

2017 HOUSE JUDICIARY

HB 1228

2017 HOUSE STANDING COMMITTEE MINUTES

Judiciary Committee
Prairie Room, State Capitol

HB 1228
1/18/2017
27051

- Subcommittee
 Conference Committee

Committee Clerk Signature

Donna Whelan

Explanation or reason for introduction of bill/resolution:

Relating to the capacity of a settlor of a revocable trust, actions contesting the validity of a trust, and powers to direct a trustee; and to provide for retroactive application.

Minutes:

Attachments 1,2,3

Vice Chairman Karen Karls: Opened the hearing on HB 1228.

Chairman K. Koppelman: Introduced the bill.

Marilyn Foss, General Counsel for North Dakota Bankers Assoc: Discussed how the uniform trust code needs updating. Things have changed and this was looked at over 10 years ago. We need to update our code to encompass all the new changes and we have people that will offer these changes. We have 6 accomplished attorneys here and they will be speaking to the substance of the bill. We found North Dakota does not have laws for a process to deal with how things have changed when you have a Legacy Trust and you want to develop a new trust. If you don't do that in a special way you create a taxable event. I talked to some of the bankers that have trust powers and asked where should we be looking at that. They stated decanting, UniTrusts and what about challenges to the validity of the trust. I checked with trust lawyers and bankers. You will hear from these people this morning. There is kind of a place holder provision in a part of the bill in response to an inquiry that was received by Representative Koppelman about perpetual trusts. There will be some amendments discussed and possibly introduced today.

Representative Klemin: This is a uniform act and the Uniform Trust Code is a uniform Act.

Marilyn Foss: Yes the Uniform Trust Code and these are changes to it. They are not part of the revised Act.

Representative Klemin: As you mentioned this was the State Bar Association Uniform Law Commission joint project. When the North Dakota part was adopted did you work with the State Bar Association and other people around North Dakota with this revision?

Marilyn Foss: The State Bar Association did not feel they could convene in a timely manner. They were invited to participate. The people who worked on it were the people who responded with interest.

Representative Klemin: I worked on that project as a Uniform Law Commissioner and you didn't contact me.

Marilyn Foss: That is correct. I did not contact you we did discuss that but then we worked within my community. Which is bankers and trust bankers. We contacted State Bar Association of North Dakota (SBAND) about it was to give the opportunity to lawyers throughout the state. They decided not to take it under its umbrella at that point. My understanding was that you worked more on real estate and my focus was to get trust bankers and lawyers that worked within the trust arena on this.

Chairman K. Koppelman: Housekeeping things on the bill, Mr. Guy whom you will hear from shortly is highly respected in his profession. We have deferred to him on many complex issues on corporate issues, LLC's and trusts.

William Guy, State Bar Association of North Dakota: See testimony in addition to the bill. (See Attachment 1) (13:10-22:10)

Chairman K. Koppelman: (22:10- I was informed prior to session that North Dakota limits Business Continuity Trusts to 99 years under current law and South Dakota in perpetuity so as a result we have a lot of North Dakota people doing this in South Dakota and that would be needless if we would change our law.

William Guy: Went over proposed amendment. (See Attachment 2). (25:33-31:00)

Representative Klemin: On the amendments was this also called an Alaska trust?

William Guy: Alaska is one of the states that repealed the ruling against perpetuity. What they have tried to do with their trust law is that it is very difficult to collect a judgement against the person who created the trust. The trust we are contemplating here is if I had mineral interests and wanted to set up a trust for my family. It wouldn't be something I did for myself to avoid estate taxes on my death or to protect it from my own creditors.

Representative Klemin: This trust could run forever?

William Guy: Yes, unless there was provision in the document to allow it to be terminated. Or if the trust gets to a point that it is impractical to continue.

Representative Klemin: You are proposing some significant changes. Where did you get them from?

William Guy: Most of the provisions you see in the bill as presented was taken from Minnesota trust law. The language you see in the amendment here comes from South Dakota and Delaware. None of it is language we wrote up ourselves.

Representative Klemin: Have you reviewed the Uniform Trust Act that has been worked on trust decanting?

William Guy: No I have not.

Representative Magrum: What happens with the trust when everyone passes away?

William Guy: If a trust has a trust department as a co-trustee it will last forever or an institution would take over. If the trust is one that enables the individuals to be involved and the trustee dies, then the children would take over. Unless they are too young then there would be a provision for another trustee until the heir would get to the right age.

Representative Magrum: What if there is no money left in it?

William Guy: The trustee would be able to terminate it. I think the state has authority to terminate the trust.

Representative Roers Jones: Has State Bar reviewed this?

William Guy: It is my understanding that the Bar Association has reviewed this and we are speaking on their behalf.

Representative Roers Jones: It sounds like you have reviewed laws from multiple different states and while you are getting portions of the law from different states, you are not dropping in another states law wholesale and trying to make it fit North Dakota's situation? Have you taken parts and made it the best for North Dakota?

William Guy: That is correct. The pieces are primarily from Minnesota and the amendments regarding dynasty trusts come from other states, South Dakota and Delaware primarily.

Representative Nelson: Is the power holder legally required to report to those beneficiaries of the trust?

William Guy: No they are not required to have the power holder do this. No the power holder has no responsibility to report to the beneficiaries because the power holder has the ability to change those beneficiaries. Explains the power holder. 41:33

Representative Nelson: Does being a beneficiary of a trust limit me in any way?

William Guy: I am sure there are circumstances where it could eliminate you from some government programs. If it eliminates your participation by virtue of assets owned, then it would simply eliminate you in some situations. It might also affect the ability to get a student loan.

Representative Nelson: You are saying the power holder could eliminate the person from the trust and then later put him back in the trust.

William Guy: It depends on the extent of power given. Typically, when it is a surviving spouse the spouse has the power to rearrange among the descendants of this couple.

Representative Roers Jones: The power to keep the ability to change the beneficiary is not being changed in the bill or is it?

William Guy: No you are absolutely right what is in here is to provide that the trustee's duty to inform the beneficiaries is modified if the person having the right to the income has the power to change the downstream beneficiaries. Then the trustee has no duty keep those beneficiaries apprised because there may never be one. The Power holder may change who receives this when he or she dies. It does not affect the power itself. The power is established in the document.

Robert Rosenvold, West Fargo SBAND: Went over testimony. (See Attachment 3) (46:30-59:44)

Representative Vetter: This UniTrust is a new thing. Where you can change the amount of interest and principal isn't that changing the terms. If I am the child, you would just be taking more of the principal to meet up with the income. How do they make that balance for the individual? With the capital gains one year will it cause a tax problem?

Robert Rosenvold: The first question on the UniTrust, yes. If you have a trust and typically if you have farm land in this trust you don't change it. But if you have a lot of investments and they don't generate a lot of income. If we change it to a UniTrust regime, if it is generating 2 % of income and the trust document says 4% then 2% of the principal will be used for the surviving spouse. That would take away from the child. If that is the case the child as a beneficiary of the trust has a right to protest. There is built in safe guards.

Representative Vetter: Can they object if they are a minor?

Robert Rosenvold: I suppose it would be a court appointed guardian for them they could. The second question on the power to adjust. It is much more discretionary for the trustee then the UniTrust. Once you set up the percentage for the UniTrust, it will be 3-5%. That is it. The power to adjust relating to the capital gains can be made in income or in kind.

Representative Klemin: Sections 2 & 3; what is the source of that language?

Robert Rosenvold: It is taken from the Uniform Principal and Income Act from 104 & 105. Which was adopted in 1995 and was omitted when it was adopted back then.

Sheri Gronhovd Schrock, NDBA, Bell Bank, Fargo: In support of HB 1228. (1:05) I just returned from the largest national estate planning conference was held in Orlando, Florida. North Dakota's low tax rate on trusts, 2.9% estate tax in comparison to California at 13%. To touch on the amendment which would repeal our rule against perpetuities and afford our ND Citizens to establish a perpetual trust. It is our understanding we would have more opportunity to maintain that type of business here with individuals and corporate trustees serving those roles if our state did repeal that rule against perpetuities. For our own citizens we could afford this option. Much of what we have talked about today like well drafted trust

instruments might be able to address in part. But if we enact 1228 it is my belief that this will provide the citizens across the state with a level playing field. Because you provide in a statutory form powers that will bring both planning and remediation solutions to our clients. There is an enormous amount of uncertainty what the transfer taxes will be today and in the future. We are bringing flexibility, solutions and a framework where our people can address these changing circumstances and this challenging environment. I would encourage enactment of 1228.

Representative Hanson: Repeat the percentage that ND pays?

Sheri Gronhovd Schrock: California is over 13%; where we are 2.9% for the income tax rate for trusts. Income tax planning is very significant. This year each individual can protect \$5.49 million from Federal transfer taxes. That is the estate tax often referred to the death tax. We would look at the best interest for the individual, should it be taxed to the trust or to the beneficiaries? It would have to be figured out for each individual case which would be more beneficial.

Representative Klemin: You are supporting the amendments to repeal the rule against perpetuities, can you explain the reason for the rule?

Sheri Gronhovd Schrock: We inherited this rule from the English colonies. The policy in England at that time didn't want the dead hand controlling property for too long of a time. There was the notion at some point it was better for the country and citizenship to have in individual have the full bundle of rights to that property.

Representative Klemin: Then that rule was continued on in this country including North Dakota because of that potential forever controlled by the dead hand? Now we are going to say that that's ok?

Sheri Gronhovd Schrock: Correct.

Representative Klemin: Is that what we are seeing around the country that this is kind of going by the wayside. South Dakota is one example.

Sheri Gronhovd Schrock: Yes it is and Wyoming has repealed it as well as over 20 other states.

Representative Vetter: I am confused about the tax thing, 39.6% would be the first level then what is the 2.9%? Please clarify that.

Sheri Gronhovd Schrock: The 2.9% rate is the ND State Income Tax and the 39.6% is the top Federal income tax bracket.

Representative Satrom: Will this help business?

Sheri Gronhovd Schrock: We actually administer a half a dozen trusts today just at Bell bank. We are serving as the investment advisor and distribution advisor. In order for our clients to take advantage of that perpetual trust they have a South Dakota Trust company named as the trustee. That does add more cost to administration because you are paying

two different parties. The clients would like to get the bundle of services right with their local provider where they have a relationship. As opposed to breaking apart those roles to have part of it with a South Dakota trust company.

Representative Maragos: The fact that they have a South Dakota trustee only for the no income tax purpose?

Sheri Gronhovd Schrock: That was primarily why they settled in SD. What has continued to make them very attractive for clients who live outside of SD is they have no income tax. They will draw from states like New York

Chairman K. Koppelman: How do we compare with a state like Minnesota?

Sheri Gronhovd Schrock: Minnesota enacted their Uniform Trust Code recently. I have looked at that act and we did borrow some parts of it. We would have the advantage of We took some language from Delaware and if enacted in provisions HB 1228 would establish a process for the creator of a trust or trustee to notify interested persons that there is a trust created and tell them that they have 120 days to file a judicial proceeding to contest the validity of that trust. That particular provision will make us only the 2nd state to have that. This will enable the creator of the trust to be able to defend that trust to challenges on competency and other issues. Today we don't have that mechanism for trusts.

Chairman K. Koppelman: What is the tax on the trusts in Minnesota?

Sheri Gronhovd Schrock: Higher but not exactly sure. There are going to be some changes nationally coming in the taxation of trusts. Minnesota regime is coming under some constitutional question right now.

Representative Roers Jones: I think that 120 day challenge period is a very interesting feature? Who is given notice about the trust when it is created?

Sheri Gronhovd Schrock: A trustee typically would notify every beneficiary named in the document and in addition the trustee would put individuals in notice that would be the default takers under ND law if someone died without a will. This notice is very specific, well written and clear language that says "if you have a challenge to the validity of this trust you have to bring that challenge within 120 days of the notice".

Representative Roers Jones: Is this an option for someone creating a trust? How does this mesh with the trustees duty to inform and report to beneficiary's being changed?

Sheri Gronhovd Schrock: This provision is optional, so I am not aware that any trustee will start this.

Tony Weiler, Executive Director of the ND Bar Assoc: In Support of HB 1228. The Bar Association was notified of these changes by Ms. Foss in June. Mr. Guy was supportive on this bill and worked on this. He mentioned there were others who worked on this in 2007 and were working on this again. What I should have done at that point was send notice of this to every member that was part of this in 2007. I did not. The Bar Association has a long history

of supporting uniform laws and amendments of those laws when they are beneficial to the state. We do support this legislation.

Chairman K. Koppelman: Mr. Guy's testimony named a number of people who have worked on this bill. Several learned people were involved.

Tony Weiler: Correct, we do rely on the Bar for their expertise to help us understand these issues.

Representative Klemin: What is the position of the bar association with respect to the repeal of the rule of perpetuities?

Tony Weiler: I had not seen that amendment until today. I do not have a position on the amendment. I could bring you some more information on.

Chairman K. Koppelman: The amendment was in the bill and was meant to clean it up.

Representative Klemin: Yes I would like to have that happen.

Doug Carpenter: NDBA, Alerus Financial in Grand Forks: In support of this bill. On decanting, we have had a couple instances that this would work extremely well for. One is an Irrevocable Trust that has 2 remainder beneficiaries. They did not anticipate issues with competence. One of the beneficiaries has developed a severe drug and alcohol problem. With decanting we would have the capabilities to solve and protect that beneficiary from receiving the assets at an inopportune time. All these provisions are not something that are going to be used on an every-day basis but they are important when circumstances arise. I urge all of you to support it.

Representative Klemin: Were you aware of the work of Uniform Law Commission on trust decanting?

Doug Carpenter: No I am not.

Chairman K. Koppelman: With the new members on the committee could you give us a definition of the term decanting?

Doug Carpenter: That is transferring assets from an existing trust to a new trust. To take advantage of circumstances that would be beneficial.

Chairman K. Koppelman: Why would it be preferable to transfer those assets to a new trust versus making modifications to the existing one?

Doug Carpenter: Usually it is an irrevocable trust that is not subject to amendments or any changes.

Representative Paur: By doing that you are making that irrevocable trust possibly a revocable trust?

Doug Carpenter: No, you would have maintain the term of the trust and it won't change an irrevocable trust to a revocable type trust. It is still going to be there for the beneficiaries.

Representative Nelson: Is every trust decantable?

Doug Carpenter: If this legislation is approved, unless the document specifically says you cannot.

Chairman K. Koppelman: You would have to maintain character of the original trust.

Doug Carpenter: Most of the trust will remain the same, but there may be instead of automatic distribution of principal now it is subject to the discretion of the trustee and it is only for certain purposes.

Representative Klemin: Question for Mr. Guy, if he could explain section 1 of the bill.

William Guy: Section 1 of the bill was prepared by the Legislative Counsel in response to Rep. Koppelmans' request. Either we should adopt the amendment and repeal the rule as shown in the amendment or we should delete section 1 as written and keep the rule. Section 1 as written should not be adopted.

Chairman K. Koppelman: Any further support or opposition to HB1228? Any neutral testimony. Seeing none.

Recessed the hearing.

2017 HOUSE STANDING COMMITTEE MINUTES

Judiciary Committee
Prairie Room, State Capitol

HB 1228
1/23/2017
27224

- Subcommittee
 Conference Committee

Committee Clerk Signature



Explanation or reason for introduction of bill/resolution:

Relating to the capacity of a settlor of a revocable trust, actions contesting the validity of a trust, and powers to direct a trustee; and to provide for retroactive application.

Minutes:

Chairman K. Koppelman: Reopened the hearing on HB 1228.

Support:

Tony Weiler, Exc. Director of State Bar: Board of Governor's met last Friday and voted to support the legislation with the amendment.

Marilyn Foss, ND Bankers Association: They met and voted to support the bill with section 1 related to the rule against perpetuities. ND's can now use this product to whom it is appropriate. Right now they can obtain this product by using the services of the trust institution in one of the 26 or so other states that make this available in their state. This does cost our bank business.

Representative Klemin: It is not going to be possible persons to put ND real property into a trust in another state that doesn't have the rule against perpetuity and still have that ND property governed by the other states law, is it?

Marilyn Foss: We have been thinking about that issue. I am not aware of a probation from and out of state owner using the laws of the other state. The law is that the trust is governed under the laws of the state where it was created.

Representative Klemin: If that was the case it would be pretty easy to have ND farmland subject to the SD corporate farming law just by having the SD corporation own the ND land.

Marilyn Foss: I have not done a title search so I cannot say whether there is land titled that way or not in ND.

Chairman K. Koppelman: People in ND are going to SD to set the trusts up there because they have a 99-year limit.

Marilyn Foss: Our trust bankers tell us that they have customers who take their trust business to SD to be able to use and benefit from SD law which is different on this point. That would incorporate all trust including business trusts. It says 21 years beyond the life of a person when the trust is created and how far that actually extends out could be 90 to 130 years.

Opposition: None

Neutral: None

Hearing closed.

2017 HOUSE STANDING COMMITTEE MINUTES

Judiciary Committee
Prairie Room, State Capitol

HB 1228
2/8/2017
28078

- Subcommittee
 Conference Committee

Committee Clerk Signature



Explanation or reason for introduction of bill/resolution:

Relating to the capacity of a settlor of a revocable trust, actions contesting the validity of a trust, and powers to direct a trustee; and to provide for retroactive application.

Minutes:

1

Chairman K. Koppelman: Opened the meeting on HB1228.

Representative Klemin: I don't have a problem with this bill. I do have a problem with perpetuities that is in the chairman's amendment. Trust lawyers have been doing a good job for their clients since the 1300's. We have had the rule against perpetuities in ND since statehood. I have proposed a new amendment. (#1). Went through the amendment and into background history on it. (5:09-16:00) Stopped with ND law right now.

Closed hearing.

2017 HOUSE STANDING COMMITTEE MINUTES

Judiciary Committee
Prairie Room, State Capitol

HB 1228
2/14/2017
28343

- Subcommittee
 Conference Committee

Committee Clerk Signature



Explanation or reason for introduction of bill/resolution:

Relating to the capacity of a settlor of a revocable trust, actions contesting the validity of a trust, and powers to direct a trustee; and to provide for retroactive application.

Minutes:

Chairman K. Koppelman: Reopened the meeting on HB 1228.

Representative Klemin:(1:30-11:20) Continued with history on European feudal days and how the trust came into being. The question is do we need it forever or is 90 years enough? Repeal of the rule against perpetuities does? In history this was an unreal rule because they thought land had to turn over once in a while. Trust don't act in a status form. They can grow and invest in more land and eventually we could be back where England was in the (14:24-18:00) History on Vanderbilt. My concern you have to think long term on this now. My children and grandchildren need to be able to own land too. So you have before you the amendment that I prepared. It removes the confusing language in the bill. It does not include the amendments to repeal the rule against perpetuities. I think this repeal is a significant change in ND law that should not be coming before the legislature as an amendment to a bill. It should have its own hearing and discussion.

Chairman K. Koppelman: I will tell you the amendment is only to clean up language in the bill. It was suggested by the attorney's and it isn't quite accurate. The whole concept of ending the idea of the trusts being able to be perpetual is the same concept that is behind redistribution of wealth. We have an estate tax; and other taxes in our country that no only fund government, but that also there to say you shouldn't have too much. To what extent should government control what you own or what you can put in a trust. I think it is important for the idea of trust dealing back to the progressive movement early in the last century when our own Teddy Roosevelt was known as a trust buster. There were abuses. The legislature will be meeting a lot of times so the question is do you want people who establish a trust in ND to be able to say this trust is going to be ongoing. That is all it is. The land issue in England I understand is pretty small. 21 Century South Dakota is more relative. In SD business continuity trusts are legal. In ND you can't so you have people in ND going to SD to set up trusts. Land isn't the only thing trusts can contain. They can contain money and personnel property and they can dictate how a business is run. It can be changed by people

in charge of the trust. Not the government to say OK here is a date in time where this all has to go away.

Representative Roers Jones: As we were listening to Rep. Klemin history on the rule of perpetuities; one of the things came to my mind was we still have the dead hand ruling from the grave; it is just a different hand. We are still abiding by the rule of the courts from the 1500s. If the concern is tying up real property; then just say the rule of perpetuities only applies to this. Then you wouldn't have an issue.

Representative Klemin: Business trusts proposed by this legislature is being considered and have not passed yet.

Representative Jones: In Wyoming they had a lot of elk come out of the mountains and come into ranches and they would use these ranches so big organizations came in and bought the ranches. Elk Unlimited came in and bought those ranches because they thought they would be good habitat forever for the elk. They were trying to get them put into perpetuity under that ownership. As it turned out; once they bought the ranches they were no longer irrigated and the hay was no longer cut so the elk would come out of the mountains and they had no desire to stay on those ranches and so they would go to the neighboring ranches where they were farmers and grazed. It was an example of something that went wrong. Had a great impact on the surrounding ranches and the state as a whole so Wyoming stepped in and said we are not going to let these things be done for perpetuity because of that so they limited them to the 99 years there.

Representative Simons: Most of us are familiar with the buffalo ranches in Montana like Ted Turner border him and he employed lots of people to run them. I cannot imagine if we let anyone do this for ever. The idea and concept of even owning land was not thought of in other countries.

Chairman K. Koppelman: A lot of that had to do with poverty as well. A lot of people could not afford it back then. Rep. Roes Jones will draft an amendment and then we can look at that.

Representative Nelson: Trusts are complicated. Is it possible to get a marked up version of this bill?

Chairman K. Koppelman: Can we get the mark ups? Not till we vote on them.

Closed.

2017 HOUSE STANDING COMMITTEE MINUTES

Judiciary Committee
Prairie Room, State Capitol

HB1228
2/14/2017
28359 PM

- Subcommittee
 Conference Committee

Committee Clerk Signature



Explanation or reason for introduction of bill/resolution:

Relating to capacity of a settlor of a revocable trust, actions contesting the validity of a trust, and powers to direct a trustee; and to provide for retroactive application.

Minutes:

1

Chairman K. Koppelman: Reopened the meeting on HB 1228.

Representative Klemin: (#1) Proposed amendment. Went over the proposal. This will retain Section 1. It is the existing statute that deals with exclusions with the statutory rule from against perpetuities. The bill has proposed new language relating to a business trust.

Motion Made to amended on Klemin amendment by Rep. Roers Jones; Seconded by Rep. Maragos

Discussion:

Representative Nelson: Are there other kinds of trust other than business that could still own real estate.

Representative Klemin: Yes, the kind of trusts that are in the rest of this bill can own real property, but they would be limited against the rule of perpetuities.

Chairman K. Koppelman: The business trust would be the only one that would have perpetual existence. The concern that has been expressed by land ownership would be resolved by not allowing those kinds of trusts to own real property.

Representative Klemin: A business trust was a predecessor of the Massachusetts trust that spread over the country. We need to contrast this would the real estate investment trust that is already legal in ND. Real estate trusts can own apartment buildings and things like that but not farmland.

Voice vote carried.

Do Pass as Amended Motion by Rep. Roers Jones; Seconded by Rep. Karls

Roll Call Vote: 13 Yes 2 No 0 Absent Carrier: Representative Klemin:

Closed.

February 14, 2017

ONE
2/14/17
101

PROPOSED AMENDMENTS TO HOUSE BILL NO. 1228

Page 2, line 11, after the underscored period insert "A business trust, whether domestic or foreign, may not own any interest in real property within this state."

Page 4, line 29, replace "section" with "chapter"

Page 24, line 6, replace "Act" with "chapter"

Renumber accordingly

Date: 2-14-17
Roll Call Vote: 1

2017 HOUSE STANDING COMMITTEE
ROLL CALL VOTES
BILL/RESOLUTION NO. 1228

House Judiciary Committee

Subcommittee

Amendment LC# or Description: Klemin Amendment #1

Recommendation: Adopt Amendment
 Do Pass Do Not Pass Without Committee Recommendation
 As Amended Rerefer to Appropriations
 Place on Consent Calendar
Other Actions: Reconsider _____

Motion Made By Louis Jomo Seconded By Rep Maragos

Representatives	Yes	No	Representatives	Yes	No
Chairman K. Koppelman			Rep. Hanson		
Vice Chairman Karls			Rep. Nelson		
Rep. Blum					
Rep. Johnston					
Rep. Jones					
Rep. Klemin					
Rep. Magrum					
Rep. Maragos					
Rep. Paur					
Rep. Roers-Jones					
Rep. Satrom					
Rep. Simons					
Rep. Vetter					

Total (Yes) _____ No _____

Absent _____

Floor Assignment _____

If the vote is on an amendment, briefly indicate intent:

*Voice
Vote
carried*

**2017 HOUSE STANDING COMMITTEE
 ROLL CALL VOTES
 BILL/RESOLUTION NO 1228**

House Judiciary Committee

Subcommittee

Amendment LC# or Description: 17.0717.01004

- Recommendation: Adopt Amendment
 Do Pass Do Not Pass Without Committee Recommendation
 As Amended Rerefer to Appropriations
 Place on Consent Calendar
 Other Actions: Reconsider _____

Motion Made By Roers Jones Seconded By Karls

Representatives	Yes	No	Representatives	Yes	No
Chairman K. Koppelman	✓		Rep. Hanson	✓	✓
Vice Chairman Karls	✓		Rep. Nelson		✓
Rep. Blum	✓				
Rep. Johnston	✓				
Rep. Jones	✓				
Rep. Klemin	✓				
Rep. Magrum	✓				
Rep. Maragos	✓				
Rep. Paur		✓			
Rep. Roers-Jones	✓				
Rep. Satrom	✓				
Rep. Simons	✓				
Rep. Vetter	✓				

Total (Yes) 13 No 2

Absent 0

Floor Assignment : Rep. Klemin

If the vote is on an amendment, briefly indicate intent:

REPORT OF STANDING COMMITTEE

HB 1228: Judiciary Committee (Rep. K. Koppelman, Chairman) recommends **AMENDMENTS AS FOLLOWS** and when so amended, recommends **DO PASS** (13 YEAS, 2 NAYS, 0 ABSENT AND NOT VOTING). HB 1228 was placed on the Sixth order on the calendar.

Page 2, line 11, after the underscored period insert "A business trust, whether domestic or foreign, may not own any interest in real property within this state."

Page 4, line 29, replace "section" with "chapter"

Page 24, line 6, replace "Act" with "chapter"

Renumber accordingly

2017 SENATE JUDICIARY

HB 1228

2017 SENATE STANDING COMMITTEE MINUTES

Judiciary Committee
Fort Lincoln Room, State Capitol

HB 1228
3/7/2017
28808

- Subcommittee
 Conference Committee

Committee Clerk Signature



Explanation or reason for introduction of bill/resolution:

Relating to actions to contest the validity of a trust, trust decanting, and directed trustees; relating to exclusions from the rule against perpetuities and a trustee's duty to inform; relating to the capacity of a settlor of a revocable trust, actions contesting the validity of a trust, and powers to direct a trustee; and to provide for retroactive application.

Minutes:

Testimony attached #

1,2,3

Chairman Armstrong called the committee to order on HB 1228. All committee members were present.

Rep. Kim Koppelman: North Dakota State Representative District 13, introduced and testified in support of the bill. No written testimony.

Senator Nelson: So that is page 2 subsection 7 that you added to the House?

Rep. Kim Koppelman: Yes, that is correct.

Marilyn Foss, General Council for North Dakota Bankers Association, briefly described how the bill came to be. (4:50-10:47)

Sheri Schrock for William L. Guy III: who could not make it, testified in support of the bill. (see attachment 1,2) (11:09- 16:02)

Senator Larson: I don't see anywhere in the bill itself other than the bill itself that says decanting. What does that mean? (16:02-16:24)

Ms. Sheri Schrock: Decanting takes the assets from an existing trust and pours them over to another trust agreement with new terms. It takes the assets from an existing trust, pours them over into a new trust agreement. (16:24- 17:15)

Sen. Larson: I noticed that the definition isn't listed in the bill? Is it someplace else in statute?

Ms. Marilyn Foss: Came up to expand on the answer (17:48-17:57).

Senator Larson: It's confusing to me that its listed in the title, but not in the bill.

Senator Nelson: Decanting is a term of ours and we have discussed with Legislative Council how the titling of the chapters that these new chapters that are being created should be done and one will be titled as Decanting because if you are in the trust, trust professional, if you are looking for this authority that is term it would use even though it is a separate provision in the bill themselves, describe what you are doing and what you need to do to engage in decanting. They talk about it in terms of distributing from one trust to another.

Ms. Sheri Schrock: Section 9 would be a new provision that codify what is already occurring in some trust agreements and that is that as the laws have been changing across the country, the traditional responsibilities and role played by a single trustee are being allocated to different fiduciaries.

Senator Nelson: In section 8 is a brand new section, would it not be advisable in section 8 the one dealing with decanting that perhaps we could put that definition into the first -02 and into the definition? I guess what I am reading out of this is your adding completely new sections of all the rules that go with number 1, section 9 is directed trust, section 8 is decanting. So, if that is what the title is going to be I really think you need to have the definition of it somewhere.

Ms. Sheri Schrock: That current trust code has in one of the early sections that we adopted into 2007, has a long definition section and so the committee did look at whether or not it made sense to try to bring in some of these definitions into the code section that actually covers definitions, but what we learned is it's alphabetical list and to include some of these definitions in that section would actually be somewhat problematic and burdensome on the legislature.

Chairman Armstrong: (22:30): Is there any professional in this industry that is not going to understand what this legislation says, because I'm a DY lawyer and I don't understand what it says, but I don't think it's written for me. Professionals in the trust business understand decanting, they understand trust, they understand the rules, this is really giving the guidance to the banks and the lawyers and the people as to what we allow in ND. Very few people set these up on their own I am assuming.

Ms. Sheri Schrock: correct.

Senator Nelson: My problem is that the printed sections are 59-16 with no point one and now were starting this new chapter with 16.1 and basically to me it, and then section 9 is 16.2. They are stand-alone sections. I'm not an attorney either but I've looked at enough of these things over the years because I get stuck with these. If there is something in here and its' going to take six pages to tell me all about it, I would like to know what decanting is right off the bat rather than go searching for it somewhere.

Robert E. Rosenvold, North Dakota Attorney, testified in support of the bill. (see attachment 3) (24:21-33:24) Specifically sections 2,3,10.

Senator Luick: 33:35 The example you gave here, does it make a difference on how those capital gains are garnered in that example you gave where there was real property . How do they come about on the capital gains?

Mr. Robert Rosenvold: It doesn't make any difference. It could be selling real estate, it could be selling stocks and bonds. (33:54-39:56)

Ms. Sheri Schrock :(40:10-44:42), Testified in support of the bill. (see attachment 2)

Senator Luick:: (44:55- 45:03) Does this take care of those problems of reciprocity or just the fact that they can now be equal in the ability to do those here in ND?

Ms. Sheri Schrock: The section 1 carves out a very narrow scope for these perpetuity trusts. In my view when the trust has a business purpose, so you can conduct business as a corporation, C corporation, a partnership. You can actually conduct business in form of a trust. Really I've used section 1 as addressing that scope, not the personal trust type of dynasty trust that you may have heard of.

Senator Luick: " Can a trust be treated as a person in law? Does it have the same category per type of definition?

Ms. Sheri Schrock: Historically, a trust wasn't per say considered an entity, because of the legal title for all the property was held by a trustee, so all suits and all legal documents are done by the bank as trustee of the Sherry Schrock evocable trust.

Senator Luick: The Trust is not actually the entity, the bank is the entity in the trust is just the mechanism of how that is carried through.

Ms. Sherry Schrock: The trust does have its own taxpayer identification number. It is considered a person for a tax purposes. When we take title to property its always like the bank it is a piece of real estate. It would be the bank as trustee of the Sherry Schrock trust under agreement dated such and such. So you reference that fiduciary and the name of the trust agreement to get that specificity under what is the controlling document. I believe in most states, for sure ND, but I would think so, but often times an unincorporated association would be kind of the nearest thing to a trust in terms of how the law would look at a business trust.

Senator Luick: (49:40) They have their own tax payer identification so wouldn't they be treated just as if they were an entity of their own, and I guess I am going with this is that why wouldn't the trust be limited to their capabilities as far as owning real estate. A corporation can't own real estate in ND, so why would a trust be able to own real estate in ND?

Ms. Sherry Schrock: There is no statute prohibiting a private trust as opposed to a business trust holding real estate.

Chairman Armstrong: An incorporation can own real estate; they just can't own farmland.

Senator Luick: Where I am going with this, can a trust set up a 9000 head dairy in ND?

Chairman Armstrong: Yes, if they are members of the trust are brothers and fall within the lineage of the corporate farming law. No if they don't. That's the answer.

Tony Wilder, Executive Director for State Bar, briefly testified in support of the bill. (50:24-50:57)

Chairman Armstrong:closed the hearing on HB 1228.

2017 SENATE STANDING COMMITTEE MINUTES

Judiciary Committee
Fort Lincoln Room, State Capitol

HB 1228 Committee Work
3/8/2017
28872

- Subcommittee
 Conference Committee

Committee Clerk Signature



Explanation or reason for introduction of bill/resolution:

Relating to actions to contest the validity of a trust, trust decanting, and directed trustees; relating to exclusions from the rule against perpetuities and a trustee's duty to inform; relating to the capacity of a settlor of a revocable trust, actions contesting the validity of a trust, and powers to direct a trustee; and to provide for retroactive application.

Minutes: **No written testimony.**

Chairman Armstrong began the discussion on HB 1228. All committee members were present.

Senator Larson: "When I spoke with Marilyn Foss who was one of the people that testified in favor of this bill, she said that they had talked to Vonette Richter from Legislative Council when they were drafting the bill and Vonette advised me that they did not need to put any definition in there because they specifically asked that question, and so at the advice of Legislative Council I'm not interested in pursuing it any further."

Senator Myrdal motioned for a Do Pass. **Senator Luick** seconded.

A Roll Call Vote was taken. Yea: 6 Nay: 0 Absent: 0.
The motion carried.

Chairman Armstrong carried the bill.

Chairman Armstrong ended the discussion on HB 228.

REPORT OF STANDING COMMITTEE

HB 1228, as engrossed: Judiciary Committee (Sen. Armstrong, Chairman)
recommends **DO PASS** (6 YEAS, 0 NAYS, 0 ABSENT AND NOT VOTING).
Engrossed HB 1228 was placed on the Fourteenth order on the calendar.

2017 TESTIMONY

HB 1228

1
HB 1228
1-18-17

TESTIMONY OF WILLIAM L. GUY III
IN SUPPORT OF
HOUSE BILL NO. 1228

January 18, 2017

Mr. Chairman and members of the Committee, I am here on behalf of a task force (consisting of Douglas Carpenter from Grand Forks, Joseph Heringer and Marilyn Foss, both from Bismarck, Robert Rosenvold, Marshall McCullough, Kevin Kercher, all from West Fargo and Jessica Foss, John Williams III, Mary Locken, Sherry Schrock and me, all from Fargo) which has undertaken the drafting of legislation to supplement the North Dakota Uniform Trust Code (Chapters 59-09 – 59-19).

Some of the highlights of the Bill include:

1. **SECTION 1** of the Bill (on page 1) will be amended and restated in its entirety with testimony on those amendments contained at the end of this presentation.
2. **SECTION 2** of the Bill (on pages 2 through 4) amends Section 59-04.2-03 and will be handled by Bob Rosenvold.
3. **SECTION 3** of the Bill (on pages 4 through 7) creates new Section 59-04.2-03.1 and will be handled by Bob Rosenvold.
4. **SECTION 4** of the Bill (on page 6) creates new Section 59-09-04.1 which provides that the capacity of an individual to create a trust is the same capacity that is required of an individual to make a will.
5. **SECTION 5** of the Bill (on pages 6 and 7) creates new Chapter 59-10.1 to set forth a process by which an individual may challenge the validity of a trust instrument and obtain a declaratory judgment of that invalidity. The chapter includes:
 - a. a determination of who must be the parties to the proceeding;
 - b. a limitation on the time in which the proceeding must occur or be barred from occurring;
 - c. a detailing of the findings required of the court; and
 - d. a process for the return of distributions made by the trustee prior to becoming aware of a possible proceeding to contest the validity of the trust.
6. **SECTION 6** of the Bill (on pages 7 and 8) creates new Section 59-14-05 and makes clear that while a trust is revocable, the trustee may follow a direction of the trust creator which is contrary to the terms of the trust (and is a transfer of identical language from subsection 1 of Section 59-16-08 . . . the remaining subsections of which were repealed and replaced with new Chapter 59-16.2).

7. **SECTION 7** of the Bill (on pages 8 and 9) amends Section 59-16-13 regarding a trustee's duty to inform and report to the beneficiaries of the trust.

a. The amendment provides that if an individual holds the power to change the beneficiaries of a trust (the "powerholder"), then the trustee's duty to inform and report runs to the powerholder and not to the beneficiaries whose status as a beneficiary could be altered or eliminated by the powerholder.

b. An example would be a charitable remainder trust that provides income to the trust creator during his or her lifetime and then distributes the trust principal to named charities upon the death of the trust creator.

(1) If the trust creator holds the power to change the names of the charitable beneficiaries who receive the trust principal upon his or her death, then the trustee's duty to inform and report to the beneficiaries of the trust runs to the power holder and not to the charities which might be eliminated as beneficiaries if the power holder exercises his/her power.

(2) The same principle holds true for individuals who would receive trust assets upon the death of the power holder but otherwise have no interest in the trust prior to the death of the power holder.

8. **SECTION 8** of the Bill (pages 9-17) creates new Chapter 59-16.1 establishing for the first time in the North Dakota Uniform Trust Code the power of trust "decanting."

a. Trust decanting is the process by which the assets of an old trust (often with obsolete language) are poured (or decanted) from the old trust to a new trust.

b. In addition to an extensive section on definitions, this chapter includes sections:

(1) that differentiate the authority given to a trustee who has unlimited discretion in invading the trust principal as opposed to trustees who have limited discretion;

(2) that makes clear that the power to invade the trust principal under this chapter is considered to be an exercise of special power of appointment by the trustee;

(3) that the term of the new trust cannot exceed a term that is longer than the term set forth in the old trust;

(4) that the trustee exercising power under this chapter has a fiduciary duty to exercise the power in the best interests of one or more of the proper objects of the power and as a prudent person who would exercise that power under the prevailing circumstances;

(5) provision is made for the handling of subsequently discovered assets after the initial transfer of assets;

(6) provision is made for the notice to be given to those interested in the old trust; and

(7) that certain aspects of the old trust may not be reduced, limited or modified in the decanting process.

c. The reasons why it may be beneficial to make changes to the terms of an existing irrevocable trust include:

(1) addressing changes in tax law;

(2) addressing changes in the needs or circumstances of the beneficiary;

(3) changing trustees; or

(4) fixing administrative provisions of the irrevocable trust.

9. **SECTION 9** of the Bill (pages 17-24) creates a new Chapter 59-16.2 (replacing Section 59-16-08) pertaining to directed trusts.

a. A directed trust is a concept that is being widely used in other states and is of significant interest to trust departments and trust companies in North Dakota.

b. In a directed trust, the trustee typically has physical custody of the assets of the trust but is subject to direction by:

(1) the "Distribution Trust Advisor"; and

(2) the "Investment Trust Advisor."

c. The "Distribution Trust Advisor" may be another trust department, or an individual who, in any event, has the authority to direct distributions of the trust assets being held by the trustee.

d. The "Investment Trust Advisor" is most often an investment advisor of the trust creator or possibly the trust creator himself or herself. In any event, the Investment Trust Advisor has the authority and the responsibility to handle the investment of the trust assets.

e. This chapter extensively details the responsibilities of the individuals in question.

10. **SECTION 10** of the Bill (pages 24-31) creates new Chapter 59-16.3 authorizing the concept of "Total Return Unitrusts," and will be handled by Bob Rosenvold.

11. **SECTION 11** of the Bill (on page 31) provides for the repeal of Sections 59-14-01, 59-14-04 and 59-16-08.

12. **SECTION 12** of the Bill (on page 31) provides that Section 8 of the Act (pertaining to trust decanting) is retroactive and applies to all trusts governed by North Dakota law.

The following amendments to House Bill No. 1228 will be introduced at today's hearing.

First, some background. For hundreds of years the duration of irrevocable trusts has been limited by the Rule Against Perpetuities.

- The ancient rule provided that a trust could not last longer than the lives of all of the then-living beneficiaries plus 21 years.
- The modern alternative in North Dakota is the longer of the ancient rule or 90 years from the date of the creation of the trust.

Since no estate taxes are paid upon the death of the beneficiary of a properly drafted trust (sometimes called a "Generation Skipping Trust" or a "Dynasty Trust"), twenty-eight (28) states (led by South Dakota in 1983) have repealed or dramatically lengthened their Rule Against Perpetuities.

The following amendments will repeal the Rule Against Perpetuities in North Dakota.

13. A new subsection 7 to Section 47-02-27.1 will be created to provide that real property and personal property held in a trust (that is not a charitable trust) will not be subject to the statutory Rule Against Perpetuities.

14. A new section (probably 47-02-27.2) will be created to repeal the common law Rule Against Perpetuities.

15. So that individuals and financial institutions in other states will not be able to use our law without associating with a North Dakota resident or a North Dakota financial institution with trust powers:

a. A new subsection 17 of Section 59-09-03 will be created to define a "Qualified Person" as:

- (1) An individual who is a North Dakota resident; or
- (2) A financial institution with trust powers that has its principal place of business in North Dakota.

b. A new subsection 2 of Section 59-09-07 will be created that will require a trust governed under North Dakota law:

- (1) To have some or all of its assets located in North Dakota;

- (2) To have a trustee who is a Qualified Person; and
- (3) To be administered in whole or in part in North Dakota.

I appreciate the opportunity to address your Committee. If you have any questions, I will be happy to answer them. Thank you.

William L. Guy III
Fredrikson & Byron P.A.
51 Broadway, Suite 400
Fargo, ND 58102-4991
Phone: 701-237-8200

60527849_4.docx

#2
1228
1-18-17

PROPOSED AMENDMENTS TO HOUSE BILL NO. 1228

Page 1, line 1, after "enact" insert "a new section to chapter 47-02,"

Page 1, line 4, after the second comma insert "59-09-03, 59-09-07,"

Page 1, line 5, after "perpetuities" insert ", uniform trust code definitions, governing law,"

Page 2, line 8, remove "Except to the extent otherwise provided in the governing instrument of a business"

Page 2, replace lines 9 through 11 with "An interest created in real property or personal property held in a trust that is not a charitable trust as defined in subsection 4 of Section 59-09-03."

SECTION 2. A new section to chapter 47-02 of the North Dakota Century Code is created and enacted as follows:

Common law rule against perpetuities.

The common law rule against perpetuities is not in force in this state.

Page 6, after line 7, insert:

"SECTION 5. AMENDMENT. Section 59-09-03 of the North Dakota Century Code is amended and reenacted as follows:

59-09-03. (103) Definitions.

Any term not specifically defined in this section has the meaning provided in title 30.1. Unless the context otherwise requires, in chapters 59-09, 59-10, 59-11, 59-12, 59-13, 59-14, 59-15, 59-16, 59-17, 59-18, and 59-19:

1. "Action", with respect to an act of a trustee, includes a failure to act.
2. "Ascertainable standard" means a standard relating to an individual's health, education, support, or maintenance within the meaning of section 2041(b)(1)(A) or 2514(c)(1) of the Internal Revenue Code.
3. "Beneficiary" means a person that:
 - a. Has a present or future beneficial interest in a trust, vested or contingent, including the owner of an interest by assignment or transfer; or
 - b. In a capacity other than that of a trustee, holds a power of appointment over trust property.
4. "Charitable trust" means a trust, or portion of a trust, created for a charitable purpose described in subsection 1 of section 59-12-05.
5. "Conservator" is as defined in section 30.1-01-06.

6. "Distributee" means any person who receives property of a trust from a trustee, other than as a creditor or purchaser.
7. "Environmental law" means a federal, state, or local law, rule, regulation, or ordinance relating to protection of the environment.
8. "Guardian" is as defined in section 30.1-01-06.
9. "Interests of the beneficiaries" means the beneficial interests provided in the terms of the trust.
10. "Internal Revenue Code" means the Internal Revenue Code of 1986, or corresponding future provisions of federal tax law.
11. "Irrevocable" means if used in reference to a trust, a trust that is not revocable, including a formerly revocable trust that has become irrevocable, whether by the death of a settlor or otherwise.
12. "Jurisdiction", with respect to a geographic area, includes a state or country.
13. "Permissible distributee" means a beneficiary who is currently eligible to receive distributions of trust income or principal, whether the distribution is mandatory or discretionary.
14. "Power of withdrawal" means a presently exercisable general power of appointment other than a power:
 - a. Exercisable by a trustee and limited by an ascertainable standard; or
 - b. Exercisable by another person only upon consent of the trustee or a person holding an adverse interest.
15. "Property" means anything that may be the subject of ownership, whether real or personal, legal or equitable, or any interest therein.
16. "Qualified beneficiary":
 - a. Means a beneficiary who, on the date the beneficiary's qualification is determined:
 - (1) Is a permissible distributee of trust income or principal;
 - (2) Would be a permissible distributee of trust income or principal if the interests of the distributees described in paragraph 1 terminated on that date without causing the trust to terminate; or
 - (3) Would be a permissible distributee of trust income or principal if the trust terminated on that date.
 - b. Does not include a contingent distributee or a contingent permissible distributee of trust income or principal whose interest in the trust is not reasonably expected to vest.
17. "Qualified person" means:
 - a. An individual:

- (1) Who, except for brief intervals, military service, attendance at an educational or training institution, or for absences for good cause shown, resides in this state;
 - (2) Whose true and permanent home is in this state;
 - (3) Who does not have a present intention of moving from this state; and
 - (4) Who has the intention of returning to this state when away;
 - b. A trust company that is organized under chapter 6-05 or under federal law and that has its principal place of business in this state; or
 - c. A bank or savings association:
 - (1) That possesses and exercises trust powers;
 - (2) Has its principal place of business in this state; and
 - (3) The deposits of which are insured by the federal deposit insurance corporation.
18. "Record" means information that is enshrined on a tangible medium or which is stored in an electronic or other medium and is retrievable in perceivable form.
- ~~18-19.~~ "Revocable", as applied to a trust, means revocable by the settlor without the consent of the trustee or a person holding an adverse interest.
- ~~19-20.~~ "Settlor" means a person, including a testator, that creates, or contributes property to a trust and if more than one person creates or contributes property to a trust, each person is a settlor of the portion of the trust property attributable to that person's contribution except to the extent another person has the power to revoke or withdraw that portion.
- ~~20-21.~~ "Signed" means:
 - a. That the signature of a person, which may be a facsimile affixed, engraved, printed, placed, stamped with indelible ink, transmitted by a facsimile telecommunication or electronically, or in any other manner reproduced on the record, is placed on a record or instrument with the present intention to authenticate the record or instrument.
 - b. With respect to a record or instrument required by this chapter to be filed with the clerk of court, that:
 - (1) The record or instrument has been signed by a person authorized to do so by this chapter or by the trust instrument; and
 - (2) The signature and the record or instrument are communicated by a method or medium acceptable to the clerk of court.
- ~~21-22.~~ "Special needs trust" means special needs trust as defined in section 59-08-01.

- 22-23. "Spendthrift provision" means a term of a trust which restrains either the voluntary or involuntary or both the voluntary and involuntary transfer of a beneficiary's interest and does not include or prevent a disclaimer of an interest of a beneficiary.
- 23-24. "State" means a state of the United States, the District of Columbia, Puerto Rico, the United States Virgin Islands, or any territory or insular possession subject to the jurisdiction of the United States.
- 24-25. "Terms of a trust" means the manifestation of the settlor's intent regarding a trust's provisions as expressed in the trust instrument or as may be established by other evidence that would be admissible in a judicial proceeding.
- 25-26. "Trust instrument" means a record signed by the settlor that contains terms of the trust, including any amendments to the record and any modifications permitted by court order or by binding nonjudicial settlement agreement.
- 26-27. "Trustee" includes an original, additional, and successor trustee, and a cotrustee, whether or not appointed or confirmed by a court."

Page 6, after line 14, insert:

"SECTION 7. AMENDMENT. Section 59-09-07 of the North Dakota Century Code is amended and reenacted as follows:

59-09-07. (107) Governing law.

1. The meaning and effect of the terms of a trust are determined by the law of the jurisdiction designated in the terms or, in the absence of a controlling designation in the terms of the trust, the law of the jurisdiction having the most significant relationship to the matter at issue.
2. Except as expressly provided by the terms of a trust instrument or by a court order, a general law or a state jurisdiction provision stating that the laws of this state govern is valid, effective, and conclusive for the trust if:
 - a. Some or all of the trust assets are deposited in this state or physical evidence of such assets is held in this state and the trust is being administered by a qualified person. In this subdivision, "deposited in this state" includes being held in a checking account, time deposit, certificate of deposit, brokerage account, trust company fiduciary account, or other similar account or deposit that is located in this state including North Dakota investments;
 - b. A trustee is a qualified person who is designated:
 - (1) As a trustee under the governing instrument or a successor trusteeship; or
 - (2) By a court having jurisdiction over the trust; and
 - c. The administration occurs wholly or partly in this state, including:
 - (1) Physically maintaining trust records in this state; and

- (2) Preparing or arranging for the preparation of, on an exclusive or nonexclusive basis, an income tax return that must be filed by the trust.
3. If the administration of the trust meets the three requirements in subsection 2, this state and its courts have jurisdiction over a trust created in a foreign jurisdiction.
4. This section may not be construed to be the exclusive means of providing a valid, effective, and conclusive state of jurisdiction provision."

Page 31, line 23, replace "8" with "11"

Renumber accordingly

3
HB 1228
1-18-17

TESTIMONY OF ROBERT E. ROSENVOLD
IN SUPPORT OF
HOUSE BILL NO. 1228

January 18, 2017

The provisions of House Bill No. 1228, which I would like to address are Sections 2, 3 and Section 10. Sections 2 and 3 concern the power of a trustee to adjust between income and principal and Section 10 concerns the power of a trustee to convert an income-only interest to a Unitrust amount which is based upon a percent of the trust value determined annually.

The purpose of these sections is to allow a trustee of income-only trusts to make investment decisions without being captive to immediate cash flow needs. More specifically, a trustee of such a trust has a fiduciary obligation to maximize the income distributions to the income beneficiary while, at the same time, to preserve the value of the trust assets for the remainder beneficiaries who will receive the trust's assets at the time of the termination of the trust. Obviously, these two concerns and obligations are often contradictory.

Income distributions to the income beneficiary, which most often involve only the surviving spouse, have been seriously reduced these last few years because of the current investment climate. Historically, bonds and certificates of deposit were excellent investments to provide substantial income distributions to the income beneficiary. However, under the current interest climate, such investments, even with a trust estate as large as \$1,000,000, will only result in income distributions to the income beneficiary of \$10,000 to \$15,000 per year. Further, investments in stocks and mutual funds will likely provide even a smaller income distribution to the income beneficiary.

Every state with the exception of North Dakota has enacted one of two methods for redefining trust income. When North Dakota adopted the Uniform Principal and Income Act in 1969, for some reason the Power to Adjust was omitted and has never been added.

Currently, forty-seven (47) states, including the District of Columbia, allow trustees to make adjustments between income and principal to allocate the trust's investment return fairly between income and remainder beneficiaries. Thirty-three (33) states have adopted Unitrust language. Thirty-one (31) states have adopted both methods.

POWER TO ADJUST

Section 2 of the Bill amends Section 59-09.2-03 to authorize a trustee, who is managing the trust assets as a prudent investor, to make adjustments between income and principal of the trust as a trustee considers necessary after taking into account all relevant factors.

Section 2 of the Bill, will allow the trustee, after careful consideration, to determine that it would be unable to administer the trust impartially and fairly to all beneficiaries without making an adjustment. The Power to Adjust works both ways. It authorizes a trustee to reallocate a portion of the trust return to income in a low interest rate environment, even though the return is attributable to principal appreciation. The Power to Adjust permits the trustee to allocate a portion of the trust income to principal.

For example, assume a trust has a value of \$1,000,000 and it generates \$10,000 in ordinary income and \$60,000 in capital gains. The trustee would have the ability to adjust all or a portion of the capital gains and treat it as income.

The Power to Adjust is totally discretionary for the trustee. The trustee does not have the Power to Adjust if the trustee is a beneficiary of the trust or, even if the trustee is not a beneficiary, the adjustment would somehow benefit the trustee directly or indirectly. If the trust has co-trustees, the Power to Adjust can be made by the co-trustee who is not a beneficiary, unless it is not permitted by the terms of the trust. If the trust clearly manifests an intention that the fiduciary shall or may favor one or more of the beneficiaries, the Power to Adjust is not given. The Power to Adjust is subject to control by the Court to prevent an abuse of discretion by the trustee. The Power to Adjust is denied to the trustee if there are any adverse tax consequences. The trust can contain language to specifically forbid the use of the Power to Adjust.

Section 3 of the Bill provides that the Court may not order a trustee to change a decision to exercise or not exercise the Power to Adjust unless it determines that the decision was an abuse of the trustee's discretion. If the trustee is hesitant to exercise its discretion, the trustee may petition the Court for instructions. It requires the Court to determine, upon a petition by the trustee, whether a proposed exercise or non-exercise of the power by the trustee would be an abuse of discretion under the general rule of paragraph 1 of Section 3. If the petition contains the information prescribed in the second sentence of paragraph 4 of Section 3, the proposed action or inaction is presumed not to be an abuse of discretion.

UNITRUST

Section 10 of House Bill No. 1228 would enact what is commonly known as a Unitrust regime. This is also known as a Total Return Trust.

Like the Power to Adjust, it is designed to allow a trustee to redefine trust income. However, trust income is defined as a percentage of the value of the trust, determined each year, without regard to traditional concepts of income or principal. The amount of income distributed annually fluctuates according to the percentage of value of the trust assets. An important advantage of the Unitrust approach is that it eliminates the inherent tension between income and remainder beneficiaries. Both have an interest in the trust gleaning the highest possible total return. This is because the amount of the annual income distribution, as well as the amount ultimately received by the remainder beneficiaries, increase with the value of the trust assets. This Bill defines the Unitrust amount in a range between 3% to 5% of the value of the

trust assets. Treasury Regulations provide that as long as the distribution is no less than 3% nor more than 5% each year, no adverse tax consequences will occur. These Final Regulations apply to tax years on or after January 2, 2004, and are applicable to both the Power to Adjust and to Unitrust.

Existing income-only trusts can be converted to a Unitrust by a trustee as long as the trustee is not an "Interested Trustee" as defined under Paragraph 4. Importantly, an "Interested Trustee" includes an individual trustee to whom the net income or principal of the trust can currently be distributed or will be distributed if the trust were then to terminate and be dissolved. If a trustee is not an "Interested Trustee," then the trustee, in its sole discretion, and without the approval of any Court, may convert an income trust to a Total Return Unitrust, reconvert a Total Return Unitrust to an income trust, or change the percentage used to calculate the Unitrust amount and the method used to determine the fair market value of the trust. This can only be done, however, if the requirements under proposed NDCC 59-16.3.02 are followed. Importantly, the trustee must send written notice of its intention to the person who created the trust, if living, all living individuals who are currently receiving, or are eligible to receive, distributions of income from the trust, and all living individuals who would receive principal of the trust if the trust were to terminate at the time of giving such notice.

If the only trustee of the trust is an "Interested Trustee" and if he or she wishes to convert the trust, the trustee may petition in Court for such order. The Court in its own discretion, or on the petition of such trustee, or any person interested in the trust, may appoint a disinterested person who, acting in a fiduciary capacity, can provide information to enable the Court to make its determination.

Guy, William

From: Tony Weiler <tony@sband.org>
Sent: Thursday, January 19, 2017 5:01 PM
To: Guy, William
Subject: FW: HB1228 Trusts
Attachments: image002.jpg; ATT00001.htm; Benjamin Orzeske.vcf; ATT00002.htm

Bill, please see the below. Hopefully this addressed Rep. Klemin's issues. TJW

Tony J. Weiler

Executive Director
State Bar Association of North Dakota
1661 Capitol Way, 104LL
Bismarck, ND 58501

(701) 255-1404 (o)
(701) 220-5846 (c)

From: Hagerty, Gail [mailto:GHagerty@ndcourts.gov]
Sent: Thursday, January 19, 2017 2:54 PM
To: Tony Weiler
Subject: Fwd: HB1228 Trusts

Sent from my iPhone

Begin forwarded message:

From: Benjamin Orzeske <borzeske@uniformlaws.org>
Date: January 19, 2017 at 2:51:52 PM CST
To: "Hagerty, Gail" <GHagerty@ndcourts.gov>, "Klemin, Lawrence R." <lklemin@nd.gov>
Subject: RE: HB1228 Trusts

Dear Gail and Larry,

Thanks for bringing HB 1228 to my attention. I'm sorry that I was not able to analyze the bill in time for the hearing yesterday, but I hope this information is still helpful.

I will address each section of the bill below, but in general I think this legislation is well thought out and reasonable. It could be improved by the minor amendments to Sections 3 and 7 suggested below. I would also be interested to know why the drafters preferred the provisions in Section 8 to the Uniform Trust Decanting Act. The provisions in Sections 9 and 10 might be reconsidered in a few years after the draft uniform acts on the same subjects are approved.

ANALYSIS:

Section 1: Allows perpetual business trusts. No effect on any uniform acts.

Section 2: Repeals and reenacts one section of the Uniform Principal and Income Act (UPAIA), adding non-uniform language as subsections 1a. and 1b. The new language provides some added protection against lawsuits for trustees. The protections are consistent with the intent of UPAIA, so they do no harm.

Section 3: Repeals and reenacts one section of the Uniform Principal and Income Act (UPAIA), adding the non-uniform phrase "was not made in good faith or" in the third line. The change is consistent with the intent of UPAIA, so it does no harm. **NOTE:** I suggest a technical amendment in the second line of this section, which reads: "...a discretionary power conferred by this section...". The word "section" should be changed to "chapter".

Section 4: Clarifies the standard for determining a settlor's capacity. Uniform Trust Code (UTC) Section 601 uses the same standard for settlors of revocable trusts, and this section expands the applicability to all settlors. Generally consistent with the common law.

Section 5: Creates a new chapter that provides rules for challenging the validity of a trust. UTC Section 604 provides a limitation period for contesting revocable trusts; the rules provided here are more comprehensive and apply to all trusts, but are reasonable and consistent with UTC Section 604.

Section 6: Clarifies a rule for revocable trusts. This is consistent with the UTC and does no harm.

Section 7: Amends a section of the ND UTC to clarify that a trustee has a duty to report to the holder of a power to change the qualified beneficiary of a trust, rather than reporting directly to the beneficiary. **NOTE:** I recommend adding the following phrase at the end of Section 1c.: "to the extent trust property is subject to the power".

Section 8: Adds a new chapter similar to the Uniform Trust Decanting Act (UTDA). While the policies behind this section are generally consistent with the UTDA, this new chapter uses different terminology and is not as detailed. The UTDA was approved in 2015, enacted by 2 states in 2016, and will be considered by legislatures in at least 7 states this year. I think the UTDA is preferable because it will accomplish the same goals but will also be consistent with the law of other states that adopt the uniform act.

Section 9: Adds a new chapter that provides rules similar to those in the draft Uniform Directed Trust Act, which is on schedule to be approved at the ULC 2017 annual meeting and will be available for adoption by the states beginning in 2018. It is impossible to compare the provisions of this version with the uniform act until the act is finalized.

Section 10: Adds a new chapter providing for conversion of an existing trust to a unitrust. The Drafting Committee to revise UPAIA is in the process of drafting very similar provisions that are likely to be incorporated into the revised version of UPAIA, scheduled to be approved in summer 2019. It is impossible to compare the provisions of this section with the uniform act until the act is finalized.

Section 11: Repeals Section 601 of the ND UTC (replaced by the provisions in Section 4), Section 604 of the ND UTC (replaced by the provisions in Section 5), and Section 808 of the ND UTC (replaced by the provisions in Section 9). Given the enactment of the above provisions, these repeals make sense.

Please contact me again if you have further questions, and many thanks to both of you for your work to enact uniform acts in North Dakota.

My best,

Mr. Chairman:

The first email in this email chain is an analysis of House Bill No. 1228 by an individual at the Uniform Law Commission (ULC). My email will respond to his comments, section by section.

1. First of all, a little history ... North Dakota's version of the Uniform Trust Code (UTC) was enacted in 2007.
 - a. Representative Klemin and about ten others (including me), constituted a drafting task force.
 - (1) When we began our work, the UTC had been adopted in six states.
 - (2) At our request, the ULC prepared a draft of the UTC with each section starting on a new page after which, state by state, were the modifications that each of those states had made to the UTC.
 - (3) The North Dakota UTC adopted many sections without modification. However, in many others the changes made by one or more of the other states were incorporated into the North Dakota UTC.
 - b. Since 2007, several minor amendments have been made to the North Dakota UTC.
2. The analysis by the ULC is very fair and even handed.
 - a. Section 1: Re the repeal of the Rule Against Perpetuities (RAP) ... As I stated during the hearing:
 - (1) As drafted, Section 1 is defective in that it deals only with the statutory RAP (i.e., 90 years maximum) and not the common law RAP (i.e., lives in being plus 21 years) and does not require a North Dakota based trustee.
 - (2) Apparently this section has generated policy issues of which the drafting task force was unaware.
 - (3) At this point my recommendation is to either:
 - (a) Enact Section 1 as amended in its entirety; or
 - (b) Set Section 1 aside for further study until the 2019 session. (I would be happy to help with such a project.)
 - b. Sections 2 and 3: Re the Uniform Principal & Income Act modifications:
 - (1) The ULC, with one minor recommended modification, finds no problems with Sections 2 and 3.

- (2) I agree.
- c. Section 4: Re the capacity needed to create a trust:
 - (1) The ULC finds no problems with Section 4.
 - (2) I agree.
- d. Section 5: Re a rule for challenging trust validity.
 - (1) The ULC finds no problems with Section 5.
 - (2) I agree.
- e. Section 6. Clarifies a rule for revocable trusts:
 - (1) The ULC finds no problems with Section 6.
 - (2) I agree.
- f. Section 7: Re the duty of a trustee to inform and report:
 - (1) The ULC, with one minor recommended modification, finds no problems with Section 7.
 - (2) I agree.
- g. Section 8: Re trust decanting (i.e., pouring an old trust into a new one):
 - (1) At this time 23 states have decanting statutes ... two of which have enacted the Uniform Trust Decanting Act (UTDA).
 - (2) Our proposal is to follow the Minnesota Statute (as we have done with many other statutes ... especially in the area of business entities) which in turn was patterned after the New York statute.
 - (3) Doing so will give us a good statute that has been designed by a neighboring Midwest state.
 - (a) We will then have time to see if more than two other states adopt the UTDA.
 - (b) If others do, then you can always amend our statute.
 - (4) Thus, on Section 8, I disagree with the ULC.

- h. Section 9: Re directed trusts.
 - (1) Once again, our drafting task force has followed the Minnesota statute which we believe will work well.
 - (2) And again, if the Uniform Directed Trust Act is approved in 2019, is adopted by other states and is working well, then you can amend our statute, if you wish.
 - (3) Thus, at this time, I recommend that Section 9 be adopted without modification.

- i. Section 10: Re converting an existing trust into a unitrust.
 - (1) Once again, our drafting task force has followed the Minnesota statute which we believe will work well.
 - (2) And again, if unitrust provisions are incorporated into the Uniform Principal & Income Act in mid-2019, are adopted by other states and are working well, then you can amend our statute, if you wish.
 - (3) Thus, at this time I recommend that Section 10 be adopted without modification.

- j. Section 11: Re the repeal of the existing sections that are replaced by new sections in HB No. 1228.
 - (1) The ULC finds no problems with Section 11.
 - (2) I agree.

- 3. Mr. Chairman, it is my understanding that the recessed committee will reconvene on Monday, January 23rd at 9:00 a.m.
 - a. Prior to that, I suggest that the ULC email and my responses to it be forwarded to the other members of the committee to help them prepare for the reconvened hearing on Monday.
 - b. If you anticipate questions and comments at that reconvened hearing, then I would like to appear to help the committee with any questions that it may have in reaching its decision.
 - c. I will also be at the Capitol on Wednesday, January 25th for a 9:30 IBL Hearing on Senate Bill No. 2223. If there are going to be questions and comments and if the hearing could be reconvened sometime on Wednesday, it would save me a trip to Bismarck.

I can be reached either by email or by telephone at 701.238.2500. Thank you Mr. Chairman. I will look forward to hearing from you.

Very truly yours,

Bill Guy

60594638_1.docx

#1
1228
2-8-17

Rep. Lawrence R. Klemin

Jan. 23, 2017

PROPOSED AMENDMENTS TO HOUSE BILL NO. 1228

Page 1, line 4, remove "47-02-27.4,"

Page 1, line 4, after "59-04.3-02" remove the comma

Page 1, line 5, remove "exclusions from the rule against perpetuities and"

Page 1, remove lines 10 through 24

Page 2, remove lines 1 through 11

Page 4, line 29, replace "section" with "chapter"

Renumber accordingly

47-02-27.1. Statutory rule against perpetuities — Invalidity of certain contingent property interests, general powers of appointment, special powers of appointment, and general testamentary powers of appointment.

1. A contingent property interest is invalid unless:

a. When the interest is created, it is certain to vest or terminate no later than twenty-one years after the death of an individual then alive; or

b. The interest either vests or terminates within ninety years after its creation.

2. A general power of appointment not presently exercisable because of a condition precedent is invalid unless:

a. When the power is created, the condition precedent is certain to be satisfied or to become impossible to satisfy no later than twenty-one years after the death of an individual then alive; or

b. The condition precedent either is satisfied or becomes impossible to satisfy within ninety years after its creation.

3. A special power of appointment or a general testamentary power of appointment is invalid unless:

a. When the power is created, it is certain to be irrevocably exercised or otherwise to terminate no later than twenty-one years after the death of an individual then alive; or

b. The power is irrevocably exercised or otherwise terminates within ninety years after its creation.

4. In determining whether a contingent property interest or a power of appointment is valid under subdivision a of subsection 1, subdivision a of subsection 2, or subdivision a of subsection 3, the possibility that a child will be born to an individual after the individual's death is disregarded.

5. If, in measuring a period from the creation of a trust or other property arrangement, language in a governing instrument seeks to disallow the vesting or termination of any interest or trust beyond, seeks to postpone the vesting or termination of any interest or trust until, or seeks to operate in effect in any similar fashion upon, the later of the expiration of a period of time not exceeding twenty-one years after the death of the survivor of specified lives in being at the creation of the trust or other property arrangement or the expiration of a period of time that exceeds or might exceed twenty-one years after the death of the survivor of lives in being at the creation of the trust or other property arrangement, that language is inoperative to the extent it produces a period of time that exceeds twenty-one years after the death of the survivor of the specified lives.

#1
1228-PM
2-14-17

Rep. Lawrence R. Klemin
Feb. 14, 2017

PROPOSED AMENDMENTS TO HOUSE BILL NO. 1228

Page 2, line 11, after the period insert: "A business trust, whether domestic or foreign, may not own any interest in real property within this state."

Page 4, line 29, replace "section" with "chapter"

Renumber accordingly

3/7/17

①

HB 1228

TESTIMONY OF WILLIAM L. GUY III
IN SUPPORT OF
HOUSE BILL NO. 1228

March 7, 2017

Mr. Chairman and members of the Committee, I am a member of a task force (consisting of Douglas Carpenter from Grand Forks, Joseph Heringer and Marilyn Foss, both from Bismarck, Robert Rosenvold, Marshall McCullough, Kevin Kercher, all from West Fargo and Jessica Foss, John Williams III, Mary Locken, Sheri Schrock and me, all from Fargo) which has undertaken the drafting of legislation to supplement the North Dakota Uniform Trust Code (Chapters 59-09 – 59-19).

Some of the highlights of the Bill include:

1. **SECTION 1** of the Bill (on pages 1 and 2) creates a new Subsection 7 to Section 47-02-27.4 and will be handled by Marilyn Foss.
2. **SECTION 2** of the Bill (on pages 2 through 4) amends Section 59-04.2-03 and will be handled by Bob Rosenvold.
3. **SECTION 3** of the Bill (on pages 4 through 6) creates new Section 59-04.2-03.1 and will be handled by Bob Rosenvold.
4. **SECTION 4** of the Bill (on page 6) creates new Section 59-09-04.1 which provides that the capacity of an individual to create a trust is the same capacity that is required of an individual to make a will.
5. **SECTION 5** of the Bill (on pages 6 and 7) creates new Chapter 59-10.1 to set forth a process by which an individual may challenge the validity of a trust instrument and obtain a declaratory judgment of that invalidity. The chapter includes:
 - a. a determination of who must be the parties to the proceeding;
 - b. a limitation on the time in which the proceeding must occur or be barred from occurring;
 - c. a detailing of the findings required of the court; and
 - d. a process for the return of distributions made by the trustee prior to becoming aware of a possible proceeding to contest the validity of the trust.
6. **SECTION 6** of the Bill (on pages 7 and 8) creates new Section 59-14-05 and makes clear that while a trust is revocable, the trustee may follow a direction of the trust creator which is contrary to the terms of the trust (and is a transfer of identical language from Subsection 1 of Section 59-16-08 . . . the remaining subsections of which were repealed and replaced with new Chapter 59-16.2).

7. **SECTION 7** of the Bill (on pages 8 and 9) amends Section 59-16-13 regarding a trustee's duty to inform and report to the beneficiaries of the trust.

a. The amendment provides that if an individual holds the power to change the beneficiaries of a trust (the "powerholder"), then the trustee's duty to inform and report runs to the powerholder and not to the beneficiaries whose status as a beneficiary could be altered or eliminated by the powerholder.

b. An example would be a charitable remainder trust that provides income to the trust creator during his or her lifetime and then distributes the trust principal to named charities upon the death of the trust creator.

(1) If the trust creator holds the power to change the names of the charitable beneficiaries who receive the trust principal upon his or her death, then the trustee's duty to inform and report to the beneficiaries of the trust runs to the power holder and not to the charities which might be eliminated as beneficiaries if the power holder exercises his/her power.

(2) The same principle holds true for individuals who would receive trust assets upon the death of the power holder but otherwise have no interest in the trust prior to the death of the power holder.

8. **SECTION 8** of the Bill (pages 9-17) creates new Chapter 59-16.1 establishing for the first time in the North Dakota Uniform Trust Code the power of trust "decanting."

a. Trust decanting is the process by which the assets of an old trust (often with obsolete language) are poured (or decanted) from the old trust to a new trust.

b. In addition to an extensive section on definitions, this chapter includes sections:

(1) that differentiate the authority given to a trustee of the old trust who has unlimited discretion in invading the trust principal as opposed to trustees who have limited discretion;

(2) that makes clear that the power to invade the trust principal under this chapter is considered to be an exercise of special power of appointment by the trustee;

(3) that the duration of the new trust cannot exceed the duration of the old trust;

(4) that the trustee exercising power under this chapter has a fiduciary duty to exercise the power in the best interests of one or more of the proper objects of the power and as a prudent person who would exercise that power under the prevailing circumstances;

(5) that provide for the handling of subsequently discovered assets after the initial transfer of assets;

- (6) that provide for the notice to be given to those interested in the old trust; and
 - (7) that certain aspects of the old trust may not be reduced, limited or modified in the decanting process. (See pages 15 and 16 for a list of prohibitions).
 - c. The reasons why it may be beneficial to make changes to the terms of an existing irrevocable trust include:
 - (1) addressing changes in tax law;
 - (2) addressing changes in the needs or circumstances of the beneficiary;
 - (3) changing trustees; or
 - (4) fixing administrative provisions of the irrevocable trust.
- 9. **SECTION 9** of the Bill (pages 17-24) creates a new Chapter 59-16.2 (replacing Section 59-16-08) pertaining to directed trusts.
 - a. A directed trust is a concept that is being widely used in other states and is of significant interest to trust departments and trust companies in North Dakota.
 - b. In a directed trust, the trustee typically has physical custody of the assets of the trust but is subject to direction by:
 - (1) the "Distribution Trust Advisor"; and/or
 - (2) the "Investment Trust Advisor."
 - c. The "Distribution Trust Advisor" may be another trust department, or an individual who, in any event, has the authority to direct distributions of the trust assets being held by the trustee.
 - d. The "Investment Trust Advisor" is most often an investment advisor of the trust creator or possibly the trust creator himself or herself. In any event, the Investment Trust Advisor has the authority and the responsibility to handle the investment of the trust assets.
 - e. This chapter extensively details the responsibilities of the individuals in question.
- 10. **SECTION 10** of the Bill (pages 24-31) creates new Chapter 59-16.3 authorizing the concept of "Total Return Unitrusts," and will be handled by Bob Rosenvold.
- 11. **SECTION 11** of the Bill (on page 31) provides for the repeal of Sections 59-14-01, 59-14-04 and 59-16-08.

12. **SECTION 12** of the Bill (on page 31) provides that Section 8 of the Act (pertaining to trust decanting) is retroactive and applies to all trusts governed by North Dakota law.

I appreciate the opportunity to provide this testimony. Thank you.

William L. Guy III
Fredrikson & Byron P.A.
51 Broadway, Suite 400
Fargo, ND 58102-4991
Phone: 701-237-8200

60527849_6.docx

3/7/17

(2)

HB 1228

TESTIMONY OF
SHERI GRONHOVD SCHROCK
IN SUPPORT OF
HOUSE BILL NO. 1228

March 7, 2017

Mr. Chairman and Members of the Senate Judiciary Committee, thank you for permitting me to present testimony on behalf of the North Dakota Bankers Association (“NDBA”) and as a participant of the legislative task force, previously described in Mr. William L. Guy III’s testimony, in support of House Bill No. 1228 (hereafter, “House Bill 1228”).

I serve as in-house legal counsel for Bell Bank’s Wealth Management Division. In that capacity, I encounter situations in which we and other fiduciaries governed by North Dakota law – corporate and individual alike – lack several statutorily-provided planning and ameliorative solutions available to fiduciaries in many other states today, including Minnesota and South Dakota. If enacted, House Bill 1228 will enable fiduciaries, working with legal and tax advisors in appropriate circumstances, to exercise these additional statutory powers and processes to resolve unmet needs of settlors and their beneficiaries.

Changing and challenging circumstances facing North Dakota trusts and their interested parties include tax and non-tax reasons. In these early days of this presidential administration, it is unclear what the structure and rate for federal income and transfer taxes (e.g., estate, gift and generation-skipping transfer taxes) will be in 2017 let alone in the future. We continue to experience a historically low and prolonged low interest rate environment for fixed income investments. Beneficiaries may experience situations not foreseen by the settlors. House Bill 1228 provides the statutory means for a fiduciary, acting consistently with the expressed or presumed intent of a settlor, to address such challenges and changed circumstances.

In January 2017, I, along with approximately 3,100 other trust and estate professionals from across the country, attended the week-long Heckerling Estate Planning Conference to hear nationally recognized legal and tax experts speak on estate planning, administration and tax matters. A consistent theme of this year’s Heckerling presentations was the need for flexibility to address changing and challenging circumstances and for all advisors to be well-equipped with solutions to deploy in appropriate instances. Not only does House Bill 1228 provide all citizens of North Dakota and their advisors such solutions - whether or not written into a governing trust instrument by a drafting attorney - but it also contains appropriate notice and procedural safeguards.

I would like to add to the testimony of Mr. Guy and Mr. Rosenvold on a few specific provisions of House Bill 1228 as follows:

Sections 2, 3 and 10 of House Bill 1228 grant fiduciaries the ability, where circumstances and conditions warrant, to modify a trust’s distributions to the current beneficiary. As current and future beneficiaries usually have competing interests, these sections of House Bill 1228 afford trustees appropriate protections from liability. As a member of the legislative task

force drafting the North Dakota Uniform Trust Code during the period 2005-2007, it is my recollection that the reason we did not include a unitrust provision was lack of guidance from the Internal Revenue Service.

Section 5 of House Bill 1228 establishes a process whereby the validity of revocable or irrevocable trusts may be challenged. Section 5 expands the scope of current NDCC Section 59-14-04, builds upon North Dakota's Uniform Probate Code (NDCC 30.1-08.1-04) which permits a testator of a Will to institute a proceeding to determine the validity of a Will and creates a 120-day statute of limitations for such challenges to revocable or irrevocable trusts.

If this section is enacted, North Dakota will join Delaware in according settlors of revocable and irrevocable trusts and their trustees a process and means to accelerate any challenges to their trusts before the courts while a settlor is living and able to participate in the defense of his or her trust. Provided the notice and documentation required by Section 5 is delivered to a person, that person must commence a judicial proceeding within 120 days of receipt of the notice. Absent the commencement of a judicial proceeding within the 120 day statute of limitation, the trust will be deemed valid as to all who received the requisite notice and documentation.

Section 8 has the support of the NDBA as statutory decanting powers will enable fiduciaries to address innumerable instances of changed circumstances. As a member of the legislative task force drafting the North Dakota Uniform Trust Code during the period 2005-2007, it is my recollection that the reason we did not include a decanting provision was lack of guidance from the Internal Revenue Service.

Section 9 will permit North Dakota citizens and resident fiduciaries to unbundle the traditional trustee roles and responsibilities among two or more additional fiduciaries such as a distribution advisor, investment advisor and trust protector. The NDBA supports this section as it brings significant clarity concerning the roles and responsibilities of the unbundled service providers and greatly limits the liability of a trustee for following the directions of the other fiduciaries.

Thank you for the opportunity to present my testimony to your Committee.

Sheri Gronhovd Schrock
Fiduciary Legal Counsel &
SVP Wealth Management Administration
Bell Bank
15 Broadway
Fargo, North Dakota 58102
(701) 451-3109
sschrock@bellbanks.com

TESTIMONY OF ROBERT E. ROSENVOLD
IN SUPPORT OF
HOUSE BILL NO. 1228

January 18, 2017

The provisions of House Bill No. 1228, which I would like to address are Sections 2, 3 and Section 10. Sections 2 and 3 concern the power of a trustee to adjust between income and principal and Section 10 concerns the power of a trustee to convert an income-only interest to a Unitrust amount which is based upon a percent of the trust value determined annually.

The purpose of these sections is to allow a trustee of income-only trusts to make investment decisions without being captive to immediate cash flow needs. More specifically, a trustee of such a trust has a fiduciary obligation to maximize the income distributions to the income beneficiary while, at the same time, to preserve the value of the trust assets for the remainder beneficiaries who will receive the trust's assets at the time of the termination of the trust. Obviously, these two concerns and obligations are often contradictory.

Income distributions to the income beneficiary, which most often involve only the surviving spouse, have been seriously reduced these last few years because of the current investment climate. Historically, bonds and certificates of deposit were excellent investments to provide substantial income distributions to the income beneficiary. However, under the current interest climate, such investments, even with a trust estate as large as \$1,000,000, will only result in income distributions to the income beneficiary of \$10,000 to \$15,000 per year. Further, investments in stocks and mutual funds will likely provide even a smaller income distribution to the income beneficiary.

Every state with the exception of North Dakota has enacted one of two methods for redefining trust income. When North Dakota adopted the Uniform Principal and Income Act in 1969, for some reason the Power to Adjust was omitted and has never been added.

Currently, forty-seven (47) states, including the District of Columbia, allow trustees to make adjustments between income and principal to allocate the trust's investment return fairly between income and remainder beneficiaries. Thirty-three (33) states have adopted Unitrust language. Thirty-one (31) states have adopted both methods.

POWER TO ADJUST

Section 2 of the Bill amends Section 59-09.2-03 to authorize a trustee, who is managing the trust assets as a prudent investor, to make adjustments between income and principal of the trust as a trustee considers necessary after taking into account all relevant factors.

Section 2 of the Bill, will allow the trustee, after careful consideration, to determine that it would be unable to administer the trust impartially and fairly to all beneficiaries without making an adjustment. The Power to Adjust works both ways. It authorizes a trustee to reallocate a portion of the trust return to income in a low interest rate environment, even though the return is attributable to principal appreciation. The Power to Adjust permits the trustee to allocate a portion of the trust income to principal.

For example, assume a trust has a value of \$1,000,000 and it generates \$10,000 in ordinary income and \$60,000 in capital gains. The trustee would have the ability to adjust all or a portion of the capital gains and treat it as income.

The Power to Adjust is totally discretionary for the trustee. The trustee does not have the Power to Adjust if the trustee is a beneficiary of the trust or, even if the trustee is not a beneficiary, the adjustment would somehow benefit the trustee directly or indirectly. If the trust has co-trustees, the Power to Adjust can be made by the co-trustee who is not a beneficiary, unless it is not permitted by the terms of the trust. If the trust clearly manifests an intention that the fiduciary shall or may favor one or more of the beneficiaries, the Power to Adjust is not given. The Power to Adjust is subject to control by the Court to prevent an abuse of discretion by the trustee. The Power to Adjust is denied to the trustee if there are any adverse tax consequences. The trust can contain language to specifically forbid the use of the Power to Adjust.

Section 3 of the Bill provides that the Court may not order a trustee to change a decision to exercise or not exercise the Power to Adjust unless it determines that the decision was an abuse of the trustee's discretion. If the trustee is hesitant to exercise its discretion, the trustee may petition the Court for instructions. It requires the Court to determine, upon a petition by the trustee, whether a proposed exercise or non-exercise of the power by the trustee would be an abuse of discretion under the general rule of paragraph 1 of Section 3. If the petition contains the information prescribed in the second sentence of paragraph 4 of Section 3, the proposed action or inaction is presumed not to be an abuse of discretion.

UNITRUST

Section 10 of House Bill No. 1228 would enact what is commonly known as a Unitrust regime. This is also known as a Total Return Trust.

Like the Power to Adjust, it is designed to allow a trustee to redefine trust income. However, trust income is defined as a percentage of the value of the trust, determined each year, without regard to traditional concepts of income or principal. The amount of income distributed annually fluctuates according to the percentage of value of the trust assets. An important advantage of the Unitrust approach is that it eliminates the inherent tension between income and remainder beneficiaries. Both have an interest in the trust gleaning the highest possible total return. This is because the amount of the annual income distribution, as well as the amount ultimately received by the remainder beneficiaries, increase with the value of the trust assets. This Bill defines the Unitrust amount in a range between 3% to 5% of the value of the

trust assets. Treasury Regulations provide that as long as the distribution is no less than 3% nor more than 5% each year, no adverse tax consequences will occur. These Final Regulations apply to tax years on or after January 2, 2004, and are applicable to both the Power to Adjust and to Unitrust.

Existing income-only trusts can be converted to a Unitrust by a trustee as long as the trustee is not an "Interested Trustee" as defined under Paragraph 4. Importantly, an "Interested Trustee" includes an individual trustee to whom the net income or principal of the trust can currently be distributed or will be distributed if the trust were then to terminate and be dissolved. If a trustee is not an "Interested Trustee," then the trustee, in its sole discretion, and without the approval of any Court, may convert an income trust to a Total Return Unitrust, reconvert a Total Return Unitrust to an income trust, or change the percentage used to calculate the Unitrust amount and the method used to determine the fair market value of the trust. This can only be done, however, if the requirements under proposed NDCC 59-16.3.02 are followed. Importantly, the trustee must send written notice of its intention to the person who created the trust, if living, all living individuals who are currently receiving, or are eligible to receive, distributions of income from the trust, and all living individuals who would receive principal of the trust if the trust were to terminate at the time of giving such notice.

If the only trustee of the trust is an "Interested Trustee" and if he or she wishes to convert the trust, the trustee may petition in Court for such order. The Court in its own discretion, or on the petition of such trustee, or any person interested in the trust, may appoint a disinterested person who, acting in a fiduciary capacity, can provide information to enable the Court to make its determination.