SIDLEY AUSTIN LLP
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TENNESSEE[1]

State Decanting Summary[2]

STATUTORY HISTORY	
Statutory citation	TENN. CODE ANN. § 35-15-816(b)(27)
Effective Date	7/01/04
Amendment Date(s)	7/01/13
ABILITY TO DECANT	
1. Discretionary distribution authority required to decant?	Yes, authority to invade principal[3]
2. Limitation on trustee who may decant?	No
CHANGES PERMITTED	
3. May new trust eliminate beneficiary's mandatory distribution rights?	No, as to income[4]
4. May new trust eliminate beneficiary's withdrawal rights?	Silent[5]
5. Must new and old trust beneficiaries be identical?	No[6]
6. Are beneficiaries of new trust limited to current beneficiaries of old trust?	Yes[7]
7. May remainder beneficiaries' interests be accelerated?	Silent
8. New and old trust require same distribution standard?	No[8]
9. May trustee grant a power of appointment in new trust?	Yes[9]
10. Must new trust grant identical power of appointment as old trust?	No[10]
11. Supplemental needs trust exception?	No
TAX RESTRICTIONS	
12. Marital deduction savings provision?	Yes[11]
13. Charitable deduction savings provision?	Yes[12]
14. Beneficiary/trustee savings provision?	No
15. Other tax savings provisions?	2503(b)[13]; 2642(c)[14]; Sub S[15]
16. Non-grantor trust to grantor trust conversion permitted?	Silent[16]
OTHER RESTRICTIONS	
17. Rule against perpetuities savings provision?	Yes[17]
18. May trustee increase trustee commission?	Silent
19. Other restrictions	
NOTICE, CONSENT & APPROVAL	
20. Notice to interested parties required prior to decanting?	No
21. Is decanting prohibited if a beneficiary objects?	Silent[18]
22. Court approval required to decant?	No
FIDUCIARY DUTIES	
23. Provision re: purposes for exercise or explicit fiduciary duty?	No
24. Provision that trustee has no duty to consider decanting?	Implied[19]
25. Standard of review?	No
TRUSTS SUBJECT TO STATUTE	
26. Provision on trusts subject to statute?	Yes[20]
MISCELLANEOUS	
27. Other unique considerations?	No

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TENNESSEE STATUTE
TENN. CODE ANN. § 35-15-816(b)(27)

(27) Unless the terms of the instrument expressly provide otherwise:

(A) A trustee who has authority, under the terms of a testamentary instrument or irrevocable inter vivos trust agreement, to invade the principal of a trust to make distributions to, or for the benefit of, one or more proper objects of the exercise of the power, may instead exercise such authority by appointing all or part of the principal of the trust in favor of a trustee of a trust under an instrument other than that under which the power to invade is created or under the same instrument; provided, however, that the exercise of such authority:

(i) Does not reduce any fixed income interest of any income beneficiary of the trust; and

(ii) Is in favor of the proper objects of the exercise of the power;

(B) The exercise of the power to invade the principal of the trust under subdivision (b)(27)(A) shall be by an instrument in writing, signed and acknowledged by the trustee and filed with the records of the trust;

(C) The exercise of the power to invade principal of the trust under subdivision (b)(27)(A) shall not extend the permissible period of the rule against perpetuities that applies to the trust; and

(D) The provisions of this section shall not be construed to abridge the right of any trustee who has a power of invasion to appoint property in further trust that arises under any other statute or under common law.

(E) The exercise of the power to appoint principal under subdivision (b)(27)(A) shall be considered an exercise of a power of appointment, other than a power to appoint to the trustee, the trustee's creditors, the trustee's estate, or the creditors of the trustee's estate;

(F) The second trust:

(i) May confer a power of appointment upon a beneficiary of the original trust to whom or for the benefit of whom the trustee has the power to distribute principal of the original trust;

(ii) The permissible appointees of the power of appointment conferred upon a beneficiary may include persons who are not beneficiaries of the original or second trust; and

(iii) The power of appointment conferred upon a beneficiary must preclude any exercise that would extend the permissible period of the rule against perpetuities that applies to the trust;

(G) If any contribution to the original trust qualified for the annual exclusion under § 2503(b) of the Internal Revenue Code, the marital deduction under §§ 2056(a) or 2523(a) of the Internal Revenue Code, or the charitable deduction under §§ 170(a), 642(c), 2055(a) or 2522(a) of the Internal Revenue Code, is a direct skip qualifying for treatment under § 2642(c) of the Internal Revenue Code, or qualified for any other specific tax benefit that would be lost by the existence of the authorized trustee's authority under subdivision (b)(27)(A) for income, gift, estate, or generation-skipping transfer tax purposes under the Internal Revenue Code, then the authorized trustee shall not have the power to distribute the principal of a trust pursuant to subdivision (b)(27)(A) in a manner that would prevent the contribution to the original trust from qualifying for or would reduce the exclusion, deduction, or other tax benefit that was originally claimed with respect to that contribution;

(H) During any period when the original trust owns stock in a subchapter S corporation as defined in § 1361(a)(1) of the Internal Revenue Code, an authorized trustee shall not exercise a power authorized by subdivision (b)(27)(A) to distribute part or all of the stock of the S corporation to a second trust that is not a permitted shareholder under § 1361(c)(2) of the Internal Revenue Code;

(I) This section applies to any trust that is administered in this state; and

(J) For purposes of this section, the term "original trust" refers to the trust from which principal is being distributed and the phrase "second trust" refers to the trust to which assets are being distributed from the original trust.

2013 COMMENTS TO OFFICIAL TEXT

Subdivision (b)(27) authorizes a trustee who possesses a discretionary power to distribute principal outright to trust beneficiaries to exercise that power in further trust. This power, which is commonly referred to as a "decanting" power, is considered a limited power of appointment.

The power may be exercised with respect to any trust that is administered in Tennessee.

In order to exercise the power, the Trustee is required to sign a written notarized instrument that is maintained with the records of the original trust as well as the second trust. The Trustee does not have to obtain consent of the beneficiaries or a Court in order to exercise the power.

The power may only be exercised in favor of the proper objects of the exercise of the discretionary power. This means that new beneficiaries cannot be added to the second trust, though the second trust does not have to benefit all of the beneficiaries of the original trust. The second trust may grant a power of appointment to a beneficiary of the original trust, which power may be exercisable in favor of beneficiaries who were not beneficiaries of the original trust.

There are several limitations on the exercise of the power that prevent loss of tax benefits:

(1) the permissible rule of perpetuities applicable to the original trust may not be extended either by exercise of the decanting power or by the exercise of a power of appointment granted to a beneficiary in the second trust;

(2) if the original trust qualified for the federal gift tax annual exclusion under Code Section 2503(b), the federal gift or estate tax marital or charitable deduction, favorable generation-skipping transfer treatment under Code Section 2642(c), or any other specific tax benefit, the decanting power may not be exercised in a manner that causes the loss of the tax benefit; and

(3) if the original trust owns stock in a Subchapter S corporation, the power may not be exercised in favor of a second trust that is not a qualified shareholder in a Subchapter S corporation.

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[1] Reviewed by Bryan Howard 8/10/13.

[2] ***Circular 230 Disclosure***. To comply with certain Treasury regulations, we inform you that these materials are not intended or written to be used, and cannot be used, by any person for the purpose of avoiding U.S. federal tax penalties that may be imposed on such person, and each taxpayer should seek advice based on the taxpayer's particular circumstances from an independent tax advisor. These materials do not constitute, and should not be treated as legal advice. Although every effort has been made to assure the accuracy of these materials, the author

and Sidley Austin LLP do not assume responsibility for any individual's reliance on these materials. The reader should independently verify all statements made in these materials and should independently determine both the tax and nontax consequences of any particular transaction before recommending or implementing that transaction.

[3] § 35-15-816(b)(27); s*ee* Comment to § 35-15-816 ("Subdivision (b)(27) authorizes a trustee who possesses a discretionary power to distribute principal outright to trust beneficiaries to exercise that power in further trust.").

[4] § 35-15-816(b)(27)(A)(i).

[5] The author understands that Tennessee attorneys construe the statute to permit the elimination of a withdrawal right over principal but not income.

[6] A trustee may decant, but the exercise of the trustee's authority must be "in favor of the proper objects of the exercise of the power[.]" § 35-15-816(b)(27)(A)(ii). This implies that the new trust must be in favor of one or more of the beneficiaries of the old trust, and the author understands this is how Tennessee attorneys construe the statute.

[7] § 35-15-816(b)(27)(A). The author understands that Tennessee attorneys construe the statute to limit the beneficiaries of the new trust to current beneficiaries of the old trust.

[8] § 35-15-816(b)(27)(A). The author understands that Tennessee attorneys construe the statute as not requiring the same distribution standard.

[9] § 35-15-816(b)(27)(F).

[10] § 35-15-816(b)(27)(F).

[11] § 35-15-816(b)(27)(G).

[12] § 35-15-816(b)(27)(G).

[13] § 35-15-816(b)(27)(G).

[14] § 35-15-816(b)(27)(G).

[15] § 35-15-816(b)(27)(H).

[16] The author understands that Tennessee attorneys construe the statute as permitting a non-grantor trust to grantor trust conversion.

[17] "The exercise of the power to invade principal of the trust under subdivision (b)(27)(A) shall not extend the permissible period of the rule against perpetuities that applies to the trust[.]" § 35-15-816(b)(27)(C). In addition, any power of appointment granted may not extend the rule against perpetuities period. § 35-15-816(b)(27)(F)(iii).

[18] The author understands that Tennessee attorneys construe the statute as not permitting decanting if a beneficiary objects.

[19] "The fact that the trustee has a power does not imply a duty that the power must be exercised." Comment to § 35-15-816.

[20] The statute applies to trusts administered in this state. § 35-15-816(b)(27)(I).