

Can a broken trust be fixed?

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An irrevocable trust has long been a key component of many estate plans. But what if it no longer serves your purposes? Is it too late to change it? Depending on applicable state law, you may have several options for fixing a “broken” trust.

How trusts break

There are several reasons a trust can break, including:

Changing family circumstances. A trust that works just fine when it’s established may no longer achieve its original goals if your family circumstances change. Some examples are a divorce, second marriage or the birth of a child.

New tax laws. Many trusts were created when gift, estate and generation-skipping transfer (“GST”) tax exemption amounts were relatively low. However, for 2021, the exemptions have risen to \$11.7 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. *(Note, however, that the exemptions are scheduled to be revert to \$5 million adjusted for inflation in 2026, and there are also pending legislative proposals that enacted would reduce the exemptions sooner - perhaps as early as this year - to \$5 million or perhaps even further to \$3.5 million and the gift tax exemption to \$1 million.)*

Mistakes. Potential errors include naming the wrong beneficiary, omitting a critical clause from the trust document, including a clause that’s inconsistent with your intent, and failing to allocate your GST tax exemption properly.

These are just a few examples of the many ways you might end up with a trust that fails to achieve your estate planning objectives.

How to fix them

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 in order 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 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, and make other changes, often without court approval.

Seek professional guidance

The rules regarding modification of irrevocable trusts are complex and vary dramatically from state to state. And there are risks associated with revising or moving a trust, including uncertainty over how the IRS will view the changes. Before you make any changes, talk to us about the potential benefits and risks.

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