

Don't worry! A broken trust can be fixed

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There are good reasons why estate planning advisors recommend you revisit and, if necessary, revise your estate plan periodically: changing circumstances, including family situations and new tax laws. While it's relatively simple to change a beneficiary, what if an irrevocable trust no longer serves your purposes? Depending on applicable state law, you may have options to fix a "broken" trust.

Reasons why a trust can break

A trust that works just fine when it's established may no longer achieve its original goals if your family circumstances change. If you divorce, for example, a trust for the benefit of your spouse may no longer be desirable. If your children grow up to be financially independent, they may prefer that you leave your wealth to *their* children. Or perhaps you prefer not to share your wealth with a beneficiary who has developed a drug or alcohol problem or has proven to be profligate.

Another reason is new tax laws. Many trusts were created when gift, estate and generation-skipping transfer ("GST") tax exemption amounts were relatively low. Today, however, the exemptions have risen to \$11.4 million, so trusts designed to minimize gift, estate and GST taxes may no longer be necessary. And with transfer taxes out of the picture, the higher income taxes often associated with these trusts — previously overshadowed by transfer tax concerns — become a more important factor.

Here are possible remedies

If you have one or more trusts in need of repair, you may have several remedies at your disposal, depending on applicable law in the state where you live and, if different, in the state where the trust is located. Potential remedies include:

Reformation. The Uniform Trust Code ("UTC"), adopted in more than half the states, provides several remedies for broken trusts. Non-UTC states may provide similar remedies. Reformation allows you to ask a court to rewrite a trust's terms to conform with the grantor's intent. This remedy is available if the trust's original terms were based on a legal or factual mistake.

Modification. This remedy may be available, also through court proceedings, if unanticipated circumstances require changes to achieve the trust's purposes. Some states permit modification — even if it's inconsistent with the trust's purposes — with the consent of the grantor and all the beneficiaries.

Decanting. Many states have decanting laws, which allow a trustee, according to his or her distribution powers, to “pour” funds from one trust into another with different terms and even in a different location. Depending on your circumstances and applicable state law, decanting may allow a trustee to correct errors, take advantage of new tax laws or another state’s asset protection laws, add or eliminate beneficiaries, extend the trust term, and make other changes, often without court approval.

Before you make any changes, it’s critical to consult your attorney and tax advisor to discuss the potential benefits and risks.

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The Law Office of Eugene Gorrin, LLC
17 Watchung Avenue, Suite 204
Chatham, NJ 07928
973.701.9300
egorrin@gorrinlaw.com
www.gorrinlaw.com