

Why Consider Tennessee for your Trust?

For almost 20 years, the Tennessee State Legislature has increasingly modernized trust laws for families and individuals to consider the “The Volunteer State” as a sustainable home for their trusts. So, what makes Tennessee such a compelling solution for trusts, and why should families consider this jurisdiction for their multigenerational wealth planning for years to come?

Flexibility and Control

One of the most important benefits for trusts moving to or being created in Tennessee is the directed trust statute. Tennessee recognizes directed trusts, which give settlors (those creating a trust) more flexibility and control in defining who will take responsibility for each function a fiduciary must handle to carry out the purpose of the trust. As an example, in a directed trust, a “directed investment advisor” or “trust director” may have the exclusive duty to invest the trust’s assets while the trustee is responsible for all other aspects of administering the trust. The trustee of a directed trust is not responsible for the decisions, actions, or inaction of the party having authority to direct the trustee. Because of this, the trustee of a directed trust faces less exposure and liability because the trustee must follow the direction of whomever the trust document appoints to direct the trustee’s actions. Another benefit of a directed trust is that multiple individuals can serve in directed advisor capacity while hiring outside advisors depending on expertise, portfolio management and investment advisory needs.

Historically, the Tennessee Trust Code permitted directed trusts to be created through one of three ways: per the terms of the trust agreement, an agreement of the qualified beneficiaries, or through a court order. Updated legislation now includes another method for the creation of a directed trust with even greater flexibility. Now, the person(s) with the power to appoint successor trustees can appoint multiple successor trustees and the person(s) with the ability to remove or replace a trustee can appoint an additional trustee to serve with a currently serving trustee.¹ This power to appoint successor trustees and additional trustees includes the power to allocate various trustee powers, including the power to direct or prevent certain actions of the trustees, exclusively to one or more of the trustees serving from time to time.

This arrangement may be particularly attractive where the settlor owns a closely held family business and wants to ensure that the business remains in the family trust for years to come—or that control of the business stays in the hands of specific individuals other than the trustee.

Protection of Trust Assets

Traditionally, the only way an individual could create an irrevocable trust and retain some benefits that could not be reached by creditors was to create an offshore trust. As an alternative, Tennessee now allows an individual to transfer assets to an irrevocable Tennessee trust. Under the terms of this trust, a settlor may continue to benefit from the assets, in the trustee’s discretion, while potentially protecting assets from most creditors.

The adoption of the Tennessee Investment Services Act of 2007 represented a significant change to Tennessee common law, which generally prohibited an individual from protecting assets from creditor claims by creating a trust for his or her own benefit. Tennessee’s statute allows individuals to create self-settled, irrevocable trusts. For a trust to qualify as a Tennessee Investment Services Trust (“TIST,” a/k/a TN domestic asset protection trusts), the trust must meet the following requirements: 1) the trust must expressly incorporate Tennessee law for purposes of validity, construction and administration, 2) the trust must be irrevocable, 3) the trust must contain a spendthrift clause, 4) the trust must have a qualified third party trustee who is a Tennessee resident or corporate trustee licensed under Tennessee law and must perform certain duties (i.e. custody of assets, tax preparation, trust administration), and 5) the Settlor cannot be the trustee.² As a result of the legislation changes that went into effect July 1, 2021, if a TIST is properly funded, it will be protected from the claims of most creditors after 18 months.

Additionally, Tennessee strictly enforces spendthrift trusts— trusts specifically created to protect beneficiaries from their own imprudence or incapacity—so that, creditors of beneficiaries cannot reach the trust assets. Tennessee trust law may provide asset and creditor protection opportunities that other states do not, making it appealing to clients with considerable wealth and those for whom personal liability is a concern.

Tax Advantages

A key objective in establishing a trust is to minimize the impact of taxes on trust assets. For those individuals who live in a state that imposes a tax on trust income and capital gains, Tennessee may be an advantageous jurisdiction for creating an irrevocable trust. Properly structured, a Tennessee trust can be administered free of Tennessee income and capital gains taxes. The trust will still be subject to federal income tax, and a beneficiary who receives a distribution from a Tennessee trust may owe income tax to the state in which he or she resides, but there is no state tax at the trust level on capital gains or accumulated income.³

Residents of states that impose income tax on trust income may benefit from moving the situs of an existing trust to Tennessee. Tax savings can be significant with Tennessee's favorable tax laws and can allow for greater growth potential of the trust assets over time.

Careful planning with your tax and trust and estate advisors should be done in consideration of the tax consequences. Nevertheless, in Tennessee, many generations of beneficiaries can enjoy the benefit of family assets while limiting the associated burden of state income tax.

Ease of Trust Administration

Tennessee's modern trust laws promote the efficient administration of trusts. Through concepts like virtual representation, non-judicial settlement agreements ("NJSAs"), trustee decanting, and trustee modification, trustees can move old trusts to Tennessee, administer trusts prudently, and modify a trust's provisions when circumstances are warranted, without having to seek court involvement which may be time consuming and expensive. Using NJSAs, trustees are afforded a flexible tool to assist in administering trusts. NJSAs are binding agreements between trustees and beneficiaries that allow those parties to compromise on a variety of issues relating to trust administration, distribution, termination, and procedural issues.⁴

Tennessee trust law allows decanting, a process by which a trustee creates a new trust and "pours" the assets from the old trust to the new trust. A trustee may exercise the power to decant for the purpose of improving the administrative provisions governing the initial trust. Through this process, older trusts can be updated to provide greater flexibility regarding investments or clarify ambiguous provisions related to distributions and trustee succession. The recently enacted legislation also provides for two significant enhancements. First, so long as the settlor is deceased, a decanting power may be exercised in a manner to allow remainder beneficiaries to become current beneficiaries of the recipient trust. Due to increased lifespans, decanting for this purpose could be appealing to an elderly beneficiary who wishes to witness their descendants enjoy trust assets during their lifetime. The second enhancement is the ability to eliminate a beneficiary's income interest, where such elimination will not give rise to adverse tax consequences. This power could be immensely helpful for families dealing with an income beneficiary who is a spendthrift or potentially dealing with substance abuse issues, where accumulation might be in the beneficiary's best interests.⁵

Multi-Generational Advantages

Unlike numerous states that limit the duration of a trust, Tennessee allows most trusts to continue on for generations. Trusts may, therefore, benefit succeeding generations of beneficiaries without incurring additional federal gift, estate, or generation skipping taxes (collectively, "transfer taxes") that can deplete family wealth. Trusts created under Tennessee law can last for up to 360 years.⁶ Under most state laws, a trust is required to terminate after two or three generations. The benefit of a trust being allowed to continue for 360 years is two-fold. First, the assets within the trust will remain protected from the beneficiaries' creditors while remaining in the trust. This benefit provides creditor protection of the trust assets for 360 years. Second, if properly prepared, a perpetual trust (also called a dynasty trust) can avoid paying estate, gift, or generation-skipping transfer taxes (after the initial funding) for up to 360 years. A wealthy family or individual will be able to pass a large sum of assets to multiple generations while providing creditor protection and avoiding transfer taxes on such assets.

Now, thanks to updated legislation, this extended timeframe can be even more widespread. Historically, if a trust were created while there were not any specific beneficiaries, it could only last for 90 years. Under Tennessee law, even if the beneficiaries are not immediately identifiable, the trust can continue for the full 360 years. This means that a settlor can create a trust for the benefit of unborn/unconceived children or grandchildren, fund it when the federal gift/estate exemptions are higher and before the exemption reduces (like it's scheduled to in 2026), and the trust can continue for 360 years instead of only 90.

Another advantage that Tennessee offers to multi-generational families is “Silent Trusts.” People often worry that the development of their children’s or grandchildren’s work ethic will suffer if he or she knows of a pending inheritance. This fear can be a real disincentive to settlors who might otherwise wish to establish trusts for family members, because their state law requires trustees to provide beneficiaries with detailed information about the trust assets. The settlor may be more comfortable establishing a “silent trust” in Tennessee. With a silent trust, the settlor can provide that the trustee is not obliged (or is even forbidden) to notify the beneficiaries of the existence of the trust, let alone its value or terms. Most states do not have statutes authorizing silent trusts, and in fact require that significant disclosures be made to beneficiaries at regular intervals. States that authorize silent trusts, on the other hand, may enable the settlor or trustees to decide what information will be provided, and when.⁷

Conclusion

The modernization of Tennessee’s trust law that began in 2004 has led to a statutory framework that includes provisions favorable to trust settlors, beneficiaries, and fiduciaries.⁸ With these advantageous provisions written into Tennessee’s laws, it is no surprise that individuals looking to establish new trusts, or “transition” a trust to a jurisdiction with friendly trust laws, are considering Tennessee. Regardless of their residency, an individual can create a domestic asset protection trust for their benefit, which would be protected from creditors; or a married couple can create a trust for their benefit, which would be protected from the creditors of one spouse. These assets could remain in trust for 360 years, providing creditor protection to descendants while avoiding transfer taxes at the death of future generations.

The recently passed updates to the Tennessee Uniform Trust Code include several additional revisions not discussed above, including electronic execution of nonjudicial settlement and modification agreements, and enhanced creditor protection for beneficiaries. These enhancements, as well as those discussed above, will enable Tennessee to maintain, if not further advance, its status as a preeminent jurisdiction for trust administration.

To learn more, please visit www.wealthspiretrust.com.

Sources:

1. T.C.A. Section 35-15-710
2. T.C.A. Section 35-16-101 to 112
3. T.C.A. Section 67-2-110(b)
4. T.C.A. Section 35-15-111
5. T.C.A. Section 35-15-816(b)(27)
6. T.C.A. Section 35-15-409(1)
7. T.C.A. Section 35-15-813(e)
8. T.C.A. Section 35-15-101-et seq.

Wealthspire Trust LLC is a non-depository Tennessee trust company and an affiliate of Wealthspire Advisors LLC, an independent registered investment advisor and subsidiary company of NFP Corp. Securities and other non-deposit investment products are not insured by the FDIC; are not deposits or other obligations of or guaranteed by Wealthspire Trust LLC, or any of its affiliates; and are subject to investment risks, including possible loss of principal invested. Wealthspire Trust LLC, and its affiliates do not provide tax or legal advice. Please consult with your tax and legal advisors regarding your specific situation. To the maximum extent provided by law, Wealthspire Trust LLC disclaims any and all liability in the event any information, commentary, analysis, opinions, advice and/or recommendations prove to be inaccurate, incomplete or unreliable or result in any investment or other loss. Eligibility for particular investment options or services is subject to final Wealthspire Trust LLC, determination, and acceptance.