



Trustee Discretion: The Better Part of Valor or Vulnerability?

When drafting a trust that gives the trustee discretion in making distributions, be sure the trustee understands the grantor's intent for exercising that discretion.

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Trust law in the U.S. has been developing since the early 1800s. For much of this time, state common law provided most of the rules regarding the creation and administration of trusts. The 21st century, however, brought with it seismic changes to both trust law and trust structure, due in part to the shift from an agriculture-based society to one based on financial assets, services, and information,¹ and to an increase in the use of trusts for both family estate planning and commercial transactions.² As more states adopt the Uniform Trust Code (UTC) (or a variation of it), common law principles of a trustee's duties and powers when granted absolute discretion are being codified and altered.³ As a result, the consequences of a grant of discretion need to be considered in light of recent trends in legislation and case law.

Traditionally, trusts provided income to a current beneficiary for life, with the remainder passing out-

right to another beneficiary on the current beneficiary's death. The trustee had no power to withhold income from the current beneficiary, or to distribute principal to him or her. The current trend in drafting trusts, and in trust legislation, is to provide the trustee with great flexibility in exercising its powers, moving away from the traditional current income beneficiary/remainder beneficiary structure. This flexibility enables the trustee to administer the trust effectively in light of current circumstances that the grantor may not have anticipated when the trust was created.

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In particular, when a grantor creates a trust, it may be difficult or impossible to anticipate whether, and the extent to which, distributions to a particular beneficiary (or even an unborn beneficiary) may be necessary or desirable. This is especially true if the trust is structured to last for multiple generations, or in perpetuity. For this reason, a grantor may choose to give a trustee very broad distribution powers, not subject to restrictions or standards.

In a fully discretionary trust, no beneficiary is entitled to any distributions, and must wait for the trustee to exercise its distribution powers. The trustee may favor the current beneficiary over the remaindermen by distributing principal to the current beneficiary, and may favor the remaindermen over the current beneficiary by accumulating income.

Discretionary powers give the trustee flexibility in administering a trust to provide for a beneficiary's

well-being, and to provide for minor or disabled beneficiaries. They also enable the trustee to address issues related to beneficiaries' marital problems, substance abuse, and lack of productivity, and to protect the trust assets from the claims of a beneficiary's creditors, including a spouse in the event of a divorce. The assets of a discretionary trust also may be protected from inclusion in a beneficiary's gross estate for estate tax purposes.

In addition to flexibility, discretionary powers bring with them both tax consequences and questions regarding the grantor's intent and the scope of the power. Accordingly, giving the trustee sole, absolute, and uncontrolled (i.e., "extended") discretion may place a heavy burden on the trustee, who is both the ultimate decision maker and the steward of the trust property.

Grantor intent

The benefits to which a beneficiary of a discretionary trust is entitled, and what may be an abuse of discretion by the trustee, depend on the terms of the discretion, including the proper construction of any accompanying standards, and on

the grantor's purposes in granting the discretionary power and creating the trust.⁴ In exercising its discretion, a trustee is guided by the grantor's intent, as described in the trust agreement.⁵

However, grantors and their counsel often give little or no thought to the words used to guide

If the trustee feels secure in its authority to exercise its discretion, the trust will be administered with optimum flexibility.

or mandate the trustee in making distributions. If the trust agreement does not contain express statements of a grantor's intent, the trustee has little guidance regarding the exercise of its discretion. Many drafting attorneys simply rely on their forms, and do not discuss distribution options or standards with clients, or thoughtfully consider

how "boilerplate" language will affect a given set of circumstances, or a particular grantor or that grantor's family. As a result, whatever intention the grantor had with respect to the scope of the trustee's exercise of discretion may not have been ascertained by counsel or preserved in the drafting.

To be influenced by and draw meaning from subtle details of wording may very well ignore both the realities of how drafting is done by a particular lawyer, and the fact that the drafting attorney may have given little thought to the particular issue or circumstances for which it has become necessary to discover or attribute intention.⁶ Rather than relying on speculation about the import of specific details of fact or wording, it often is more instructive to analyze the variety of beneficial interests and other provisions of the trust as a whole, with any other available evidence, in a broader effort to ascertain why the trust was created and what role the particular discretionary power was to play in the trust plan.⁷

Drafting distribution provisions is not a "one size fits all" proposition. The drafting attorney should counsel the client regarding the dis-

¹ See Langbein, "Why Did Trust Law Become Statute in the United States?" 58 Ala. L. Rev. 1069 (2007).

² Prefatory Note to the Uniform Trust Code.

³ Taback and Pratt, "When the Rubber Meets the Road: A Discussion Regarding a Trustee's Exercise of Discretion," 49 Real Prop., Tr. & Est. L. J. 491 (Winter 2015).

⁴ Restatement (Third) of Trusts § 50(2) (2012).

⁵ See, e.g., N.H. Rev. Stat. Ann. § 564-B:1-112 (2018) ("In interpreting or construing the terms of a trust, the settlor's intent shall be sovereign to the extent that the settlor's intent is lawful, not contrary to public policy, and possible to achieve. For the purposes of determining the benefit of the beneficiaries, the settlor's intent as expressed in the terms of the trust shall be paramount.")

⁶ Restatement (Third) of Trusts § 50 comment g.
⁷ *Id.*

⁸ See, e.g., *Rowe v. Rowe*, 347 P.2d 968 (Oregon 1959), where the court stated, "the difficulty in many if not most of these [abuse of discretion] cases is finding the purpose of the grantor with sufficient definiteness to be helpful ... the grantor's specific design in framing a discretionary trust is normally unexpressed or vaguely outlined."

⁹ Both the Model UTC (§ 504) (Discretionary Trusts; Effect of Standard) and the Restatement (Third) of Trusts (§ 60) (Transfer or Attachment of Discretionary Interests) eliminate the distinction between discretionary and support trusts, unifying the rules for all trusts fitting within either of those categories. However, the comment to Model UTC § 504 states: "Eliminating this distinction affects only the rights of creditors.... It does not affect the rights of a beneficiary to compel a distribution. Whether the trustee has a duty in a given situation to make a distribution depends on factors such as the breadth of the discretion granted and whether the terms of the trust include a support or other standard." Model UTC § 506 (Overdue Distribution) provides that regardless of whether a trust contains a spendthrift provision, a creditor can reach a mandatory distribution from the trust if the trustee has not made the distribution within a reasonable period from the distribution date. For this purpose, the term "mandatory distribution" does not include a distribution subject to the exercise of the trustee's discretion, even if: (1) the discretion is expressed in the form of a standard of distribution; or (2) the terms of the trust authorizing a distribution couple language of discretion with language of distribution. Lawyers frequently and habitually

use "shall" to mean different things, one of which is "may," and the comment to § 506 of the Model UTC recognizes this, by concluding that a provision stating that "my trustees shall, in their absolute discretion, distribute such amounts as are necessary for the beneficiary's support," is discretionary, not mandatory. See Millard, "Rights of a Trust Beneficiary's Creditors under the Uniform Trust Code," 34 ACTEC J. 58 (Fall 2008).

¹⁰ Halback, Problems of Discretion in Discretionary Trusts, 61 Columbia L. Rev. 1425 (1961).

¹¹ *Id.*

¹² Restatement (Third) of Trusts § 50(2) and comment b.

¹³ Restatement (Third) of Trusts § 87 comment c.

¹⁴ Historically, open disclosure of information to beneficiaries has been viewed as an indicia of a trustee acting in good faith. See Restatement (Third) of Trusts § 82 (Duty to Furnish Information to Beneficiaries). However, some states allow a grantor to create a "quiet" trust, which limits or eliminates a beneficiary's ability to request or receive information regarding the administration of the trust. See, e.g., 12 Del. C. § 3303(c) (2018), Nev. Rev. Stat. § 163.004(1)(a) (2015) and N.H. Rev. Stat. Ann. § 564-B:8-813 (2008).

tribution options and their possible consequences. Failure to do so may result in the trustee having no guidance in making distributions, creating in beneficiaries rights that the grantor does not intend to confer, or failing to provide for a beneficiary in a manner that the grantor intends. Accordingly, the drafting attorney should encourage the grantor to articulate his intentions with respect to the purpose and scope of the trustee's discretionary powers, and incorporate those intentions into the trust agreement. Unfortunately, it is unusual to see explicit and customized expressions of intent in trust documents. This can lead to conflict among the beneficiaries with respect to the grantor's intent,⁸ and force the trustee to make discretionary distribution decisions with no guidance at all, which could lead to beneficiary claims of abuse of discretion.

In drafting distribution provisions, the attorney should consider the grantor's specific purposes in creating the trust, the beneficiary's personal and economic circumstances, potential tax consequences, and the potential for conflict between the beneficiaries. The trust language should both protect the trustee from second-guessing and possible reversal by a judge, and enable the beneficiary to protect his or her right to receive what the grantor intended him or her to have. The use of a distribution standard coupled with discretion (e.g., "My trustee *shall* distribute to my son so much of the net income and/or principal as the trustee, in its *sole and absolute discretion*, determines is necessary for my son's health, support and maintenance") provides limited insight into the grantor's intent and may, in fact, have a meaning other than what the grantor actually intended.⁹

If the trustee feels secure in its authority to exercise its discretion, the trust will be administered with optimum flexibility. However, if the trustee is in doubt regarding the scope of its discretion and the grantor's intent, it is likely to be conservative in exercising its discretion and making distributions, because underpayment, in the absence of bad faith or abuse of discretion, would result merely in the beneficiary's obtaining a court order directing increased distributions. On the other hand, an overpayment could result in a suit against the trustee by the remainder beneficiaries for breach of fiduciary duty. That suit could be brought long after the funds have been paid out, and are no longer recoverable.¹⁰ The problem, of course, is that if the trustee limits distributions to the current beneficiary, it is probably limiting distributions to the person to whom the grantor intended the trustee to be the most generous.¹¹

What may be an abuse of discretion by the trustee depends on basic fiduciary duties and principles, the terms of the discretion, including the proper construction of any accompanying standards, and on the grantor's purposes in granting the discretionary power and in creating the trust.¹² An abuse of discretion may occur if the trustee acts dishonestly (e.g., if the trustee

receives an improper inducement for exercising the power in question), if the trustee acts from an improper, but not dishonest, motive (e.g., a trustee who has the discretionary power to make distributions for a beneficiary's "support" makes well-intentioned, otherwise reasonable, distributions that are not support-related), if the trustee, arbitrarily or without knowledge of or inquiry into relevant circumstances, fails to exercise its discretion, or if the trustee fails to exercise or otherwise abuses its discretionary authority because of mistaken interpretation of the terms of the trust or power, or a misunderstanding of applicable fiduciary law.¹³

In this context, relevant fiduciary principles include the trustee's general duty to act, reasonably informed, with impartiality among the various beneficiaries and interests, and its duty to provide the beneficiaries with information about the trust and its administration. This combination of duties entitles the beneficiaries and the court to accounting information and to relevant, general information about the bases upon which the trustee exercises its discretion.¹⁴ Appropriate disclosure usually can be provided in general terms that allow reasonable protection for confidential, private, or sensitive information.

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Extrinsic evidence and letters of wishes

When the language of a trust is clear, a court will look only at that language when interpreting it.¹⁵ Extrinsic evidence cannot be used to contradict or change the written terms, but only to remove or explain an existing uncertainty or ambiguity.¹⁶ When there is evidence of ambiguity regarding the grantor's intent, the court may consider extrinsic evidence. For example, post-funding affidavits may be admissible as affirmative evidence of the grantor's intent.¹⁷

A letter of wishes is a written communication from the grantor to the trustee designed to offer the trustee of a discretionary trust some guidance in the exercise of his or her discretion. Such a letter may be useful if the trust agreement provides limited guidance, or does not address a particular circumstance. There is very little primary or secondary authority regarding letters of wishes to a trustee,¹⁸ although in 2019 New Hampshire enacted a statute that specifically defines letters of wishes and provides that they are not part of the trust agreement or binding on the trustee.¹⁹

One of the issues raised by the use of a letter of wishes is whether the letter becomes part of the terms of the trust. The Model UTC (§ 103(18)) defines the "terms of the trust" as "the manifestation of the grantor's intent regarding a trust's provisions as expressed in the trust instrument or as may be expressed by other evidence that would be admissible in a judicial proceeding." The comment to § 103(18) recognizes that, although the trust agreement itself is always the most important determinant of the trust's terms, the phrase "terms of the trust" is not limited to just the trust agreement. Oral statements, the situation of the beneficiaries, the purposes of the trust, the circumstances under which the trust

is to be administered, and, to the extent the trust is otherwise silent, rules of construction, all may have a bearing on the trust's meaning.²⁰ The comment further provides that a manifestation of a grantor's intent is not evidence of a trust's terms if it would be inadmissible in a judicial proceeding in which the trust's terms are in question. For example, state law may require that trusts of real property be in writing,²¹ and the parol evidence rule may exclude evidence otherwise relevant to determining the terms of the trust.

The argument for including a letter of wishes as part of the trust is that if the purposes for which the power was conferred on the trustee by the grantor are revealed only in the letter of wishes, then, in order to monitor and enforce their beneficial interests, the beneficiaries must be able to review both the trust agreement and the letter of wishes.²² However, the counterargument is that if the trust is otherwise complete and enforceable, and the grantor provides a non-binding letter of wishes solely to

advise the trustee of the grantor's state of mind in connection with the trustee's exercise of discretion in different situations, the letter of wishes should not become part of the trust or discoverable by the beneficiaries.

A letter of wishes may be problematic because it may contain ambiguities, conflict with the trust agreement, contain information that would be hurtful to the beneficiaries or have adverse transfer tax consequences (i.e., it may result in the grantor's transfer to the trust being an incomplete gift, or the inclusion of the trust property in the grantor's gross estate).²³ Also, the letter may be of limited utility, because it probably will not address all situations that the trustee could encounter in the exercise of his or her discretion.

Rather than relying on a letter of wishes, the better course of action is to include the grantor's ideas in the trust agreement. However, that may not always be possible (e.g., circumstances change after the trust is created). If a letter of wishes is used, it should be clear that it is not

¹⁵ See, e.g., *Harrison v. Marcus*, 486 N.E.2d 710 (Mass. 1985) ("Trust instruments must be construed to give effect to the intention of the settlor as ascertained from the language of the whole instrument considered in the light of the attendant circumstances.")

¹⁶ See *Ferri v. Powell-Ferri*, 72 N.E.3d 541 (Mass. 2017), citing General Convention of the New Jerusalem in the U.S. of Am., Inc. v. MacKenzie, 874 N.E.2d 1084 (Mass. 2007).

¹⁷ See, e.g., *Ferri vs. Powell-Ferri*, *supra* note 16 (grantor's affidavit, executed in 2012 with respect to a trust he created in 1983, provided affirmative evidence of trustee's authority to decant, where the trust agreement neither expressly permitted nor barred decanting). See also *Morse v. Kraft*, 992 N.E. 2d 1021 (Mass. 2013) (court permitted grantor, drafting attorney, and disinterested trustee to submit affidavits to demonstrate that they intended trust to allow distributions to new trusts without consent or approval of any beneficiary or court); and Restatement (Third) of Property: Wills and Other Donative Transfers § 10.2 and comment g (2003).

¹⁸ Bove and Langa, "Distinguishing Discretion in Discretionary Trusts—the Letter of Wishes," *Mass. Lawyers Weekly* (1/23/2006); Restatement (Third) of Trusts § 87.

¹⁹ N.H. Rev. Stat. Ann. § 564-B:1-113 (2019).

²⁰ Model UTC § 103(18) (comment).

²¹ Absent a specific statutory provision, such as one that requires transfers of real property to be in writing, an oral trust can be established

by clear and convincing evidence. Model UTC § 407 (comment).

²² Restatement (Third) of Trusts § 82 comment a, and § 87.

²³ See Reg. 25.2511-2 (incomplete gift) and Section 2036(a)(2) (inclusion in gross estate).

²⁴ Bove and Langa, *supra* note 18.

²⁵ *Id.*

²⁶ Restatement (Third) of Trusts § 60 comment a. See also footnote 9, *supra*.

²⁷ See, e.g., S.D. Codified Laws § 55-1-25 (2015).

²⁸ In *Jenkins*, 428 F.2d 538, 25 AFTR2d 70-1578 (CA-5, 1970), *cert. den.* 400 U.S. 829 (1970), an inter vivos power to appoint property to the powerholder or the powerholder's creditors was held sufficient to make the power a general power of appointment for estate tax purposes. The statutory definitions of general powers of appointment under Section 2041(b) (estate tax) and Section 2514(c) (gift tax) are identical, as are the definitions provided by the applicable regulations. See Reg. 20.2041-1(c)(1) and Reg. 25.2514-1(b)(1). Powers of appointment thus have the same meaning under both the gift and estate tax provisions and are construed together. See Rev. Rul. 75-351, 1975-2 CB 368.

²⁹ It is possible for an individual to both serve as the trustee (having legal title) and be a beneficiary (having equitable title) of a trust. See Restatement (Third) of Trusts § 32 comment b and § 43 comment a.

binding on the trustee, so that it does not become part of the trust “documents,” and thus discoverable or enforceable by the beneficiaries. Discretion is a function of objective judgment, and binding instructions can interfere with the concept of full discretion, and undermine or diminish the opportunity for exercising that judgment.²⁴

Ascertainable standards

The scope of the trustee’s discretion is frequently limited by the standard of “health, support, maintenance and education” (often referred to as an “ascertainable” or “HEMS” standard). Because these words are so commonly used, the trustee must interpret them in light of the grantor’s frame of reference and intent as otherwise expressed in the terms of the agreement. When a HEMS standard is accompanied (as it typically is, by habit or custom, if nothing else) by words enlarging the trustee’s discretion, such as sole, absolute, unfettered, or uncontrolled, the scope of the standard becomes even more uncertain.²⁵

Both the Restatement (Third) of Trusts (§ 60) and the Model UTC (§ 504) decouple the rights of a beneficiary’s creditors from the beneficiary’s power to enforce a trust, regardless of whether the trust is purely discretionary or imposes a standard for distributions, because the distinction between a discretionary trust and a support trust is, according to these sources, arbitrary and artificial, and attempting to differentiate them leads to different results, on a case-by-case basis, even where the beneficiaries appear to be similarly situated.²⁶ However, some states have expressly maintained the distinction between discretionary and support trusts, and reject the positions of the Restatement and Model UTC in this regard.²⁷

There is a continuum of discretionary trusts, with the terms of the distributive powers ranging from the most objective (e.g., an ascertainable standard under IRC Section 2041) to the most open-ended or vague (e.g., “happiness”), or even with no standard at all (for which the court may impose a standard of reasonableness). A trust may use any combination of terms and standards to structure the scope of the trustee’s distribution powers (i.e., the trust may mix discretion with a standard), but all of the possibilities are still subject to the principle that the court will interfere only to prevent abuse.

Words used to modify the grant of discretion to the trustee do not have transparent and unchanging meanings, but instead vary greatly, depending on the circumstances in which they are used, and by whom they are used. The trustee always must interpret the language of the trust agreement within the grantor’s frame of reference.

The words “health, support, maintenance and education” are terms of art in the tax Code, and often (but not always) are used to limit a trustee/beneficiary’s discretion in order to avoid adverse federal wealth transfer tax consequences for the trustee/beneficiary. A trustee’s power to distribute trust property is a general power of appointment for transfer tax purposes if the power may be exercised for the trustee’s direct or indirect benefit.²⁸ This generally is an issue only if the trustee is also a beneficiary.²⁹ A “general power of appointment” is any power that may be exercised in favor of one or more of the following:

1. The powerholder.
2. The powerholder’s estate.
3. The powerholder’s creditors.
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The exercise or lapse of a general power of appointment may result in the trustee making a gift, or having the property that is subject to the power included in the trustee's estate for estate tax purposes. However, if the exercise of a power of appointment is limited or restricted in such a way that the power is not the equivalent of ownership, the power is not a general power of appointment. Specifically, if the power is limited by an ascertainable standard relating to the health, education, support, or maintenance of the powerholder, it is not a general power of appointment. For this reason, it is not unusual to see a grant of discretion to a trustee modified by the standard of "health, support, maintenance and education." Although the use of these words will avoid conferring a general power of appointment upon a trustee/beneficiary (and thus eliminate adverse transfer tax consequences for a trustee/beneficiary), using them in the absence of tax reasons for doing so (e.g., because a beneficiary can never serve as trustee) may not make the trustee's job any easier.³⁰

The question, then, is what effect the definitions of the terms in the tax code and regulations should have—beyond their tax implications—when used to set the parameters of a trustee's discretion. State law determines property

rights and interests, and federal law determines how to tax them.³¹ In other words, state law, not the tax code or regulations, will be used to interpret the language of a trust agreement. The tax code and regulations merely will deter-

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mine how the tax laws apply to the property interests that language creates.

Some states' laws contain "default" rules, so that the meaning of the words "health, support, maintenance and education," for state property law purposes, is the same as for federal tax law purposes.³² The Model UTC also contains a definition of "ascertainable standard," and a limitation on the ability of a trustee/beneficiary to distribute trust property to or for the benefit of himself or herself, that is consistent with the ascertainable standard definitions that apply in the transfer tax context.³³

If the property is being held in trust solely as a tax-induced substitute for an outright gift (i.e., to avoid the imposition of estate taxes on the beneficiary's death), or to eliminate the ability of a beneficiary's creditors to reach the trust property, the use of any ascertainable standard at all should be limited to situations in which the beneficiary is also the trustee, and the trust agreement should clearly state that the trustee is authorized and encouraged to distribute the trust property liberally to or for the benefit of the beneficiary, if that is, in fact, what the grantor actually intends.

Although the use of a HEMS standard in trust agreements is very common, the terms "health," "support," "maintenance," and "education" are surprisingly ill defined, and there is no shortage of cases illustrating attempts by beneficiaries and trustees to determine their meaning when the trust agreement provides no guidance.³⁴

The Treasury Regulations do not define the term "health," and only provide that the term "health," and the phrase "medical, dental, hospital and nursing expenses and expenses of invalidism," create ascertainable standards.³⁵

The Regulations say that the terms "support" and "maintenance" are synonymous, and that their meanings are not limited to the basic necessities

³⁰ The comment to Model UTC § 814 states that the UTC's curative provisions (including imposing an ascertainable standard on the discretion of a trustee/beneficiary) "are often overbroad, applying not only to trusts intended to qualify for tax benefits, but also to smaller trust situations where taxes are not a concern."

³¹ *U.S. v. Rogers*, 461 U.S. 677, 52 AFTR2d 83-5042 (1983).

³² See, e.g., N.H. Rev. Stat. Ann. § 564-A:3, IV(a)(1)(A) (2005) ("Due to the inherent conflict of interest that exists between a trustee who is a beneficiary and other beneficiaries of the trust, unless the terms of a trust refer specifically to this paragraph and provide expressly to the contrary, any power conferred upon a trustee ... shall not include the [power to] make discretionary distributions of either principal or income to or for the benefit of such trustee,

except to provide for that trustee's health, education, maintenance, or support as described under ... Code sections 2041 and 2514.")

³³ Model UTC § 103(2) (definition of "ascertainable standard") and § 814(b)(1) (a trustee/beneficiary with the power to distribute trust property in his discretion can only exercise that power for his own benefit in accordance with an ascertainable standard).

³⁴ See, e.g., *In re Brooks*, 2014 Mich. App. LEXIS 2046 (2014) (appellate court found that trial court properly examined traditional dictionary definitions for the word "health" and found it to include such concepts as mental health and the health of one's mind, spirit, and soul, but not "anything that makes a person 'feel good'").

³⁵ See Reg. 20.2041-1(c)(2). The Restatement

provides some further clarification, but cites no cases solely defining the term "health." See Restatement (Third) of Trusts § 50 comment d(3).

³⁶ Reg. 20.2041-1(c)(3); Restatement (Third) of Trusts § 50 comment d(2).

³⁷ See, e.g., *Akers v. Fidelity & Columbia Tr. Co.*, 234 SW 725 (Kentucky 1921); Halback, *supra* note 10, at 1435 (footnote 56).

³⁸ Halback, *supra* note 10, at 1435.

³⁹ Restatement (Third) of Trusts § 50 comment d(2).

⁴⁰ *Robison v. Elston Bank & Trust Co.*, 48 N.E.2d 181 (Indiana 1943).

⁴¹ Halback, *supra* note 10. See also *Pfannenstiehl v. Pfannenstiehl*, 55 N.E.3d 933 (Mass. 2016) (beneficiary's interest in a discretionary trust not considered part of the marital estate).

⁴² Restatement (Third) of Trusts § 50 comment d(3).

of life.³⁶ A discretionary power to make payments for a beneficiary's support or maintenance is not a particularly broad power, and covers a beneficiary's normal living expenses,³⁷ the continuation of accustomed patterns of vacation and gifts, and expenses related to maintaining the beneficiary's accustomed standard of living.

Inferences regarding the intended manner of support will be affected by the size of the trust, relative to the purposes for which distributions are to be made. A small trust may limit the amount that the trustee distributes for the support of any beneficiary, and the trustee may end up making distributions that are less than those actually necessary to support the beneficiary or maintain the beneficiary's accustomed standard of living. Conversely, a beneficiary's rights under a large trust normally would not be enlarged to whatever the trust will bear.³⁸ With respect to a married beneficiary, the term "support" usually is construed to mean that the beneficiary is entitled to distributions sufficient to support the beneficiary himself and also the beneficiary's spouse and minor children.³⁹

Absent specific language in the trust agreement to the contrary, it is unlikely that a grantor intends to provide for the support of an individual beneficiary and "let [the beneficiary's] wife and children go without."⁴⁰ However, these are questions of construction, and should not be confused with the legal question of whether a beneficiary's interest in a spendthrift or discretionary trust is subject to satisfaction of a claim based on a support or alimony decree.⁴¹ Even if distributions for the support of the family members of a beneficiary are proper, those family members themselves are not, by association, beneficiaries of the trust. The family

members are merely relevant factors in determining the amounts required to maintain the designated beneficiary in his or her accustomed manner of living.

The Regulations also do not define the term "education," and state only that the term "education" creates an ascertainable standard. The Restatement provides clarification, stating that the term "education" usually means the payment of living expenses, fees, and other costs of attending an institute of higher education.⁴² The trust agreement should make clear the level of education intended, and whether other types of training or broadening experiences are to be included. The agreement also should specify how long the educational benefits should continue.

Sample language regarding payments for a beneficiary's education might be:

The Trustee, in its sole and absolute discretion, may pay out of the net income or principal, or both, to or for the benefit of the primary beneficiary of such trust (i.e., the grandchild in whose name the trust is established) such amount or amounts as the Trustee, in its sole and uncontrolled judgment, determines are reasonably necessary to

cover the costs of the primary beneficiary's post-secondary education. Any net income not so paid shall be added to principal. In exercising this discretion, it is the Grantor's wish (but not direction) that when possible, the Trustee will make distributions directly to the educational provider(s) instead of to the primary beneficiary himself or herself. For purposes of this Paragraph, the costs of the primary beneficiary's post-secondary education may include, but are not limited to, tuition, fees, room, board, books, supplies, transportation, and computer hardware and software. The Trustee's determination of what expenses constitute costs of the primary beneficiary's post-secondary education shall be final and not subject to question by any person interested in the trust estate.

Trust agreements often contain other terms that are not ascertainable standards, but are intended to guide the trustee. However, without clear statements of grantor intent, the trustee may not know exactly what those terms mean. The use of these terms may cause uncertainty regarding the circumstances under which the trustee may exercise its discretion.

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The Treasury Regulations provide that the term “comfort,” when used alone, is not an ascertainable standard.⁴³ However, the terms “support in reasonable comfort” and “maintenance in health and reasonable comfort” are ascertainable standards. The word “comfort” often accompanies a support standard, but the term adds nothing to the usual meaning of the term “support” for a beneficiary whose lifestyle is already reasonably comfortable, although it may allow for an elevated standard of support if the beneficiary’s lifestyle has been more modest. Courts are often asked to interpret the meaning of the term “comfort,” and grantors and drafters would be wise to modify the term, and provide the trustee with additional guidance, with respect to what the grantor actually means by the term.

The terms “welfare” and “happiness” are often considered to be synonymous. They are not ascertainable standards. The term “happiness” is considered to be a much broader term than the term “support,” and suggests an intention that the trustee exercise its judgment generously and without relatively objective limitations.⁴⁴ The primary effect of the term “happiness” is to immunize from challenge

by remainder beneficiaries almost any reasonably affordable distributions. This, however, does not mean that the trustee cannot properly resist any reasonable request by the beneficiary, because the decision remains one within the trustee’s discretion.⁴⁵

If the trustee is a beneficiary, and the trustee can make distributions for “emergencies,” the trustee/beneficiary may have a general power

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of appointment.⁴⁶ “Emergency” and similar terms accompanying discretionary powers generally are strictly construed, and usually refer to extreme need.⁴⁷ However, “emergency” does not only encompass things such as injury, illness, and economic catastrophe, but also extends to general inadequacy of resources and of earning capacity.⁴⁸

Other tax considerations

If a trustee/beneficiary has a legal obligation to support another beneficiary (e.g., the trustee’s minor child is also a beneficiary), and that support obligation may be satisfied by a distribution from the trust in the trustee’s discretion, the trustee’s discretionary distribution power is a general power of appointment, *even if* it is measured by an ascertainable standard relating to the health, education, support, or maintenance of the beneficiary.⁴⁹ For this reason, trusts often include an *Upjohn* provision that prohibits the trustee from making distributions that would discharge the trustee’s legal obligations of support.⁵⁰ The trust income may be taxable to the grantor (i.e., the trust may be a grantor trust) if the trustee has discretion to distribute the income for the support or maintenance of a beneficiary whom the grantor is legally obligated to support or maintain, and actually makes the distribution.⁵¹

Below is sample language for a revocable trust to eliminate a general power of appointment for a trustee/beneficiary:

No Trustee (other than the Grantor) may: (1) make any distribution to or for the benefit of a beneficiary of the subject trust that

⁴³ Reg. 20.2041-1(c)(2).

⁴⁴ Restatement (Third) of Trusts § 50 comment d(3). See also *Amoskeag Trust Co. v. Wentworth*, 111 A.2d 198 (N.H. 1955) (trust agreement that directed payment of income to sole beneficiary “in order that his personal necessities and needs may be paid” ruled out payments that might contribute to beneficiary’s happiness, contentment, and peace of mind, regardless of his need for them).

⁴⁵ Restatement (Third) of Trusts § 50 comment d(3).

⁴⁶ See, e.g., *Estate of Sowell*, 708 F.2d 1564, 52 AFTR2d 83-6408 (CA-10, 1983), *rev’g* 74 TC 1001 (1980) (“The Tax Court erred in its underlying assumption that the word ‘emergency’ has an inherent meaning broader than health, education and support. The key characteristic of the meaning of ‘emergency’ is that of need. The Tax Court also erred in concluding that the concept of an ‘emergency’ included broader uses than for support or maintenance.... We have exhaustively researched this issue and have not discovered a case which broadly construes the term ‘emergency’ so as to allow a general power of appointment, sufficient to

render a fund taxable to an estate.”) But see Ltr. Rul. 7841006 (trustee’s power to invade corpus of trust in cases of illness or emergency created a general power of appointment).

⁴⁷ Halback, *supra* note 10.

⁴⁸ Halback, *supra* note 10, *citing* Application of Sabol, 191 N.Y.S.2d 773 (Sup. Ct. of N.Y. 1959). See also Restatement (Third) of Trusts § 50 comment d(4) (the term “emergency” is construed as authorizing distributions only when the described circumstances arise, and then only to the extent appropriate to alleviate the emergency).

⁴⁹ Reg. 25.2514-1(c)(1) and Reg. 20.2041-1(c)(1).

⁵⁰ See *Upjohn*, 30 AFTR2d 72-5918 (DC Mich., 1972). § 814(b)(2) of the Model UTC contains a similar provision (“A trustee may not exercise a power to make discretionary distributions to satisfy a legal obligation of support that the trustee owes another person.”).

⁵¹ The mere possibility that the trust income may be used to discharge the legal obligation of the grantor or the grantor’s spouse to support

someone does not itself cause a trust to be taxable to the grantor under Section 677(b), unless the individual whose support may be paid is the grantor’s spouse.

⁵² Regs. 20.2041-1(b)(1) and 25.2514-1(b)(1). See also Rev. Rul. 95-58, 1995-2 CB 191, and Ltr. Rul. 201702016.

⁵³ See N.H. Rev. Stat. Ann. § 564-B:8-814(b) (2008) (“[I]f a distribution to or for the benefit of a beneficiary is subject to the exercise of the trustee’s discretion, whether or not the terms of a trust include a standard to guide the trustee in making distribution decisions, then the beneficiary’s interest is neither a property interest nor an enforceable right, but a mere expectancy”); *Pfannenstiehl v. Pfannenstiehl*, 55 N.E.3d 933 (Mass. 2016) (husband/beneficiary’s interest in discretionary trust was nothing more than an expectancy and not assignable to the marital estate); and Ausness, “Discretionary Trusts: An Update,” 43 ACTEC L.J. 231 (Winter 2018).

⁵⁴ 139 S.Ct. 2213 (2019).

⁵⁵ Halback, *supra* note 10.

would discharge such Trustee's legal obligation to support such beneficiary; or (2) participate in the exercise of any discretionary power to distribute income or principal to or for the benefit of himself or herself (unless subject to an ascertainable standard).

If a trustee has discretion to make distributions to a beneficiary, and the beneficiary has the power to remove and replace the trustee, and appoint a successor trustee who is related or subordinate to the beneficiary, or to appoint the beneficiary himself as the successor trustee, then the beneficiary will have a general power of appointment.⁵² A draftsman considering granting a trust beneficiary the power to remove or replace a trustee who has the power to make discretionary distributions to that beneficiary should add the restriction that the replacement trustee cannot be the beneficiary himself or a trustee who or which is related or subordinate to the beneficiary.

Below is sample language for a revocable trust:

If any individual (other than the Grantor) is removed as a Trustee hereunder, and such individual is authorized to appoint a successor Trustee, such individual shall not participate in any decision to appoint such successor Trustee. If any individual (other than the Grantor) is serving as a Trustee hereunder, and such individual is authorized to remove such Trustee, such individual shall not participate in any decision to remove himself or herself as a Trustee.

Notwithstanding the provisions of [applicable state law], after the Grantor's death, each of the persons designated below (the "Removal Powerholder") shall have the power to remove the Trustee designated below for any reason. The removal of a Trustee shall be accomplished by an instrument signed by the Removal Powerholder and mailed or delivered to such Trustee and the

person(s) authorized to appoint a successor Trustee. Such removal shall become effective only upon the written acceptance of a successor Trustee. Upon removal of any Trustee, a successor Trustee shall be appointed as provided in Paragraph ____, above; provided, however, that if the Removal Powerholder is the person authorized to appoint a successor Trustee, then such successor Trustee shall not be the Removal Powerholder himself or herself, or related or subordinate [within the meaning of Code § 672(c)] to the Removal Powerholder.

The presence or lack of a standard of distribution also may have income tax consequences. In a fully discretionary trust, no beneficiary is entitled to any distributions, and must wait for the trustee to exercise its distribution powers; the beneficiary's interest in the trust is a "mere expectancy."⁵³ Currently, 43 states impose an income tax on trusts, and all of those states tax the undistributed income of a nongrantor trust as a "resident trust" based on criteria that vary from state to state. Recently, the United States Supreme Court, in *NC Dept. of Revenue v. Kimberly Rice Kaestner 1992 Family Trust*,⁵⁴ considered whether a state could tax a fully discretionary trust, where the only connection between the state and the trust was the beneficiary's residence there. Because the resident beneficiary had no possession, control, or enjoyment over the trust property, or a right to receive any trust property (due to the trustee's

extended discretion), and the beneficiary had not actually received any distributions from the trust in the year in question, a unanimous Court held that the state tax was unconstitutional. Although the *Kaestner* opinion is fact specific, it reaffirms the concept that although beneficiaries of fully discretionary trusts may be the equitable owners of the trust property, they do not control it.

Scope of discretion

When a trustee has simple discretion, it has discretion that is not "sole," "absolute," or "unlimited." Use of those words as modifiers enlarges the scope of the trustee's discretion. Such enlarged discretion is referred to as "extended discretion." The difference between simple and extended discretion is one of degree, and not of kind.⁵⁵

Below is sample language defining the scope of the trustee's discretion:

The Trustee may pay out of the net income or principal, or both, of the Family Trust such amount or amounts (whether equal or unequal and whether the whole or a lesser amount) as the Trustee, in its sole and absolute discretion, determines to or for the benefit of such one (1) or more persons then living as the Trustee, in its sole and absolute discretion, may select out of a class composed of the Grantor's wife and the Grantor's then living issue; provided, however, that while any such beneficiary is serving as Trustee, the beneficiary as Trustee: (1) may distribute net income or principal, or both, to himself or herself

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only at such times and in such amounts as is necessary for his or her health, maintenance, support, and education; and (2) shall not exercise discretion to make any distributions to any person in such class that will relieve any legal obligation of the beneficiary to support such person. Any net income not so paid shall be added to principal. In exercising this discretion, the Trustee may, but need not, consider any other resources of the Grantor's wife and issue, and it is the Grantor's hope, but not direction, that the Trustee will give primary consideration to the needs and desires of the Grantor's wife.

Model UTC § 814 provides that even if the trust agreement confers on a trustee extended discretion, the trustee still must exercise its discretionary power in good faith and in accordance with the terms and purposes of the trust and the interests of the beneficiaries. Unfortunately, the Model UTC does not define the term "good faith." The comment to § 814 states that the trustee's obligation to act in good faith is a fundamental concept of fiduciary law, "although there are different ways it can be expressed."⁵⁶

In general, the trustee's duty to act in "good faith" means that the trustee has a duty to act honestly,

and without fraud or collusion. It also may require the trustee to observe the common standards of decency, fairness, and reasonableness in accordance with the terms of the trust, the trust's purposes and the interests of the beneficiaries, as those interests are defined in the terms of the trust.⁵⁷ The trustee can-

No grant of discretion is ever absolute; a grantor cannot relieve a trustee of all accountability, because if the beneficiaries have no rights enforceable against the trustee, there is no trust.

not act in bad faith (e.g., for fraudulent, selfish, or improper purposes) or capriciously.⁵⁸

Although extended discretion may discourage challenges by remainder beneficiaries to the generosity of trustees, it also may make it difficult for a discretionary beneficiary to obtain judicial intervention when a trustee's judgments are highly

conservative with respect to matters that fall within the grantor's authorized purposes. There is little case law relating to the standard to be applied in deciding the appropriateness of a trustee's exercise of a power to make distributions from a trust where the discretion is unlimited.

Court intervention

In every U.S. jurisdiction, a trustee's exercise of discretionary authority, including absolute discretionary authority, is subject to judicial review.⁵⁹ In general, the exercise of discretion by a trustee who has extended discretion (e.g., "sole," "absolute," or "sole and absolute") cannot be upset unless the exercise is unreasonable.⁶⁰ These terms provide the trustee with greater latitude in exercising its discretion, but do not give it unlimited latitude. No grant of discretion is ever absolute; a grantor cannot relieve a trustee of all accountability, because if the beneficiaries have no rights enforceable against the trustee, there is no trust.⁶¹

A court generally will not instruct a trustee on how to exercise its discretion. It will, however, intervene in the exercise of a trustee's discretion to prevent the trustee from misinterpreting the trust agreement, abusing its discretion, acting in bad

⁵⁶ See comment to Model UTC § 1012 (Protection of Person Dealing with Trustee), which states, "The Code does not define 'good faith' for purposes of this and the next section [Certification of Trust]. Defining good faith with reference to the definition used in the state's commercial statutes would be consistent with the purpose of this section, which is to treat commercial transactions with trustees similar to other commercial transactions."

⁵⁷ See, e.g., 12 Del. C. § 101 (2018) (defining "good faith" for all purposes of Title 12 ("Decedents' Estates and Fiduciary Relations") as "honesty in fact and the observance of reasonable standards of fair dealing"), and N.H. Rev. Stat. Ann. § 564-B:103-30(A) (2017) (defining "good faith" with respect to a fiduciary and beneficiary "as the observance of common standards of honesty, decency, fairness, and reasonableness in accordance with the terms of the trust, the trust's purposes, and the interests of the beneficiaries as their interests are defined under the terms of the trust").

⁵⁸ Rounds, Jr. and Rounds, III, *Loring and Rounds: A Trustee's Handbook* § 3.5.3.2(a) (2017).

⁵⁹ Taback and Pratt, *supra* note 3.

⁶⁰ Porter, "Exercising Discretion and Managing Intergenerational Conflicts" (materials from the Chicago Estate Planning Council Meeting) (5/13/2009), p. 20. However, state statute may limit the extent to which a court may review a trustee's distribution discretion. See, e.g., S.D. Codified Laws § 55-1-43(3) (2009), which provides: "A court may review a trustee's distribution discretion only if the trustee: (a) Acts dishonestly; (b) Acts with an improper motive; or (c) Fails, if under a duty to do so, to act." The statute further provides, "A reasonableness standard may not be applied to the exercise of discretion by the trustee with regard to a discretionary interest. Other than for the three circumstances listed in this subdivision, a court has no jurisdiction to review the trustee's discretion or to force a distribution."

⁶¹ The grant of discretion simply establishes a range within which the trustee may act—the greater the grant of discretion, the broader the range. Comment to Model UTC § 814.

⁶² Restatement (Third) of Trusts § 87 comment d.

⁶³ Restatement (Third) of Trusts § 50 comment c and § 87 comment d.

⁶⁴ Restatement (Third) of Trusts § 50 comment b.

⁶⁵ *Id.*

⁶⁶ Halback, *supra* note 10, at 1429.

⁶⁷ Taback and Pratt, *supra* note 3, at 493.

⁶⁸ Model UTC § 814(a). The Model UTC uses the term "best interests" only in § 802(g), which requires the trustee to act in the best interests of the beneficiaries with respect to voting shares of stock and the selection of directors and managers of business entities solely owned by the trust.

⁶⁹ See also comment to Model UTC § 103 ("Except as limited by public policy, the extent of a beneficiary's interest is determined solely by the settlor's intent") and § 105 ("With only limited exceptions, the ... rights and interests of a beneficiary are as specified in the terms of the trust.")

⁷⁰ Comment to Model UTC § 105.

⁷¹ Restatement (Third) of Trusts § 87 comment c.

⁷² State law, however, may eliminate the reasonableness standard with respect to a trustee's discretion to make distributions. See, e.g., Nev. Rev. Stat. § 163.419 (2017) ("A trustee given discretion in a trust instrument that is

faith, or without regard to the terms and purposes of the trust or in the interests of the beneficiaries, or for some purpose or motive other than the accomplishment of the purposes of the discretionary power.⁶² A court also may intervene to prevent the trustee from failing to act, either arbitrarily or from a misunderstanding of the trustee's power or duty,⁶³ or if (in the absence of extended discretion) it finds that the distributions made, or not made, are unreasonable as a means of carrying out the terms of the trust.⁶⁴

Judicial intervention is not warranted simply because the court would have exercised the discretion differently.⁶⁵ In fact, it is reversible error for a court to "improve upon" the trustee's reasonable decision to distribute amounts it deems necessary and proper for a beneficiary's support and maintenance.⁶⁶ This is because judicial interference may undermine the grantor's intent in granting broad discretion to the trustee.⁶⁷

The Model UTC requires the trustee to exercise its discretion in accordance with the terms and purposes of the trust, and the "interests" (not the "best interests") of the beneficiaries.⁶⁸ Model UTC § 103(8) defines the "interests of the beneficiaries" as "the beneficial

interests as provided in the terms of the trust," and not as determined by the beneficiaries.⁶⁹ Absent some other restriction, a grantor is always free to specify the trust's terms to which the trustee must comply.⁷⁰ Because the words contained in the discretionary distribution provision are often the only indication of the grantor's intent, it is important that the drafter consider the choice of words carefully. Using the same terms in every trust, for every grantor, is inappropriate, and makes it difficult to determine what the grantor was, in fact, trying to accomplish.

Reasonableness

Ideally, the trust agreement will include a statement of the purposes of a trust, the purposes for which the trust was created, and of the general frame of mind in which the grantor wants the trustee to act. Litigation involving a trustee's abuse of discretion frequently involves a claim that the trustee, in exercising a power, has acted unreasonably (i.e., beyond the bounds of reasonable judgment).⁷¹

A court might impose a general standard of reasonableness even if the trust agreement does not expressly provide one.⁷² In some cases, there is an objective standard by which the reasonableness of the trustee's conduct can be measured, but expressed standards are not necessary in order for a good-faith decision of the trustee to be found unreasonable.⁷³ In either event, judicial intervention on the ground of abuse is called for, not because the court would have exercised the discretion differently, but because the trustee's decision is one that would not be accepted as reasonable by persons of prudence.⁷⁴ Model UTC § 814 (Discretionary Powers) does not impose an obligation that a trustee's decision be within the bounds of reasonable

judgment, although it recognizes that such an interpretive standard may be imposed by the courts if the document adds a standard whereby the reasonableness of the trustee's judgment can be tested.⁷⁵

The reasonableness standard can be eliminated through drafting. It is important to eliminate it because the standard is "mushy" and gives a court considerable discretion to overrule a trustee's exercise of discretion.⁷⁶

Below is sample language for eliminating the reasonableness standard of review:

The exercise of any Trustee's discretionary power shall be final unless such Trustee has acted in bad faith. The Grantor recognizes and intends that an effect of the preceding sentence is to eliminate the application of the reasonableness standard to the Trustee's exercise (or non-exercise) of its discretion to distribute the property of a fully discretionary trust created hereunder.

Fiduciary duties in decision making

In general, a trustee must administer a trust in good faith, in accordance with the terms and purposes of the trust, and in the interests of the beneficiaries.⁷⁷ A trustee must consider whether to exercise discretion or not—it cannot fail to deliberate, and cannot remain passive. A trustee breaches its duty if it refuses to make a determination regarding the exercise of discretion.

When exercising its discretion, the trustee should consider the distribution request in light of prior requests, and how the trustee has responded to them. The trustee should evidence in writing any exercise of its discretion, to create for the trust file a readily accessible history of distribution requests and decisions. Examples of what documents should be obtained to support the approval or denial of distribution requests include:⁷⁸

described as sole, absolute, uncontrolled, unrestricted or unfettered discretion, or with similar words, has no duty to act reasonably in the exercise of that discretion"), and S.D. Codified Laws § 55-1-43 ("A reasonableness standard may not be applied to the exercise of discretion by the trustee with regard to a discretionary interest.").

⁷³ See Ausness, *supra* note 53 (noting that the Restatement has adopted a reasonableness standard, but the Model UTC has not (but has chosen a good-faith standard)).

⁷⁴ Restatement (Third) of Trusts § 87 comment c.

⁷⁵ Comment to Model UTC § 814, *citing* Restatement (Second) of Trusts § 187 (similar).

⁷⁶ Porter, *supra* note 60.

⁷⁷ Model UTC § 801 (Duty to Administer Trust) and § 105(b)(2) (providing that the terms of the trust agreement cannot override the trustee's duties described in § 801).

⁷⁸ If the trust is a directed trust, the distribution fiduciary should prepare and compile the documents and information described, and then provide the trustee with a written direction to make the distribution.

- A written distribution request, including the reason the beneficiary is requesting the distribution (a request from a minor beneficiary should be made by the beneficiary's parent).
- Documents evidencing the information the trustee takes into account when considering distribution requests (e.g., tax returns, budgets, information about a beneficiary's other resources, etc.).
- A memo evidencing the trustee's consideration of the beneficiary's interest in the trust. If there are multiple beneficiaries, this should include an assessment of their interests, to ensure that the distribution is consistent with the trustee's duty of impartiality.⁷⁹

The trustee's file also should include a copy of the written approvals of all of the relevant fiduciaries.

When exercising its discretion, the trustee must be reasonably informed. The trustee must be intimately familiar with the terms of the trust agreement. This means that the trustee must read the entire agreement, and ideally, prepare an abstract of the most important provisions. It will be impossible for the trustee to exercise its discretion, or fulfill its other fiduciary duties, if the trustee is unaware of the nature and extent of those duties and its discretion, or of the grantor's intent, as expressed in the trust agreement. Even if the trustee acts in good faith, its decision regarding the exercise of discretion may be reversed if the trustee improperly interprets the trust agreement.⁸⁰

The trustee must administer the trust, and make distributions, impartially,⁸¹ and give due regard to the beneficiaries' respective interests (e.g., the current and the remainder beneficiaries).⁸² The duty to act impartially does not require

the trustee to treat the beneficiaries equally. The trustee must treat the beneficiaries equitably in light of the terms and purposes of the trust. If the grantor wants the trustee to favor the interests of one beneficiary over those of others, he or she should include appropriate guidance for the trustee in the trust agreement, including whether the trustee is authorized to deplete the trust principal in its entirety in favor of the primary beneficiary.⁸³

Below is sample language for this:

The Grantor desires (but does not direct) that the Trustee of any child's trust created hereunder will exercise its discretion hereunder and make distributions to or for the benefit of the Grantor's child, as the primary beneficiary of such trust, in accordance with the needs and desires of the primary beneficiary, as determined by the disinterested Trustee, in its sole and uncontrolled judgment, and such needs and desires will take precedence, even if such distributions deplete the trust estate in its entirety, leaving nothing for the secondary beneficiaries (i.e., the issue of the primary beneficiary) or the remainder beneficiaries. The Trustee's exercise of discretion to distribute or not to distribute trust income or principal to or for the benefit of the primary beneficiary shall not be subject to question by any person interested in the trust estate.

If the grantor wishes to relieve the trustee completely of its duty of impartiality with respect to the trustee's exercise of its discretion, the trust agreement should provide language to that effect. Below is sample language for this:

Whenever a Trustee has discretion to distribute trust income and/or principal among a class of beneficiaries, the Trustee shall have the full power and absolute discretion to exclude any beneficiary in such class from any such payments or applications of income or principal, and shall have no obligation to maintain or achieve equality among the beneficiaries of the subject trust. The Grantor hereby explicitly waives the Trustee's duty of impartiality with respect to distributions of trust property that are subject to the Trustee's discretion.

Other resources

Whether the trustee must consider a beneficiary's other resources before making a discretionary distribution is a frequently litigated issue. If the trust agreement is silent on the consideration of other resources, it is unlikely that the grantor specifically considered the issue. The trustee then must determine what would the grantor have intended, if the drafting attorney had presented the question to him.

⁷⁹ In *Hodges v. Johnson*, 177 A.3d 86 (N.H. 2017), the New Hampshire Supreme Court addressed the relationship between a trustee's duties to the beneficiaries and the power to decant (via the exercise of discretion) to a trust that eliminated the interests of some of the beneficiaries. The trial court voided the decantings *ab initio*, on the ground that the trustees exercised the decanting power "without considering the [plaintiff beneficiaries'] beneficial interests." On appeal, a divided court (2 to 1) affirmed the trial court's results, but on different grounds, concluding that the trustees violated the duty of impartiality by failing to give any consideration to the future beneficial interests of the plaintiff beneficiaries, even though those interests were contingent and non-vested.

⁸⁰ Restatement (Third) of Trusts § 50 comment c, Illustration 3.

⁸¹ Restatement (Third) of Trusts § 79(1).

⁸² Model UTC § 803. See also Restatement (Third) of Trusts § 50 comment f (in most sit-

uations, there is an inference that the beneficiary at the top of a line of descendants is favored over the beneficiary's own issue, and the settlor's spouse also is favored, whether or not an ancestor of the others).

⁸³ See Comment to Model UTC § 803, *citing* Restatement (Second) of Trusts § 183 comment a (1959).

⁸⁴ Restatement (Third) of Trusts § 50 comment e. Note, however, that the position of the Restatement (Third) is contrary to the position of the Restatement (Second) on this issue.

⁸⁵ Halback, *supra* note 10, at 1448.

⁸⁶ Restatement (Third) of Trusts § 50 comment e(1). See also *In re Murray*, 45 A.2d 636 (Maine 1946) (trustees who distributed money to beneficiary upon her request were surcharged because they did not use their discretion or judgment in authorizing distribution to beneficiary, and did not discover information regarding the beneficiary's financial situation that was readily available to them).

The general rule of construction is that the trustee must consider the beneficiary's other resources, but has some discretion in the matter.⁸⁴ However, numerous cases hold both for and against consideration of a beneficiary's other means of support, including state or local public assistance, and the same wording that is stressed in one case may be disregarded in the next.⁸⁵

If the trustee must or may consider a beneficiary's resources, the trustee must determine which resources will influence the trustee's exercise of discretion. A beneficiary's other resources usually include the beneficiary's income and other periodic receipts, such as pension and other annuity payments, and court-ordered support payments. In considering these resources, the trustee also should take into account whether an unemployed or underemployed beneficiary is unable or simply unwilling to work, whether the beneficiary's spouse has financial resources available to the beneficiary, and whether the beneficiary's parents have a legal obligation to support the beneficiary.

The trustee must act in a reasonable manner in attempting to ascertain the beneficiary's resources, and generally may rely on the beneficiary's representations and other readily available, minimally intrusive information requested of the beneficiary. For this purpose, the requested information probably will include the beneficiary's income tax returns, financial statements, balance sheet and budgets, as well as information regarding any other sources of support for the beneficiary (e.g., public benefits, alimony, parental support, etc.). Reliance on the beneficiary's representations will be inappropriate, however, when the trustee has reason to suspect that the information supplied is inaccurate or incomplete.⁸⁶

If the trust agreement allows, but does not require, the trustee to con-

sider a beneficiary's resources, the trustee affirmatively must determine under what circumstances it will consider them (if at all), and should consider how the beneficiary is using distributions the trust already has made to him or her (e.g., mandatory income).

Document whether there any conditions that must be satisfied in order for a distribution to be made (e.g., beneficiary must be a certain age, have attained a certain level of education, etc.).

If the trustee must consider the beneficiary's other resources, the trustee must take into account the legal obligation of another person to support the beneficiary. If the trustee did not take that into account, then someone other than the named beneficiary will indirectly receive the benefit of the trust, by being relieved of his obligation of support.

Best practices for trustees

When administering trusts, trustees should adopt policies and procedures for addressing the discretionary distributions. Some "best practices" may include:

- Read the trust agreement, and any amendments, letters of wishes, or affidavits from the grantor regarding the grantor's intent. Prepare a concise but accurate abstract of the agreement for reference by the trust administrator and staff.
- Determine and document the standard, if any, for making discretionary distributions, including any precatory lan-

guage in the trust agreement intended to guide the trustee in exercising its discretion.

- For trusts with multiple current beneficiaries, determine whether any beneficiary is the "primary beneficiary," and, if so, determine the circumstances under which discretion might be exercised in favor of the non-primary beneficiaries.
- Keep complete, accurate, and current records of the trust assets.
- Determine whether and which resources of the beneficiary must be considered when exercising discretion, and document the procedure for requesting or otherwise obtaining information about the resources.
- Document all beneficiary requests for distributions, as well as the trustee's response to them (i.e., decision to distribute or not distribute, and the basis for the decision).
- Document whether any conditions must be satisfied in order for a distribution to be made (e.g., beneficiary must be a certain age, have attained a certain level of education, etc.).
- Coordinate the trust's investment policy with required or anticipated distributions.

Conclusion

A fully discretionary trust provides the trustee with great flexibility, and allows it to adapt the administration of the trust to future circumstances. However, it also may place a heavy burden on the trustee to determine when and how to exercise the discretion. Careful drafting of the trust agreement, and thoughtful administration of the trust, will allow the trustee to make distributions in a manner that is consistent with the grantor's intent and the interests of the beneficiaries. ■