338(a), as amended by 80 Del. Laws 153, § 3 (2015).

(2) trust beneficiaries, who will generally be those with a present interest in the trust and those whose interest in the trust would vest, without regard to the exercise or non-exercise of any power of appointment, if the present interests in the trust terminated on the date of the nonjudicial settlement agreement;

(3) the trustor of the trust, if living; and

(4) all other persons having an interest in the trust according to the express terms of the governing instrument (such as, but not limited to, holders of powers and persons having other rights, held in a nonfiduciary capacity, relating to trust property).

A nonjudicial settlement agreement must not violate a material purpose of the trust and may only include changes that could be approved by the court.⁷² The six specific matters that may be resolved by a nonjudicial settlement agreement include the resignation or appointment of a trustee and the change of a trust's principal place of administration.⁷³

The situations in which the statute is useful will be developed over time.

F. Consent Petition Proceeding in Court of Chancery

In 2012, Chancellor Strine issued Rules 100–104 that govern the consent-petition procedure in the Court of Chancery.⁷⁴ Because they are more burdensome than the requirements that preceded them, this procedure is more expensive and more time consuming than in the past. In 2015, the Delaware Court of Chancery denied a petition to modify a trust that departed from the testator's intent.⁷⁵

III. THE POWER TO ADJUST AND UNITRUST REGIME

A. Power to Adjust Statute

Effective August 1, 2005, Delaware adopted the power to adjust receipts and disbursements between income and principal under § 104 of the 1997 Uniform

⁷² 12 Del. C. § 3338(c).

⁷³ 12 Del. C. § 3338(d).

⁷⁴ Del. Ch. Ct. Rs. 100–104.

⁷⁵ In re Trust of Flint, 2015 Del. Ch. Lexis 170 (Del. Ch. 2015).

Principal and Income Act (“UPAIA”). This provision permits a trustee to adjust between principal and income (by allocating income to principal or principal to income) in an income trust if it manages trust investments under the prudent-investor rule and if, after administering the trust in accordance with the governing instrument and the principal and income act, the trustee is unable to administer the trust impartially between the current and remainder beneficiaries (except to the extent that the governing instrument clearly manifests an intention that the trustee favor one or more beneficiaries).⁷⁶ The trustee must consider several factors in determining whether, and to what extent, to exercise the power to adjust,⁷⁷ and the statute enumerates the situations in which the power to adjust is not available.⁷⁸ A trustee who is a beneficiary or who (as a result of having or exercising the power to adjust) would become an owner of a trust for federal income-tax purposes or would have the trust included in his or her gross estate for federal estate-tax purposes, may not participate in the decision to make an adjustment, but other trustees may act.⁷⁹ A trustee may release the power to adjust,⁸⁰ and the statute specifies instances in which the power to adjust is not available.⁸¹ The statute gives the trustee discretion to require a beneficiary to pay income tax on capital gains adjusted to income.⁸²

A court may not change a trustee’s decision to exercise or not to exercise the power to adjust unless it finds that the trustee abused its discretion.⁸³ If a court so finds, the primary remedy is to restore the income and remainder beneficiaries to their proper positions by distributing additional amounts to, or by withholding future distributions from, the income beneficiary. If this remedy is not sufficient, the court may surcharge the trustee.⁸⁴

B. Total-Return Unitrust-Conversion Statute

On June 21, 2001, Governor Minner signed Delaware’s total-return unitrust-conversion statute that took effect on that date.⁸⁵ The statute was amended in 2004⁸⁶ to take account of the regulations that the Internal Revenue Service (“IRS”) issued under IRC § 643 early that year (“IRC § 643 regulations”). It was

⁷⁶ 12 Del. C. § 61-104.

⁷⁷ 12 Del. C. § 61-104(b).

⁷⁸ 12 Del. C. § 61-104(c).

⁷⁹ 12 Del. C. § 61-104(d).

⁸⁰ 12 Del. C. § 61-104(e).

⁸¹ 12 Del. C. § 61-104(f)–(g).

⁸² 12 Del. C. § 61-104(h).

⁸³ 12 Del. C. § 61-105(a)–(b).

⁸⁴ 12 Del. C. § 61-105(c).

⁸⁵ 12 Del. C. § 3527, 73 Del. Laws 48, § 1 (2001).

⁸⁶ 74 Del. Laws 270, §§ 1–12 (2004).

amended again in 2009,⁸⁷ and, in 2010, the statute was moved to the Delaware UPAAIA.⁸⁸

Under the Delaware statute, a trustee may convert an income trust into a total-return unitrust, reconvert a total-return unitrust into an income trust, or change the percentage used to calculate the unitrust amount and/or the method used to determine the fair market value of the trust.⁸⁹ One procedure applies if the trustee is not an interested trustee (“disinterested trustee”),⁹⁰ and another procedure applies if the trust has an interested trustee.⁹¹ Rules are provided for trusts that have multiple trustees.⁹²

A disinterested trustee may convert an income trust into a total-return unitrust without court approval if it adopts a written policy, satisfies notice requirements, and does not receive written objections.⁹³ It must follow a similar procedure to reconvert a total-return unitrust into an income trust or to change the unitrust percentage or the valuation method.⁹⁴

To convert an income trust, a disinterested trustee must adopt a written policy providing that future distributions from the trust will be unitrust amounts rather than net income.⁹⁵ It also must send notice of the proposed conversion to:⁹⁶

- (1) The trustor, if living;
- (2) All living persons who are currently receiving or are eligible to receive income distributions;
- (3) Without regard to the exercise of any power of appointment, all living persons who would receive principal if the trust were then to terminate and all living persons who would be eligible to receive distributions of income or principal if the interests of all the beneficiaries currently eligible to receive income under (2) were then to terminate; and
- (4) All advisers or protectors.

⁸⁷ 77 Del. Laws 98, §§ 8–11 (2009).

⁸⁸ 12 Del. C. § 3527, redesignated as 12 Del. C. § 61-106, by 77 Del. Laws 330, § 10 (2010).

⁸⁹ 12 Del. C. § 61-106.

⁹⁰ 12 Del. C. § 61-106(b).

⁹¹ 12 Del. C. § 61-106(c).

⁹² 12 Del. C. § 61-106(b), (c).

⁹³ 12 Del. C. § 61-106(b).

⁹⁴ 12 Del. C. § 61-106(b).

⁹⁵ 12 Del. C. § 61-106(b).

⁹⁶ 12 Del. C. § 61-106(b).

At least one person receiving notice under (2) and (3) above must be legally competent.⁹⁷ The written notice must contain copies of the trustee's written policy and the Delaware statute.⁹⁸ A person must file written objections within 30 days of receiving notice.⁹⁹

An interested trustee may convert an income trust into a total-return unitrust without court approval if the policy, notice, and objection requirements described above are satisfied and if it appoints a disinterested person to determine the unitrust percentage and related matters in a fiduciary capacity.¹⁰⁰ The trustee's notice must contain the disinterested person's determinations.¹⁰¹

A trustee may petition the Delaware Court of Chancery for guidance if it is unable to convert the trust to a unitrust under the above procedures (e.g., because a beneficiary objects or because a competent beneficiary is not in the current and the next generation) or if it decides not to convert the trust without court approval.¹⁰² If the trustee is an interested trustee, the court, in its own discretion or on petition, may appoint a disinterested person to determine the unitrust percentage and related matters in a fiduciary capacity.¹⁰³

The trustee must determine the fair market value of the trust at least annually, and it may use such valuation date or dates or averages of valuation dates as it deems appropriate.¹⁰⁴ It may value illiquid assets using valuation methods it deems reasonable, and it may exclude assets used by a beneficiary, such as a residence or tangible personal property, in computing the unitrust amount.¹⁰⁵

The unitrust percentage must be a reasonable current return from the trust and must be no less than 3% nor more than 5%.¹⁰⁶ In establishing the unitrust percentage, the trustee must consider the intentions of the trustor as expressed in the governing instrument, the needs of the beneficiaries, general economic conditions, projected current earnings and appreciation, and projected inflation and its impact.¹⁰⁷ The trustee may average or "smooth" distributions using any

⁹⁷ 12 Del. C. § 61-106(b).

⁹⁸ 12 Del. C. § 61-106(b).

⁹⁹ 12 Del. C. § 61-106(b).

¹⁰⁰ 12 Del. C. § 61-106(c).

¹⁰¹ 12 Del. C. § 61-106(c).

¹⁰² 12 Del. C. § 61-106(d).

¹⁰³ 12 Del. C. § 61-106(d).

¹⁰⁴ 12 Del. C. § 61-106(e).

¹⁰⁵ 12 Del. C. § 61-106(e).

¹⁰⁶ 12 Del. C. § 61-106(f).

¹⁰⁷ 12 Del. C. § 61-106(f).

prior valuations. Thus, it might smooth distributions using valuations for the last three years or for the last eight quarters.

Originally, the trustee had to distribute the greater of the income or the unitrust amount to a spouse for whom a marital-deduction trust was created and to the current beneficiary of a trust that was grandfathered for GST-tax purposes if income had to be distributed currently. After issuance of the IRC § 643 regulations, the 2004 amendments revised the Delaware statute to require the trustee of such a trust to distribute just the unitrust amount. The 2004 amendments extended the scope of the statute to cover wholly charitable trusts.¹⁰⁸

The Delaware statute contains a tax-ordering rule. Hence, the trustee must treat unitrust distributions as coming first from net accounting income determined as if the trust were not a unitrust and then from ordinary income not allocable to net accounting income. After calculating capital gain net income, the trustee may consider the unitrust distribution as paid from net short-term capital gains and then from net long-term capital gains. The balance is considered paid from principal.¹⁰⁹

Subject to the terms of the governing instrument, the trustee may determine the effective date of a conversion, the timing of distributions, whether distributions are to be made in cash or in kind, and other administrative issues.¹¹⁰ Conversion of an income trust into a unitrust does not affect any other provision of the governing instrument regarding principal distributions.¹¹¹

Under the Delaware statute, an income trust cannot be converted into a unitrust if the governing instrument requires the trustee to distribute an amount other than a reasonable current return from the trust, the trust is a pooled-income fund or a charitable-remainder trust (“CRT”), or the governing instrument specifically prohibits its use.¹¹²

A trustee or disinterested person who, in good faith, takes or fails to take any action under the Delaware statute is not personally liable to any affected person. Such affected person’s exclusive remedy is to obtain a court order directing the trustee to convert an income trust into a total-return unitrust, to reconvert a total-return unitrust into an income trust, or to change the unitrust percentage.¹¹³

For purposes of the Delaware statute, an “interested trustee” is an individual trustee to whom the net income or principal of the trust can currently be

¹⁰⁸ 12 Del. C. § 61-106(g).

¹⁰⁹ 12 Del. C. § 61-106(h).

¹¹⁰ 12 Del. C. § 61-106(i).

¹¹¹ 12 Del. C. § 61-106(j).

¹¹² 12 Del. C. § 61-106(l).

¹¹³ 12 Del. C. § 61-106(m).

distributed or would be distributed if the trust were then to terminate and be distributed; a trustee who may be removed and replaced by an interested distributee; and/or an individual trustee whose legal obligation to support a beneficiary may be satisfied by distributions of income and principal.¹¹⁴ An “interested distributee” is a person to whom distributions of income or principal may currently be made who has the power to replace the existing trustee with a person who may be a “related or subordinate party” with respect to such distributee within the meaning of IRC § 672(c).¹¹⁵ The “trustor” is the creator of an inter vivos or a testamentary trust.¹¹⁶

The Delaware statute is available to trusts in existence on June 21, 2001, or created thereafter,¹¹⁷ and covers trusts converted into total-return unitrusts under the laws of other jurisdictions.¹¹⁸ It is to be construed as pertaining to the “administration” of a trust and is available to any trust that is administered in Delaware under Delaware law or to any trust, regardless of its place of administration, whose governing instrument provides that Delaware law governs matters of construction or administration.¹¹⁹ Given that it is easier to change the law that governs the administration of a trust than it is to change the law that governs its construction¹²⁰ and because questions concerning the allocation of receipts and disbursements to principal or income often are treated as matters of construction,¹²¹ the Delaware statute stipulates that any action taken under it is a matter of administration.¹²²

C. New Total-Return Unitrust Statute

Attorneys are drafting trusts that provide for the distribution of a unitrust amount rather than income to the current beneficiary. Given that the IRC § 643 regulations specify that such distributions will be treated as income for federal-tax purposes only if they are provided for by state statute, effective August 1, 2004, Delaware law contemplates that trusts will be drafted in this manner.¹²³ In 2010, the Delaware statute was moved to the Delaware UPAIA.¹²⁴ Such trusts may be

¹¹⁴ 12 Del. C. § 61-106(a)(4).

¹¹⁵ 12 Del. C. § 61-106(a)(3).

¹¹⁶ 12 Del. C. § 61-106(a)(7).

¹¹⁷ 12 Del. C. § 61-106(n).

¹¹⁸ 12 Del. C. § 61-106(a)(5), (b)(2), (b)(3), (l).

¹¹⁹ 12 Del. C. § 61-106(l).

¹²⁰ See Restatement (Second) of Conflict of Laws §§ 267–282 (1971).

¹²¹ See Restatement (Second) of Conflict of Laws § 268 cmt. h (1971).

¹²² 12 Del. C. § 61-106(l).

¹²³ 12 Del. C. § 3527A, 74 Del. Laws 270, § 13 (2004).

¹²⁴ 12 Del. C. § 3527A, redesignated as 12 Del. C. § 61-107, by 77 Del. Laws 330, § 10 (2010).

converted into income trusts or have their unitrust percentages adjusted under Delaware's total-return unitrust-conversion statute.¹²⁵

IV. TRUST DURATION

Delaware has permitted perpetual trusts since 1933. In that year, it enacted a statute¹²⁶ that provides that the exercise of a nongeneral or general power of appointment begins a new perpetuities period.¹²⁷ Thus, if a beneficiary exercised a nongeneral power of appointment to extent a trust in each generation, the trust could last forever free of federal transfer tax.

In 1986, Delaware abolished the common-law rule against perpetuities for trusts and replaced it with a requirement that all trust interests in real and personal property had to end within 110 years.¹²⁸

In 1995, though, Delaware eliminated the 110-year limitation for personal property so that stocks, bonds, and other personal property may remain in trust forever.¹²⁹ Real property held in trust continues to be governed by the 110-year limitation that was enacted in 1986,¹³⁰ but this limitation can be avoided by placing real property in a limited-liability company ("LLC") or a family-limited partnership ("FLP") because an interest in such an entity is personal property under Delaware law.¹³¹

Delaware abolished the rule against accumulations when it abolished the common-law rule against perpetuities in 1986.¹³²

V. USE OF REVOCABLE "POUR OVER" TRUSTS VERSUS TESTAMENTARY DOCUMENTS

As the value of personal property in a Delaware estate increases, the importance of avoiding probate also increases. This is because the Registers of Wills for Delaware's three counties charge a fee on the value of personal property in the probate estate.¹³³ The probate fee is 1.75% in New Castle County and Kent County.¹³⁴ Accordingly, the

¹²⁵ 12 Del. C. § 61-107(e).

¹²⁶ 38 Del. Laws 198 (1933).

¹²⁷ 25 Del. C. § 503(c).

¹²⁸ 65 Del. Laws 422 (1986).

¹²⁹ 25 Del. C. § 503.

¹³⁰ 25 Del. C. § 503(b).

¹³¹ 25 Del. C. § 503(e).

¹³² 25 Del. C. § 506. See *Equitable Trust Co. v. Ward*, 48 A.2d 519, 528–29 (Del. Ch. 1946) (direction to accumulate income from Pennsylvania real estate by Delaware trustee of testamentary trust did not violate Pennsylvania rule against accumulations).

¹³³ See 12 Del. C. §§ 2510–2511.

¹³⁴ See www.nccde.org/152/Register-of-Wills (New Castle County); co.kent.de.us/register-of-wills-office (Kent County) (last visited Oct. 14, 2015).

savings from creating and funding a declaration of trust or revocable trust in these counties is \$1,750 for \$100,000 of personal property, \$17,500 for \$1,000,000 of personal property, and \$175,000 for \$10,000,000 of personal property. The probate fee is 1.25% in Sussex County.¹³⁵

The added privacy offered by a trust arrangement also is seen as an advantage.

VI. DIRECTED TRUSTS

Delaware has honored directed trusts since early in the 20th century, and the practice was codified in 1986.¹³⁶ The directed trust statute—12 Del. C. § 3313—currently provides in pertinent part:¹³⁷

(a) Where 1 or more persons are given authority by the terms of a governing instrument to direct, consent to or disapprove a fiduciary's actual or proposed investment decisions, distribution decisions or other decision of the fiduciary, such persons shall be considered to be advisers and fiduciaries when exercising such authority provided, however, that the governing instrument may provide that any such adviser (including a protector) shall act in a nonfiduciary capacity.

(b) If a governing instrument provides that a fiduciary is to follow the direction of an adviser, or is not to take specified actions except at the direction of an adviser, and the fiduciary acts in accordance with such a direction, then except in cases of wilful misconduct on the part of the fiduciary so directed, the fiduciary shall not be liable for any loss resulting directly or indirectly from any such act. . . .

(d) For purposes of this section, unless the terms of the governing instrument provide otherwise, "investment decision" means with respect to all of the trust's investments (or, if applicable, to investments specified in the governing instrument), the retention, purchase, sale, exchange, tender or other transaction or decision affecting the ownership thereof or rights therein (including the

¹³⁵ See www.sussexcountyde.gov/register-wills (Sussex County) (last visited Oct. 14, 2015).

¹³⁶ 12 Del. C. § 3313.

¹³⁷ 12 Del. C. § 3313(a), (b), (d), (e), (f), as amended by 80 Del. Laws 153, § 3 (2015).

powers to borrow and lend for investment purposes), all management, control and voting powers related directly or indirectly to such investments (including, without limitation, nonpublicly traded investments), the selection of custodians or sub-custodians other than the trustee, the selection and compensation of, and delegation to, investment advisers, managers or other investment providers, and with respect to nonpublicly traded investment, the valuation thereof, and an adviser with authority with respect to such decisions is an investment adviser.

(e) Whenever a governing instrument provides that a fiduciary is to follow the direction of an adviser with respect to investment decisions, distribution decisions, or other decisions of the fiduciary or shall not take specified actions except at the direction of an adviser, then, except to the extent that the governing instrument provides otherwise, the fiduciary shall have no duty to:

- (1) Monitor the conduct of the adviser;
- (2) Provide advice to the adviser or consult with the adviser; or
- (3) Communicate with or warn or apprise any beneficiary or third party concerning instances in which the fiduciary would or might have exercised the fiduciary's own discretion in a manner different from the manner directed by the adviser.

Absent clear and convincing evidence to the contrary, the actions of the fiduciary pertaining to matters within the scope of the adviser's authority (such as confirming that the adviser's directions have been carried out and recording and reporting actions taken at the adviser's direction), shall be presumed to be administrative actions taken by the fiduciary solely to allow the fiduciary to perform those duties assigned to the fiduciary under the governing instrument and such administrative actions shall not be deemed to constitute an undertaking by the fiduciary to monitor the adviser

or otherwise participate in actions within the scope of the adviser's authority.

(f) For purposes of this section, the term "adviser" shall include a "protector" who shall have all of the power and authority granted to the protector by the terms of the governing instrument, which may include but shall not be limited to:

- (1) The power to remove and appoint trustees, advisers, trust committee members, and other protectors;
- (2) The power to modify or amend the governing instrument to achieve favorable tax status or to facilitate the efficient administration of the trust; and
- (3) The power to modify, expand, or restrict the terms of a power of appointment granted to a beneficiary by the governing instrument.

In Duemler v. Wilmington Trust Company (2004),¹³⁸ a Delaware Vice Chancellor ruled that a corporate trustee was not liable for the failure of a sophisticated (i.e., securities lawyer) investment adviser to direct it on an investment decision where the trustee had forwarded relevant information to the adviser. The Vice Chancellor held:¹³⁹

The Court . . . finds that section 3313(b) of title 12 of the Delaware Code insulates fiduciaries of a Delaware trust from liability associated with any loss to the trust where a governing instrument provides that the fiduciary is to follow the direction of an advisor, the fiduciary acts in accordance with such direction and the fiduciary did not engage in willful misconduct. The trust agreement involved in this case appointed Plaintiff as the investment advisor to the Trust and, at all times, Plaintiff made all of the investment decisions for the Trust, including not to tender the securities in the Exchange Offer. In connection with Plaintiff's decision not to tender the securities in the Exchange

¹³⁸ Duemler v. Wilmington Trust Co., 2004 Del. Ch. Lexis 206 (Del. Ch. 2004).

¹³⁹ 2004 Del. Ch. Lexis 206 at 1–3.

Offer, Wilmington Trust acted in accordance with Plaintiff's instructions, did not engage in willful misconduct by not forwarding the Exchange Offer materials to Plaintiff and had no duty to provide information or ascertain whether Plaintiff was fully informed of all relevant information concerning the Exchange Offer. Accordingly, 12 Del. C. § 3313(b) insulates Wilmington Trust from all liability for any loss to the Trust resulting from plaintiff's decision not to tender the securities in the Exchange Offer.

VII. DUTY TO DISCLOSE AND ACCOUNT

A current area of controversy in the world of trusts regards the circumstances, if any, in which a trustee must provide present and future beneficiaries with copies of trust instruments, trust statements, and accountings. In Delaware, the extent of the duty of the trustee of an existing trust to keep beneficiaries informed is unsettled.¹⁴⁰ However, a testator or trustor creating a new trust may restrict the distribution of information. For example, a Delaware statute specifies that an instance in which a governing instrument may depart from usual trust rules involves "the right to be informed of the beneficiary's interest for a period of time."¹⁴¹ Given that this example is illustrative only, a testator or trustor may tailor a governing instrument further in this area. Hence, he or she may provide for the disclosure of information to a protector, adviser, or surrogate for periods when information is not being shared with beneficiaries.

VIII. LEGAL FEES AND FIDUCIARY COMMISSIONS

A. Personal Representatives and Their Attorneys

A Delaware statute provides that:¹⁴²

Commissions and attorneys' fees shall be allowed as provided by rule of the Court of Chancery.

Delaware Court of Chancery Rule 192(a) says that:¹⁴³

Commissions of personal representatives, and fees of the attorneys who represent them, shall be allowed in a reasonable amount.

Rule 192(b)¹⁴⁴ gives factors to consider when evaluating the reasonableness of compensation, and Rule 192(d)¹⁴⁵ allows the court to reduce excessive

¹⁴⁰ See McNeil v. Bennett, 792 A.2d 190 (Del. Ch. 2001), aff'd in part, rev'd in part, 798 A.2d 503 (Del. 2002).

¹⁴¹ 12 Del. C. § 3303(a).

¹⁴² 12 Del. C. § 2305(a).

¹⁴³ Del. Ch. Ct. R. 192(a).

commissions and fees. Illustrative cases are In re Estate of Howell (2002)¹⁴⁶ and In re Estate of Bandurski (2008).¹⁴⁷

My firm—Wilmington Trust Company—has a published fee schedule for settling Delaware estates. Any attorney who assists us charges on an hourly basis. Typically, individual personal representatives and their attorneys charge on an hourly basis as well.

B. Trustees

A Delaware statute provides in pertinent part that:¹⁴⁸

Trustees under wills, trustees under inter vivos deeds of trust, both revocable and irrevocable, and successors to such trustees, are entitled to reasonable compensation for their services in accordance with the instrument creating the trust.

On petition, the Court of Chancery may raise or lower commissions for specified reasons.¹⁴⁹

To the extent not specified in the governing instrument, commissions of corporate trustees are based on published fee schedules.¹⁵⁰ An illustrative case is In re Trust Under Agreement of Christopher L. Ward (2001).¹⁵¹

The commissions of other trustees are determined as follows:¹⁵²

For other trustees, the Court of Chancery shall from time to time promulgate a rule fixing the method by which trustees other than qualified trustees may be allowed compensation for their services.

The applicable rule is Delaware Court of Chancery Rule 132.¹⁵³

¹⁴⁴ Del. Ch. Ct. R. 192(b).

¹⁴⁵ Del. Ch. Ct. R. 192(d).

¹⁴⁶ In re Estate of Howell, 2002 Del. Ch. Lexis 153 at 19–24 (Del. Ch. 2002).

¹⁴⁷ In re Estate of Bandurski, 2008 Del. Ch. Lexis 280 (Del. Ch. 2008).

¹⁴⁸ 12 Del. C. § 3560(a).

¹⁴⁹ 12 Del. C. § 3560(a).

¹⁵⁰ 12 Del. C. § 3561(a), (b)(1).

¹⁵¹ In re Trust Under Agreement of Christopher L. Ward, 2001 Del. Ch. Lexis 158 at 15–20 (Del. Ch. 2001).

¹⁵² 12 Del. C. § 3561(b)(2).

¹⁵³ Del. Ch. Ct. R. 132.

My firm has a published fee schedule. It provides for graduated rates for fully managed trusts, reduced graduated rates for directed trusts, and flat fees for directed trusts just holding LLC or FLP interests. Individual trustees' commissions depend on the circumstances. Again, the Court of Chancery may adjust commissions that it finds to be unreasonable.¹⁵⁴

IX. NO CONTEST CLAUSES

A. Introduction

Delaware has statutory mechanisms to ensure that a client's wishes will be implemented.

B. Lifetime Court Proceeding

A beneficiary may not bring a judicial proceeding to contest whether a trust was validly created more than 120 days after the trustee provides such beneficiary with specified written information.¹⁵⁵ The statute covers irrevocable trusts, revocable trusts, and amendments to revocable trusts and currently reads in pertinent part:¹⁵⁶

(a) A judicial proceeding to contest whether a revocable trust or any amendment thereto, or an irrevocable trust was validly created may not be initiated later than the first to occur of:

(1) One hundred twenty days after the date that the trustee notified in writing the person who is contesting the trust's existence, of the trustee's name and address, of whether such person is a beneficiary, and of the time allowed under this section for initiating a judicial proceeding to contest the trust provided, however, that no trustee shall have any liability under the governing instrument or to any third party or otherwise for failure to provide any such written notice. For purposes of this paragraph, notice shall have been given when received by the person to whom the notice was given and, absent evidence to the contrary, it shall be presumed that notice mailed or delivered to the last known address of such person constitutes receipt by such person.

¹⁵⁴ 12 Del. C. § 3562.

¹⁵⁵ 12 Del. C. § 3546(a)(1), as amended by 80 Del. Laws 153, § 4 (2015).

¹⁵⁶ 12 Del. C. § 3546(a)(1), as amended by 80 Del. Laws 153, § 4 (2015).

Delaware attorneys find this procedure to be effective in forestalling litigation if it is initiated upon the creation of an inter vivos trust because a disgruntled beneficiary must come forward while the trust's creator still is available to testify. The Supreme Court of Delaware upheld the statute and its notice procedure in Ravet v. Northern Trust Co. (2015).¹⁵⁷ If the trustee does not follow the foregoing procedure, a beneficiary is barred from bringing such a judicial proceeding at the first to occur of: (1) two years after the client's death; (2) the expiration of the period in which a petition for review of a Will could be filed if the trust was revocable at the client's death and if the trust was specifically referred to in the client's Will; or (3) the date the beneficiary's right to contest was precluded by adjudication, consent, or other limitation.¹⁵⁸

In 2015, similar procedures were made available for the pre-mortem validation of Wills and the exercise of testamentary powers of appointment.¹⁵⁹

C. No-Contest Clauses

Consistent with the policies of honoring a testator's or trustor's intent and discouraging litigation relating to it, a no-contest or in terrorem or penalty clause is valid in Delaware. Thus, a provision of a Will or trust that reduces or eliminates the interest of a beneficiary who contests such Will or trust is enforceable.¹⁶⁰ Recognizing that such clauses must be applied judiciously, though, the statute provides that a no-contest clause does not apply to: (1) an action brought by a trustee or personal representative; (2) an action in which a court determines that a beneficiary prevailed substantially; (3) a settlement agreement among beneficiaries of a Will or trust; (4) an action to determine whether a proceeding constitutes a contest; or (5) a construction proceeding brought by a beneficiary of a Will or trust.¹⁶¹

D. Statute of Limitations

Absent fraud or misrepresentation, a beneficiary may not bring a surcharge action against a trustee later than two years after the trustee provides a report that contains specified information.¹⁶² Thus, if a trustee discloses activity to a beneficiary that is consistent with the testator's or trustor's intent but that is objectionable to the beneficiary, the beneficiary must act within a relatively short period of time. The statute bars a claim arising from activity that a trustee does not disclose in the foregoing manner within five years after the first to occur of

¹⁵⁷ Ravet v. Northern Trust Co., 2015 Del. Lexis 76 (Del. 2015).

¹⁵⁸ 12 Del. C. § 3546(a)(2)–(4).

¹⁵⁹ 12 Del. C. §§ 1311–1312, added by 80 Del. Laws 153, § 2 (2015).

¹⁶⁰ 12 Del. C. § 3329(a). See Mitchell v. Reynolds, 2009 Del. Ch. Lexis 3 at 53 (Del. Ch. 2009) (“Delaware law generally enforces no-contest clauses absent certain exceptions not implicated here.”).

¹⁶¹ 12 Del. C. § 3329(b).

¹⁶² 12 Del. C. § 3585(a).

the removal, resignation, or death of the trustee; the termination of the beneficiary's interest in the trust; or the termination of the trust.¹⁶³

X. SELF-SETTLED TRUSTS

A. Introduction

On July 9, 1997, Governor Carper signed the Delaware Qualified Dispositions in Trust Act (“Delaware Act”).¹⁶⁴ The Delaware Act has been amended several times since its enactment.¹⁶⁵ Because it probably will be amended in the future, an attorney should confirm that he or she is working with the current statute in a particular case.

B. How to Create a Delaware APT

To create an APT under the Delaware Act (“Delaware APT”), a person must create an irrevocable trust that contains a spendthrift clause; provides that Delaware law governs the trust's validity, construction, and administration; and appoints at least one “qualified trustee.”¹⁶⁶ A “qualified trustee” is either an individual who resides in Delaware or a corporation that is authorized to conduct trust business in Delaware and is regulated by the Delaware Bank Commissioner or a federal agency.¹⁶⁷ The qualified trustee or trustees must maintain or arrange for custody in Delaware of some trust property, maintain records for the trust, prepare or arrange for the preparation of fiduciary income-tax returns, or otherwise materially participate in the administration of the trust.¹⁶⁸ If only one qualified trustee is acting, it will be deemed to have resigned if it ceases to meet these requirements.¹⁶⁹ Similarly, a trustee of a Delaware APT automatically ceases to serve if a court declines to apply Delaware law in determining the validity, construction, or administration of such trust, or the effect of its spendthrift clause, in a proceeding involving such trustee.¹⁷⁰ If a trustee ceases to act for one of these reasons, any successor trustee designated in the trust will take its place and the Delaware Court of Chancery may fill any vacancy. The trust

¹⁶³ 12 Del. C. § 3585(d).

¹⁶⁴ 12 Del. C. §§ 3570–3576, 71 Del. Laws 159 (1997).

¹⁶⁵ 71 Del. Laws 159 (1997); 71 Del. Laws 254 (1998); 71 Del. Laws 343 (1998); 72 Del. Laws 59 (1999); 72 Del. Laws 195 (1999); 72 Del. Laws 341 (2000); 73 Del. Laws 378 (2002); 74 Del. Laws 100 (2003); 75 Del. Laws 97 (2005); 75 Del. Laws 301 (2006); 76 Del. Laws 90 (2007); 76 Del. Laws 254 (2008); 77 Del. Laws 98 (2009); 77 Del. Laws 330 (2010); 78 Del. Laws 117 (2011); 79 Del. Laws 198 (2014); 80 Del. Laws 153 (2015). The current Delaware Act is available at www.delcode.delaware.gov/title12/c035/sc06/index.shtml (last visited Oct. 14, 2015).

¹⁶⁶ 12 Del. C. § 3570(11)(a)–(c).

¹⁶⁷ 12 Del. C. § 3570(8)(a).

¹⁶⁸ 12 Del. C. § 3570(8)(b).

¹⁶⁹ 12 Del. C. § 3570(8)(e).

¹⁷⁰ 12 Del. C. § 3572(g).

may have non-Delaware co-trustees¹⁷¹ and Delaware or non-Delaware advisers with authority to replace advisers and qualified trustees, participate in investment decisions, and/or perform other duties.¹⁷²

The Delaware Act specifically permits the trustor of a Delaware APT to have the power to:

1. Consent to or direct investment changes;
2. Veto distributions;
3. Replace trustees or advisers; and/or
4. Effective in 2015, reacquire trust assets in a nonfiduciary capacity under IRC § 675(4)(C).¹⁷³

The Delaware Act also expressly authorizes the trustor to have:

1. The ability to receive income or principal pursuant to broad discretion or a standard as determined by Delaware trustees, non-Delaware trustees, and/or advisers;
2. The right to receive current income distributions;
3. An interest in a CRT, an interest in a qualified personal residence trust (“QPRT”), or a qualified annuity interest created if a residence in a QPRT ceases to be used as a personal residence;
4. An interest in a grantor-retained annuity trust (“GRAT”), an interest in a grantor-retained unitrust (“GRUT”), or up to a 5% interest in a total-return unitrust;
5. A nongeneral lifetime or testamentary power of appointment; and/or
6. The ability to provide for the payment of debts, expenses, and taxes following death.¹⁷⁴

The Delaware Act addresses Rev. Rul. 2004-64,¹⁷⁵ which held, inter alia, that the grant of discretion to a trustee to reimburse the trustor for income

¹⁷¹ 12 Del. C. § 3570(8)(f).

¹⁷² 12 Del. C. § 3570(8)(c).

¹⁷³ 12 Del. C. §§ 3570(8)(d), 3570(11)(b), as amended by 80 Del. Laws 153, § 4 (2015).

¹⁷⁴ 12 Del. C. § 3570(11)(b).

¹⁷⁵ Rev. Rul. 2004-64, 2004-2 C.B. 7 (July 6, 2004).

taxes that he or she must pay on a grantor trust will not cause estate-tax inclusion under IRC § 2036 if applicable local law does not subject the trust assets to the claims of the trustor's creditors.¹⁷⁶ The trustor might be reimbursed for such taxes pursuant to discretion given to the trustee, adviser, or protector under a Delaware APT.¹⁷⁷ For trustors who do not want to grant such broad discretion, the Delaware Act permits a Delaware APT simply to grant discretion to reimburse the trustor for income taxes attributable to the trust.¹⁷⁸

Most Delaware APTs are structured as incomplete gifts. In such a trust, it is not disadvantageous from an estate-planning standpoint to have the trust pay its share of income taxes. So, a Delaware APT may direct the trustee to pay income taxes attributable to the trust.¹⁷⁹

Under the Delaware Act, the trustor may not be a trustee¹⁸⁰ and may only have the interests and powers described above.¹⁸¹ Furthermore, the trustor has only the powers and authorities conferred by the trust instrument, and any agreement or understanding purporting to grant or permit the retention of any greater rights or authority is void.¹⁸² To be conservative, Delaware attorneys counsel clients not to retain powers and interests that are not specifically authorized by the Delaware Act. Consequently, the trustor probably should not have the express right to get the assets back. Although the Delaware Act permits a variety of interests and powers, certain provisions might be inappropriate in a particular case. For example, the use of co-trustees in the trustor's state of residence or business might increase a trust's susceptibility to process in that jurisdiction and the possibility that Delaware law might be found not to govern the trust or, more importantly, the rights of beneficiaries and their creditors. Under the Delaware Act,¹⁸³ a spendthrift clause will be deemed to be a restriction on the transfer of the trustor's beneficial interest in the trust that is enforceable under applicable nonbankruptcy law within the meaning of the United States Bankruptcy Code.¹⁸⁴

C. Who May Defeat a Delaware APT

¹⁷⁶ 2004-2 C.B. 7 at 9.

¹⁷⁷ 12 Del. C. § 3570(11)(b)(3), (6).

¹⁷⁸ 12 Del. C. § 3570(11)(b)(9).

¹⁷⁹ 12 Del. C. § 3570(11)(b)(9).

¹⁸⁰ 12 Del. C. § 3570(8)(d).

¹⁸¹ 12 Del. C. § 3571.

¹⁸² 12 Del. C. § 3571.

¹⁸³ 12 Del. C. § 3570(11)(c).

¹⁸⁴ 11 USC § 541(c)(2).

1. Introduction

Any action to set aside a Delaware APT (including an action to enforce a judgment from another jurisdiction) must be based on § 1304 or § 1305 of the Delaware Uniform Fraudulent Transfer Act (“UFTA”) and any related changes to the Delaware UFTA by the Delaware Act.¹⁸⁵ The Delaware Act vests the Delaware Court of Chancery with exclusive jurisdiction over any action involving a Delaware APT.¹⁸⁶

2. Creditors Who May Defeat a Delaware APT

Certain federal “super-creditors” (including the IRS, the Securities and Exchange Commission (“SEC”), the Federal Trade Commission (“FTC”), and minor children seeking support) may reach the assets of a domestic APT, Delaware or otherwise. Under the Delaware Act, the following four categories of creditors may defeat Delaware APTs.

(a) Pre-Transfer Claims

If a creditor’s claim arose before the trust was created, the creditor must bring suit within four years after the trust’s creation or, if later, within one year after the creditor discovered (or should have discovered) the trust¹⁸⁷ and must prove, by clear and convincing evidence, that creation of the trust was a fraudulent transfer. To minimize the effect of the one-year limitation, the trustor might notify known pre-transfer creditors of the trust’s existence within three years of its creation. If multiple transfers are made to the same trust, a subsequent transfer is disregarded in determining whether a creditor’s claim with respect to a prior transfer is extinguished as provided above;¹⁸⁸ distributions to beneficiaries are deemed to come from the latest transfer.¹⁸⁹

(b) Post-Transfer Claims

If a creditor’s claim arose after the trust was created, the creditor must bring suit within four years after the trust’s creation and must prove, by clear and convincing evidence, that creation of the trust was made with actual intent to defraud—not hinder or delay—that creditor.¹⁹⁰ Hence, as a practical matter, this exception is not

¹⁸⁵ 12 Del. C. § 3572(a); 6 Del. C. §§ 1301–1311.

¹⁸⁶ 12 Del. C. § 3572(a).

¹⁸⁷ 12 Del. C. § 3572(b)(1).

¹⁸⁸ 12 Del. C. § 3572(f)(1).

¹⁸⁹ 12 Del. C. § 3572(f)(2).

¹⁹⁰ 12 Del. C. § 3572(a), (b)(2).

available for a creditor who does not exist or is not foreseeable when a Delaware APT is created because it will be extremely hard to prove that a trustor intended to defraud a nonexistent, unforeseen creditor. If multiple transfers are made to the same trust, a subsequent transfer is disregarded in determining whether a creditor's claim with respect to a prior transfer is extinguished as provided above;¹⁹¹ distributions to beneficiaries are deemed to come from the latest transfer.¹⁹²

(c) Family Claims

A person whose claim results from an agreement or court order providing for alimony, child support, or property division “incident to a judicial proceeding with respect to a separation or divorce” may reach the assets of a Delaware APT,¹⁹³ but only a spouse who was married to the trustor of the trust before it was created may invoke this exception.¹⁹⁴

Shortly after the IRS issued it, the Delaware Act was amended to address Rev. Proc. 2005-24,¹⁹⁵ which required spouses of trustors of certain post-June 27, 2005, inter vivos CRTs to waive rights to reach such trusts by electing against the Will. Under § 2-205 of the Uniform Probate Code (“UPC”), a surviving spouse may reach the assets of an inter vivos CRT created during his or her marriage to the deceased spouse (but not while the deceased spouse was unmarried or was married to a prior spouse) by electing against the Will.¹⁹⁶ Section 2-205 (or the comparable provision of the earlier version of the UPC) is in effect in at least 14 states—Alaska, Colorado, Hawaii, Kansas, Maine, Minnesota, Montana, Nebraska, New Jersey, North Dakota, South Dakota, Utah, Virginia, and West Virginia.¹⁹⁷

¹⁹¹ 12 Del. C. § 3572(f)(1).

¹⁹² 12 Del. C. § 3572(f)(2).

¹⁹³ 12 Del. C. § 3573(1).

¹⁹⁴ 12 Del. C. § 3570(9).

¹⁹⁵ 2005-1 C.B. 909 (Apr. 18, 2005).

¹⁹⁶ UPC § 2-205(2)(A) (2010).

¹⁹⁷ See Alaska Stat. § 13.12.205(2)(A); Colo. Rev. Stat. § 15-11-205(2)(a); Haw. Rev. Stat. § 560:2-205(2)(A); Kan. Stat. Ann. § 59-6a205(b)(1); Me. Rev. Stat. Ann. tit. 18-A, § 2-202(1)(i); Minn. Stat. § 524.2-205(2)(i); Mont. Code Ann. § 72-2-222(2)(b)(ii)(A); Neb. Rev. Stat. § 30-2314(a)(1)(i); NJSA § 3B:8-3(a); N.D. Cent. Code § 30.1-05-02(2)(b)(2)(a); S.D. Codified Laws § 29A-2-205(2)(i); Utah Code § 75-2-205(2)(a)(i); Va. Code Ann. § 64.2-305(A)(3)(a); W. Va. Code § 42-3-2(b)(2)(iii)(A).

The surviving spouse of a Delaware decedent never has been able to reach trust assets by electing against the Will,¹⁹⁸ and Delaware law does not defer to the law of a decedent's domicile to determine a surviving spouse's elective-share rights.¹⁹⁹ Since the passage of the Delaware Act, Delaware attorneys have been of the view that a spouse may reach the assets of a Delaware APT only for the specified purposes (i.e., alimony, child support, or property division incident to a separation or divorce proceeding) and that, because they do not include elective-share rights, the surviving spouse of the trustor of a Delaware APT may not reach the assets of the trust by electing against the Will, whether or not the trustor lived in Delaware at death. To respond to Rev. Proc. 2005-24, the Delaware Act made this explicit. Thus, the final sentence of the pertinent section of the Delaware Act provides that a Delaware APT may not be reached to satisfy a claim for elective share.²⁰⁰ Although the Internal Revenue Service ("IRS") deferred the effective date of the revenue procedure in 2006,²⁰¹ it alerted taxpayers in 2008²⁰² and again in 2014²⁰³ that it has not forgotten the issue by requesting comments on procedures to ensure that elective rights do not affect assets for which a charitable deduction was taken on the creation of a CRT. A client therefore should consider structuring a CRT as a Delaware APT so that the trust's assets will be protected in case the IRS issues similar restrictions in the future or in case a surviving spouse actually elects against the Will.

The trustor of a CRT that is structured as a Delaware APT may release a retained interest in favor of charity.²⁰⁴

In appropriate circumstances (e.g., if a trustor wants to make a completed gift and to exclude assets from the gross estate), it is worth exploring whether a current or former spouse is willing to waive this provision.

(d) Tort Claims

¹⁹⁸ 12 Del. C. §§ 901(a), 908(b). See Machulski v. Boudart, 2008 Del. Super. Lexis 104 at 7 (Del. Super. Ct. 2008) ("A transfer of the house into a trust, even two months before the decedent's death, would have removed it from his 'contributing estate,' regardless of whether it removed it from his elective estate").

¹⁹⁹ 12 Del. C. § 901(b).

²⁰⁰ 12 Del. C. § 3573.

²⁰¹ Notice 2006-15, 2006-1 C.B. 501 (Feb. 21, 2006).

²⁰² 2008 Tax Notes Today 93-33 (May 13, 2008).

²⁰³ 2014 Tax Notes Today 67-32 (Apr. 8, 2014).

²⁰⁴ 12 Del. C. §§ 3536(e), 3570(11)(b)(4). See Rev. Rul. 86-60, 1986-1 C.B. 302 (Jan. 1986); PLRs 200834013 (Apr. 15, 2008), 200808018 (Nov. 7, 2007), 200802024 (Sept. 14, 2007).

A person who suffers death, personal injury, or property damage before a Delaware APT is established for which the trustor is liable may reach the trust assets.²⁰⁵

D. Consequences if a Delaware APT Is Defeated

If one of the above exceptions applies (and after payment of the trustee's costs as described below), the Delaware APT is defeated only to the extent necessary to pay that creditor's claim together with related costs, including attorneys' fees allowed by the court.²⁰⁶ Thus, if a trustor is confronted by multiple creditors with the type of claim that is permitted to be pursued, each creditor must bring a separate action for avoidance.

Unless a creditor proves by clear and convincing evidence that a trustee acted in bad faith in accepting and administering the trust, that trustee may use trust assets to pay its costs of litigating the claim before satisfying the claim and related costs, if any.²⁰⁷ A trustee's mere acceptance of the trust is presumed not to be in bad faith. Similarly, a beneficiary who received a distribution before a creditor brings a successful suit to defeat a Delaware APT may keep the distribution unless the creditor proves by clear and convincing evidence (by a preponderance of the evidence if the beneficiary is the trustor) that he or she acted in bad faith.²⁰⁸

In Delaware, "the Delaware Fraudulent Transfer Act does not create a cause of action for aiding and abetting, or conspiring to commit, a fraudulent transfer."²⁰⁹ In addition, the Delaware Act provides that the creation of a Delaware APT will not be treated as fraudulent or otherwise contrary to law for purposes of any action against any trustee, adviser, or protector acting under a trust instrument or against any attorney or other professional adviser involved in establishing the trust.²¹⁰

E. Moving Trusts to Delaware

A trustee may create a Delaware APT either by establishing a Delaware APT or by effectuating the transfer of a trust that meets the requirements of the Delaware Act to Delaware²¹¹ except that the trust does not have to provide that Delaware law governs.²¹² If a trustee of an irrevocable spendthrift trust creates a Delaware

²⁰⁵ 12 Del. C. § 3573(2).

²⁰⁶ 12 Del. C. § 3574(a).

²⁰⁷ 12 Del. C. § 3574(b)(1), (c).

²⁰⁸ 12 Del. C. § 3574(b)(2), (c).

²⁰⁹ Edgewater Growth Capital Partners, L.P. v. H.I.G. Capital, Inc., 2010 Del. Ch. Lexis 42 at 7 (Del. Ch. 2010) (citing earlier cases).

²¹⁰ 12 Del. C. § 3572(d)–(e).

²¹¹ 12 Del. C. § 3570(10).

²¹² 12 Del. C. § 3570(11), penultimate sentence.

APT, the time that the trust existed before it is moved to Delaware counts toward the four-year period for pursuing post-transfer claims against the trust.²¹³ Thus, it might be possible for the trustee of an existing onshore or offshore trust to create a Delaware APT that cannot be defeated under the Delaware Act.

Under the Delaware Act, a trustor may have a lifetime or testamentary power to appoint to anyone except the trustor, the trustor's estate, the trustor's creditors, or creditors of the trustor's estate.²¹⁴ An existing trust will not qualify under the Delaware Act if it gives the trustor an inter vivos or testamentary general power of appointment. The existing trustee may, with the written consent of the trustor, bring such a trust into conformity with the Delaware Act by deleting the excessive power.²¹⁵

F. Infrastructure

An important factor in evaluating the effectiveness of Delaware APTs is that Delaware has a long-standing tradition of leadership in the financial services industry. The original version of the Delaware Act was written and enacted over a three-month period in 1997, and amendments have been drafted and enacted in short order.

Delaware has been a trust-friendly jurisdiction for generations. As evidence of this, a 2006 empirical study, which analyzed pertinent data beginning in 1969, found that, "Delaware was clearly attracting trust funds from out of state in the early 1970s,"²¹⁶ and that, "[i]n 1986 Delaware had a disproportionate share of the nation's trust funds."²¹⁷

The Chancellor and Vice Chancellors of the Delaware Court of Chancery (which the Wall Street Journal described in 2014 as "the nation's most influential business court"²¹⁸) and the Justices of the Delaware Supreme Court (the courts that handle corporate matters and that would handle challenges to APTs in Delaware) are not elected. Instead, the Delaware Constitution requires that they be appointed by the Governor with the consent of a majority of the members of the Senate and that all Delaware judges come as equally as possible from the two major political parties.²¹⁹ For this and other reasons, Delaware's liability system

²¹³ 12 Del. C. §§ 3572(c), 3575.

²¹⁴ 12 Del. C. § 3570(11)(b)(2).

²¹⁵ 12 Del. C. § 3572(c).

²¹⁶ Schanzenbach & Sitkoff, Perpetuities or Taxes? Explaining the Rise of the Perpetual Trust, 27 Cardozo L. Rev. 2465, 2495–96 (Apr. 2006).

²¹⁷ 27 Cardozo L. Rev. at 2479 (footnote omitted). See Sitkoff & Schanzenbach, Perpetuities, Taxes, and Asset Protection: An Empirical Assessment of the Jurisdictional Competition for Trust Funds, 42 U. Miami Inst. on Est. Plan. ¶ 1400 (2008); Sitkoff & Schanzenbach, Jurisdictional Competition for Trust Funds: An Empirical Analysis of Perpetuities and Taxes, 115 Yale L.J. 356, 375 n.62, 393–94 (Nov. 2005).

²¹⁸ Hoffman, Tough Judge Polices Merger Scene, Wall St. J., July 15, 2014, at C1.

²¹⁹ Del. Const. art. IV, § 3.

was ranked as the best in the country in a 2015 U.S. Chamber of Commerce study.²²⁰

In TrustCo Bank v. Mathews (2015),²²¹ Vice Chancellor Parsons of the Delaware Court of Chancery held that creditors' claims that transfers to Delaware APTs constituted fraudulent transfers were time-barred.²²² In other contexts, Delaware judges have demonstrated a willingness to enforce Delaware statutes in difficult cases, similar to those that might arise if creditors were to challenge Delaware APTs.

The following excerpt from the opinion of Vice Chancellor Berger in Gibson v. Speegle (1984)²²³ is representative:

In the absence of a statute, I would not hesitate to . . . allow Aetna's claim. I am not at all comfortable with the fact that Virginia Barwick, by use of a spendthrift trust, assisted her son in avoiding his obligation to pay for his crimes. [He was indicted on eight counts of arson, burglary, and criminal mischief and pled guilty to the lesser included offenses of criminal trespass in the first degree, arson in the third degree, and criminal mischief.] However, it is not the Court's function to write the law but only to interpret it. The statute enacted by the General Assembly contains no exceptions. . . . The proposed statute, which contained an exception for tort claimants . . . was available to the General Assembly in 1959 when § 3536 was amended. The fact that such a modification was not enacted leaves me no choice but to conclude that the General Assembly intended § 3536 to [be] an 'unrestrained' form of spendthrift provision. As a result, I reluctantly conclude that Aetna is a creditor within the meaning of § 3536 and its proof of claim must be denied.

In another difficult case—Delaware Trust Co. v. Partial (1986), Chancellor Allen of the Delaware Court of Chancery said that:²²⁴

²²⁰ U.S. Chamber of Commerce Institute for Legal Reform 2015 Lawsuit Climate Survey: Ranking the States (Sept. 2015), available at www.instituteforlegalreform.com/states (last visited Oct. 14, 2015).

²²¹ TrustCo Bank v. Mathews, 2015 Del. Ch. Lexis 18 (Del. Ch. 2015).

²²² 2015 Del. Ch. Lexis 18 at 48–49.

²²³ Gibson v. Speegle, 1984 Del. Ch. Lexis 475 at 6–7 (Del. Ch. 1984) (citations and internal quotation marks omitted).

²²⁴ Delaware Trust Co. v. Partial, 517 A.2d 259, 262 (Del. Ch. 1986).

The policy of the legislature with respect to the seizure or garnishment of funds held by Delaware banks is clear. I cannot conclude that that policy may be ignored by the simple expedient of denominating the writ sought as one of injunction rather than one of garnishment. Therefore, I conclude that irrespective of the strong probability of merit shown by the complaint, it would be inappropriate for this Court to grant the remedy now sought insofar as it seeks to restrain pendente lite the disposition by the Wilmington Trust Company of funds held by it.

G. Tenancy-by-the-Entireties Property Contributed to Trust

Several states recognize tenancies by the entireties in real and personal property.²²⁵ In 2007, Vice Chancellor Parsons of the Delaware Court of Chancery described the rules for tenancy by the entireties in Delaware real property as follows:²²⁶

In Delaware, a husband and wife generally hold title to real property in a tenancy by the entirety. Consequently, neither interest can be sold, attached, or liened except by the joint act of both spouses. Specifically, a judgment against the husband cannot be executed against a property interest he holds in a tenancy by the entirety.

A tenancy by the entireties also may be created in Delaware personal property.²²⁷

From an estate-planning standpoint, working with tenancy-by-the-entireties property is problematic because:²²⁸

When assets held as TBE are transferred to a trust in which only one party maintains control, the terms of the trust eliminate any TBE protection.

Once the property's character is destroyed, it cannot later be restored.²²⁹

²²⁵ See Franke, Asset Protection and Tenancy by the Entirety, 34 ACTEC J. 210 (Spring 2009).

²²⁶ Wilmington Sav. Fund Soc'y, FSB v. Kaczmarczyk, 2007 Del. Ch. Lexis 33 at 12–13 (Del. Ch. 2007) (footnotes omitted). See 25 Del. C. § 309.

²²⁷ 2007 Del. Ch. Lexis 33 at 43.

²²⁸ Quaid v. Baybrook Home of Polk County, 2011 U.S. Dist. Lexis 132299 at 5 (M.D. Fla. 2011).

²²⁹ In re Cowles, 143 B.R. 5, 10–11 (Bankr. D. Mass. 1992) (citation omitted). Accord In re Goldman, 111 B.R. 230, 232–33 (Bankr. E.D. Mo. 1990).

[E]ven if the trust were revoked, the Debtor provides no legal support for the assertion that the property will return to the Debtor and his wife as tenants by the entirety, and the Court can find nothing that would support such an assertion. To the contrary, the initial transfer of the property to the trust thirteen years ago terminated the tenancy by the entirety. While it is true that one spouse acting alone cannot terminate a tenancy by the entirety without the consent of the other, nothing prevents such termination by the two acting together. In the present case, when the Debtor and his wife together transferred the property to the trust, to be controlled by the Debtor alone, they terminated the joint ownership and control that is a requirement of a tenancy by the entirety. Such a tenancy does not renew itself automatically in the future. For these reasons, the Debtor's argument that creditors will only be able to reach his fifty percent interest in the property is irrelevant.

In 2010, Delaware enacted a statute that allows tenancy-by-the-entireties property contributed to a revocable trust to retain its character and thereby its ability to protect the property from a spouse's separate creditors.²³⁰ The statute, as amended in 2011 and 2013,²³¹ provides as follows:²³²

Where spouses make a contribution of property to 1 or more trusts, each of which is revocable by either or both of them, and, immediately before such contribution, such property or any part thereof or any accumulation thereto was, pursuant to applicable law, owned by them as tenants by the entireties, in any action concerning whether a creditor of either or both spouses may recover the debt from the trust, the sole remedy available to the creditor with respect to trust property shall be an order directing the trustee to transfer the property to both spouses as tenants by the entireties.

²³⁰ 12 Del. C. § 3334. I would like to thank Jonathan Gopman of Akerman Senterfitt, Naples, Florida, for suggesting this legislative change. See Gopman, STET: Delaware Introduces New Asset Protection Trust for Tenancy by the Entireties Property, LISI Asset Protection Planning Newsletter #161 (Sept. 8, 2010), www.leimbergservices.com.

²³¹ 78 Del. Laws 117, § 4 (2011), 79 Del. Laws 172, § 2 (2013).

²³² 12 Del. C. § 3334.

Illinois, Maryland, Missouri, Tennessee, Virginia, and Wyoming offer similar protection.²³³

The Delaware Act provides one more level of protection for tenancy-by-the-entireties property added to a Delaware APT. Hence, under the Delaware Act, tenancy-by-the-entireties property transferred to a Delaware APT retains its character until the death of the first spouse,²³⁴ and, if the trust is set aside (e.g., as a fraudulent transfer or a sham), the property retains its traditional protection from creditors.²³⁵ The current provision says:²³⁶

Where spouses make a qualified disposition of property to 1 or more trusts and, immediately before such qualified disposition, such property or any part thereof or any accumulation thereto was, pursuant to applicable law, owned by them as tenants by the entireties, in any action concerning whether a creditor of either or both spouses may recover the debt from the trust, upon avoidance of the qualified disposition, the sole remedy available to the creditor with respect to such trust property shall be an order directing the trustee to transfer the property to both spouses as tenants by the entireties.

In addition, the Delaware Act allows multiple transferors to contribute undivided interests to a Delaware APT as follows:²³⁷

“Qualified disposition” means a disposition by or from a transferor (or multiple transferors in the case of property in which each such transferor owns an undivided interest) to 1 or more trustees, at least 1 of which is a qualified trustee, with or without consideration, by means of a trust instrument.

The conflict-of-laws issues relating to the funding of a Delaware APT with tenancy-by-the-entireties property are comparable to those for Delaware APTs. In short, Delaware and non-Delaware residents should be able to take advantage of this technique for tenancies in personal property, but its effectiveness for

²³³ 765 Ill. Comp. Stat. 1005/lc; Md. Code Ann., Est. & Trusts § 14.5-511, Md. Code Ann., Cts. & Jud. Proc. § 11-504(b)(8)–(9); RSMo. § 456.950; Tenn. Code Ann. § 35-15-510; Va. Code Ann. § 55-20.2(B); Wyo. Stat. § 4-10-402(c), (d).

²³⁴ 12 Del. C. § 3574(f), as amended by 78 Del. Laws 117, § 13 (2011), 79 Del. Laws 198, § 1 (2014).

²³⁵ 12 Del. C. § 3574(f).

²³⁶ 12 Del. C. § 3574(f).

²³⁷ 12 Del. C. § 3570(7).

tenancies in non-Delaware real property is questionable.²³⁸

H. Lifetime QTIP and Other Trusts

1. The Delaware Statute

Thanks to recent federal tax legislation, the federal gift-tax, estate-tax, and GST-tax exemptions have jumped to \$5,430,000 per individual for 2015.²³⁹ This might cause wealthier spouses to create inter vivos QTIP trusts for less wealthy spouses to enable the latter to use their estate and GST exemptions in whole or in part. One concern with this strategy is that the trust might be treated as self-settled if the donor spouse will benefit from trust assets if he or she survives the donee spouse, thereby producing adverse tax and asset protection results. Long ago, the Treasury Department issued regulations specifying that trust assets would not be included in a donor spouse's gross estate under IRC § 2036 or § 2038 if this eventuated.²⁴⁰ However, whether creditors could reach trust assets under state law remained unresolved for many years.

In 2009, Delaware amended its spendthrift trust statute to provide that an inter vivos marital-deduction trust generally will not be treated as self-settled because the donor spouse might benefit from trust assets by surviving the donee spouse.²⁴¹ In 2014, the statute was expanded to cover lifetime credit-shelter trusts and other lifetime trusts.²⁴² The protection now extends to:²⁴³

[A] beneficial interest that is contingent upon surviving the trustor's spouse such as, but not limited to, an interest in an inter vivos marital deduction trust in which the interest of the trustor's spouse is treated as qualified terminable interest property under § 2523(f) of the Internal Revenue Code of 1986 [26 U.S.C. § 2523(f)], as amended, an

²³⁸ See Ruben & Gopman, Delaware Statutory Tenancy By the Entireties Trusts: Potentially Powerful Asset Protection for Couples Across the Country, 39 Tax Mgmt. Est., Gifts & Tr. J. 123, 126 (May 8, 2014).

²³⁹ Rev. Proc. 2014-61, 2014-47 I.R.B. 860, 867 § 3.33 (Nov. 17, 2014).

²⁴⁰ Reg. § 25.2523(f)-1(f), Ex. 11.

²⁴¹ 12 Del. C. § 3536(c)(2), as amended by 77 Del. Laws 98, § 16 (2009).

²⁴² 12 Del. C. § 3536(c)(1), as amended by 79 Del. Laws 352, § 4 (2014).

²⁴³ 12 Del. C. § 3536(c)(1), as amended by 79 Del. Laws 352, § 4 (2014). States with similar statutes include Arizona (Ariz. Rev. Stat. § 14-10505(E)); Florida (Fla. Stat. § 736.0505(3)); Kentucky (Ky. Rev. Stat. Ann. § 386B.5-020(8)); Maryland (Md. Code Ann., Est. & Trusts § 14.5-1003(a)(2)); Michigan (Mich. Comp. Laws § 700.7506(4)); New Hampshire (N.H. Rev. Stat. Ann. § 564-B:5-505(a)(2)(C)–(D)); North Carolina (N.C. Gen. Stat. § 36C-5-505(c)); Oregon (Or. Rev. Stat. § 130.315(4)); South Carolina (S.C. Code Ann. § 62-7-505(b)); Texas (Tex. Prop. Code § 112.035(g)); Virginia (Va. Code Ann. § 64.2-747(B)(2)); Wyoming (Wyo. Stat. Ann. 4-10-506(e)–(f)).

interest in an inter vivos marital deduction trust that is treated as a general power of appointment trust for which a marital deduction would be allowed under § 2523(a) and (e) of the Internal Revenue Code of 1986 [26 U.S.C. § 2523(a) and (e)], as amended, and an interest in an inter vivos trust commonly known as a “credit shelter trust” that used all or a portion of the trustor’s unified credit under § 2505 of the Internal Revenue Code [26 U.S.C. § 2505], as amended, . . .

2. The Supercharged Credit Shelter TrustSM

In 2007, Mitchell Gans, Jonathan Blattmachr, and Diana Zeydel introduced the concept of the Supercharged Credit Shelter TrustSM,²⁴⁴ under which a donor spouse creates an inter vivos QTIP trust for a donee spouse who subsequently dies and creates a credit-shelter trust for the donor spouse. The credit-shelter trust is “supercharged” because it is treated as a grantor trust with respect to the donor spouse for federal income-tax purposes.²⁴⁵ The Treasury Regulation mentioned above allays any IRC §§ 2036 and 2038 concerns, but it is silent regarding IRC § 2041. Accordingly, the designers of the Supercharged Credit Shelter TrustSM recommend subjecting distributions to an ascertainable standard and creating the trust in a state that recognizes self-settled trusts.²⁴⁶ Attorneys creating such trusts for clients also should consider the Delaware statute which was passed subsequent to introduction of the Supercharged Credit Shelter TrustSM concept, as an alternative to a self-settled trust because it is a straightforward solution and presents far fewer unresolved issues than the domestic APT.

XI. DOMESTIC APT TAX ISSUES

A. Structuring a Domestic APT to Be an Incomplete Gift

To date, most domestic APTs have been designed to offer protection from creditor claims but not to be completed gifts or excluded from the gross estate. For federal gift-tax purposes, an individual makes a taxable transfer when he or she parts with dominion and control over property.²⁴⁷ The traditional rule against self-settled trusts prevented taxpayers from making taxable gifts because they

²⁴⁴ Gans, Blattmachr & Zeydel, Supercharged Credit Shelter TrustSM, 21 Prob. & Prop. 52 (July/Aug. 2007). See Blattmachr, Gans & Zeydel, Supercharged Credit Shelter TrustSM Versus Portability, 28 Prob. & Prop. 11 (Mar./Apr. 2014).

²⁴⁵ 21 Prob & Prop. at 54–55.

²⁴⁶ 21 Prob. & Prop. at 56–57.

²⁴⁷ Reg. § 25.2511-2(b).

could incur debt and relegate creditors to trust assets. The domestic APT statutes are intended to change this result.

Early private letter rulings involving APTs concluded that the trustor's retention of a nongeneral testamentary power of appointment was sufficient, by itself, to prevent a completed gift.²⁴⁸ But, more recently, the IRS announced a change of position.²⁴⁹ It now requires that the trustor be able to prevent the making of gifts from the trust during his or her lifetime. Thus, in five 2013 rulings,²⁵⁰ several 2014 rulings,²⁵¹ and a series of 2015 rulings,²⁵² it said that a trustor will not make a completed gift to a self-settled trust if he or she keeps a nongeneral lifetime power of appointment and/or a power to prevent trustees, advisers, or protectors from making distributions to other beneficiaries as well as a nongeneral testamentary power of appointment.

B. Structuring a Domestic APT To Be a Completed Gift and Excludable From the Gross Estate

In 2009, the IRS ruled that the transfer of assets by an Alaska resident to an Alaska APT was a completed gift and that the trustee's discretion to pay income and principal to the trustor, the trustor's spouse, and the trustor's descendants was not sufficient, by itself, to cause inclusion of the trust's assets in the trustor's gross estate.²⁵³ But, the IRS warned that:²⁵⁴

We are specifically not ruling on whether Trustee's discretion to distribute income and principal of Trust to Grantor combined with other facts (such as, but not limited to, an understanding or pre-existing arrangement between Grantor and trustee regarding the exercise of this discretion) may cause inclusion of Trust's assets in Grantor's gross estate for federal estate tax purposes under § 2036.

²⁴⁸ See PLRs 200731019 (May 1, 2007), 200729025 (Apr. 10, 2007), 200715005 (Jan. 3, 2007), 200647001 (Aug. 7, 2006), 200637025 (June 5, 2006), 200612002 (Nov. 23, 2005), 200502014 (Sept. 17, 2004), 200247013 (Aug. 14, 2002), 200148028 (Aug. 27, 2001).

²⁴⁹ See IRS CCA 201208026 (Sept. 28, 2011). See also Zeydel, When is a Gift to a Trust Complete—Did CCA 201208026 Get it Right?, 117 J. Tax'n 142 (Sept. 2012); Covey & Hastings, Powers of Withdrawal; Gift Tax Annual Exclusion; Taxable Gifts; IRC Sec. 2702, Prac. Drafting 10770, 10773–76 (Apr. 2012).

²⁵⁰ PLRs 201310002–006 (Nov. 7, 2012).

²⁵¹ PLRs 201440008–012 (Dec. 31, 2013), 201436028–032 (Dec. 30, 2013), 201436023–027 (Dec. 19, 2013), 201436018–022 (Dec. 24, 2013), 201436013–017 (Jan. 3, 2014), 201436008–012 (Dec. 27, 2013), 201430003–007 (Feb. 7, 2014), 201426014 (Feb. 24, 2014), 201410001–010 (Oct. 21, 2013).

²⁵² PLRs 201510001–008 (Oct. 10, 2014).

²⁵³ PLR 200944002 (July 15, 2009).

²⁵⁴ PLR 200944002 (July 15, 2009).

Although Delaware allows the assets of APTs to be reached to pay certain claims of current and former spouses and minor children, the author of a recent Chief Counsel Advice Memorandum observed that:²⁵⁵

[T]he Supreme Court considered various situations in which a trust instrument purported to divest the respective grantor of all dominion and control over property to the extent that the property could not be returned to the grantor except by reason of contingencies beyond his control. In these cases, the Court noted that the respective grantor lost all economic control upon making the transfer, which he would not regain unless certain contingencies occurred. The Court concluded that the respective gifts were complete

To support the above proposition, the writer cited two United States Supreme Court cases and one Tax Court case.²⁵⁶ The foregoing authorities and cases involving the acts-of-independent-significance doctrine indicate that completed gift treatment should be available in Delaware.²⁵⁷

Apparently without studying the Nevada Act closely, some commentators have opined that Nevada is comparable to Alaska for these purposes.²⁵⁸ Nevada permits the assets of APTs to be accessed not only to pay fraudulent-transfer claims but also if “the transfer violates a legal obligation owed to the creditor under a contract or a valid court order that is legally enforceable by that creditor.”²⁵⁹ I am not aware of any authority that supports the proposition that a transfer to an APT will be a completed gift and excludible from the gross estate where such an open-ended exception exists.

In any event, in 2011, my firm—Wilmington Trust Company—engaged counsel to attempt to obtain a Delaware private letter ruling comparable to the Alaska

²⁵⁵ IRS CCA 201208026 (Nov. 7, 2012).

²⁵⁶ See Smith v. Shaughnessy, 318 U.S. 176, 181 (1943) (“grantor has neither the form nor substance of control and never will have unless he outlives his wife”); Robinette v. Helvering, 318 U.S. 184, 187 (1943) (property “could not be returned to them except because of contingencies beyond their control”—whether daughter had children); Kolb Est. v. Comr., 5 T.C. 588, 596 (1945) (“the donor decedent had no power to modify the trust in any way and never could have except upon the happening of an event beyond his control”—birth of more grandchildren).

²⁵⁷ See U. S. v. Byrum, 408 U.S. 125, 150 (1972); Ellis v. Comr., 51 T.C. 182, 187–88 (1968), aff’d, 437 F.2d 442 (9th Cir. 1971); Tully Est. v. U.S., 528 F.2d 1401, 1406 (Ct. Cl. 1976); TAM 8819001 (Jan. 6, 1988); PLR 9141027 (July 11, 1991).

²⁵⁸ See Gassman, Crotty & Pless, Safe Trust Guide—Why Your Family Needs a Safe Trust and What to Do to Implement One by the End of 2012 (the Spouse and Family Exempt (“SAFE”) Trust), 37 Tax Mgmt. Est., Gifts & Tr. J. 193 (May 10, 2012); Rothschild, et al., IRS Rules Self-Settled Alaska Trust Will Not Be In Grantor’s Estate, 37 Est. Plan. 3, 12 (Jan. 2010).

²⁵⁹ Nev. Rev. Stat. § 166.170(3).

ruling. Late in the year, representatives of the IRS told counsel that the IRS was not willing to issue the ruling. According to counsel, the IRS's unwillingness to rule was not attributable to Delaware's family exceptions, etc. Rather, the IRS appears to be troubled by commentary about the 2011 In re Mortensen²⁶⁰ bankruptcy case in Alaska. The IRS representative said that the Alaska ruling probably would not be issued if they were looking at it now and that the IRS since has declined other Alaska ruling requests.

C. Structuring a Domestic APT to Be an Incomplete Gift and a Nongrantor Trust: The DING Trust

Most domestic APTs are grantor trusts for federal income-tax purposes under § 677(a) because the trustee may distribute income to—or accumulate it for—the trustor without the approval of an adverse party. But, a client might use a type of domestic APT known as the Delaware Incomplete Nongrantor Trust (“DING Trust”) to avoid income tax on undistributed ordinary income and capital gains imposed by a state (i.e., Pennsylvania or Tennessee) that has not adopted the federal grantor-trust rules or, if the client is willing to subject distributions to himself or herself to the control of an adverse party, to avoid income tax on such income imposed by one of the 42 states (e.g., Connecticut or New Jersey) that have adopted the federal grantor-trust rules. In five 2013 private letter rulings,²⁶¹ several 2014 rulings,²⁶² and a series of 2015 rulings,²⁶³ the IRS ruled that domestic APTs that followed the DING-Trust approach qualified as nongrantor trusts. Most—if not all—of the trusts in question were created under Nevada law in large part because, at the time, Nevada was the only domestic APT state that allowed a trustor to keep a lifetime nongeneral power of appointment. Delaware now offers that option as well.²⁶⁴

The trustor of a DING Trust might be able to receive tax-free distributions of the untaxed income in later years.²⁶⁵

²⁶⁰ In re Mortensen, 2011 WL 5025252 (Bankr. D. Alaska 2011); In re Mortensen, 2011 Bankr. Lexis 5560 (Bankr. D. Alaska 2011); In re Mortensen, 2011 Bankr. Lexis 5004 (Bankr. D. Alaska 2011).

²⁶¹ PLRs 201310002–006 (Nov. 7, 2012).

²⁶² PLRs 201440008–012 (Dec. 31, 2013), 201436028–032 (Dec. 30, 2013), 201436023–027 (Dec. 19, 2013), 201436018–022 (Dec. 24, 2013), 201436013–017 (Jan. 3, 2014), 201436008–012 (Dec. 27, 2013), 201430003–007 (Feb. 7, 2014), 201426014 (Feb. 24, 2014), 201410001–010 (Oct. 21, 2013).

²⁶³ PLRs 201510001–008 (Oct. 10, 2014).

²⁶⁴ 12 Del. C. § 3570(11)(b)(2).

²⁶⁵ See Akhavan, DINGing State Income Taxes in Artwork Transactions, 153 Tr. & Est. 31 (June 2014); Schaller, Reduce State Tax With DINGs, NINGs, WINGs, and Other THINGs, 41 Est. Plan 23, 24–26 (Apr. 2014); Brown & Lambourne, California ING Trusts: A Cautionary Tale of Your Future State Law?, LISI Inc. Tax Planning Newsltr. #63 (Mar. 11, 2014), www.leimbergservices.com; Flubacher & Goodwin, DINGed but not Dented, 152 Tr. & Est. 14 (July 2013).

Effective June 1, 2014, DING Trusts no longer work in New York,²⁶⁶ but the technique still is viable for residents of Connecticut, New Jersey, and other states.

XII. FLP/LLC LAWS

A good trust jurisdiction should have favorable FLP and LLC statutes. Specifically, those statutes should provide that a charging order is a creditor's sole remedy and that other remedies, particularly foreclosure, are not available. Delaware meets these requirements (including for single-member LLCs).²⁶⁷ But Connecticut²⁶⁸ and New York²⁶⁹ allow foreclosure and other remedies. New Jersey satisfies the requirements for LLCs²⁷⁰ but still does not prohibit the foreclosure of FLP interests.²⁷¹

Because there has been some confusion over the status of FLPs and LLCs in Delaware, I summarize those rules briefly here. Not only do Delaware's FLP and LLC statutes stipulate that a charging order is a creditor's sole remedy and that other remedies, including foreclosure, are unavailable, but Delaware and non-Delaware caselaw confirms these results.

Specifically, the pertinent provision of Delaware's LLC statute provides that:²⁷²

The entry of a charging order is the exclusive remedy by which a judgment creditor of a member or of a member's assignee may satisfy a judgment out of the judgment debtor's limited liability company interest and attachment, garnishment, foreclosure or other legal or equitable remedies are not available to the judgment creditor, whether the limited liability company has 1 member or more than 1 member.

The synopsis to the 2005 legislation that enacted the original version of the above provision describes the law in Delaware as follows:²⁷³

²⁶⁶ See N.Y. Tax Law § 612(b)(41), added by 2014 N.Y. Laws 59, Part I, § 2 (2014).

²⁶⁷ 6 Del. C. § 17-703(d) (FLPs); 6 Del. C. § 18-703(d) (LLCs).

²⁶⁸ Conn. Gen. Stat. § 34-30, Madison Hills Limited Partnership II v. Madison Hills, Inc., 644 A.2d 363, 370 (Conn. App. Ct. 1994) (FLPs); Conn. Gen. Stat. § 34-171, PB Real Estate v. DEM II Properties, 1997 Conn. Super. Lexis 2654 at 9–10 (Conn. Super. Ct. 1997) (LLCs).

²⁶⁹ N.Y. Partnership Law §§ 111(3), 121-703 (FLPs); N.Y. Ltd. Liab. Co. Law § 607 (LLCs). See Merric, Comer & Monasky, Updated Limited Partnership Asset Protection Planning Table, LISI Asset Protection Planning Newsltr. #189 (Jan. 10, 2012), www.leimbergservices.com; Merric, Comer & Monasky, Updated LLC Asset Protection Planning Table, LISI Asset Protection Planning Newsltr. #190 (Jan. 23, 2012), www.leimbergservices.com.

²⁷⁰ NJSA § 42:2C-43.

²⁷¹ NJSA § 42:2A-48.

²⁷² 6 Del. C. § 18-703(d).

²⁷³ 75 Del. Laws 51, synopsis to §§ 9–15 (2005). A bill's synopsis constitutes legislative history in Delaware.

Sections 9, 10, 11, 12, 13, 14 and 15. These sections amend Section 18-703 to clarify the nature of a charging order and provide that a charging order is the sole method by which a judgment creditor may satisfy a judgment out of the limited liability company interest of a member or a member's assignee. Attachment, garnishment, foreclosure or like remedies are not available to the judgment creditor and a judgment creditor does not have any right to become or to exercise any rights or powers of a member (other than the right to receive the distribution or distributions to which the member would otherwise have been entitled, to the extent charged).

Delaware's FLP statute²⁷⁴ and the synopsis to the 2005 legislation that updated it²⁷⁵ contain comparable language. In 2010, Judge Sleet of the U.S. District Court for the District of Delaware wrote:²⁷⁶

Because Delaware law does not permit foreclosure on charging orders, Bay Guardian would be unable to foreclose against New Times and the entities.

In the same year, Judge Erickson of the United States District Court for the District of Minnesota wrote:²⁷⁷

[A] charging order is the exclusive remedy under Delaware law by which a judgment creditor may satisfy a judgment out of a member's interest in a limited liability company.

If a resident of State 1 creates an FLP or LLC of personal property in State 2, does State 1 or State 2 law determine whether a creditor may reach a partner's or member's interest? A 2011 article suggests that State 2 law should be used:²⁷⁸

[I]f an individual resides in one state but has a personal property interest in a limited partnership or

²⁷⁴ 6 Del. C. § 17-703.

²⁷⁵ 75 Del. Laws 31, synopsis to §§ 10–16 (2005).

²⁷⁶ New Times Media, LLC v. Bay Guardian Co., Inc., 2010 U.S. Dist. Lexis 64395 at 8 (D. Del. 2010).

²⁷⁷ General Elec. Capital Corp. v. JLT Aircraft Holding Co., 2010 U.S. Dist. Lexis 76384 at 7 (D. Minn. 2010).

²⁷⁸ Gassman & Denicolo, Pass-Through Entities Have Protections in Charging Order Law, 38 Est. Plan. 31, 36 (Nov. 2011).

LLC located in another state, he or she may be held to the law of the state where the entity is located. The courts have consistently leaned toward finding that the controlling law with respect to the entity is the state law where the entity was formed

Nevertheless, a federal district court in Florida held in Wells Fargo Bank, N.A. v. Barber (2015)²⁷⁹ that Florida law would determine whether a creditor could reach a Florida resident's interest in a single-member Nevis LLC.²⁸⁰

²⁷⁹ Wells Fargo Bank, N.A. v. Barber, 2015 U.S. Dist. Lexis 13488 (M.D. Fla. 2015). See Gassman & Arango, Wells Fargo v. Barber: The Barber of Seville Replaces No Time For Sargeants, LISI Asset Protection Planning Newsltr. #287 (Mar. 24, 2015), www.leimbergservices.com.

²⁸⁰ 2015 U.S. Dist. Lexis 13488 at 16–17.