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The REPTL Reporter is the official journal of the Real Estate, Probate, and Trust Law Section of the State Bar of Texas (REPTL). It is published by REPTL to provide education and information for REPTL members in the areas of real estate, probate, trust, guardianship, tax, and water law. A copy of each issue is furnished to the members of REPTL as part of their section dues.

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My Two Cents: Two Provisions to Include in Trusts Governed by the New Texas Rule Against Perpetuities Period

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I. Introduction

The current environment of federal tax law uncertainty and the increased focus on our own mortality amid the COVID-19 pandemic has unquestionably had an effect on how wealthy individuals and families approach estate and trust planning. Not only has there been a significant surge in will drafting due to COVID-19, any estate planning professional will attest that in years of increased tax law uncertainty there is generally a correlation of increased interest in the creation of irrevocable trusts.⁵

A fundamental determination that must be initially addressed in creating an irrevocable trust is *the appropriate duration of the trust*. In some instances, it may be fitting for a trust agreement to contain “age-terminating” distributions to the beneficiary. A common and simplistic example would require the trustee of a trust to distribute one-third of the fair market value of the trust to the beneficiary outright once the beneficiary reaches age twenty-five, one-half at age thirty and the remaining trust estate at age thirty-five, at which time the trust would terminate.⁶ In other situations, the best practice would be to have the trust last for the lifetime of the primary beneficiary, or for as long as state law allows.⁷ For many decades, Texans relied upon the common law rule against perpetuities (RAP) period contained in the Texas Property Code, and could draft trust agreements based on the understanding that remaining trust assets would pay out to those beneficiaries who were living twenty-one years after the death of the last designated life in being at that time.⁸ If Texas settlors desired a longer period, they would have to look to other states for that option.

With Texas’s new RAP period, as it applies to non-charitable trusts, the duration of Texas trusts that became irrevocable on or after September 1, 2021, will now have a fixed 300-year time limit.⁹ While a detailed discussion of the new RAP period is beyond the scope of this article, it is difficult for parents, grandparents, or any settlor to fathom creating a trust that will exist for 300 years.¹⁰ At the end of the RAP period, trust assets will ultimately distribute to descendants so remote the settlor will not have personally known the beneficiary, or even the beneficiary’s grandparent. At this point, the attorney is

* The author does not represent JPMorgan Chase & Co., or its affiliates, in a legal capacity.

⁵ Rachel Ripp, [More West Texans Drafting Wills Due to COVID-19](#), NEWS WEST 9, Sept. 10, 2021.

⁶ A discussion regarding factors to consider when choosing an age-terminating trust or a trust with a longer duration is beyond the scope of this article, but questions to consider are size and asset composition of the trust, maturity and financial sophistication of the beneficiaries, need for protection from creditors or divorce, and general intent of the settlor.

⁷ Allowing the trust estate to stay intact for as long as possible generally provides the beneficiary with optimal protection from creditors, and may preserve a settlor’s transfer tax exemption amounts for future generations.

⁸ See [TEX. PROP. CODE § 112.036](#).

⁹ [TEX. PROP. CODE § 112.036](#); see Catherine Bright Haws & Ashley E. McMillan, [A New Texas Rule Against Perpetuities for Trusts](#), 59 REAL ESTATE PROB. & TR. L. REP. 3, 2021.

¹⁰ See Howard Zaritsky, [The Rule Against Perpetuities: A Survey of State \(and D.C.\) Law](#), AM. COLL. OF TR. AND EST. COUNSEL 1 (last visited Oct. 6, 2020).

not merely drafting for conventional “unforeseen” family circumstances (such as a child’s hidden substance addiction) but is drafting for a trust that will not terminate until some time after the year 2300.

This creates challenges for practitioners and families alike because it becomes unrealistic to have expectations about one’s lineage so far into the future. How can a settlor properly plan for all possible contingencies? What is a proper balance of restriction, flexibility, access, and control for beneficiaries born a couple hundred years from now? If there is a need to change, amend or modify the irrevocable trust, what is the path of least resistance to avoid the need for judicial intervention? This article addresses two highly effective strategies that will provide future trustees and beneficiaries the means to manage and administer trusts that may now exist for 300 years. Practitioners should consider whether their current drafting style or forms should be modified to include these provisions in light of the new extended Texas RAP period.

II. Discretion to Decant

Since September 1, 2013, the ability to “decant” an existing trust has been an extraordinarily powerful tool in the Texas estate planner’s toolbox.¹¹ To decant a trust, an “authorized” trustee distributes some or all of the principal from an existing trust to a new trust that has different and more favorable terms.¹² This was a welcomed addition to the Texas Trust Code because modification or alterations to a trust can now be accomplished through the trustee’s own action, including providing the required notice to the beneficiaries in compliance with the governing statutes.¹³ Prior to enactment, an irrevocable trust could generally only be modified by techniques such as non-judicial settlement agreements, judicial modifications, or trust mergers; each method having its own limitations.¹⁴

Decanting can be used to modify an existing trust agreement to achieve a variety of goals. Some goals are as follows: to correct drafting errors, build out fiduciary succession provisions, change the situs of the trust to a friendlier jurisdiction, allow state income tax flexibility, add or change trust beneficiaries, provide beneficiaries with the power to redirect trust assets, change certain distribution provisions, extend the duration or terminate a trust or change a trust to qualify for special needs trust treatment.¹⁵ This example list is by no means exhaustive.

In light of the extended Texas RAP period, it may make sense to draft a trust agreement in a way that maximizes the trustee’s ability to decant. With a trust agreement that clearly paves the way to decant, the latitude of a future trustee’s options for modifying the trust appreciably expands. To accomplish this, the trust agreement itself can contain explicit provisions drafted by the attorney permitting decanting, or the drafting attorney may rely on [TEX. PROP. CODE §§ 112.071–87](#). These

¹¹ [TEX. PROP. CODE § 112.071](#).

¹² [TEX. PROP. CODE §§ 112.071–73](#). An authorized trustee is a person, other than the settlor, who has authority under the terms of a first trust to distribute the principal of the trust to or for the benefit of one or more current beneficiaries. [PROP. §112.071\(1\)](#).

¹³ [TEX. PROP. CODE §§ 112.071–87](#).

¹⁴ For additional reading on decanting and other modification options, see Toby Eisenberg, *Uncontested Trust Modifications: Tips and Techniques*, 45 STATE BAR OF TEX. ANN. ADVANCED REAL EST. & PROB. (2021).

¹⁵ A discussion of decanting and potential transfer tax issues is beyond the scope of this article. For a detailed discussion, see William R. Culp, Jr. & Briani Bennett-Mellen, [Trust Decanting—State Law and Federal Tax Considerations](#), [BLOOMBERG LAW PRORFOLIO 871](#)-2ND T.M. (last visited Oct. 15, 2021).

statutes contain the authority for decanting. Notably, the statutes contain a critical distinction between “full discretion” trustees and “limited discretion” trustees. The trustee’s level of discretion, whether full or limited, gives rise to the scope of its authority in making modifications to the existing trust agreement.

“Full discretion” means that the trustee of the existing trust has a power to distribute principal to or for the benefit of one or more of the beneficiaries of a trust, and that the trust is not a trust with limited discretion. Conversely, “limited discretion” means either (1) a power to distribute principal according to mandatory distribution provisions under which the trustee has no discretion, such as the age-terminating example referenced in the introduction; or (2) a power to distribute principal to or for the benefit of one or more beneficiaries of a trust that is limited by an ascertainable standard, including the health, education, support, or maintenance of the beneficiary.¹⁶

Trustees with either full or limited discretion may decant to modify administrative provisions such as fiduciary succession provisions. The disparity in authority between full discretion trustees and limited discretion trustees becomes apparent when modifying the more substantive provisions of an existing trust. Should a trustee wish to decant in order to change the original beneficiaries of the first trust, the trustee must have full discretion to do so. [Section 112.072\(a\)](#) of the Texas Property Code provides that a trustee with full discretion may distribute trust principal to a second trust for the benefit of one, more than one, or all of the current beneficiaries of the first trust and for the benefit of one, more than one, or all of the successors or presumptive remainder beneficiaries of the first trust. A trustee with full discretion may also alter the class or objects of a power of appointment granted under the first trust.¹⁷ These options are not available to trustees with limited discretion.

It should be noted that a trustee cannot use the decanting statute to extend the RAP period of the existing trust, eliminate certain vested rights of a beneficiary, or make certain changes to benefit himself. The decanting trustee cannot eliminate a right of removal for his position, decrease his fiduciary duties, reduce liability for breach of those duties, or solely change trustee compensation provisions.¹⁸

Granting full discretion to a trustee in a trust agreement will ensure maximum flexibility to decant under current Texas law. Although, as one might imagine, a settlor may not want to provide the trustee with the power to distribute trust principal in absence of an ascertainable standard, as this course of action could be contrary to the settlor’s intent in creating an irrevocable trust. A variety of personal or delicate reasons may come into play. Additional considerations arise when a beneficiary or related party is also serving as a trustee with full discretion. In this situation, distributions must be limited to an ascertainable standard, generally health, education, maintenance, and support. This is so that the trust not only retains its integrity as an asset protection vehicle, but also retains any favorable transfer tax characteristics.

To guard against these concerns, the trust agreement could allow for the appointment of an independent trustee. The independent trustee is generally authorized to make distributions to the beneficiary above and beyond an ascertainable standard, while still maintaining asset protection and transfer tax benefits.¹⁹ The independent trustee could then decant with the expanded powers enumerated in the statute or as described in the existing trust agreement. As such, the drafting attorney

¹⁶ [TEX. PROP. CODE § 112.071\(5\), \(6\)](#).

¹⁷ [TEX. PROP. CODE § 112.072\(b\)–\(d\)](#).

¹⁸ [TEX. PROP. CODE § 112.085](#).

¹⁹ [TEX. PROP. CODE § 112.079](#).

should carefully consider and build out the following provisions relating to the role of an independent trustee: (i) scope of authority (that could include powers beyond non-discretionary distributions); (ii) fiduciary duties; (iii) standard of care; (iv) liability; (v) indemnity, if any; (vi) compensation; (vii) succession, removal and vacancy; and (viii) provisions describing what happens if there is no independent trustee ready and willing to serve.

Though including an independent party will allow the trust agreement to be pliable, this option requires the settlor to entrust a certain level of control to someone other than their partner, descendants, or other related individuals that are not qualified to serve as an independent party under state or federal law. Additionally, if the settlor considers appointing a bank or trust company as an independent trustee, the settlor should speak with the trust department prior to the appointment as some institutions may not be keen to accept appointment only to exercise the authority to decant. Similar to institutions, individuals might be hesitant to serve because of the exposure to liability, as well as difficulty navigating thorny income and transfer tax issues.

Despite potential challenges in executing a decanting, it may make sense to draft the trust agreement to leave the door open for the future trustee to consider whether decanting helps meet the needs of the trust's beneficiaries. The trustee's level of discretion in the trust agreement is a vital consideration in the decanting analysis. In fact, drafting a trust agreement in such a way as to utilize the Texas decanting statute to its fullest may serve as a savings mechanism if other more flexible provisions are not contained in the trust agreement, because the decanting statute could later be used to modify the existing trust to include such provisions.

III. Power to Redirect Trust Assets

The ability of a beneficiary (or another individual generally called a powerholder) to direct the trustee to distribute trust assets to other individuals, entities, or to one's self is undoubtedly one of the most significant tools for creating the elasticity a trust agreement may require to stand the test of time. A "power of appointment" allows the beneficiary to adapt to family changes, changes in tax laws and other situations that cannot be contemplated at the time a trust agreement is executed. A power may be "exercised" or used during a beneficiary's lifetime, or at her death through her testamentary documents. Testamentary documents usually include a will or codicil that recite facts regarding the power and provide instructions for the redirection of the trust property.

A power of appointment can be extremely broad, permitting a beneficiary to give property held in trust to an appointee (which can be any person or entity). This is referred to as a general power of appointment, and this type of power may cause unintended consequences such as loss of spendthrift protection or estate tax inclusion.²⁰ For example, suppose Mom creates an irrevocable trust for Child, with a general power that allows Child to redirect trust assets to anyone upon Child's death. All of the assets subject to the power are included in Child's estate for federal estate tax purposes, which in most cases is not the intended result.²¹ Despite the potential adverse tax consequences, in some specific situations estate planning practitioners will use a general power to achieve certain transfer tax benefits. For example, a general power may be "triggered" in circumstances such as to obtain a "step-up" in income tax basis at a beneficiary's death or to allow a beneficiary to use her own generation-skipping transfer (GST) tax exemption on the trust property. As one can see, general powers can have quite

²⁰ I.R.C. §§ [2041](#) & [2514](#).

²¹ [I.R.C. § 2041](#).

serious income, gift, estate, and GST tax consequences.²²

Use of a non-general power may avoid some of these potential tax pitfalls.²³ A non-general power limits the scope of appointees to whom a beneficiary may redirect trust assets. Non-general powers are often referred to as limited or special powers of appointment. Structured properly, this type of power should not give rise to loss of creditor protection or estate tax issues, as long as the beneficiary did not create the power herself and cannot direct trust property to (i) herself, (ii) her estate, (iii) her creditors or (iv) the creditors of her estate. A popular example is the following scenario: Dad creates an irrevocable trust for Child and gives her lifetime and testamentary limited power of appointment. Child may only redirect trust property to her own descendants, the spouses of her own descendants in trust and to charitable organizations as defined in the [Internal Revenue Code](#). If Child chooses not to exercise this power, the remaining trust property will be distributed to the Child's own descendants at her death. This means during her lifetime and in her will, Child may distribute the trust property only to her descendants, the spouses of those descendants, and to charity, but in any amounts as she sees fit and either in further trust or outright. Should one of her children not need as much due to his or her own success, she can redirect trust property to her other children. Should Child need to alter the plan to fit her own circumstances, such as creating a trust at her death for the benefit of her partner to help maintain the household, Child is able to do so. Exercising a lifetime power of appointment, however, may cause adverse gift tax consequences depending on the specific distribution provisions of the trust agreement and other factors.²⁴

Powers of appointment provide a unique opportunity for modifying the original distribution of trust assets by allowing a beneficiary to change the ultimate disposition of trust property. Years, decades, perhaps centuries after a trust is created, a beneficiary may be in a better position than the settlor to determine who should ultimately benefit from the trust assets, based on their current family situation. Instead of outright transfers, trust assets could be funneled to a new trust with more favorable terms given the current needs and current laws in effect. Similar to decanting though, a power of appointment cannot be used to extend the original RAP period of the original governing document.

Powers of appointment may produce similar concerns to decanting. A settlor may not be enthusiastic about granting such a potentially broad power to a non-fiduciary powerholder. For added protection, the settlor could include a provision requiring the consent of an independent party to exercise the power. This may hedge against a settlor's fears regarding the ultimate use of the property, but again, the drafting attorney should fully augment the appointment utilizing any other relevant provisions to the intended scope of this role.

IV. Conclusion

The new fixed 300-year time limit for non-charitable irrevocable trusts requires a shift in perspective on the way that trusts have been traditionally drafted for the last few decades. Practitioners

²² Additionally, an inter vivos exercise or release of a general power of appointment is a transfer of property that may be subject to gift tax under [I.R.C. §2514](#). A general power may also inadvertently trigger the grantor trust rules in I.R.C. §§ [671–79](#).

²³ The exercise of a limited power can also result in a taxable transfer if a donee has the right to trust income and also has the power to direct income distributions to another. For a detailed discussion, see Christopher P. Cline, *Powers of Appointment—Estate, Gift, and Income Tax Considerations*, *Bloomberg Law Portfolio 825-4th T.M.* (last visited Oct. 15, 2021).

²⁴ *Id.*

should invest the time to research decanting and powers of appointments and revise their form language in accordance with best practices. Practitioners should also place a higher emphasis on the settlor's understanding of the duration of an irrevocable trust and the settlor's views on the potential need to modify, amend, or alter the trust. Engaging in conversations regarding decanting, powers of appointment, and other techniques will lead to the best result for the settlor and the many future generations of trust beneficiaries.