

Selecting a Trust Situs

What Should a Trustee Consider?

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Choosing a trust situs involves several considerations, both at the inception of a trust and during its ongoing administration. This article reviews situs considerations, including a trustee's duty to consider a transfer of situs and options for completing a transfer.

With Nevada and Wyoming in close proximity to Colorado, the question often arises whether trustees should move a trust's principal place of administration (or situs) to one of these states for more favorable asset protection or income tax treatment. In recent years, Colorado has provided clarity and flexibility in trust administration through various legislation, including the Colorado Uniform Directed Trust Act (2014), the Colorado Uniform Trust Decanting Act (2016), and most recently the Colorado Uniform Trust Code (CUTC) (2019 and 2021).¹ These laws provide statutory guidance for trustees and facilitate trust administration, making Colorado a more attractive trust situs than many other states.

A number of factors should be considered when choosing a trust situs, both when forming a

trust and during its ongoing administration. This article discusses relevant considerations when evaluating trust situs, including circumstances in which trustees may have a duty to maintain a situs in a certain state or transfer situs to another state.

Initial Situs Selection

The settlor's location is often chosen as the initial situs, especially for testamentary trusts created in wills and revocable trusts that become irrevocable upon the settlor's death. But other relevant factors may include preferential state law; state income tax; and locations of the trustee, trust assets, and beneficiaries.²

A settlor's existing relationship with a trustee may significantly impact the settlor's situs choice. In addition, the settlor and/or the trustee may have professional advisors, including

attorneys and accountants, who will serve in connection with the trust administration. Having a trusted advisory team in place can greatly increase the settlor's comfort with implementing the trust plan and promote efficiency in the trust administration. Trusted advisors should ensure that the settlor considers all relevant situs options and makes a decision based on the key factors that the settlor considers important.

Trustee's Ongoing Duty to Consider Situs

Under the CUTC, "[a] trustee is under a continuing duty to administer the trust at a place appropriate to its purposes, its administration, and the interests of the beneficiaries."³ Trustees should take the following steps to meet this mandate.

First, a trustee must consider the trust's purposes, which requires analyzing the settlor's intent.⁴ For example, the settlor may have created a special needs trust to provide assistance to a beneficiary without affecting the beneficiary's eligibility for government benefits. In this circumstance, it may be best to have the trust administered in the same state where the beneficiary resides with a trustee who understands that state's government assistance programs. Or the settlor may have created a directed trustee arrangement to separate the trustee's investment and administrative functions.⁵ In this case, the trustee would need to consider whether this arrangement could be maintained if the trust's situs were transferred to a new state. In addition, a trust may have been created under a specific state's statutory scheme, such as one allowing a domestic asset protection trust (DAPT), which requires the trust to remain in that jurisdiction.⁶

Second, the trustee should consider whether the situs is appropriate for the trust's administration.⁷ This inquiry may involve practical and logistical issues. For example, if the sole beneficiary of the trust lives in Colorado, it might not make sense to administer the trust in California. Likewise, if the trust's sole asset is a ranch in Colorado, it might not be efficient to administer the trust in Delaware. While it is possible to administer a trust under such circumstances, the efficiency of administration may suffer.

Third, the trustee should consider the beneficiaries' interests.⁸ This refers to the beneficial interests provided in the trust's terms.⁹ For example, a trustee might consider moving the trust to a state that does not impose an income tax to save that expense, as discussed below. In addition, it could be beneficial to move the trust to a state with strong asset protection laws to protect beneficiaries from divorce and creditors.

Unless substantial changes occur after the trust's creation, the trustee likely has no affirmative duty to transfer the trust situs to a different state. "Ordinarily, absent a substantial change or circumstances, the trustee may assume that the original place of administration is also the appropriate place of administration."¹⁰ However, as discussed above, if circumstances

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have changed or there is a compelling reason to transfer situs, the trustee should likely consider a transfer. "A trustee may have a duty to move the situs of the trust if to do so would substantially further the interest of the beneficiaries, would not be in contravention of the terms of the trust, and would be both possible and practical."¹¹

When evaluating whether a trust situs should be transferred to another state, it is important to understand the laws of both states.¹² For example, if "[t]he state in which the trust was established . . . might attempt to continue to tax the income of the trust even after all the trustees and all the beneficiaries had moved elsewhere,"¹³ there is no point in moving the trust for state income tax purposes.

After a trust is formed, situs is typically where the trustee is located.¹⁴ Accordingly, a situs transfer may require the trustee's resignation.

If the trust beneficiaries wish to change the situs and there is a compelling reason to do so, they may be able to remove the trustee if the trustee refuses to resign. A trustee's change to the place of administration or the relocation of beneficiaries or other developments "may result in costs or geographic inconvenience serious enough to justify removal of a trustee."¹⁵ Similarly, if a trustee relocates and situs should stay in the original state, that trustee may have a duty to resign to allow a new trustee to continue to administer the trust.

Duty to Inform and Report

When considering a situs transfer, one issue that varies by state is the trustee's duty to provide information to the beneficiaries. In Colorado, this duty is codified in the CUTC, and only certain portions of the duty can be changed by the trust's terms.¹⁶ The mandatory duties in Colorado include the duty to provide notice of the existence of an irrevocable trust, the trustee's identity, and the right to request trustee's reports to current or permissible distributees of such trust at any age, or to other qualified beneficiaries of such trust who have attained age 25.¹⁷ In addition, the trustee must respond to a qualified beneficiary's request for reports and other information reasonably related to the trust.¹⁸ A trustee's report includes a list of the trust's assets, liabilities, receipts, and disbursements; trustee compensation; and a list of market values, if feasible.¹⁹

Other states may require more or less disclosure and may have a different definition of the type of beneficiary that is entitled to such information. Accordingly, a trustee should consider whether transfer to a new situs that requires additional disclosure may be contrary to the settlor's intent.

State Income Tax

Trustees should consider state income tax and related factors when analyzing trust situs. It may be possible to create substantial tax savings by modifying the location where the trustee administers the trust.

Grantor trusts are taxed in the state where the grantor resides, so the situs of administration is not an income tax factor for such trusts. But

state income tax can be a significant factor when evaluating the trust situs of a non-grantor trust. States differ in their approaches to determining whether a particular trust is subject to tax and in their tax rates. Some states tax trusts based on a broad swath of connections to the state, including, among other factors, the situs of administration, the residences of beneficiaries and trustees, the location of trust assets, and the settlor's domicile.²⁰ Other states, such as Wyoming and Nevada, do not impose any state income tax on trust income and are therefore appealing locations for administering trusts.

Colorado's state income tax is a relatively moderate 4.55% as of January 1, 2021.²¹ Colorado imposes state income tax on trusts based on whether a trust is a "resident trust," which is a trust that is administered in Colorado.²² Even a nonresident trust (one that is not administered in Colorado) may be subject to Colorado state income tax on Colorado source income, which includes income derived from a business conducted in Colorado, income from property ownership in Colorado, and other similar categories of income.²³ Thus, when evaluating the impacts of state income tax on a trust, it is important to consider source income as part of the analysis. If a trust has substantial Colorado source income, administering that trust outside of Colorado may not create significant tax savings, but other factors impacting the trustee's

decision regarding where to administer the trust may significantly outweigh the impact of state income tax.

Determining whether a trust is administered in Colorado and therefore subject to Colorado state income tax is not as simple as it may initially sound. To determine jurisdiction over a trust, the trust terms designating the trust's principal place of administration may be valid and controlling if (1) the trustee's usual place of business or residence is within that jurisdiction, or (2) all or part of the administration takes place within the jurisdiction.²⁴ Further, the trustee of a trust with its principal place of administration in Colorado may register the trust with the appropriate court in Colorado.²⁵ While these factors are relevant to determining jurisdiction, none will likely be dispositive with respect to whether a trust is a resident trust. Whether Colorado state income tax applies is based on the facts and circumstances surrounding the particular trust's administration, and there is a lack of clear guidance on this issue; no published regulations, rulings, or court cases outline how to make this determination. But in analyzing whether Colorado state income tax applies, it is reasonable to focus on where the actual trust administration takes place, including the amount and significance of the administrative activities occurring both inside and outside of Colorado.²⁶

A key factor in this regard is where the trustee makes its most important decisions regarding the trust,²⁷ because a trustee may have multiple places of business inside and outside Colorado. In particular, where the trustee makes significant investment decisions such as developing its overall investment strategy for the trust; deciding to buy, sell, or exchange assets; and hiring investment managers makes a difference in determining whether the trust is administered in Colorado. Another substantial factor in this analysis is where the trustee makes decisions regarding distributions to the trust beneficiaries. Other important factors include where the trustee maintains the trust records and executes important documents related to the trust and the location of regular meetings of the trustee or trustees. Finally, it is important to consider where the trustee can be reached and where its communications with beneficiaries originate.

State income tax has become an even more significant factor in selecting trust situs since the passage of the 2017 Tax Cuts and Jobs Act (2017 Tax Act). Specifically, the 2017 Tax Act limited the deduction previously available under Internal Revenue Code § 164 for state income tax to \$10,000 per year for taxpayers, including non-grantor trusts, through 2025. The Biden administration has indicated that it will seek to reverse some of the changes that were included



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in the 2017 Tax Act. The limit on the deduction for state income taxes has not been popular, but a complete restoration of this deduction may not be a priority for lawmakers. As a result, at least for wealthier taxpayers, state income tax will likely continue to be an area of concern.

Asset Protection

Another factor when considering trust situs is a state's asset protection laws. Colorado recently enacted Part 5 of the Uniform Trust Code,²⁸ which addresses the validity of spendthrift clauses and a creditor's ability to reach a trust to collect against a beneficiary and a settlor.²⁹

There are two main types of irrevocable trusts to consider when thinking about asset protection, self-settled DAPTs and irrevocable trusts created by a third party. There are currently 19 states that allow some form of DAPT.³⁰ In Colorado, CRS § 38-10-111 was previously interpreted to support the formation of DAPTs, but the Colorado Supreme Court confirmed that was not the case in 1999.³¹ Colorado's enactment of Part 5 of the Uniform Trust Code further confirms that Colorado does not support the formation of a self-settled DAPT.³²

Regarding irrevocable trusts created by a third party, Colorado case law provides some creditor protection to a beneficiary of a purely discretionary trust.³³ The new CUTC provides clearer direction on this issue. Subject to narrow exceptions, including for child support, a beneficiary's interest in a third-party irrevocable trust is well protected if distributions are subject to the trustee's discretion.³⁴ This protection exists even if the trust includes a standard of distribution (e.g., health, education, maintenance and support) and the beneficiary is his or her own trustee.³⁵ However, if a beneficiary is entitled to a mandatory distribution under the trust, the trustee cannot simply choose to withhold it to try to avoid the beneficiary's creditors.³⁶

The CUTC thus strengthens and clarifies Colorado's asset protection laws and makes Colorado a more attractive trust situs.

The Drafter's Role in Determining Situs

The trust drafter has a significant impact on initial situs and decisions related to the trust's

future situs. The settlor and his or her advisors should discuss the pros and cons of various options related to a trust's situs and the settlor's views on changing situs in the future. For trusts that will last for generations after the settlor has passed away, flexibility to move a trust to a new jurisdiction may be a key goal. Changes in the law, the trust assets, or the beneficiaries' locations are factors that might precipitate a move.

Settlors who are considering establishing a trust should outline their goals with respect to the trust. Is it important for the trustee to have a significant ongoing relationship with the beneficiaries? If so, selecting a trust jurisdiction where the beneficiaries are located may be important. Is there a particular asset that the settlor would like to see preserved? In this case, the opportunity for a directed trustee relationship, or at least the ability to limit the trustee's obligation to diversify the trust assets, may be paramount. Are there certain features that appeal to the settlor, such as protecting the trust assets from potential future divorces? Jurisdictions vary with respect to the enforceability of these protections. Some settlors wish to keep their trust as private as possible, and the applicable law would have a substantial impact on the amount of information to which the beneficiaries are entitled. Other settlors favor significant transparency with respect to the trust beneficiaries.

These are just some examples of practical concerns and priorities that can impact the selection of a trust's situs. A trust agreement may specify the settlor's goals and outline the settlor's perspective on whether the trustee should consider a change in situs in the future to further the stated goals.

How to Change Situs

There are several ways to transfer situs. First, the trust document itself may provide a mechanism for changing situs. Second, the CUTC provides a procedure for changing situs under which the trustee must give notice of the proposed transfer to the qualified beneficiaries of the trust not less than 60 days before initiating the transfer.³⁷ If a qualified beneficiary objects, the trustee loses authority to transfer situs until that objection is resolved.³⁸ The trustee could ask the court

to approve a situs transfer over a beneficiary's objection if the court concludes the transfer is in the best interests of all trust beneficiaries.³⁹ Third, if the trust directs that it be administered in a certain state but the trustee determines that a transfer would be in the best interests of the beneficiaries, the trustee could decant the trust or modify it to remove the restriction.⁴⁰ Decanting or modifying a trust may be beneficial even if not strictly necessary to transfer situs. For example, a Colorado trust could be decanted under Colorado law into a Wyoming trust with appropriate state law provisions.

To transfer situs, often the trustee needs to resign and allow a new trustee to be appointed to administer the trust in the new situs. This is not always best for the beneficiaries, particularly if the settlor wanted a specific trustee to administer the trust. The trustee may have a history with the family or certain expertise desired by the settlor.

There are options to allow the trustee to transfer situs yet continue to be involved in the trust administration. For example, a trustee in the new state could be appointed as either a co-trustee or an administrative trustee in a directed trustee arrangement. This may complicate the situs issue because Colorado law provides that, unless the trust states otherwise, if one co-trustee is a corporate trustee, the situs is the corporate co-trustee's usual place of business.⁴¹ Similarly, if one co-trustee is a professional and there is no corporate co-trustee, the situs is the professional's place of business. Finally, if there are two individual trustees, the situs is as agreed upon by them.⁴² A careful analysis of both states' laws would be necessary to ensure either a co-trustee or directed trustee arrangement would be adequate to transfer situs.

Private Trust Companies

Another common technique to transfer situs is the use of a private family trust company (PTC). Several states allow an unregulated PTC; those closest to Colorado are Nevada and Wyoming.⁴³ A PTC is an entity formed and operated in the state where a family wishes to situs their trusts. There should be at least one officer of the trust company who is a resident of the state where the entity is formed and that officer should maintain a place of business in that state. One

advantage of a PTC is that family members or trusted advisors from other states may serve as committee members and participate in decision making related to the trust. PTCs often have separate committees for making decisions related to investments, specific assets, and distributions to beneficiaries. This structure permits family members or other individuals who reside in other states to participate in key parts of the trust administration while providing an anchor for situs in a state that may be more advantageous.

The PTC also provides continuity and succession planning for the trusteeship of family trusts, allowing a smoother transition between generations.⁴⁴ Members of younger generations can serve on committees with older family members and with key professional advisors. This provides an opportunity for younger family members to learn about the trust and its assets while benefiting from the guidance of more seasoned committee members. A PTC can also be a vehicle for educating younger generations regarding the family's philosophy and values and how those values are reflected in the family's management and distribution of assets. A PTC's committees should meet regularly in the state where the trust situs is located. This regular meeting schedule can also provide an opportunity for family members to gather and maintain deep connections with one another.

Families must be careful to ensure that the PTC and its committee members truly administer the trust in the desired state. The family must maintain discipline to make decisions related to the trust during meetings held in the trust situs and ensure that communications, maintenance of trust records, and execution of trust-related documents all occur in that state.

Conclusion

A trust situs must be chosen with care at the trust's inception. Changing situs requires similar attention to factors affecting the trust's administration. A trustee has a duty to administer a trust in a place that is appropriate to the trust's purposes, its efficient administration, and the best interests of the beneficiaries. Colorado is an attractive situs and may be appropriate, but each trust and family is unique, and no one

situs is perfect in every situation. Fiduciaries and advisors should therefore be ever mindful of the requirements for both selecting and transferring situs. ^{CL}



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NOTES

1. CRS §§ 15-16-801 et seq. and -901 et seq.; CRS §§ 15-5-101 et seq.)
2. Unif. Tr. Code § 108, cmt.
3. CRS § 15-5-108(3). While the CUTC was only recently enacted, prior law on this issue was similar. See CRS § 15-16-305 (repealed effective Jan. 1, 2019).
4. CRS § 15-5-108(3).
5. CRS §§ 15-16-801 et seq.
6. For example, W.S. §§ 4-10-510 through -523.
7. CRS § 15-5-108(3).
8. *Id.*
9. Unif. Tr. Code § 108, cmt.
10. *Id.*
11. Loring and Rounds, *A Trustee's Handbook* § 6.2.1.3 (Wolters Kluwer 2020 ed.).
12. It is possible for a trust situs to be in one state, the governing law to be another state, and for the trust to be subject to income tax in one or more other states. See generally Uniform Trust Code §§ 107 and 108. Typically, the interpretation and construction of a trust is governed by the law that governed its creation. The administration of a trust, however, is usually governed by the law in the place where the trust is administered. An analysis of governing law versus principal place of administration is beyond the scope of this article, but for purposes of this article, it is assumed that a situs transfer would include application of the new state's laws to the trust administration.
13. Loring and Rounds, *supra* note 11 at § 6.2.1.3.
14. CRS § 15-5-108; Unif. Tr. Code § 108, cmt. "A trust's principal place of administration ordinarily will be the place where the trustee is located."
15. *Restatement (Third) of Trusts* § 76, cmt.(b)(2) (Am. Law Inst. 2012).
16. CRS §§ 15-5-813 and -105.
17. CRS § 15-5-105(2)(h).
18. CRS § 15-5-105(2)(i).
19. CRS § 15-5-813(3).
20. Note, however, that the ability of states to tax trusts based solely on the residence of the

trust beneficiaries was curtailed by *N.C. Dep't of Revenue v. Kimberley Rice Kaestner 1992 Family Tr.*, 139 S.Ct. 2213 (2019).

21. Co. Exec. Order No. D 2020 302 (Dec. 31, 2020).
22. CRS § 39-22-103(10).
23. CRS § 39-22-403.
24. CRS § 15-5-108(1).
25. CRS § 15-5-205.
26. This approach is consistent with the approach taken by the Wisconsin Supreme Court in *Wis. Dep't of Taxation v. Pabst*, 112 N.W.2d 161 (1961); and *Pabst v. Wis. Dep't of Taxation*, 120 N.W.2d 77 (1963). Wisconsin's statutory language is similar to Colorado's.
27. As noted above, no published regulations or rulings outline the factors that should be considered in determining whether a trust is administered in Colorado and subject to its state income tax. As a result, the factors outlined here are based on the authors' experience with the Colorado Department of Revenue and *Pabst*, 112 N.W.2d 161, and *Pabst*, 120 N.W.2d 77.
28. CRS §§ 15-5-501 et seq. (effective Sept. 7, 2021); Unif. Tr. Code §§ 501 et seq.
29. Colorado included some Colorado-specific amendments to the uniform act. See CRS §§ 15-5-501 et seq. and Unif. Tr. Code §§ 501 et seq.
30. Shaftel, ed., Twelfth ACTEC Comparison of the Domestic Asset Protection Trust Statutes (Aug. 2019), www.actec.org/assets/1/6/Shaftel-Comparison-of-the-Domestic-Asset-Protection-Trust-Statutes.pdf.
31. *In re Cohen*, 8 P.3d 429 (Colo. 1999).
32. CRS § 15-5-505.
33. *In re Marriage of Jones*, 812 P.2d 1152 (Colo. 1991); *In re Marriage of Rosenblum*, 602 P.2d 892 (Colo.App. 1979); *In re Marriage of Balanson*, 25 P.3d 28 (Colo. 2001); *Univ. Nat'l Bank v. Rhoadarmer*, 827 P.2d 561 (Colo.App. 1991).
34. CRS §§ 15-5-502 through -504. A creditor against whom a spendthrift provision cannot be enforced is limited to the remedy of attaching the beneficiary's present or future distributions.
35. CRS § 15-5-504.
36. CRS § 15-5-506.
37. CRS § 15-5-108(5).
38. CRS § 15-5-108(6).
39. Unif. Tr. Code § 108, cmt; CRS § 15-5-201.
40. CRS § 15-5-411; CRS §§ 15-16-901 et seq.
41. CRS § 15-5-108(2).
42. *Id.* Note that this analysis of situs is for state law purposes; the analysis for income tax is different.
43. W.S. §§ 13-5-701 et seq.; N.R.S. § 669A.100.
44. Weeg, *Private Trust Companies: A DIY for the Uber Wealthy*, <https://actecfoundation.org/wp-content/uploads/THE-PRIVATE-TRUST-COMPANY-A-DIY-FOR-THE-UBER-WEALTHY.pdf>.