

ALLOWING GREATER FLEXIBILITY IN TRUST ADMINISTRATION AND INVESTMENT MANAGEMENT

2015 Nevada Legislation Update



September 2015

Nevada continues to be a leader in enacting laws that allow for greater flexibility in trust administration and investment management. Effective **October 1, 2015**, several new provisions will be added to Nevada's trust laws, with existing laws expanded. All of the changes will apply to new and existing trusts.

SUMMARY OF CHANGES

One of the more significant changes allows parties to enter into non-judicial settlement agreements to interpret and modify existing irrevocable trusts. In addition, the legislation addresses the application of Nevada law and the jurisdiction of Nevada courts over trusts created under Nevada law. Trusts moved to Nevada from another state will be governed under Nevada law and can reap the benefits of Nevada's trust laws.

ADDITIONAL CHANGES

- Nevada's decanting statute has been changed to permit modification of certain income interests and to expand the interests of beneficiaries under a new trust receiving assets from an existing trust.
- Changes to the directed trust statute recognize that trustees are protected when they are directed "not to act" as well as when they are directed to act. These changes also provide definitional clarity for the roles of "directed fiduciary" and "directing trust adviser."
- Nevada's Notice of Proposed Action process has been modified to apply to "any act of trust administration within the scope of their authority" enabling trustees, advisers and protectors to take action without filing petitions with the court for authorization.
- Nevada now recognizes the inclusion of arbitration clauses in trusts to resolve disputes, except those related to the validity of trust instruments.
- "Public benefit" trusts can now be created under Nevada law. These noncharitable trusts do not have identifiable beneficiaries and are established to further one or more specifically declared religious, scientific, literary, educational, community development, personal improvement or philanthropic purpose.
- The new law provides consistency and additional clarity on a trustee's duty to inform and account to beneficiaries of testamentary and nontestamentary trusts, including the ability to establish confidential trusts.

The following discussion highlights these changes to Nevada's trust law in greater detail, and describes how they could provide potential benefits for individuals creating trusts under Nevada law, beneficiaries of Nevada trusts and Nevada trustees.



NON-JUDICIAL SETTLEMENT AGREEMENT PERMITTED

Nevada law now permits the use of a non-judicial settlement agreement (NJSA) as a method for resolution of trust administration and investment matters without court approval. The statute provides the following list of matters that can be addressed by a NJSA, but the list is not intended to be exclusive:

- The investment or use of trust assets;
- The lending or borrowing of money;
- The addition, deletion or modification of a term or condition of the trust;
- The interpretation or construction of a term of the trust;
- The designation or transfer of the principal place of administration of the trust;
- The approval of a trustee's report or accounting;
- The choice of law governing the construction of the trust instrument or administration of the trust, or both;
- Direction to a trustee to perform or refrain from performing a particular act;
- The granting of any necessary or desirable power to a trustee;
- The resignation or appointment of a trustee and the determination of a trustee's compensation;
- The merger or division of trusts;
- The granting of approval or authority for a trustee to make charitable gifts from a non-charitable trust;
- The transfer of a trust's principal place of administration;
- Negating the liability of a trustee for an action relating to the trust and providing indemnification therefor; and
- The termination of the trust.

Two tests must be met for a valid NJSA:

1. The agreement cannot violate a material purpose of the trust; and
2. Its terms and conditions must be ones that can be properly approved by a court.

These two requirements mirror the Uniform Trust Code provisions on NJSAs. The Nevada statute's enumerated powers are more expansive than those listed under the Uniform Trust Code's non-judicial settlement provisions, although the list under the Uniform Trust Code is also nonexclusive.

A NJSA must be signed by all "indispensable parties" to be effective. Indispensable parties include all persons whose consent would be required for a binding settlement by a court. The ultimate determination as to who must be included in the class of indispensable beneficiaries depends upon the purposes of and matters involved in a NJSA. Nevada's virtual representation statute applies to NJSAs to allow for the representation of minors.

If an indispensable party does not sign or object in writing to the NJSA then the trustee can consider proceeding with a "Notice of Proposed Action" under Nevada law (see section on Expansion of Proposed Actions, *infra*). This process allows a trustee to send notice to all indispensable parties advising them of the following:

- The notice is being provided under Nevada law with a specific citation to the statute;
- The name and mailing address of the trustee;
- The name and telephone number of the person from whom the parties can receive additional information;
- A description of the proposed action (acceptance and compliance with the NJSA) and the reasons for taking the action;
- The time during which objections can be made (not less than 30 days after notice is mailed); and
- The date on which the action is to be effective.

All objections must be sent to the person identified and within the time frame set forth in the notice. It is important to note that a party's failure to object to a Notice of a Proposed NJSA constitutes acceptance of the terms of the NJSA. If the trustee receives no objections, it can proceed with the NJSA without liability to a present or future beneficiary.

If the trustee receives an objection to a NJSA, it can petition the court for an order to implement the NJSA. Beneficiaries who failed to object to the NJSA upon receipt of the notice would not be stopped from opposing the action in court. The burden, however, is on the objecting beneficiary to prove that the NJSA should not be executed or should be modified in some manner.

NJSAs can be extremely useful in a variety of situations beyond the interpretation of unclear terms in a trust or definition of a trustee's duties and responsibilities. They can be used to add investment or distribution advisers and to modernize trust provisions for added flexibility in trust administration. They're also an excellent tool to move existing trusts to Nevada to take advantage of its flexible trust laws.

ACCOUNTINGS

Trustees of both testamentary and nontestamentary trusts have a duty to account to current and remainder beneficiaries as required by the terms of the will, court order or trust instrument. The new statute outlines how a trustee can satisfy its duty to account and when a trustee does not have a duty to account to certain beneficiaries depending upon their interests. For example, the trustee must only account to the settlor of a revocable trust unless the court has appointed a guardian for the settlor. Trustees do not have to account to beneficiaries whose only interest in the trust is discretionary or in cases where beneficiaries have waived their rights to accounts or where a discretionary trust is confidential and prohibits disclosure for a period.

The trustee shall deliver a required account within 90 days after the end of the accounting period, which may be extended by consent of the beneficiary or court order.

A trustee can petition the court for instructions to confirm the right of the beneficiary to receive an account, the sufficiency of a beneficiary's demand for an account, or the extent of the account required to satisfy the trustee's duty to account under a confidential trust. The trustee must deliver an annual account by certified, registered, ordinary first-class mail, by overnight delivery or by personal delivery; or by electronic mail or through a secure website on the internet.

An account is considered approved if no written objection is delivered to the trustee within 90 days after delivery of the account by all beneficiaries who received accounts; for all beneficiaries who are not required to receive an account (including non-vested, contingent, remote, minor, and unborn or unknown beneficiaries) if the account has been approved by a beneficiary who has a preceding interest in the trust; and any beneficiary who has waived the right to receive an account.

A beneficiary who has not been provided with an account may send the trustee a written demand for an account. The demand must identify the beneficiary, their address, the accounting period and the legal basis for the demand. Within 14 days after receipt of the demand, the trustee shall notify the beneficiary of its acceptance or rejection of the demand or if the trustee will seek court instructions. The trustee shall:

- Provide an account within 60 days unless modified with the consent of a beneficiary or a court order;
- Notify a beneficiary of the grounds for rejecting the demand for an account and inform the beneficiary of the 60 day period to petition the court to review the rejection; or
- File a petition with the court requesting instructions regarding the demand or right of the beneficiary to receive an account within 15 days.

If the trustee fails to take any action in response to a demand for an accounting, the demand is considered rejected. The "rejection date" is 14 days after the delivery of the demand to the trustee. A beneficiary whose demand is rejected must file a petition seeking the court's review of the rejection within 60 days after the rejection date or they are thereafter barred from demanding an account for the same period.

A trustee who fails to provide an account under the terms of the trust instrument or when required shall be personally liable to each person entitled to receive an account who demanded the account in writing and for all costs reasonably incurred. The trustee shall not expend trust funds to satisfy the trustee's personal liability for its failure to account.

EXPANSION OF PROPOSED ACTION PROCEDURE

Since 2003, Nevada law has allowed a trustee to follow the Notice of Proposed Action process to notify adult beneficiaries of a proposed action. In the absence of written objections from those parties within a defined time period (not less than 30 days), a trustee could proceed with the proposed action without liability to a present or

future beneficiary. Action is defined to include a course of action (e.g. decanting of a trust) or a decision not to take an action (e.g. not making an equitable adjustment as requested by a beneficiary). The prior statute applied to any matter involving the investment and management of trust assets, actions taken under the Nevada Principal and Income Act or decanting.

The specific requirements for the notice are discussed in the NJSA section above. This process can now be used by trust advisers, including investment and distribution advisers, as well as trust protectors *for any aspect of trust administration* that falls within their authority. The Notice of Proposed Action reduces the need to seek court authorization for specific actions of the trustee, trust advisers or trust protectors. Where there is a single, discrete action that is desirable, such as an equitable adjustment or decanting, a Notice of Proposed Action may be preferable to an NJSA.

If the trustee, trust adviser or trust protector decides not to take an action for which a notice has been sent, the trustee, trust adviser or trust protector also must notify the beneficiaries of its decision *not* to proceed with the proposed action. They are not liable to any present or future beneficiary for the decision not to act. A beneficiary has the option to petition the court for an order mandating that the trustee, trust adviser or trust protector take the previously proposed action, with the burden on the beneficiary to prove that the proposed action should be taken.

DISCRETIONARY INTERESTS IN TRUST

Nevada law now expressly provides that a beneficiary who has a discretionary interest in trust (no mandatory rights to income or principal) does not have an *enforceable* right to a distribution from a trust. This change provides enhanced protection for beneficiaries from creditors, spouses or other third party claims seeking recourse from trust assets. The legislature also changed the standard by which a court can review a trustee's exercise of its power to make discretionary distributions to beneficiaries.

Under prior law, a court could review a trustee's exercise of its discretionary distribution authority if the trustee acted dishonestly, with improper motive or failed to act. A trustee acting with improper motive or its failure to act has been deleted as grounds for judicial review of a trustee's discretion. The new standard for judicial review of a trustee's exercise of discretion is where a trustee has acted dishonestly, *with bad faith or willful misconduct*.

DECANTING

The amendments to the statute make the following changes:

- Provide that beneficiaries of the original trust to whom distributions can be made *at a future time or event* can be current beneficiaries of the new trust;
- Specify that the statute can be used whenever Nevada law applies, or whenever the trust is administered in Nevada;
- Clarify that a trustee can declare a new trust without the requirement of having a grantor execute the new trust;
- Revise provisions regarding beneficiaries who have the power to remove the trustee;
- Change the provisions regarding marital and charitable trusts while also adding a provision regarding GRATS; and
- Place restrictions upon trustees who are also beneficiaries.

Nevada Decanting Law Prior to the Amendments

Before describing the changes in the amended statute, it is interesting to note some of the existing provisions of Nevada's decanting statute. The statute allows a trustee to decant if the trustee has discretion to distribute *income or principal*, whereas many states' decanting statutes limit decanting to the trustee's ability to distribute principal. Like several states, Nevada allows a trustee to decant even if the original trust is subject to an ascertainable standard. However, unlike some states where the new trust would be limited by any ascertainable standard found in the original trust, Nevada does not limit the new trust to the same standard unless the trustee who is decanting is also a beneficiary. In those instances, any ascertainable standards applicable to distributions to the trustee/beneficiary under the original trust must also exist in the new trust.

The statute does not require court consent but explicitly permits a trustee to petition the court for approval, which can give a trustee certainty before proceeding. Nevada also permits a trustee to utilize the Notice of Proposed Action as described above to create a time period in which parties may file an objection, after which time a trustee can proceed without liability if there are no objections. The statute specifically provides that decanting is an exercise of a power of appointment held by the trustee and is not a modification and, therefore, the trust can be decanted even if it is an irrevocable trust and even if the trust instrument provides that the trust cannot be amended.

Accelerating Interests of Beneficiaries

The statute provides that the definition of a beneficiary of the new trust includes a beneficiary of the original trust to whom a distribution of income or principal may be made from the original trust at a future time or upon a specified event. There is no requirement that the distribution to the beneficiary from the new trust be limited to the future date or specified event.

Application of Nevada Law

The amendments provide that Nevada's decanting statute applies to a trust as long as it is governed by Nevada law or administered in or under the laws of Nevada. If a trust is moved to Nevada from another state, the Nevada decanting statute can be used regardless of the original governing law of the trust. While this is similar to some other states' decanting laws, unlike some other states Nevada's statute also specifies that the statute can be used for any trust that is governed by Nevada law. So, in theory, Nevada's decanting statute could be applied to a trust administered in another state if it is legitimately subject to Nevada law for any purpose.

Trustee Can Declare New Trust

Under the amendments, the new trust can be established by any party, including a trustee, without violating the requirement under Nevada statute that a trust instrument be signed by a settlor. This change makes it easier for a trustee of the initial trust to declare a new trust where the grantor is no longer alive, or if there is a reason that the grantor does not want to settle the new trust.

Trustee Can be Removed by Beneficiaries

Under the prior law a trustee could not decant if under the new trust discretionary distributions not subject to an ascertainable standard could be made to a beneficiary who has the power to remove and replace the trustee of the new trust with a beneficiary of the new trust, or with a trustee that is related to or subordinate to a beneficiary of the new trust.

Under the new law, there is no longer a complete prohibition. Rather, if a trustee can be removed by a beneficiary of the original trust, the trustee cannot decant to the extent that the decanting would have the effect of increasing the distributions that could be made from the new trust to such beneficiary, unless any distributions from the second trust to a person who is both a beneficiary and a trustee is limited to an ascertainable standard.

Trusts that Qualify for Tax Deductions or Exclusions

Prior to the amendments, the statute provided that a trustee cannot decant if the contribution to the original trust qualified for an estate or gift tax exclusion or deduction for federal or state income, gift or estate taxes, *and the terms of the new trust include a provision which if included in the original trust would prevent the original trust from qualifying for the tax deduction or exclusion.* The amendment changes this to provide that the trustee cannot decant if doing so would reduce any income interest of any income beneficiary of the original trust if the transfer of assets to the original trust qualified for a marital deduction or charitable deduction for federal or state income, gift or estate tax purposes. This same amendment also prohibits reducing any income interest where the initial trust is a GRAT or unitrust.

Note that the limitation is based solely on the reduction of an income interest, and the revised statute does not contain the language specifically prohibiting the new trust from having provisions that would have prevented the original trust from qualifying for the tax deduction or exclusion. Thus, in theory, a trust that qualified for a marital or charitable deduction could be decanted into a new trust that does not reduce the income paid to any beneficiary, but grants a power of appointment to a beneficiary of the new trust. Depending on the scope of the power of appointment granted, this in turn could prevent the new trust from qualifying for the same tax deduction or exclusion.

DIRECTED TRUSTS

The amendments clarify the laws related to directed trusts, changing the term “excluded fiduciary” to “*directed fiduciary*” and defining the term “*directing trust adviser*.” Under the amended statute, the directed fiduciary is excluded from liability for following the directions of a directing trust adviser.

The term “directed fiduciary” has been added to replace “excluded fiduciary” as it better reflects the fact that the trustee is acting at the direction of another party. The amendment clarifies that a fiduciary is a directed fiduciary with respect to any action that the fiduciary:

- Has no power to take under the terms of the governing instrument;
- Is mandated to take by the governing instrument and for which the fiduciary has no discretion to act otherwise; and
- Is directed to take or prohibited from taking by a directing trust adviser.

The statute already provided for the roles of investment trust adviser, distribution trust adviser, and trust protector. The amendment adds the term “*directing trust adviser*” to mean a trust adviser (which the statute defines to include a distribution trust adviser or investment trust adviser), trust protector *or other person designated in the trust instrument who has the authority to give directives that must be followed by the fiduciary*. This last category is new and expands the role of the party directing the fiduciary to enable a trustee to be directed on various items, rather than being limited to direction by the three adviser roles mentioned above. The statute provides that a party is not a directing trust adviser if they are only giving recommendations, counsel or advice that the fiduciary is not required to follow under the terms of the trust instrument.

These revisions make it clear that a directed fiduciary is not liable for any loss that results from the directed fiduciary following the directions of the directing trust adviser. The statute continues to provide that the directed fiduciary is not liable for any loss if the directing trust adviser does not consent to any recommendation made by that directed fiduciary. However, the amendments add that the directed fiduciary is not liable for not acting after making a recommendation if the recommendation was contingent upon a condition that was not met or satisfied.

The statute continues to provide that the directed fiduciary has no duty to review or make any recommendations or evaluation with respect to any *investments* made by the directing trust adviser. Note, however, that this section does not discuss any obligation of a directed fiduciary to review actions or directions from a directing trust adviser other than investments.

NEVADA JURISDICTION AND LAW OF NEVADA GOVERNING THE VALIDITY AND CONSTRUCTION OF A TRUST

There has been case law outside of Nevada that called into question whether a trust that moves to a new state can be subject to the jurisdiction and governing law of the new state. The amendments to the Nevada statute specifically address the following:

- When Nevada law governs the validity and construction of a trust;
- When the Nevada court can assume jurisdiction over a trust; and
- What is required to constitute nexus with Nevada.

Nevada Law Governing the Validity and Construction of a Trust

Nevada law will govern the validity and construction of a trust if either of the following exists:

- The instrument so provides a person with the power under the trust instrument to designate the governing law of the trust and designates that Nevada law applies; or
- The trust instrument does not specify the governing law, no one with power under the instrument to designate the governing law has made any designation, and the settlor or trustee of the trust was a resident of Nevada at the time the trust was created or at the time the trust became irrevocable.

When the Court May Assume Jurisdiction Over the Trust

If the Nevada district court determines that there is a clear and sufficient nexus between a trust and Nevada, the court may assume jurisdiction during a proceeding *unless any of the following exists*:

- Another court has properly assumed jurisdiction in accordance with the laws of that jurisdiction;
- The trust instrument expressly provides that the situs of the trust is outside of Nevada or that a court of a jurisdiction other than Nevada has jurisdiction over the trust; or
- A situs or jurisdiction other than Nevada has been designated for the trust, by a person who held the power to make such a designation under the trust instrument.

If a court of a jurisdiction outside Nevada has jurisdiction over a trust and grants an order authorizing a transfer of jurisdiction over the trust to Nevada, the district court has the power to assume jurisdiction over the trust and to otherwise supervise the administration of the trust, assuming there is sufficient nexus as defined below.

The statute was also amended to provide that if the Nevada court has *in rem* jurisdiction over a trust during a proceeding concerning that trust, it shall also be deemed to have personal jurisdiction over any person involved in that proceeding.

Nexus Defined

There is a clear and sufficient nexus between a trust and Nevada if the trust owns real property in Nevada. In addition, if the trust owns personal property, wherever situated, there is clear and sufficient nexus with Nevada if the trustee or co-trustee is any of the following:

- A resident of Nevada;
- Incorporated or authorized or licensed under Nevada law to do business in Nevada;
- A family trust company as defined under Nevada law; or
- A national association having an office in Nevada.

Furthermore, sufficient nexus exists if one or more beneficiaries of the trust reside in Nevada, or at least part of the administration of the trust occurs in Nevada. However, for these two rules to apply with respect to a co-trustee, the co-trustee must have the authority to maintain records for the trust and to prepare income tax returns for the trust, even if such authority may also be exercised by another co-trustee.

MISCELLANEOUS CHANGES

- A definition of “trust instrument” has been added to include a will, trust agreement, declaration, court order or *any other instrument that creates, defines or modifies the duties and powers of a trustee or modifies the terms of a trust.*
- Trustees now have the authority to combine two or more trusts or to divide a trust into two or more separate trusts as long as the actions do not impair the rights of any beneficiary, substantially affect the accomplishment of the trust’s purposes or violate the rule against perpetuities. Trustees must send a Notice of Proposed Action before combining or dividing trusts. The notice must include information on expected tax consequences, if any, of the proposed combination or division.
- “Public Benefit Trusts” are now recognized as valid trusts in Nevada. These non-charitable trusts do not have identifiable beneficiaries, but are created for specifically declared religious, scientific, literary, educational, community development, personal improvement or philanthropic purposes. Distributions may only be applied for the trust’s intended use and the trust must provide a benefit to the general public or to one or more classes/groups of persons at the trustee’s discretion. No trustee can benefit from the trust, except for the payment of reasonable compensation and reimbursement of expenses. In addition, the purpose of the trust must not be illegal or against public policy.
 - Public benefit trusts must appoint a person to enforce the provisions of the trust. If the designated “enforcer” is no longer willing or able to serve, then the Attorney General, the district attorney or a person appointed by the court in the county where the trust is domiciled may enforce the terms of the trust. If no trustee is designated, willing or able to act, the court shall name one or more trustees and may also make other orders and determinations to carry out the interest of the settlor and the purposes of the trust. Upon termination, any assets of the trust, including any undistributed income must be distributed in accordance with the terms of the trust or, in the absence of such terms, to the estate of the settlor.
- Clauses in a trust or will requiring the arbitration of disputes other than disputes regarding the validity of all or part of a will or trust are now enforceable. Unless otherwise specified in the will or trust, an arbitration clause shall be presumed to require binding arbitration under the arbitration statutes of Nevada.
- Nevada’s prudent investor rule has been amended to provide that the trustee is not liable for not diversifying the trust assets if the trustee determined in good faith not to diversify the assets.

CONCLUSION

The 2015 amendments reflect several improvements to what are already flexible and useful trust laws. Two examples include additional methods to modify a trust, and a roadmap as to when Nevada law applies to a trust that is moved to Nevada from another state. These flexible and modern laws combined with a court system in Nevada that is readily available to hear trust matters, make Nevada a favorable state in which to create a trust.

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