Legislative Analysis

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REVISE RULE AGAINST PERPETUITIES

Senate Bills 22 & 23 as passed by the Senate
Sponsor: Sen. Tonya Schuitmaker
House Committee: Judiciary
Senate Committee: Judiciary

First Analysis (2-21-11)

BRIEF SUMMARY: Senate Bill 22 would revise an exception to provisions of the Uniform Statutory Rule Against Perpetuities for property subject to the Personal Property Trust Perpetuities Act. Senate Bill 23 would amend the Personal Property Trust Perpetuities Act to make the act inapplicable to a trust to the extent it is a "special appointee trust."

FISCAL IMPACT: There would be little or no fiscal impact on state or local government.

THE APPARENT PROBLEM:

Two bills enacted in 2008 exempted personal property from the rule against perpetuities under certain conditions. Public Act 148 of 2008 (enrolled House Bill 5909) created the Personal Property Trust Perpetuities Act and Public Act 149 of 2008 (enrolled House Bill 4602) amended the Uniform Statutory Rule Against Perpetuities.

In brief, the rule against perpetuities prevents people from tying up assets in trusts that can go on forever. A perpetual trust (or dynasty trust, as it is called) is a technique that allows the creator of the trust to pass wealth from generation to generation without incurring transfer taxes, such as the federal generation-skipping transfer tax. The changes made by Public Acts 148 and 149 of 2008 allowed for the creation of perpetual trusts involving ***personal property***. Placing ***real property*** in perpetual trusts continues to be prohibited.

Apparently, under provisions of Public Act 148 of 2008, the exercise of a nongeneral power of appointment over a trust that is "grandfathered" under certain federal effective-date regulations (meant to prevent those trusts from being subject to the federal generation-skipping tax) can still trigger the generation-skipping tax under certain circumstances. Legislation has been offered to make further amendments in this area of the law.

THE CONTENT OF THE BILLS:

<u>Senate Bill 22</u> would amend the Uniform Statutory Rule Against Perpetuities (MCL 554.75). Currently, the act does not apply to an interest <u>in</u>, or power of appointment <u>over</u>, <u>personal property held in a trust that is either revocable on or created after the effective date of</u> the 2008 Personal Property Trust Perpetuities Act. The bill would delete the underlined portions to read instead, that except as provided in the act, the act would

not apply to an interest or power of appointment to which the Personal Property Trust Perpetuities Act applied. The bill would also specify that Section 2 of the act would apply to an interest or power of appointment to which the Personal Property Trust Perpetuities Act applied under certain listed circumstances.

Senate Bill 23 would amend the Personal Property Trust Perpetuities Act (MCL 554.94). Currently, the act applies only to a nonvested interest in, or power of appointment over, property held in a trust that is either revocable on May 28, 2008, or created after that date (the effective date of Public Act 148 of 2008). The bill would add that this provision would apply only to the extent that the trust was ***not a special appointee trust***. For purposes of this provision, a trust would be a special appointee trust to the extent it includes assets that were held in a trust that was irrevocable on September 25, 1985, if both of the following apply to the assets:

- The assets have continuously been held in trust since September 25, 1985.
- The assets have not become subject to a general power of appointment since September 25, 1985.

BACKGROUND INFORMATION:

Senate Bills 22 and 23 are reintroductions of House Bills 5009 and 5010 of the 2009-2010 Legislative Session. Those bills addressed the issue described above by amending some provisions of Public Act 148 and 149 so that the Personal Property Trust Perpetuities Act would not apply to certain trusts. The Senate did not act on the bills.

(For more information on the common law rule against perpetuities, the Uniform Statutory Rule Against Perpetuities, and a discussion of the impact of eliminating the rule against perpetuities, see the House Fiscal Agency analysis on House Bills 6365 and 6366 of the 2005-2006 legislative session dated 11-28-06.)

The following information was derived from the Senate Fiscal Agency's analysis of Senate Bills 22 and 23 dated 1-27-11:

Rule Against Perpetuities. The common law rule against perpetuities was designed to restrict the power of a landowner to tie up property in long-term or perpetual family trusts. (Under the common law rule, a nonvested property interest is invalid unless it must vest, if at all, within 21 years, plus the period of gestation, after some life or lives in being at the time the interest is created.) Because the common law rule could invalidate some property transfers that otherwise would be considered reasonable, Michigan enacted the Uniform Statutory Rule Against Perpetuities in 1988. Under this law, an interest that would be valid under the common law rule remains valid, but an interest that would violate the common law rule is invalid only if it does not actually vest or terminate within 90 years after its creation.

In order to allow people to establish dynasty trusts for personal property in Michigan, the Personal Property Trust Perpetuities Act was enacted in 2008 and the statutory rule was eliminated with respect to property subject to the act.

Generation-Skipping Transfer Tax. The federal GST tax applies to outright gifts and transfers in trust to grandchildren and others deemed to be two or more generations below that of the person making the transfer. The present rate of the GST tax is 35 percent of the value of the assets. The law also allows a lifetime exemption for each individual making a transfer or transfers. The amount of the exemption is presently $5.0 million. If Congress does not act, the rate will rise to 55 percent and the exemption will drop to $1.0 million after 2012.

As noted above, the GST tax does not apply to a trust that was irrevocable and in existence on September 25, 1985, to the extent the trust's assets are not added to after that date. Under U.S. Treasury regulations, the exercise of a power of appointment (other than a general power of appointment) will not be considered an addition to the trust, and will not subject the assets to the GST tax, if it is exercised in a manner that will not postpone the vesting of an interest beyond what amounts to the 21-year common law rule against perpetuities or the 90-year uniform statutory rule.

ARGUMENTS:

For:

The rule against perpetuities (RAP) is a complicated area of law. Generally speaking, the purpose of dynasty trusts is to enable wealthy individuals to pass assets to future descendants far into the future without those assets being subject to the federal Generation Skipping Transfer (GST) tax. Even though Michigan only repealed the RAP as it relates to personal property, the legislation failed to anticipate every scenario. As a result, an inexperienced or unsophisticated estate planner may fail to recognize the potential pitfalls that the federal GST tax presents to future generations and thus inadvertently expose the trust to the GST tax. The amendments offered in Senate Bills 22 and 23 are intended to prevent this from occurring by preventing the appointment of assets from so called "GST grandfathered trusts" into trusts allowed under Public Act 148 of 2008 in such a way as to trigger the GST tax. The bills only affect personal property held in trust and do not affect the current ban on perpetual trusts for real property.

POSITIONS:

A representative of Dickinson Wright, PLLC testified in support of the bills. (2-17-11)

The Michigan Bankers Association indicated support for the bills. (2-17-11)

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■ This analysis was prepared by nonpartisan House staff for use by House members in their deliberations, and does not constitute an official statement of legislative intent.