

HB4662



97TH GENERAL ASSEMBLY

State of Illinois

2011 and 2012

HB4662

by Rep. Emily McAsey

SYNOPSIS AS INTRODUCED:

760 ILCS 5/16.4 new

Amends the Trusts and Trustees Act. Provides conditions and requirements for the distribution of trust principal to a second trust. Provides that the changes apply to any trust in existence on the effective date and to any trust created on or after the effective date.

LRB097 14569 AJ0 59425 b

A BILL FOR

1 AN ACT concerning civil law.

2 **Be it enacted by the People of the State of Illinois,**
3 **represented in the General Assembly:**

4 Section 5. Trust and Trustees Act is amended by adding
5 Section 16.4 as follows:

6 (760 ILCS 5/16.4 new)

7 Sec. 16.4. Distribution of trust principal in further
8 trust.

9 (a) Definitions. In this Section:

10 "Absolute discretion" means the right to distribute
11 principal that is not limited or modified in any manner to or
12 for the benefit of one or more beneficiaries of the trust,
13 whether or not the term "absolute" is used. A power to
14 distribute principal that includes purposes such as best
15 interests, welfare, or happiness shall constitute absolute
16 discretion.

17 "Authorized trustee" means an entity or individual, other
18 than the settlor, who has authority under the terms of the
19 first trust to distribute the principal of the trust for the
20 benefit of one or more current beneficiaries.

21 "Code" means the United States Internal Revenue Code of
22 1986, as amended from time to time, including corresponding
23 provisions of subsequent internal revenue laws and

1 corresponding provisions of State law.

2 "Current beneficiary" means a person who is currently
3 receiving or eligible to receive a distribution of principal or
4 income from the trustee on the date of the exercise of the
5 power.

6 "Distribute" means the power to pay directly to the
7 beneficiary of a trust or make application for the benefit of
8 the beneficiary.

9 "First trust" means an existing irrevocable inter vivos or
10 testamentary trust part or all of the principal of which is
11 distributed in further trust under subsection (c) or (d).

12 "Presumptive remainder beneficiary" means a beneficiary of
13 a trust, as of the date of determination and assuming
14 non-exercise of all powers of appointment, who either (i) would
15 be eligible to receive a distribution of income or principal if
16 the trust terminated on that date, or (ii) would be eligible to
17 receive a distribution of income or principal if the interests
18 of all beneficiaries currently eligible to receive income or
19 principal from the trust ended on that date without causing the
20 trust to terminate.

21 "Principal" includes the income of the trust at the time of
22 the exercise of the power that is not currently required to be
23 distributed, including accrued and accumulated income.

24 "Second trust" means any irrevocable trust to which
25 principal is distributed in accordance with subsection (c) or
26 (d).

1 "Successor beneficiary" means any beneficiary other than
2 the current and presumptive remainder beneficiaries, but does
3 not include a potential appointee of a power of appointment
4 held by a beneficiary.

5 (b) Purpose. An independent trustee who has discretion to
6 make distributions to the beneficiaries shall exercise that
7 discretion in the trustee's fiduciary capacity, whether the
8 trustee's discretion is absolute or limited to ascertainable
9 standards, in furtherance of the purposes of the trust.

10 (c) Distribution to second trust if absolute discretion. An
11 authorized trustee who has the absolute discretion to
12 distribute the principal of a trust may distribute part or all
13 of the principal of the trust in favor of a trustee of a second
14 trust for the benefit of one, more than one, or all of the
15 current beneficiaries of the first trust and for the benefit of
16 one, more than one, or all of the successor and remainder
17 beneficiaries of the first trust.

18 (1) If the authorized trustee exercises the power under
19 this subsection, the authorized trustee may grant a power
20 of appointment (including a presently exercisable power of
21 appointment) in the second trust to one or more of the
22 current beneficiaries of the first trust, provided that the
23 beneficiary granted a power to appoint could receive the
24 principal outright under the terms of the first trust.

25 (2) If the authorized trustee grants a power of
26 appointment, the class of permissible appointees in favor

1 of whom a beneficiary may exercise the power of appointment
2 granted in the second trust may be broader than or
3 otherwise different from the current, successor, and
4 presumptive remainder beneficiaries of the first trust.

5 (3) If the beneficiary or beneficiaries of the first
6 trust are described as a class of persons, the beneficiary
7 or beneficiaries of the second trust may include one or
8 more persons of such class who become includible in the
9 class after the distribution to the second trust.

10 (d) Distribution to second trust if no absolute discretion.
11 An authorized trustee who has the power to distribute the
12 principal of a trust but does not have the absolute discretion
13 to distribute the principal of the trust may distribute part or
14 all of the principal of the first trust in favor of a trustee
15 of a second trust, provided that the current beneficiaries of
16 the second trust shall be the same as the current beneficiaries
17 of the first trust and the successor and remainder
18 beneficiaries of the second trust shall be the same as the
19 successor and remainder beneficiaries of the first trust.

20 (1) If the authorized trustee exercises the power under
21 this subsection (d), the second trust shall include the
22 same language authorizing the trustee to distribute the
23 income or principal of a trust as set forth in the first
24 trust.

25 (2) If the beneficiary or beneficiaries of the first
26 trust are described as a class of persons, the beneficiary

1 or beneficiaries of the second trust shall include all
2 persons who become includible in the class after the
3 distribution to the second trust.

4 (3) If the authorized trustee exercises the power under
5 this subsection (d) and if the first trust grants a power
6 of appointment to a beneficiary of the trust, the second
7 trust shall grant such power of appointment in the second
8 trust and the class of permissible appointees shall be the
9 same as in the first trust.

10 (4) Supplemental Needs Trusts.

11 (i) Notwithstanding the other provisions of this
12 subsection (d), the authorized trustee may distribute
13 part or all of the principal of a disabled
14 beneficiary's interest in the first trust in favor of a
15 trustee of a second trust which is a supplemental needs
16 trust if the authorized trustee determines that to do
17 so would be in the best interests of the disabled
18 beneficiary.

19 (ii) Definitions. For purposes of this subsection

20 (d):

21 "Best interests" of a disabled beneficiary
22 include, without limitation, consideration of the
23 financial impact to the disabled beneficiary's
24 family.

25 "Disabled beneficiary" means a current
26 beneficiary, presumptive remainder beneficiary, or

1 successor beneficiary of the first trust who the
2 authorized trustee determines has a disability
3 that substantially impairs the beneficiary's
4 ability to provide for his or her own care or
5 custody and that constitutes a substantial
6 handicap, whether or not the beneficiary has been
7 adjudicated a "disabled person".

8 "Governmental benefits" means financial aid or
9 services from any State, Federal, or other public
10 agency.

11 "Supplemental needs second trust" means a
12 trust that complies with paragraph (iii) of this
13 paragraph (4) and that relative to the first trust
14 contains either lesser or greater restrictions on
15 the trustee's power to distribute trust income or
16 principal and which the trustee believes would, if
17 implemented, allow the disabled beneficiary to
18 receive a greater degree of governmental benefits
19 than the disabled beneficiary will receive if no
20 distribution is made.

21 (iii) Remainder beneficiaries. A supplemental
22 needs second trust may name remainder and successor
23 beneficiaries other than the disabled beneficiary's
24 estate, provided that the second trust names the same
25 presumptive remainder beneficiaries and successor
26 beneficiaries to the disabled beneficiary's interest,

1 and in the same proportions, as exist in the first
2 trust. In addition to the foregoing, where the first
3 trust was created by the disabled beneficiary or the
4 trust property has been distributed directly to or is
5 otherwise under the control of the disabled
6 beneficiary, the authorized trustee may distribute to
7 a "pooled trust" as defined by federal Medicaid law for
8 the benefit of the disabled beneficiary or the
9 supplemental needs second trust must contain pay back
10 provisions complying with Medicaid reimbursement
11 requirements of federal law.

12 (iv) Reimbursement. A supplemental needs second
13 trust shall not be liable to pay or reimburse the State
14 or any public agency for financial aid or services to
15 the disabled beneficiary except as provided in the
16 supplemental needs second trust.

17 (e) Notice. An authorized trustee may exercise the power to
18 distribute in favor of a second trust under subsections (c) and
19 (d) without the consent of the settlor or the beneficiaries of
20 the first trust and without court approval, if the authorized
21 trustee sends written notice of the trustee's decision,
22 specifying the manner in which the trustee intends to exercise
23 the power and the prospective effective date for the
24 distribution to the following beneficiaries, determined as of
25 the date the notice is sent and assuming non-exercise of all
26 powers of appointment:

1 (1) all of the legally competent current beneficiaries
2 and presumptive remainder beneficiaries; provided,
3 however, there are one or more legally competent current
4 beneficiaries and one or more legally competent
5 presumptive remainder beneficiaries; and

6 (2) no beneficiary to whom notice was sent objects to
7 the distribution in writing delivered to the trustee within
8 60 days after the notice is sent ("notice period").

9 (3) A trustee is not required to provide a copy of the
10 notice to a beneficiary who is known to the trustee but who
11 cannot be located by the trustee after reasonable diligence
12 or who is not known to the trustee.

13 (f) Court involvement.

14 (1) The trustee may for any reason elect to petition
15 the court to order the distribution, including, without
16 limitation, the reason that the trustee's exercise of the
17 power to distribute under this Section is unavailable, such
18 as:

19 (a) a beneficiary timely objects to the
20 distribution in a writing delivered to the trustee
21 within the time period specified in the notice; or

22 (b) there are no legally competent current
23 beneficiaries or legally competent presumptive
24 remainder beneficiaries.

25 (2) If the trustee receives a written objection within
26 the notice period, either the trustee or the beneficiary

1 may petition the court to approve, modify, or deny the
2 exercise of the trustee's power. A beneficiary objecting to
3 the exercise of the trustee's power has the burden of
4 proving that the proposed exercise of the power should not
5 be permitted.

6 (3) In a judicial proceeding under this subsection (f),
7 the trustee may, but need not, present the trustee's
8 opinions and reasons for supporting or opposing the
9 proposed distribution, including whether the trustee
10 believes it would enable the trustee to better carry out
11 the purposes of the trust. A trustee's actions in
12 accordance with this Section shall not be deemed improper
13 or inconsistent with the trustee's duty of impartiality
14 unless the court finds from all the evidence that the
15 trustee acted in bad faith.

16 (g) Term of the second trust. The second trust to which an
17 authorized trustee distributes the assets of the first trust
18 may have a term that is longer than the term set forth in the
19 first trust, including, but not limited to, a term measured by
20 the lifetime of a current beneficiary; provided, however, that
21 the second trust shall be limited to the same permissible
22 period of the rule against perpetuities that applied to the
23 first trust, unless the first trust expressly permits the
24 trustee to do so.

25 (h) Divided discretion. If an authorized trustee has
26 absolute discretion to distribute the principal of a trust and

1 the same trustee or another trustee has the power to distribute
2 principal under the trust instrument which power is not
3 absolute discretion, such authorized trustee having absolute
4 discretion may exercise the power to distribute under
5 subsection (c).

6 (i) Later discovered assets. To the extent the authorized
7 trustee does not provide otherwise:

8 (1) The distribution of all of the assets comprising
9 the principal of the first trust in favor of a second trust
10 shall be deemed to include subsequently discovered assets
11 otherwise belonging to the first trust and undistributed
12 principal paid to or acquired by the first trust subsequent
13 to the distribution in favor of the second trust.

14 (2) The distribution of part but not all of the assets
15 comprising the principal of the first trust in favor of a
16 second trust shall not include subsequently discovered
17 assets belonging to the first trust and principal paid to
18 or acquired by the first trust subsequent to the
19 distribution in favor of a second trust; such assets shall
20 remain the assets of the first trust.

21 (j) Other authority to distribute in further trust. This
22 Section shall not be construed to abridge the right of any
23 trustee to distribute property in further trust that arises
24 under the terms of the governing instrument of a trust, any
25 provision of applicable law, a court order, or a non-judicial
26 settlement agreement in accordance with Section 16.1.

1 (k) Need to distribute not required. An authorized trustee
2 may exercise the power to distribute in favor of a second trust
3 under subsections (c) and (d) whether or not there is a current
4 need to distribute principal under the terms of the first
5 trust.

6 (l) No duty to distribute. Nothing in this Section is
7 intended to create or imply a duty to exercise a power to
8 distribute principal, and no inference of impropriety shall be
9 made as a result of an authorized trustee not exercising the
10 power conferred under subsection (c) or (d). Notwithstanding
11 any other provision of this Section, a trustee has no duty to
12 inform beneficiaries about the availability of this Section and
13 no duty to review the trust to determine whether any action
14 should be taken under this Section.

15 (m) Express prohibition. A power authorized by subsection
16 (c) or (d) may not be exercised if expressly prohibited by the
17 terms of the governing instrument, but a general prohibition of
18 the amendment or revocation of the first trust or a provision
19 that constitutes a spendthrift clause shall not preclude the
20 exercise of a power under subsection (c) or (d).

21 (n) Restrictions. An authorized trustee may not exercise a
22 power authorized by subsection (c) or (d) to affect any of the
23 following:

24 (1) to reduce, limit or modify any beneficiary's
25 current right to a mandatory distribution of income or
26 principal, a mandatory annuity or unitrust interest, a

1 right to withdraw a percentage of the value of the trust or
2 a right to withdraw a specified dollar amount provided that
3 such mandatory right has come into effect with respect to
4 the beneficiary, except with respect to a second trust
5 which is a supplemental needs trust;

6 (2) to decrease or indemnify against a trustee's
7 liability or exonerate a trustee from liability for failure
8 to exercise reasonable care, diligence, and prudence;
9 except to indemnify or exonerate one party from liability
10 for actions of another party with respect to distribution
11 that unbundles the governance structure of a trust to
12 divide and separate fiduciary and nonfiduciary
13 responsibilities among several parties, including without
14 limitation one or more trustees, distribution advisors,
15 investment advisors, trust protectors, or other parties,
16 provided however that such modified governance structure
17 may reallocate fiduciary responsibilities from one party
18 to another but may not reduce them;

19 (3) to eliminate a provision granting another person
20 the right to remove or replace the authorized trustee
21 exercising the power under subsection (c) or (d); provided,
22 however, such person's right to remove or replace the
23 authorized trustee may be eliminated if a separate
24 independent, non-subservient individual or entity, such as
25 a trust protector, acting in a nonfiduciary capacity has
26 the right to remove or replace the authorized trustee;

1 (4) to reduce, limit or modify the perpetuities
2 provision specified in the first trust in the second trust,
3 unless the first trust expressly permits the trustee to do
4 so.

5 (o) Exception. Notwithstanding the provisions of paragraph
6 (1) of subsection (n) but subject to the other limitations in
7 this Section, an authorized trustee may exercise a power
8 authorized by subsection (c) or (d) to distribute to a second
9 trust; provided, however, that the exercise of such power does
10 not subject the second trust to claims of reimbursement by any
11 private or governmental body and does not at any time interfere
12 with, reduce the amount of, or jeopardize an individual's
13 entitlement to government benefits.

14 (p) Tax limitations. If any contribution to the first trust
15 qualified for the annual exclusion under Section 2503(b) of the
16 Code, the marital deduction under Section 2056(a) or 2523(a) of
17 the Code, or the charitable deduction under Section 170(a),
18 642(c), 2055(a) or 2522(a) of the Code, is a direct skip
19 qualifying for treatment under Section 2642(c) of the Code, or
20 qualified for any other specific tax benefit that would be lost
21 by the existence of the authorized trustee's authority under
22 subsection (c) or (d) for income, gift, estate, or
23 generation-skipping transfer tax purposes under the Code, then
24 the authorized trustee shall not have the power to distribute
25 the principal of a trust pursuant to subsection (c) or (d) in a
26 manner that would prevent the contribution to the first trust

1 from qualifying for or would reduce the exclusion, deduction,
2 or other tax benefit that was originally claimed with respect
3 to that contribution.

4 (1) Notwithstanding the provisions of this subsection
5 (p), the authorized trustee may exercise the power to pay
6 the first trust to a trust as to which the settlor of the
7 first trust is not considered the owner under Subpart E of
8 Part I of Subchapter J of Chapter 1 of Subtitle A of the
9 Code even if the settlor is considered such owner of the
10 first trust. Nothing in this Section shall be construed as
11 preventing the authorized trustee from distributing part
12 or all of the first trust to a second trust that is a trust
13 as to which the settlor of the first trust is considered
14 the owner under Subpart E of Part I of Subchapter J of
15 Chapter 1 of Subtitle A of the Code.

16 (2) During any period when the first trust owns
17 subchapter S corporation stock, an authorized trustee may
18 not exercise a power authorized by paragraph (c) or (d) to
19 distribute part or all of the S corporation stock to a
20 second trust that is not a permitted shareholder under
21 Section 1361(c) (2) of the Code.

22 (3) During any period when the first trust owns an
23 interest in property subject to the minimum distribution
24 rules of Section 401(a)(9) of the Code, an authorized
25 trustee may not exercise a power authorized by subsection
26 (c) or (d) to distribute part or all of the interest in

1 such property to a second trust that would result in the
2 shortening of the minimum distribution period to which the
3 property is subject in the first trust.

4 (q) Limits on compensation of trustee.

5 (1) Unless the court upon application of the trustee
6 directs otherwise, an authorized trustee may not exercise a
7 power authorized by subsection (c) or (d) solely to change
8 the provisions regarding the determination of the
9 compensation of any trustee; provided, however, an
10 authorized trustee may exercise the power authorized in
11 subsection (c) or (d) in conjunction with other valid and
12 reasonable purposes to bring the trustee's compensation
13 into accord with reasonable limits in accord with Illinois
14 law in effect at the time of the exercise.

15 (2) The compensation payable to the trustee or trustees
16 of the first trust may continue to be paid to the trustees
17 of the second trust during the terms of the second trust
18 and may be determined in the same manner as otherwise would
19 have applied in the first trust; provided, however, that no
20 trustee shall receive any commission or other compensation
21 imposed upon assets distributed due to the distribution of
22 property from the first trust to a second trust pursuant to
23 subsection (c) or (d).

24 (r) Written instrument. The exercise of a power to
25 distribute principal under subsection (c) or (d) must be made
26 by an instrument in writing, signed and acknowledged by the

1 trustee, and filed with the records of the first trust and the
2 second trust.

3 (s) Terms of second trust. Any reference to the governing
4 instrument or terms of the governing instrument in this Act
5 includes the terms of a second trust established in accordance
6 with this Section.

7 (t) Settlor. The settlor of a first trust is considered for
8 all purposes to be the settlor of any second trust established
9 in accordance with this Section.

10 (u) Remedies. A trustee who reasonably and in good faith
11 takes or omits to take any action under this Section is not
12 liable to any person interested in the trust. An act or
13 omission by a trustee under this Section is presumed taken or
14 omitted reasonably and in good faith unless it is determined by
15 the court to have been an abuse of discretion. If a trustee
16 reasonably and in good faith takes or omits to take any action
17 under this Section and a person interested in the trust opposes
18 the act or omission, the person's exclusive remedy is to obtain
19 an order of the court directing the trustee to exercise
20 authority in accordance with this Section in such manner as the
21 court determines necessary or helpful for the proper
22 functioning of the trust, including without limitation
23 prospectively to modify or reverse a prior exercise of such
24 authority. Any claim by any person interested in the trust that
25 an act or omission by a trustee under this Section was an abuse
26 of discretion is barred if not asserted in a proceeding

1 commenced by or on behalf of the person within 2 years after
2 the trustee has sent to the person or the person's personal
3 representative a notice or report in writing sufficiently
4 disclosing facts fundamental to the claim such that the person
5 knew or reasonably should have known of the claim. The
6 preceding sentence shall not apply to a person who was under a
7 legal disability at the time the notice or report was sent and
8 who then had no personal representative. For purposes of this
9 subsection (u), a personal representative refers to a court
10 appointed guardian or conservator of the estate of a person.

11 (v) Application. This Section is available to trusts in
12 existence on the effective date of this amendatory Act of the
13 97th General Assembly or created on or after the effective date
14 of this amendatory Act of the 97th General Assembly. This
15 Section shall be construed as pertaining to the administration
16 of a trust and shall be available to any trust that is
17 administered in Illinois under Illinois law or that is governed
18 by Illinois law with respect to the meaning and effect of its
19 terms, including a trust whose governing law has been changed
20 to the laws of this State, unless the governing instrument
21 expressly prohibits use of this Section by specific reference
22 to this Section. A provision in the governing instrument in the
23 form: "Neither the provisions of Section 16.4 of the Trusts and
24 Trustees Act nor any corresponding provision of future law may
25 be used in the administration of this trust" or a similar
26 provision demonstrating that intent is sufficient to preclude

1 the use of this Section.