



SPONSOR: Sen. Sharp
& Rep. Wagner

DELAWARE STATE SENATE

140th GENERAL ASSEMBLY

SENATE BILL NO. 313

AN ACT TO AMEND CHAPTER 5, TITLE 25 OF THE DELAWARE CODE RELATING TO THE RULE AGAINST PERPETUITIES AND POWERS OF APPOINTMENT.

BE IT ENACTED BY THE GENERAL ASSEMBLY OF THE STATE OF DELAWARE:

1 Section 1. Amend Subsection (c) of Section 503 of Title 25, Delaware Code, by adding the following
2 sentence at the end thereof:

3 “Notwithstanding the foregoing, in the case of a power of appointment described in §504 of this
4 title as a “first power,” trusts created by the exercise of the power of appointment, whether by will, deed or
5 other instrument, shall be deemed to have become irrevocable by the trustor or testator on the date on
6 which the first power was created.”

7 Section 2. Amend Title 25, Delaware Code, by adding a new section 504 to read as follows:

8 “§504. Certain Powers of Appointment.

9 Notwithstanding any other provision of this chapter, in the case of a power of appointment over
10 property held in trust (the “first power”), if the trust is not subject to, or has an inclusion ratio of zero for
11 purposes of, the tax on generation-skipping transfers imposed pursuant to chapter 13 of the Internal
12 Revenue Code [26 U.S.C. Ch. 13] or any successor provision thereto and the first power may not be
13 exercised in favor of the donee, the donee’s creditors, the donee’s estate, or the creditors of the donee’s
14 estate, then every estate or interest in property, real or personal, created through the exercise, by will, deed
15 or other instrument, of the first power, irrespective of:

16 (1) The manner in which the first power was created or may be exercised, or

17 (2) Whether the first power was created before or after the passage of this section,

18 shall, for the purpose of any rule of law against perpetuities, remoteness in vesting, restraint upon the
19 power of alienation or accumulations now in effect or hereafter enacted, be deemed to have been created at

20 the time of the creation of, and not at the time of the exercise of, the first power. For purposes of applying
21 the foregoing rule, if any part of an estate or interest in property created through the exercise of the first
22 power includes another power of appointment (the "second power"), then the second power of appointment
23 and any estate or interest in property (including additional powers of appointment) created through the
24 exercise of the second power shall be deemed to have been created at the time of the creation of the first
25 power."

26 Section 3. This Act shall apply to wills, deeds, and other instruments exercising powers of appointment
27 that are executed after the date on which this Act is enacted into law without regard to when any power of
28 appointment so exercised was created.

SYNOPSIS

Under Section 2041(a)(3) of the Internal Revenue Code, when the donee of a limited power of appointment exercises the power at death to create another power, the property subject to the second power is includible in the donee's gross estate if under the governing local law the second power can be validly exercised to postpone the absolute ownership of the property subject to the second power for a time period ascertainable without regard to the date of creation of the first power.

A similar rule applies for federal gift tax purposes when the donee of a power effectively exercises the power during lifetime.

If the donee of a power is unaware of these somewhat obscure provisions of the federal tax law (known as the "Delaware Tax Trap"), the donee might inadvertently incur federal transfer tax upon exercising the power.

In light of the vast and increasing nationwide popularity of Delaware trusts, and particularly Delaware dynasty trusts that are exempt from all federal transfer taxes, concerns have been raised that donees of powers over property held in such trusts might inadvertently and unnecessarily incur federal transfer taxes when exercising their powers.

At present, practitioners familiar with these rules can avoid falling into the Delaware Tax Trap. Nevertheless, the Act is intended to prevent donees of powers of appointment over property held in trusts exempt from the federal generation-skipping tax from inadvertently incurring federal gift or estate taxes when exercising their powers.

Author: Sen. Sharp