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Spendthrift and Discretionary Trusts: Alive and Well under the Uniform Trust Code

Alan Newman*

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I. Introduction

Among the provisions of the Uniform Trust Code (“UTC” or the “Code”) that have attracted the most attention¹ are those of Article 5: Creditor’s Claims; Spendthrift and Discretionary Trusts. Although much of the UTC is a codification of the common law of trusts,²

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¹ See, e.g., Mark Merric and Steven J. Oshins, *How Will Asset Protection of Spendthrift Trusts Be Affected by the UTC?*, 31 EST. PLAN. 478 (Oct. 2004).

² See UNIF. TRUST CODE, Prefatory Note (2005). The “common law of trusts” is, of course, difficult to pin down, particularly in recent years. As noted by Professor Halbach, during the latter part of the twentieth century, particularly during the 1990s, trust law “experienced a period of rigorous, comprehensive reexamination.” Edward C. Halbach, *Uniform Acts, Restatements, and Trends in American Trust Law at Century’s End*, 88 CAL. L. REV. 1877, 1881 (2000).

there are many differences among the states in their handling of various creditors' rights issues,³ and many jurisdictions have no law on some of those issues.⁴ As a result, there is no well-accepted, established common law on some of the issues addressed by Article 5. Further, while the UTC's approach to many creditors' rights issues is consistent with the common law in many states, in other respects the UTC's approach is innovative and differs from existing law in many states.⁵ In some ways, Article 5 enhances the asset protection planning traditionally afforded by trusts,⁶ while at least in the context of the right of a child, spouse, or former spouse of a beneficiary of a discretionary trust to compel distributions he or she can reach, in many states the UTC would enhance creditors' rights.⁷

This Article addresses spendthrift and discretionary trust issues under the UTC in a question and answer format that is intended to respond to concerns, issues, and claims that have been raised or made with respect to the UTC's creditors' rights provisions. As it demonstrates, much of the criticism the UTC has received over this subject is unwarranted. Some of the criticism, however, has been instrumental in recent revisions to creditors' rights provisions of the Code and its comments.⁸ While those revisions may not have satisfied all of the concerns of some of the UTC's critics, they clarify that the Code will not have the adverse effects on the protections trusts have traditionally provided that its critics predict.

II. Spendthrift: Protection and Exceptions

Sections 502 and 503 of the UTC address spendthrift provisions and the exceptions to the protection they provide. They are the best places to start to understand the UTC's creditors' rights provisions.

A. *What is the effect of a valid spendthrift provision?* Under UTC § 502(c), if the terms of the trust include a valid spendthrift provision, "except as otherwise provided in this [article], a creditor or assignee of the beneficiary may not reach the interest or a distribution by the trustee before its receipt by the beneficiary."⁹ Thus, as a general rule, most creditors of a beneficiary of a spendthrift trust may not reach the beneficiary's interest, or the assets of the trust (unless and until trust assets are distributed to the beneficiary and then reached by the creditor in the beneficiary's hands).

³ For a discussion of the different treatment states afford spendthrift provisions, for example, see IIA AUSTIN W. SCOTT & WILLIAM FRANKLIN FRATCHER, *THE LAW OF TRUSTS* § 152.1 (4th ed. 1987).

⁴ Professor Scott's treatise notes, for example, that "[t]here is little authority on the question whether the interest of the beneficiary of a spendthrift trust can be reached by persons against whom he has committed a tort." *Id.* at § 157.5. For two recent cases denying tort claimants access to criminal tortfeasors' interests in spendthrift trusts, see *Scheffel v. Krueger*, 782 A.2d 410 (N.H. 2001) and *Duvall v. McGee*, 826 A.2d 416 (Md. Ct. App. 2003).

⁵ For example, the UTC does not classify trusts as "discretionary trusts" or "support trusts" for creditors' rights purposes. See *infra* section VI.

⁶ For example, under the UTC, generally creditors of a beneficiary of a discretionary trust may not compel distributions they can reach even if they have provided support to the beneficiary and the trust is for the beneficiary's support. See *infra* section VI.

⁷ See *infra* notes 111-118 and accompanying text.

⁸ See *infra* notes 3576-3645 and accompanying text.

⁹ UNIF. TRUST CODE § 502(c) (2005).

1. *May the trustee make protected distributions from a spendthrift trust to third parties for the beneficiary's benefit?* The UTC does not explicitly address this question. Presumably, however, the answer is “yes.” Trust instruments commonly authorize the trustee to make distributions to third parties for the benefit of the beneficiary, as well as directly to the beneficiary.¹⁰ Section 502(c) prohibits a beneficiary's creditor from reaching a distribution “before its receipt by the beneficiary.”¹¹ Because a distribution for the benefit of a beneficiary that is made to a third party would never be received by the beneficiary, the beneficiary's creditor presumably would be unable to reach it. Thus, for example, it appears that distributions from a spendthrift trust in the form of payments to certain creditors of the beneficiary (for example, a credit card company or the lessor of an automobile to the beneficiary) would not be reachable by most creditors of the beneficiary.¹² Finally, while section 501 provides that a beneficiary's creditors may attach distributions “to or for the benefit of the beneficiary,” it explicitly applies only “[t]o the extent a beneficiary's interest is not subject to a spendthrift provision.”¹³

Protected indirect distributions for the benefit of a spendthrift trust beneficiary likely will also be allowed even if the instrument does not expressly authorize the trustee to make them. In such a case, presumably the beneficiary would have acquiesced in the indirect distributions¹⁴ and most creditors of a beneficiary of a spendthrift trust have no claim against the trustee, the trust assets, or the beneficiary's interest in the trust. The Restatement (Third) of Trusts contemplates that such distributions may be made by the trustee, although not in the context of creditor avoidance.¹⁵ Note, however, that the UTC's explicit authorization of a trustee to make distributions for the benefit of a beneficiary, instead of directly to the beneficiary, applies only with respect to incapacitated beneficiaries.¹⁶

2. *Are there limits on the size of a trust that may be protected by a spendthrift provision, or on the amount of distributions that may be made to or for the benefit of a beneficiary of a spendthrift trust?* No. Unlike the law in some states, the UTC does not limit the amount of protected distributions that may be made from a spendthrift trust to or for the benefit of its beneficiary to, for example, amounts necessary to provide for the beneficiary's support.¹⁷ Further, spendthrift protection is not limited by the size of the trust¹⁸ or to a fixed amount of annual income.¹⁹

¹⁰ Such provisions effectively define, in part, the beneficiary's interest in the trust. According to the Third Restatement, in determining the extent of the interest of a trust beneficiary, “[t]he terms of the trust . . . will be respected and given effect unless contrary to public policy.” RESTATEMENT (THIRD) OF TRUSTS § 49 cmt. a (2003).

¹¹ UNIF. TRUST CODE § 502(c) (2005).

¹² Note that UTC § 503(c) contemplates distributions for the benefit of the beneficiary, instead of directly to the beneficiary, by providing that the claim of a spendthrift exception creditor may reach distributions “to or for the benefit of the beneficiary.” UNIF. TRUST CODE § 503(c) (2005).

¹³ UNIF. TRUST CODE § 501 (2005).

¹⁴ See UNIF. TRUST CODE § 1009 (2005) (protecting the trustee from liability for conduct that otherwise would constitute a breach when there is a consent, release, or ratification by the beneficiary of the trustee's conduct).

¹⁵ See RESTATEMENT (THIRD) OF TRUSTS § 49 cmt. c (2003) (stating that “[a] trustee who improperly applies or distributes income in good faith for the support, care, or other needs of the beneficiary (whether or not under a legal disability) is entitled to credit in the trust accounts to the extent the beneficiary would otherwise be unjustly enriched.”).

¹⁶ See UNIF. TRUST CODE § 816(21) (2005).

¹⁷ For a discussion of statutes so limiting the effect of spendthrift provisions in a number of states, see IIA SCOTT & FRATCHER, *supra* note 3, at § 152.1.

B. *What constitutes a valid spendthrift provision?* A spendthrift provision is valid under the UTC “only if it restrains both voluntary and involuntary transfer of a beneficiary’s interest.”²⁰ As a result, a settlor may not provide spendthrift protection from the beneficiary’s creditors, while authorizing the beneficiary to voluntarily transfer the beneficiary’s interest.²¹ Thus, if the beneficiary may sell, encumber, or otherwise transfer the interest, the beneficiary’s creditors may reach it.²²

While spendthrift protection is available under the UTC only if there is a valid spendthrift provision,²³ it may not be necessary that the instrument itself include one. Under the Code, “spendthrift provision” is defined as a “term of a trust,”²⁴ and the “terms of a trust” are defined as “the manifestation of the settlor’s intent regarding a trust’s provisions as expressed in the trust instrument or as may be established by other evidence that would be admissible in a judicial proceeding.”²⁵ No magic words are required to evidence the settlor’s intent that the trust be spendthrift. Rather, for example, simply providing that the beneficiary’s interest is held subject to a “spendthrift trust” is sufficient.²⁶

C. *What creditors’ claims are not barred by a spendthrift provision?* Section 503 lists three creditors (“exception creditors”) who may reach a beneficiary’s interest in a spendthrift trust: (i) the beneficiary’s child, spouse, or former spouse who has a judgment or court order against the beneficiary for support or maintenance; (ii) a judgment creditor who has provided services for the protection of a beneficiary’s interest in the trust; and (iii) the state or the United States to the extent a statute of the state or federal law so provides.²⁷

¹⁸ Prior to its amendment in 2001, Virginia’s spendthrift statute limited its protection to \$1,000,000 of trust assets. VA. CODE ANN. § 55-19 (Michie 2001).

¹⁹ See, e.g., OKLA. STAT. ANN. tit. 60, § 175.25 (West 2001) (\$25,000 per calendar year protected).

²⁰ UNIF. TRUST CODE § 502(a) (2005). The UTC does not address the question whether a trust provision allowing the beneficiary to voluntarily transfer his or her interest, but only with the consent of a third party, sufficiently restrains the transfer to make the spendthrift provision valid.

²¹ In its enactment of the UTC, Missouri modified § 502(a) to validate a spendthrift provision that restrains either voluntary or involuntary transfers, or both. See MO. REV. STAT. §456.5-502.1 (2005).

²² Although the decision to bar the claim of a beneficiary’s creditor from reaching the beneficiary’s interest only if the beneficiary also is barred from voluntarily transferring it was policy based, the settlor effectively can give the beneficiary the power to assign the interest without jeopardizing spendthrift protection by giving the beneficiary a power of appointment. See David M. English, *The Uniform Trust Code (2000): Significant Provisions and Policy Issues*, 67 MO. L. REV. 143, 181 (2002).

²³ See UNIF. TRUST CODE § 502 (2005).

²⁴ UNIF. TRUST CODE § 103(15) (2005).

²⁵ UNIF. TRUST CODE § 103(17) (2005). Extrinsic evidence, if admissible in a judicial proceeding, that may establish terms of a trust include “[o]ral 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 settlor was otherwise silent, rules of construction.” UNIF. TRUST CODE § 103 cmt. (2005). Note that the UTC allows even unambiguous trust instruments, including wills creating testamentary trusts, to be reformed to correct mistakes of fact or law, whether of expression or inducement, if there is clear and convincing evidence of both the settlor’s intent and the terms of the trust. See UNIF. TRUST CODE § 415 (2005).

²⁶ See UNIF. TRUST CODE § 502(b) (2005). If the express terms of the trust impose a restraint on either voluntary or involuntary transfers, but not both, the intent to restrain the other may be implied. See IIA SCOTT & FRATCHER, *supra* note 3, at § 152.4.

²⁷ See UNIF. TRUST CODE § 503(b) (2005).

D. *Is the exception for claims of a child, spouse, or former spouse consistent with common law?* Yes.²⁸ As the comment to section 503 notes, this exception has been codified in many states and is consistent with federal bankruptcy law.²⁹ Of the first twelve jurisdictions to enact the UTC,³⁰ however, eight have modified this exception or deleted it entirely.³¹

E. *What kind of creditor might assert a claim against a spendthrift trust under the exception for the claim of a judgment creditor who has provided services for the protection of a beneficiary's interest in the trust?* An attorney is one example of such a creditor. The comment to section 503 notes that “[t]his exception allows a beneficiary of modest means to overcome an obstacle preventing the beneficiary’s obtaining services essential to the protection or enforcement of the beneficiary’s rights under the trust.”³²

1. *Is this exception consistent with common law?* It is consistent with the Restatements.³³ Case law, however, is sparse and not definitive, so it is difficult to determine what the common law on this subject is.³⁴

2. *Would this exception apply to allow another exception creditor of a beneficiary (for example, a child support or alimony claimant) who successfully asserts a claim against the beneficiary's interest in a spendthrift trust to recover his or her attorney's fees from the beneficiary's interest in the trust?* It should not. By its terms, this exception is for “a judgment creditor who has provided services for the protection of a beneficiary’s interest in the trust.”³⁵ An exception creditor of a beneficiary who reaches his or her interest in the trust would not have provided services for the protection of the beneficiary’s beneficial interest in the trust. Similarly, if a beneficiary’s former spouse is awarded his or her attorney’s fees against the beneficiary, the claim to recover such fees should not be recoverable against the beneficiary’s interest in the trust under the exception related to services provided for the protection of the

²⁸ See, e.g., RESTATEMENT (SECOND) OF TRUSTS § 157(a) (1959).

²⁹ UNIF. TRUST CODE § 503 cmt. (2005). Note also that the Employee Retirement Income Security Act requires qualified pension plans to subject a participant’s benefits to a qualified domestic relations order. See 29 U.S.C. § 1056(d)(3) (1997).

³⁰ Kansas (see KAN. STAT. ANN. §§ 58a-101 to 58a-1106 (2005)); Wyoming (see WYO. STAT. ANN. §§ 4-10-101 to 4-10-1001 (Michie 2005)); New Mexico (see N.M. STAT. ANN. §§ 46A-1-10 to 46A-11-1104 (Michie 2005)); Nebraska (see NEB. REV. STAT. ANN. §§ 30-3801 to 30-3810 (Michie 2005)); the District of Columbia (see D.C. CODE ANN. §§ 19-1301 to 19-1311.03 (2005)); Utah (see UTAH CODE ANN. §§ 75-7-101 to 75-7-1103 (2005)); Maine (see ME. REV. STAT. ANN. tit. 18B, §§ 101-1004 (West 2005)); Tennessee (see TENN. CODE ANN. §§ 35-15-101 to 35-15-1103 (2005)); New Hampshire (see N.H. REV. STAT. ANN. §§ 564-B: 1-101 to 564-B: 11-1104 (2005)); Missouri (see MO. REV. STAT. §§ 456.1-101 to 456.11-1106 (2005)); Arkansas (see 2005 Ark. Acts §§ 28-73-101 to 28-73-1105); Virginia (see 2005 Va. Acts ch. 31, §§ 55-541.01 to 55-551.06).

³¹ Arkansas, Kansas, Maine, and Tennessee do not protect children or spouses. See 2005 Ark. Acts § 28-73-503; KAN. STAT. ANN. § 58a-503 (2005); ME. REV. STAT. ANN. tit. 18B, § 503 (West 2005); TENN. CODE ANN. § 35-15-503 (2005). Wyoming, the District of Columbia, and Virginia protect children but not spouses. See WYO. STAT. ANN. § 4-10-503 (Michie 2005); D.C. CODE ANN. § 19-1305.03 (2005); 2005 Va. Acts ch. 31, § 55-545.03.B. New Hampshire limits a spouse’s protection by requiring that the judgment or court order for alimony “expressly specifies the alimony amount attributable to the most basic food, shelter and medical needs of the spouse or former spouse.” N.H. REV. STAT. ANN. § 564-B: 1-503 (2005).

³² UNIF. TRUST CODE § 503 cmt. (2005).

³³ See RESTATEMENT (SECOND) OF TRUSTS § 157(c) (1959); RESTATEMENT (THIRD) OF TRUSTS § 59(b) (2003).

³⁴ See RESTATEMENT (THIRD) OF TRUSTS § 59, Reporter’s Notes to cmts. (c) and (d) (2003).

³⁵ UNIF. TRUST CODE § 503(b)(2) (2005).

beneficiary's interest in the trust. Note, however, that under section 1004, "[i]n a judicial proceeding involving the administration of a trust, the court, as justice and equity may require, may award costs and expenses, including reasonably attorney's fees, to any party, to be paid by another party or from the trust that is the subject of the controversy."³⁶

F. Is the exception for claims of the state or the United States consistent with the common law? It is narrower than the exception for claims of the government under the Second Restatement. The UTC excepts from spendthrift protection claims of the state or the United States only to the extent another state statute or federal law so provides.³⁷ By contrast, the Second Restatement provides that a spendthrift provision will not protect the beneficiary's interest from a claim of a state or the United States without regard to whether another state statute or federal law so provides.³⁸

G. Does the exception for claims of the state or the United States allow the list of exception creditors to be expanded? If existing or new federal law allows the United States to reach the interests of beneficiaries in spendthrift trusts (to satisfy a beneficiary's federal income tax obligations, for example), it will preempt a state's version of the UTC (or any other state law).³⁹ Further, a state always has the prerogative of enacting new legislation, including legislation with respect to the enforceability of a spendthrift provision against a claim of the state, regardless of whether it has enacted the UTC.

1. Why does the UTC include a provision making the state a spendthrift exception creditor to the extent another statute of the state so provides? According to Professor English, the UTC Reporter, this exception "leav[es] to other state law the extent to which a state can pierce a trust to collect for the costs of institutionalized care."⁴⁰ If an enacting state had such a statute (or one that, for example, allowed it to reach spendthrift trusts to collect delinquent income taxes) and it enacted the UTC's spendthrift provisions without this exception, the newly enacted spendthrift provisions would be inconsistent with, and arguably would effectively repeal, the existing state statutes.

2. Why does this provision of the UTC also refer to claims of the United States? Perhaps simply for transparency purposes. As mentioned, under standard preemption doctrine, if federal law (whether existing at enactment or arising subsequent to enactment) allows the federal government to reach spendthrift trusts, it will not matter whether a state has or does not have a statute allowing such claims.⁴¹

³⁶ UNIF. TRUST CODE § 1004 (2005). According to the comment to § 1004, it "codifies the court's historic authority to award costs and fees, including reasonable attorney's fees, in judicial proceedings grounded in equity." *Id.* cmt.

³⁷ See UNIF. TRUST CODE § 503(b)(3) (2005).

³⁸ RESTATEMENT (SECOND) OF TRUSTS § 157(d) (1959)

³⁹ See, e.g., *La Salle Nat'l Bank v. U.S.*, 636 F. Supp. 874 (N.D. Ill. 1986); *U.S. v. Riggs Nat'l Bank*, 636 F. Supp. 172 (D.D.C. 1986); *First Northwestern Trust Co. v. I.R.S.*, 622 F.2d 387, 390 (8th Cir. 1980).

⁴⁰ English, *supra* note 22, at 183.

⁴¹ Thus, deleting the reference in UTC § 503(b)(3) to claims of the United States should have no substantive effect. For a § 503 enactment that includes an exception for claims of the state under other state statutes, but does not reference claims of the United States, see TENN. CODE ANN. § 35-15-503 (2005).

H. *Are claims of those who have provided necessities (for example, support) to the beneficiary barred by a spendthrift provision?* Yes. Unlike under the Restatements,⁴² the UTC provides that a spendthrift provision will bar the claims of those who provided necessities to the beneficiary.⁴³ The most important consequence of the UTC's omission of this exception from section 503 is that a reimbursement claim of a public benefits provider against a trust of which the recipient is a beneficiary would be barred by a spendthrift provision. While a state's reimbursement claim with respect to Medicaid benefits should be a part of its estate recovery program that will not arise until after the death of the beneficiary and the beneficiary's spouse,⁴⁴ reimbursement claims for other state provided public benefits will be barred by a spendthrift provision. The UTC does not include a necessities provider's spendthrift exception to avoid making law that would give the state a right to reimbursement from spendthrift trusts.⁴⁵ If, however, there is another state statute that gives the state such a right, the UTC will not affect the state's right to reimbursement from the trust under that other statute.⁴⁶ Thus, the UTC drafters chose not to address this policy oriented, public benefits issue one way or the other, instead leaving the issue to other state law.

I. *Under the UTC, may a tort claimant reach a beneficiary's interest in a spendthrift trust?* No. In another departure from the Restatements,⁴⁷ the UTC bars a tort claimant from reaching the interest of a beneficiary tortfeasor in a spendthrift trust, regardless of the nature of the beneficiary's conduct that gave rise to the tort claim. Under UTC section 502(c), creditors may not reach a beneficiary's interest in a spendthrift trust, "except as otherwise provided in this [article]."⁴⁸ There is no provision in Article 5 for a tort claimant exception (or for the court to recognize additional spendthrift exceptions on policy grounds).⁴⁹ Rather, the list of spendthrift exceptions in section 503 is expressly made exclusive by section 502(c).⁵⁰

J. *What rights does the UTC grant an exception creditor?* While the answer to this question under the UTC as initially promulgated was uncertain, the uncertainty has been removed by amendments made to the UTC and its comments in 2005. Section 503(c) now provides that: "A claimant against whom a spendthrift provision cannot be enforced may obtain from a court an order attaching present or future distributions to or for the benefit of the beneficiary."⁵¹ While section 503(c) does not explicitly provide that attachment is the exclusive UTC provided remedy for spendthrift exception creditors, its comment does.⁵²

⁴² See RESTATEMENT (THIRD) OF TRUSTS § 59(b) (2003); RESTATEMENT (SECOND) OF TRUSTS § 157(b) (1959).

⁴³ See UNIF. TRUST CODE §§ 502 and 503 (2005).

⁴⁴ See 42 U.S.C. § 1396p(b)(1) (1993).

⁴⁵ See David M. English, *Is There a Uniform Trust Act in Your Future?*, PROB. & PROP. 25, 31 (Jan.-Feb. 2000).

⁴⁶ See UNIF. TRUST CODE § 503(b)(3) (2005).

⁴⁷ See RESTATEMENT (THIRD) OF TRUSTS § 59 cmt. a (2003); RESTATEMENT (SECOND) OF TRUSTS § 157 cmt. a (1959).

⁴⁸ UNIF. TRUST CODE § 502(c) (2005).

⁴⁹ Further, the comment to § 503 specifically notes that the UTC drafters "declined to create an exception for tort claimants." UNIF. TRUST CODE § 503 cmt. (2005). For a case with compelling facts in which the court nevertheless refused to create a public policy, tort claimant exception to similar statutory spendthrift protection, see *Scheffel v. Krueger*, 782 A.2d 410 (N.H. 2001).

⁵⁰ UNIF. TRUST CODE § 502(c) (2005).

⁵¹ UNIF. TRUST CODE § 503(c) (2005). Prior to its amendment in 2005, § 503 specified attachment as a remedy for two of the three spendthrift exception creditors (a child or spousal support claimant and a judgment creditor who had provided services for the protection of the beneficiary's interest in the trust). See UNIF. TRUST CODE § 503(b)

1. *Would an exception creditor be able to attach discretionary as well as mandatory distributions?* Presumably, yes.⁵³ Section 503(c) allows attachment of present or future distributions without reference to such distributions being mandatory or discretionary.⁵⁴ Furthermore, in the context of a claim by a beneficiary's child, spouse, or former spouse with a judgment or court order for support, the comment to section 503 specifically provides that the child or spouse may reach discretionary distributions.⁵⁵

2. *Is allowing an exception creditor to attach discretionary distributions a change in the common law?* The law is not well settled on the question whether a creditor of a beneficiary of a discretionary trust may attach future discretionary distributions. This subject is discussed in section III.D.2.

3. *What are the rights of the United States with respect to the beneficiary of a discretionary trust who has unpaid federal income tax liabilities?* First, as previously noted, a spendthrift provision would be ineffective against such a claim, regardless of the terms of the UTC or other state law.⁵⁶ If the terms of the trust gave the trustee the discretion to make distributions for the beneficiary's support, the federal tax lien would attach to the beneficiary's interest in the trust.⁵⁷ If the trust instrument did not include a support standard and gave the trustee broad discretion with respect to distributions, the federal tax lien would not attach to the

(2004). The remedy for the state or the United States was not specified, perhaps on the assumption that the other state statute or federal law allowing the state or the United States to reach a spendthrift trust would provide a remedy. *See* UNIF. TRUST CODE § 503(c) (2004). Compounding the problem was an inconsistency in § 501 and its comment. Section 501, which allows creditors broader remedies than attachment, provided that it was applicable “[t]o the extent a beneficiary’s interest is not protected by a spendthrift provision.” UNIF. TRUST CODE § 501 (2004). That language arguably made the section’s broader remedies available not only to creditors of beneficiaries of trusts without spendthrift provisions, but also to exception creditors of trusts with spendthrift provisions. The comment to § 501, however, referred to it being applicable “[a]bsent a valid spendthrift provision.” UNIF. TRUST CODE § 501 cmt. (2004). The 2005 amendments resolve these uncertainties. First, the introductory clause of § 501 has been revised to read: “To the extent a beneficiary’s interest is not *subject to* a spendthrift provision...” UNIF. TRUST CODE § 501 (2005) (emphasis added). Second, the comment to § 501 also was amended in 2005. It now provides, in part:

This section applies only if the trust does not contain a spendthrift provision or the spendthrift provision does not apply to a particular beneficiary’s interest. A settlor may subject to spendthrift protection the interests of certain beneficiaries but not others. A settlor may also subject only a portion of the trust to spendthrift protection such as an interest in the income but not principal.

UNIF. TRUST CODE § 501 cmt. (2005).

⁵² *See* UNIF. TRUST CODE § 503 cmt. (2005). Note, however, that other creditor law of a jurisdiction may provide an exception creditor with additional remedies. *Id.*

⁵³ Note, though, that allowing a creditor to attach discretionary distributions the trustee chooses to make does not mean the creditor can compel discretionary distributions it can reach. *See* section IV.)

⁵⁴ *See* UNIF. TRUST CODE § 503(c) (2005).

⁵⁵ *See* UNIF. TRUST CODE § 503 cmt. (2005).

⁵⁶ *See supra* note 39 and accompanying text.

⁵⁷ *See* *Magavern v. United States*, 550 F.2d 797 (2d Cir. 1977), *aff’g* 415 F. Supp. 217 (W.D.N.Y. 1976), *cert. denied*, 434 U.S. 826. *See also* I.R.S. Chief Couns. Adv. 200036045 (May 16, 2000).

beneficiary's interest in the trust,⁵⁸ but the United States would be able to attach future distributions the trustee decided to make in the exercise of its discretion.⁵⁹

4. *If an exception creditor attaches distributions that otherwise would be made to the beneficiary, would the beneficiary be able to benefit from the trust before the creditor was paid in full?* Perhaps. Section 503(c), as amended in 2005, authorizes the court to “limit the [creditor’s] award to such relief as is appropriate under the circumstances.”⁶⁰ Presumably, this authority would allow the court to consider the beneficiary’s needs, as well as the claim of the exception creditor.⁶¹

K. *May a trustee withhold distributions from a beneficiary of a spendthrift trust to prevent the beneficiary’s creditor from reaching them in the hands of the beneficiary?* A trustee could withhold discretionary distributions.⁶² As previously discussed,⁶³ distributions presumably may be made from spendthrift trusts to third parties for the beneficiary’s benefit to prevent creditors from reaching them. If, however, a “mandatory distribution of income or principal, including a distribution upon termination of the trust,” is not made “to the beneficiary within a reasonable time after the designated distribution date,” the creditor may reach it.⁶⁴

I. *What is a “mandatory distribution”?* As originally promulgated, the UTC did not define “mandatory distribution.”⁶⁵ The comment to section 506 referred to them as distributions that are “required to be made by the express terms of the trust.”⁶⁶ Thus, if the terms of a trust require current distributions of all income, or a unitrust amount, or all or part of the principal at specified times, those amounts clearly would constitute mandatory distributions. In light of section 504(b), which prohibits most creditors from compelling discretionary distributions without regard to whether the trust terms include a support or other standard,⁶⁷

⁵⁸ See I.R.S. Chief Couns. Adv. 200036045 (May 16, 2000). See also *U.S. v. O’Shaughnessy*, 517 N.W.2d 574 (Minn. 1994) (holding that a beneficiary’s interest in a purely discretionary trust is not “property” or “any right to property,” within the meaning of the federal tax lien statute, before the trustee has exercised its discretionary power of distribution under the trust agreement).

⁵⁹ See *U.S. v. Cohn*, 855 F. Supp. 572 (D. Conn. 1994). See also Richard W. Nenno, *Delaware Asset Protection Trusts*, in 14A ASSET PROTECTION: DOMESTIC AND INTERNATIONAL LAW AND TACTICS (Duncan E. Osborne and Elizabeth Morgan Schurig eds. 1995).

⁶⁰ UNIF. TRUST CODE § 503(c) (2005).

⁶¹ Section 501, which addresses trusts the terms of which do not include spendthrift provisions, similarly allows the court to limit a creditor’s award as appropriate under the circumstances. UNIF. TRUST CODE § 501 (2005). Prior to its amendment in 2005, the comment to § 501 provided that the court could consider the support needs of a beneficiary and the beneficiary’s family. UNIF. TRUST CODE § 501 cmt. (2004). Because of concerns of the potential effect of that language on a beneficiary of a supplemental needs trust who was receiving public benefits, it was amended in 2005 to refer not to the “support needs” of the beneficiary and the beneficiary’s family, but to their “circumstances.” UNIF. TRUST CODE § 501 cmt. (2005). See note 81.

⁶² See *infra* section IV (discussing the inability of most creditors of a beneficiary to compel discretionary distributions).

⁶³ See *supra* notes 10-16 and accompanying text.

⁶⁴ UNIF. TRUST CODE § 506 (2005). Presumably a mandatory distribution made for the benefit of a beneficiary within the requisite reasonable time would preclude a creditor of a beneficiary from reaching the distribution under § 506. See *supra* notes 10-16 and accompanying text. To avoid any question in that regard, § 506 could be amended to instead refer to distributions made “to or for the benefit of the beneficiary.”

⁶⁵ See UNIF. TRUST CODE §§ 103 and 506 (2004).

⁶⁶ UNIF. TRUST CODE § 506 cmt. (2004).

⁶⁷ See *infra* section IV (discussing § 504(b)).

“mandatory distributions” arguably should not have been construed to include distributions subject to the trustee’s discretion, regardless of whether one or more standards (for example, support) were provided to guide the trustee in the exercise of its discretion.

Section 504(b), however, by its express terms applies to “a distribution that is subject to the trustee’s discretion....”⁶⁸ As a result, terms of a trust that do not expressly grant the trustee discretion and that mandate distributions pursuant to a support standard (for example, “the trustee shall make distributions of income and principal to provide for the beneficiary’s support”), arguably could be construed as describing “mandatory distributions” within the meaning of section 506 that are not covered by section 504(b). Section 504, however, “eliminates the distinction between discretionary and support trusts, unifying the rules for all trusts fitting within either of the former categories....By eliminating this distinction, the rights of a creditor are the same whether the distribution standard is discretionary, subject to a standard, or both.”⁶⁹ Thus, such an argument should be unsuccessful, section 504(b) should apply to trusts that require distributions for the beneficiary’s support, and such distributions should not be “mandatory distributions” within the meaning of section 506, as originally promulgated.

Because of concerns that were expressed in that regard, however, section 506 was amended in 2005 to include a definition of “mandatory distribution.”⁷⁰ Under the 2005 amendment, a mandatory distribution is:

a distribution of income or principal which the trustee is required to make to a beneficiary under the terms of the trust, including a distribution upon termination of the trust. The term 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 direction.⁷¹

2. *What is a “reasonable time” for the trustee to make a mandatory distribution?* The UTC does not address this question.⁷²

3. *May a creditor of a beneficiary reach distributions the trustee could, in the exercise of its discretion, make to or for the benefit of the beneficiary by arguing that the beneficiary could compel the distribution,⁷³ and thus that the distribution is a mandatory one that is subject to the creditor’s claim if not made within a reasonable time?* No. Such an argument would be to compel a discretionary distribution the creditor could reach. New section

⁶⁸ UNIF. TRUST CODE § 504(b) (2005).

⁶⁹ UNIF. TRUST CODE § 504 cmt. (2005).

⁷⁰ The amendment was intended to be clarifying: “No change of substance is intended by this amendment.” UNIF. TRUST CODE § 506 cmt. (2005).

⁷¹ UNIF. TRUST CODE § 506(a) (2005). Further, the comment to §506, also as amended in 2005, states: “Under both §§ 504 and 506, a trust is discretionary even if the discretion is expressed in the form of a standard, such as a provision directing a trustee to pay for a beneficiary’s support.” *Id.* cmt.

⁷² See UNIF. TRUST CODE § 506 & cmt. (2005).

⁷³ While § 504 prohibits most creditors of a beneficiary from compelling distributions, even if the trustee has abused its discretion or failed to comply with a standard for distributions, *see infra* section IV, it “does not limit the right of a beneficiary to maintain a judicial proceeding against a trustee for an abuse of discretion or failure to comply with a standard for distribution.” UNIF. TRUST CODE § 504(d) (2005).

506(a) explicitly defines “mandatory distributions” to exclude discretionary distributions⁷⁴ and section 504(b) expressly prohibits most creditors from compelling discretionary distributions.⁷⁵

III. In the Absence of a Spendthrift Provision

If a trust instrument does not include a spendthrift provision, the rights of creditors of a beneficiary who is not a settlor of the trust are addressed in section 501.

A. *Is section 501 applicable only to trusts the terms of which do not include spendthrift provisions?* Yes. While the answer to that question was not clear under the Code as originally promulgated, it has been clarified by the 2005 amendments.⁷⁶ Section 501 is now applicable only “[t]o the extent a beneficiary’s interest is not subject to a spendthrift provision.”⁷⁷ Its comment explicitly provides that section 501 “applies only if the trust does not contain a spendthrift provision or the spendthrift provision does not apply to a particular beneficiary’s interest.”⁷⁸

B. *If the instrument does not include a spendthrift provision, what rights does a creditor of a trust beneficiary have?* In such a case, “the court may authorize a creditor or assignee of the beneficiary to reach the beneficiary’s interest by attachment of present or future distributions to or for the benefit of the beneficiary or other means.”⁷⁹

C. *If the instrument does not include a spendthrift provision and a creditor properly asserts a claim under section 501, would the beneficiary be able to benefit from the trust before the creditor is paid in full?* Perhaps. Under section 501, “[t]he court may limit the [creditor’s] award to such relief as is appropriate under the circumstances.”⁸⁰ The comment explains that, “[i]n exercising its discretion to limit relief, the court may appropriately consider the circumstances of a beneficiary and the beneficiary’s family.”⁸¹

D. *In the absence of a spendthrift provision, do the creditor’s rights depend on whether the beneficiary has a right to receive mandatory distributions or whether distributions are at the trustee’s discretion?* Yes.

1. *What if the beneficiary has a right to receive mandatory distributions?* If the beneficiary is entitled to receive mandatory distributions, or to have them made for his or her

⁷⁴ UNIF. TRUST CODE § 506(a) (2005).

⁷⁵ See UNIF. TRUST CODE § 504(b) (2005) (stating that “a creditor of a beneficiary may not compel a distribution that is subject to the trustee’s discretion, even if ... the discretion is expressed in the form of a standard of distribution...”). See also *infra* section IV (discussing § 504(b)).

⁷⁶ See *supra* note 51.

⁷⁷ UNIF. TRUST CODE § 501 (2005).

⁷⁸ UNIF. TRUST CODE § 501 cmt. (2005).

⁷⁹ UNIF. TRUST CODE § 501 (2005).

⁸⁰ UNIF. TRUST CODE § 501 (2005).

⁸¹ UNIF. TRUST CODE § 501 cmt. (2005). Prior to its amendment in 2005, the comment referred not to the “circumstances” of the beneficiary and the beneficiary’s family, but to their “support needs.” UNIF. TRUST CODE § 501 cmt. (2004). The change was made to avoid a potential argument that a supplemental needs trust could be treated as available for the beneficiary’s support and thus disqualify the beneficiary from receiving public benefits.

benefit (for example, all income, a unitrust amount, or one-third of the trust assets upon reaching a designated age), the creditor's remedies include attaching those distribution rights.⁸² In such a case, the trustee must pay the creditor instead of the beneficiary part or all of the amount⁸³ distributable to or for the benefit of the beneficiary.⁸⁴

2. *What if there is no spendthrift provision and distributions are at the trustee's discretion instead of mandatory?* If the trustee is authorized to make discretionary distributions to or for the benefit of the beneficiary, most creditors of the beneficiary may not compel the trustee to exercise its discretion to make distributions they can reach.⁸⁵ If, however, the trustee decides to make a discretionary distribution to or for the benefit of the beneficiary (and the terms of the trust do not include a spendthrift provision), part or all⁸⁶ of the distribution must be paid to the creditor. Case law in a number of states supports the UTC's allowing a beneficiary's creditor to attach future discretionary distributions (in the absence of a spendthrift provision).⁸⁷ There are also states in which the creditor may not do so,⁸⁸ and there likely are states in which this issue has not been addressed.

E. *If the terms of the trust do not include a spendthrift provision, would a creditor be able to force a judicial sale of the beneficiary's interest?* Perhaps. Section 501 provides that in the absence of a spendthrift provision, a beneficiary's creditor may reach the beneficiary's interest by attachment "or other means."⁸⁹ Creditors' remedies under section 501, however, are at the court's discretion, as the section provides that "[t]o the extent a beneficiary's interest is not subject to a spendthrift provision, the court *may authorize* a creditor or assignee of the beneficiary to reach the beneficiary's interest by attachment of present or future distributions to

⁸² See UNIF. TRUST CODE § 501 (2005).

⁸³ See *supra* notes 80-81 and accompanying text.

⁸⁴ The comment to § 501 notes that it

does not prescribe the procedures for reaching a beneficiary's interest or of priority among claimants, leaving those issues to the enacting State's laws on creditor rights. The section does clarify, however, that an order obtained against the trustee, whatever state procedure may have been used, may extend to future distributions whether made directly to the beneficiary or to others for the beneficiary's benefit. By allowing an order to extend to future payments, the need for the creditor periodically to return to court will be reduced.

UNIF. TRUST CODE § 501 cmt. (2005). Prior to its amendment in 2005, the comment also included a general description of the process by which a creditor would pursue its claim, along with the statement that the creditor could, "in theory, force a judicial sale of a beneficiary's interest." UNIF. TRUST CODE § 501 cmt. (2004). The 2005 amendment of the comment deleted the general description and the reference to a judicial sale. See UNIF. TRUST CODE § 501 cmt. (2005).

⁸⁵ See *infra* section IV.

⁸⁶ See *supra* notes 80-81 and accompanying text.

⁸⁷ See RESTATEMENT (THIRD) OF TRUSTS § 60, Reporter's Notes to cmts. b and c (2003). See also RESTATEMENT (SECOND) OF TRUSTS § 155(2) (1959) (stating that a trustee of a discretionary trust who has notice of a creditor's claim and who makes a discretionary distribution to the beneficiary is liable to the creditor for the amount of the distribution).

⁸⁸ See, e.g., *Shelley v. Shelley*, 354 P.2d 282, 289 (Or. 1960); *Samson v. Bertok*, 1986 WL 14819 (Ohio Ct. App. 1986).

⁸⁹ UNIF. TRUST CODE § 501 (2005).

or for the benefit of the beneficiary or other means.”⁹⁰ The remedy a court would authorize in a given situation likely would depend on the circumstances.⁹¹

1. *What would guide a court in deciding whether to order a judicial sale of a beneficiary’s interest?* The UTC does not address this question. Under section 106: “The common law of trusts and principles of equity supplement this [Code], except to the extent modified by this [Code] or another statute of this State.”⁹² Thus, if an enacting state had case law on this subject,⁹³ a court presumably would follow it. A court might also look to the Restatements.⁹⁴ Under the Third Restatement, a beneficiary’s discretionary trust interest is not subject to execution sale.⁹⁵ Under the Second Restatement: “If the interest of the beneficiary of a trust is so indefinite or contingent that it cannot be sold with fairness to both the creditors and the beneficiary, it cannot be reached by his creditors.”⁹⁶

2. *Is the UTC’s allowance of a judicial sale of a beneficiary’s interest (in the absence of a spendthrift provision) a change in the common law?* No. A beneficiary’s interest in a trust “is now generally recognized as a property right and liable for the beneficiary’s debts equally with his legal interests, unless specially exempted by statute or by direction of the settlor” (footnotes omitted).⁹⁷ The general rule of the Second Restatement is that “creditors of the beneficiary of a trust can by appropriate proceedings reach his interest and thereby subject it to the satisfaction of their claims against him.”⁹⁸ That this rule contemplates judicial sales of beneficial interests is evident in the exception under the Second Restatement under which such a sale is not allowed if it could not be accomplished in a fair manner with respect to both the beneficiary and the creditor.⁹⁹ Given the almost universal use of spendthrift provisions,¹⁰⁰ the

⁹⁰ *Id.* (emphasis added). Prior to its amendment in 2005, the comment to § 501 stated: “The creditor may also, in theory, force a judicial sale of a beneficiary’s interest.” UNIF. TRUST CODE § 501 cmt. (2004). That statement, along with the rest of the paragraph in which it was included, was deleted from the comment in 2005. *See* UNIF. TRUST CODE § 501 cmt. (2005).

⁹¹ As noted in Professor Scott’s treatise: “In a proceeding in equity to reach the interest of the beneficiary of a trust, the court will give to the creditor such relief as is under all the circumstances fair and reasonable.” IIA SCOTT & FRATCHER, *supra* note 3, at § 147.2.

⁹² UNIF. TRUST CODE § 106 (2005).

⁹³ *See, e.g.,* Showalter v. G. H. Nunnelley Co., 257 S.W. 1027 (Ky. 1924) (appointing a receiver to provide for the payment of the debt of an income beneficiary’s creditor out of trust income, rather than ordering a sale of the interest, because of concerns that a sale would prejudice both the creditor and the debtor/beneficiary).

⁹⁴ The comment to § 106 notes the Restatements as sources of the common law of trusts and principles of equity that supplement the Code. UNIF. TRUST CODE § 106 cmt. (2005).

⁹⁵ *See* RESTATEMENT (THIRD) OF TRUSTS § 60 cmt. c (2003).

⁹⁶ RESTATEMENT (SECOND) OF TRUSTS § 162 (1959).

⁹⁷ GEORGE GLEASON BOGERT & GEORGE TAYLOR BOGERT, THE LAW OF TRUSTS AND TRUSTEES § 193 (rev. 2d ed. 1992).

⁹⁸ RESTATEMENT (SECOND) OF TRUSTS § 147 (1959). *See also* IIA SCOTT & FRATCHER, *supra* note 3, at § 147.2; BOGERT & BOGERT, *supra* note 97, at § 193.

⁹⁹ *See* RESTATEMENT (SECOND) OF TRUSTS § 162 (1959).

¹⁰⁰ *See* Alan Newman, *The Rights of Creditors of Beneficiaries Under the Uniform Trust Code: An Examination of the Compromise*, 69 TENN. L. REV. 771, 777 n.36 (2002). Note, however, that while spendthrift provisions provide substantial protection against claims of beneficiaries’ creditors, they reduce beneficiaries’ flexibility in dealing with their trust interests. *See* KATHRYN G. HENKEL, ESTATE PLANNING AND WEALTH PRESERVATION ¶ 4.02[2][d] (1997); JOHN R. PRICE, PRICE ON CONTEMPORARY ESTATE PLANNING 896-97 (1992); Howard M. Zaritsky, *A QPRT Checklist*, PROB. PRAC. REP. 1, 3-4 (May 2000).

UTC's limitation of the remedies available to spendthrift exception creditors to attachment,¹⁰¹ and the prohibition on sales of discretionary interests under the Third Restatement, judicial sales of beneficial interests in a UTC enacting jurisdiction should continue to be very rare.

IV. The Inability of Creditors of Beneficiaries to Compel Discretionary Distributions They Can Reach

Whether a creditor of a beneficiary of a discretionary trust may compel distributions the creditor can reach is addressed by section 504. It applies regardless of whether the trust instrument includes a valid spendthrift provision.¹⁰²

A. *May a creditor of a beneficiary of a third-party created trust force the trustee to make discretionary distributions the creditor can reach?* Generally, no. In another departure from the Third Restatement (that may be more apparent than real¹⁰³), section 504(b) provides the general rule: “[W]hether or not a trust contains a spendthrift provision, a creditor of a beneficiary may not compel a distribution that is subject to the trustee’s discretion, even if: (1) the discretion is expressed in the form of a standard of distribution; or (2) the trustee has abused the discretion.”¹⁰⁴

1. *What if the trust terms require the trustee to make distributions for the beneficiary’s support?* Section 504(b) prohibits most creditors from compelling a distribution “that is subject to the trustee’s discretion.”¹⁰⁵ If the terms of the trust require distributions for support (for example, “the trustee shall make distributions of income and principal for the beneficiary’s support”), an argument can be made that the prohibition of section 504(b) is not applicable, because the required support distributions arguably would not be subject to the trustee’s discretion within the meaning of section 504(b). For at least four reasons, such an argument would fail. First, section 504(b)(1) makes the general rule applicable to discretionary distributions “even if...the discretion is expressed in the form of a standard of distribution.”¹⁰⁶ Thus, the use of a standard of distribution in the terms of the trust is treated by the statute as a grant of discretion over distributions. Second, the comment to section 504 notes that the section does not distinguish between support and discretionary trusts and refers to a provision in the

¹⁰¹ See UNIF. TRUST CODE § 503(c) (2005).

¹⁰² UNIF. TRUST CODE § 504(b) (2005).

¹⁰³ See RESTATEMENT (THIRD) OF TRUSTS § 60 cmt. e (2003). Under comment e to § 60, a beneficiary’s creditor, as well as the beneficiary, is entitled to judicial protection against an abuse of discretion by the trustee. *Id.* However, the comment also provides that a trustee’s exercise of its discretion might not be actionable by a creditor in circumstances when it would be actionable by the beneficiary. *Id.* The explanation for the difference in treatment is that

the extent to which the designated beneficiary might actually benefit from a distribution is relevant to the justification and reasonableness of the trustee’s decision in relation to the settlor’s purposes and the effects on other beneficiaries.... Thus, the balancing process typical of discretionary issues becomes, in this context, significantly weighted against creditors....

Id.

¹⁰⁴ UNIF. TRUST CODE § 504(b) (2005).

¹⁰⁵ *Id.*

¹⁰⁶ UNIF. TRUST CODE § 504(b)(1) (2005).

Third Restatement under which support trusts are treated as discretionary trusts with support standards.¹⁰⁷ Third, if such terms – “the trustee shall make distributions of income and principal for the beneficiary’s support” – are not treated as providing for distributions at the trustee’s discretion, presumably they would have to be treated as calling for mandatory distributions. As discussed in section II.K.1, above, however, the 2005 amendments to the UTC explicitly define mandatory distributions to exclude distributions pursuant to a standard. Fourth, the comment to section 506, as amended in 2005, explicitly states that a trust is discretionary even if it includes “a provision directing a trustee to pay for a beneficiary’s support.”¹⁰⁸

2. *If the creditor’s claim is based on having provided support to the beneficiary, and the trust terms include a support standard for distributions, may the creditor compel distributions it can reach to reimburse it for the support it provided to the beneficiary?* No. Under the UTC, no creditor of a beneficiary (including the state) may compel discretionary distributions to satisfy claims based on the creditor having provided support to the beneficiary.¹⁰⁹ In this regard, the UTC provides greater protection against creditors’ claims than does the law in some states.¹¹⁰

B. *Does the UTC allow any creditor of a beneficiary of a third-party created trust to compel distributions the creditor can reach?* Yes. There is an exception to the general rule of section 504(b). Under section 504(c)(1), in specified circumstances the court may order discretionary distributions that the beneficiary’s child, spouse, or former spouse can reach.¹¹¹

1. *Under what circumstances may such a creditor compel distributions he or she can reach?* There are three limitations on the ability of a beneficiary’s child, spouse, or former spouse to compel discretionary distributions he or she can reach. First, the child, spouse, or former spouse must have a judgment or court order against the beneficiary for support or maintenance.¹¹² Second, section 504(c)(1) does not require the court to order a distribution to satisfy such a judgment or court order. Rather, it authorizes the court to do so.¹¹³ Third, such an order may be entered only “[t]o the extent a trustee has not complied with a standard of distribution or has abused a discretion.”¹¹⁴ Presumably, the burden will be on the creditor to establish the trustee’s failure to comply with a standard of distribution or abuse of discretion.

2. *Would the court order the trustee to satisfy the entire amount of the unpaid child or spousal support or alimony?* Presumably a court often would do so, but that will

¹⁰⁷ See UNIF. TRUST CODE § 504 cmt. (2005), citing RESTATEMENT (THIRD) OF TRUSTS § 60, Reporter’s Notes to cmt. a (2003).

¹⁰⁸ UNIF. TRUST CODE § 506 cmt. (2005).

¹⁰⁹ See UNIF. TRUST CODE § 504(b) (2005).

¹¹⁰ See, e.g., *Bureau of Support v. Kreitzer*, 243 N.E.2d 83 (Ohio 1968); *Estate of Lackmann*, 320 P.2d 186, 189 (Cal. Ct. App. 1958); *Constanza v. Verona*, 137 A.2d 614, 617 (N.J. Ch. Div. 1958); *Cronin’s Case*, 192 A. 397, 401 (Pa. 1937); *State v. Rubion*, 308 S.W.2d 4, 11 (Tex. 1958). See also IIA SCOTT & FRATCHER, *supra* note 3, at § 157.2.

¹¹¹ See UNIF. TRUST CODE § 504(c)(1) (2005). Note that because these creditors also are exception creditors with respect to spendthrift protection under § 503(b), they may compel distributions from discretionary spendthrift trusts. See UNIF. TRUST CODE § 503(b)(1) (2005).

¹¹² See UNIF. TRUST CODE § 504(c)(1) (2005).

¹¹³ *Id.*

¹¹⁴ UNIF. TRUST CODE § 504(c) (2005).

not necessarily be the case. Rather, the amount awarded to the child, spouse, or former spouse for back support would depend on the circumstances. Under section 504(c)(2), the court is to order payment to the child, spouse, or former spouse of “such amount as is equitable under the circumstances but not more than the amount the trustee would have been required to distribute to or for the benefit of the beneficiary had the trustee complied with the standard or not abused the discretion.”¹¹⁵ According to the comment to the section, however, “[b]efore fixing this amount, the court ... should consider that in setting the respective support award, the family court has already considered the respective needs and assets of the family.”¹¹⁶

3. *Under non-UTC trust law, may a beneficiary’s child, spouse, or former spouse, with a court order or judgment for support or maintenance, compel discretionary distributions they can reach?* According to the Third Restatement,¹¹⁷ there is some support – in the context of a trust for the support of the beneficiary – for this policy-oriented rule of the UTC,¹¹⁸ but it likely would make new law in many jurisdictions, particularly as to trusts that do not include support standards for discretionary distributions.¹¹⁹

4. *Does the inability of creditors (other than a child, spouse, or former spouse with a judgment or court order for support or maintenance) to compel discretionary distributions affect the beneficiary’s ability to do so?* No. Section 504(d) provides: “This section does not limit the right of a beneficiary to maintain a judicial proceeding against a trustee for an abuse of discretion or failure to comply with a standard for distribution.”¹²⁰

V. Creditors’ Claims Against a Beneficiary/Settlor

If a beneficiary also is a settlor of a trust, the rights of his or her creditors under the UTC are governed by section 505.

¹¹⁵ UNIF. TRUST CODE § 504(c)(2) (2005).

¹¹⁶ UNIF. TRUST CODE § 504 cmt. (2005).

¹¹⁷ See RESTATEMENT (THIRD) OF TRUSTS § 60, Reporter’s Note to cmt. e (2003).

¹¹⁸ See RESTATEMENT (THIRD) OF TRUSTS § 60, Reporter’s Note to cmt. e (2003). [For a recent case upholding a lower court’s order directing the trustee of a third-party created discretionary support trust to pay the beneficiary’s child support obligations, see *Drevenik v. Nardone*, 862 A.2d 635 \(Pa. Super. 2004\).](#)

¹¹⁹ See IIA SCOTT & FRATCHER, *supra* note 3, at § 155. See also Carolyn L. Dessin, *Feed a Trust and Starve a Child: The Effectiveness of Trust Protective Techniques Against Claims for Support and Alimony*, 10 GA. ST. U. L. REV. 691 (1994); M.L. Cross, Annotation, *Trust Income or Assets as Subject to Claim Against Beneficiary for Alimony, Maintenance, or Child Support*, 91 A.L.R.2d 262 (1963). The UTC’s exception allowing a child, spouse, or former spouse with a judgment or court order for support to compel discretionary distributions has been deleted in five of the twelve jurisdictions that have adopted a version of the UTC: Arkansas (*see* 2005 Ark. Acts § 28-73-504); Kansas (*see* KAN. STAT. ANN. § 58a-502 (2005)); Maine (*see* ME. REV. STAT. ANN. tit. 18B, § 504 (West 2005)); Tennessee (*see* TENN. CODE ANN. § 35-15-504 (2005)); and Missouri (*see* MO. ANN. STAT. § 456.5-504 (West 2005)). Wyoming and Virginia provide the protection of § 504(c) to child support, but not spousal support, claimants. *See* WYO. STAT. ANN. § 4-10-504 (Michie 2005); 2005 Va. Acts ch. 31, § 55-545.04.C. The § 504(c) exception has been enacted in New Mexico (*see* N.M. STAT. ANN. § 46A-5-504 (Michie 2005)); Nebraska (*see* NEB. REV. STAT. ANN. § 30-3849 (Michie 2005)); Utah (*see* UTAH CODE ANN. § 75-7-504 (2005)); and New Hampshire (*see* N.H. REV. STAT. ANN. § 564-B: 5-504 (2005)). The District of Columbia’s UTC enactment does not include § 504 at all, but reserves the appropriate section number. *See* D.C. CODE ANN. § 19-1305.04 (2005)

¹²⁰ UNIF. TRUST CODE § 504(d) (2005).

A. *May the creditors of a settlor of a revocable trust reach the trust assets during the settlor's lifetime?* Yes. Section 505(a) so provides, regardless of whether the terms of the trust include a spendthrift provision.¹²¹

1. *Is the holder of a power of withdrawal from a third-party created trust treated as the settlor of a revocable trust for creditors' rights purposes?* Yes, but only during the period the power may be exercised, and only to the extent of the property subject to the power.¹²²

2. *Does that mean that the creditor of a Crummey power holder may reach property subject to the Crummey withdrawal right?* Yes, but again, only during the period the power may be exercised. In order to reach property subject to the withdrawal power, the creditor would have "to take action prior to the expiration of the [withdrawal] period."¹²³ The question of what action the creditor would have to take during the withdrawal period is not addressed.

3. *If the power holder allows the power to lapse, or releases or waives it, will the power holder thereafter be treated as the settlor of a revocable trust for creditors' rights purposes as to a portion of the trust determined by reference to the amount the power holder could have, but did not, withdraw?* The power holder will not be so treated if the amount subject to withdrawal was limited to the greater of the federal gift tax annual exclusion amount¹²⁴ (determined without regard to gift splitting) or the five or five amount¹²⁵ under the Internal Revenue Code. With respect to any excess, such as would exist when a hanging power is used and is outstanding, the power holder will be treated as the settlor of a revocable trust for creditors' rights purposes.¹²⁶

4. *Is the UTC's treatment of the holder of a power of withdrawal as the settlor of a revocable trust for creditors' rights purposes a change in the common law?*

According to the Restatement ([Second](#)) of Property, this rule of the UTC is inconsistent with the law of most states.¹²⁷ There is not uniformity in non-UTC law on this subject, however, [and the current draft of the Restatement \(Third\) of Property adopts the UTC rule.](#)¹²⁸ The rule under the Restatement ([Second](#)) of Property is that creditors of an unexercised, presently exercisable general power of appointment may not reach the property subject to the power except to the

¹²¹ See UNIF. TRUST CODE § 505(a)(1) (2005). While the UTC does not explicitly recognize homestead rights and other exemptions from creditors' claims under other state law as limitations on creditors' rights under § 505(a), it cites a comment to the Third Restatement that does so. See UNIF. TRUST CODE § 505 cmt. (2005), *citing* RESTATEMENT (THIRD) OF TRUSTS § 25 cmt. e (2003) (stating that property held in a revocable trust is subject to claims of the settlor's creditors "if the same property belonging to the settlor... would be subject to the claims of the creditors, taking account of homestead rights and other exemptions."). Further, the General Comment to § 505 explicitly provides that Article 5 does not supersede state exemption statutes (nor state fraudulent transfer acts). See UNIF. TRUST CODE Art. 5, gen. cmt. (2005).

¹²² See UNIF. TRUST CODE § 505(b)(1) (2005).

¹²³ UNIF. TRUST CODE § 505 cmt. (2005).

¹²⁴ See I.R.C. § 2503(b) (1994).

¹²⁵ See I.R.C. §§ 2041(b)(2) and 2514(e) (1994).

¹²⁶ See UNIF. TRUST CODE § 505(b)(2) (2005).

¹²⁷ See RESTATEMENT (SECOND) OF PROPERTY: DONATIVE TRANSFERS § 13.2, Reporter's Note (1986).

¹²⁸ [See RESTATEMENT \(THIRD\) OF PROPERTY: WILLS AND OTHER DONATIVE TRANSFERS § 20.3 \(Preliminary Draft No. 11, 2005\).](#)

extent a statute provides otherwise.¹²⁹ Statutes in a number of states so provide,¹³⁰ although in most, creditors may reach the appointive assets only if other property available for payment of their claims is insufficient.¹³¹ The rule under the Restatement (Third) of Trusts,¹³² and under federal bankruptcy law,¹³³ is that the power holder's creditors may reach property subject to a presently exercisable general power of appointment. Case law in several states is to the contrary,¹³⁴ as are statutes in Alaska and Rhode Island that do not allow a power holder's creditors to reach the property subject to the power unless it not only is a general power, but also is exercised in favor of the holder, the holder's estate, or the creditors of either.¹³⁵ The rationale for the UTC rule, which treats "a power of withdrawal as the equivalent of a power of revocation [is that] the two powers are functionally equivalent."¹³⁶

5. *May a beneficiary serve as a trustee of a third-party created trust (for example, a surviving spouse as trustee of a credit shelter trust) without being treated as the settlor of a revocable trust for creditors' rights purposes?* Section 505(b)(1) provides that the holder of a "power of withdrawal" is treated as the settlor of a revocable trust (during the period the power may be exercised and with respect to the property subject to the power).¹³⁷ The term "power of withdrawal" initially was defined as "a presently exercisable general power of appointment other than a power exercisable only upon consent of the trustee or a person holding an adverse interest."¹³⁸ Although the UTC does not define a "presently exercisable general power of appointment,"¹³⁹ arguably a trustee/beneficiary's power to distribute to him or herself, even if limited by an ascertainable standard relating to health, education, maintenance, or support, would be such a power that would cause the trustee/beneficiary to be treated as the settlor of a revocable trust for creditors' rights purposes under section 505(b)(1).¹⁴⁰ To avoid such a result,

¹²⁹ See RESTATEMENT (SECOND) OF PROPERTY: DONATIVE TRANSFERS § 13.2 (1986).

¹³⁰ See, e.g., N.Y. EST. POWERS & TRUSTS LAW §§ 10-7.2 and 10-7.4 (McKinney 1998).

¹³¹ See CAL. CIV. CODE § 1390.3 (West 1982); MICH. COMP. LAWS § 556.123 (1979); MINN. STAT. § 502.70 (1982); OKLA. STAT. tit. 60, § 299.9 (1981); WIS. STAT. § 702.17 (1980).

¹³² See RESTATEMENT (THIRD) OF TRUSTS § 56 cmt. b (2003).

¹³³ See 11 U.S.C.A. § 541(b) (1994).

¹³⁴ See, e.g., Univ. Nat'l Bank v. Rhoadarmer, 827 P.2d. 561 (Colo. Ct. App. 1991); Irwin Union Bank & Trust Co. v. Long, 312 N.E.2d 908 (Ind. Ct. App. 1974).

¹³⁵ See ALASKA STAT. § 34.40.115 (Michie 2005); R.I. GEN. LAWS § 34-22-13 (1969).

¹³⁶ UNIF. TRUST CODE § 505 cmt. (2005). For criticisms of the traditional rule under which creditors of the holder of a presently exercisable general power of appointment may not reach property subject to the power, see 5 AMERICAN LAW OF PROPERTY § 23.17 (A.J. Casner ed. 1952); LEWIS SIMES & ALLEN F. SMITH, FUTURE INTERESTS § 944 (2d ed., 1956); Olin L. Browder, Jr., *Future Interest Reform*, 35 N.Y.U. L. REV. 1255, 1272 (1960); Berger, *The General Power of Appointment as an Interest in Property*, 40 NEB. L. REV. 104, 119-20 (1960); and Roy Lee Steers, Jr. Note, *Creditors' Ability to Reach Assets Under a General Power of Appointment*, 24 VAND. L. REV. 367 (1971).

¹³⁷ UNIF. TRUST CODE § 505(b)(1) (2005).

¹³⁸ UNIF. TRUST CODE § 103(10) (2000).

¹³⁹ See UNIF. TRUST CODE § 103 (2005).

¹⁴⁰ See RESTATEMENT (THIRD) OF TRUSTS § 56 cmt. b (2003) (referring to such a power as one by which the property may be appointed to the donee); RESTATEMENT (THIRD) OF TRUSTS § 60 cmt. g (2003) (noting that a trustee-beneficiary's "rights and authority represent a limited form of ownership equivalence analogous to certain general powers"); RESTATEMENT (SECOND) OF PROPERTY: DONATIVE TRANSFERS § 11.1 cmt. a (1986) (providing that powers of appointment may be held in a fiduciary as well as in a non-fiduciary capacity). A power of distribution held by a fiduciary was not, however, a "power of appointment" under the Restatement (First) of Property. RESTATEMENT OF PROPERTY § 318(2) (1940). Also, note that the definition of "power of withdrawal" under § 103(11) of the UTC excludes a power if it is exercisable only with the trustee's consent. See UNIF. TRUST

the definition of “power of withdrawal” was amended in 2004 to exclude a power “exercisable by a trustee and limited by an ascertainable standard.”¹⁴¹ The 2004 amendments also defined “ascertainable standard” as one relating to an individual’s health, education, support, or maintenance.¹⁴² Accordingly, a beneficiary may serve as trustee of a third-party created trust without being treated as the settlor of a revocable trust for creditors’ rights purposes, if the beneficiary’s power to distribute to him or herself is limited by the requisite ascertainable standard.

6. *If a trustee/beneficiary’s power to distribute to him or herself is not limited by an ascertainable standard, will the trustee/beneficiary be treated as the settlor of a revocable trust for creditors’ rights purposes?* The analysis of the UTC prior to its 2004 amendments described in the answer to the preceding question arguably leads to that conclusion. Further, an inference to that effect may be drawn from the 2004 amendment to the definition of “power of withdrawal,” under which a power exercisable by a trustee/beneficiary is not treated as a power of withdrawal if it is limited by an ascertainable standard. A comment to the 2004 amendments, however, states that “[t]he Code does not specifically address the extent to which a creditor of a trustee/beneficiary may reach a beneficial interest of a beneficiary/trustee that is not limited by an ascertainable standard.”¹⁴³

B. *May the creditors of a settlor of a revocable trust reach the trust assets after the settlor’s death?* Subject to two limitations, yes, as may creditors with respect to (i) costs of administration of the settlor’s estate, (ii) the expenses of the settlor’s funeral and disposal of remains, and (iii) statutory allowances to a surviving spouse and children.¹⁴⁴ First, the settlor may direct the source from which such liabilities will be paid.¹⁴⁵ Second, the trust assets are subject to such liabilities only to the extent the settlor’s probate estate is inadequate to satisfy them.¹⁴⁶

C. *May the creditors of a settlor of an irrevocable trust reach the settlor’s beneficial interest in the trust?* Yes, regardless of whether the terms of the trust include a spendthrift provision.¹⁴⁷ The UTC rejects the approach taken in recent years in a few states under which a settlor may retain a beneficial interest in a trust that is immune from claims of his or her creditors.¹⁴⁸ Rather, following the traditional common law rule, section 505(a)(2) allows creditors of the settlor to “reach the maximum amount that can be distributed to or for the settlor’s benefit.”¹⁴⁹

CODE § 103(11) (2005). Whether that exclusion would prevent a trustee/beneficiary from being treated as the holder of a power of withdrawal, and thus the settlor of a revocable trust for creditors’ rights purposes, was not clear.

¹⁴¹ See UNIF. TRUST CODE § 103(11) (2004).

¹⁴² See UNIF. TRUST CODE § 103(2) (2004).

¹⁴³ UNIF. TRUST CODE § 504 cmt. (2004).

¹⁴⁴ See UNIF. TRUST CODE § 505(a)(3) (2005).

¹⁴⁵ *Id.*

¹⁴⁶ *Id.*

¹⁴⁷ See UNIF. TRUST CODE § 505(a)(2) (2005).

¹⁴⁸ See, e.g., ALASKA STAT. § 34.40.110(a)-(b) (Michie 2000); DEL. CODE ANN. tit. 12, §§ 3570-3576 (2000); NEV. REV. STAT. ANN. § 166.010 (Michie 1993); R.I. GEN. LAWS §§ 18-9.2 (2000); UTAH CODE ANN. § 25-6-14(a)(ii) (2004); MO. REV. STAT. § 456.5-505.3 (2005).

¹⁴⁹ UNIF. TRUST CODE § 505(a)(2) (2005).

VI. Discretionary and Support Trusts Under the UTC

The UTC's creditors' rights provisions in Article 5 do not distinguish between trusts that traditionally would have been characterized as "discretionary trusts" and those that traditionally would have been characterized as "support trusts."¹⁵⁰ This has been a source of much of its criticism.¹⁵¹

A. *Does the UTC eliminate the distinction between discretionary and support trusts?* In some ways, the UTC eliminates this distinction; in others it does not. The distinction between the two is eliminated for creditors' rights purposes. The comment to section 504 provides: "This section, similar to the Restatement, eliminates the distinction between discretionary and support trusts, unifying the rules for all trusts fitting within either of the former categories."¹⁵² As revised in 2005, however, the comment to section 504 explains:

By eliminating this distinction, the rights of a creditor are the same whether the distribution standard is discretionary, subject to a standard, or both. Other than for a claim by a child, spouse or former spouse, a beneficiary's creditor may not reach the beneficiary's interest. 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. *See* Section 814 comment.¹⁵³

Thus, while Article 5 treats discretionary trusts with and without support standards alike, it does not address or change the traditional rules that govern the trustee's exercise of discretion with respect to making distributions to or for the benefit of the beneficiary.¹⁵⁴

1. *For creditors' rights purposes, does the UTC treat a trust for the beneficiary's support as a discretionary trust?* Yes. Under section 504, most creditors of a beneficiary (including those who have provided for the beneficiary's support) may not compel discretionary distributions they can reach regardless of whether the terms of the trust include a support standard.¹⁵⁵ Similarly, if the terms of a trust do not include a spendthrift provision, section 501 applies without regard to whether the trust terms include a support standard, or

¹⁵⁰ *See* UNIF. TRUST CODE § 504 cmt. (2005).

¹⁵¹ *See, e.g.,* Merric & Oshins, *supra* note 1, at 481-86.

¹⁵² UNIF. TRUST CODE § 504 cmt. (2005).

¹⁵³ *Id.* The comment to § 814 cited at the end of the quote in the text provides:

[W]hether the trustee has a duty in a given situation to make a distribution depends on the exact language used, whether the standard grants discretion and its breadth, whether this discretion is coupled with a standard, whether the beneficiary has other available resources, and, more broadly, the overriding purposes of the trust.

UNIF. TRUST CODE § 814 cmt. (2005).

¹⁵⁴ For a discussion of the rights and duties of the beneficiary and trustee with respect to distributions in the context of § 814(a), which establishes outer limits on the trustee's discretion, *see infra* section VII.

¹⁵⁵ *See supra* section IV.

whether the creditor's claim was for having provided for the beneficiary's support.¹⁵⁶ The comment to section 504 cites the Third Restatement, which provides that "[t]he so-called support trust is viewed here as a discretionary trust with a support standard."¹⁵⁷

2. *Does the UTC treat a discretionary trust without a support standard as a trust for the beneficiary's support?* No. Although section 504 (prohibiting most creditors of the beneficiary from compelling discretionary distributions they can reach) and section 501 (providing creditors' remedies when the terms of the trust do not include a spendthrift provision) do not distinguish between discretionary trusts with and without support standards,¹⁵⁸ with limited exceptions the UTC does not address the rights of beneficiaries – and the duties of trustees – with respect to distributions to be made from such trusts.¹⁵⁹ Because the UTC generally does not address those subjects, they would be governed by common law and principles of equity.¹⁶⁰ Thus, a beneficiary's right, if any, to receive a distribution from a discretionary trust, with or without a support standard, would be determined under the same rules under the UTC as it would be without the UTC. Under those rules, discretionary trusts without support standards are not treated as trusts for the beneficiaries' support.¹⁶¹

B. *To the extent it has done so, why has the UTC eliminated the distinction between discretionary and support trusts?* The comment to section 504, which states that section 504 has eliminated the distinction, refers to the Third Restatement, under which support trusts are treated as discretionary trusts with a support standard.¹⁶² The traditional formal distinction between discretionary trusts and support trusts¹⁶³ is described in the Restatement as "arbitrary and artificial," and rejected in part because trust instruments commonly both give the trustee discretion and include support standards.¹⁶⁴ The analysis of an Iowa court in a recent case is similar:

¹⁵⁶ See UNIF. TRUST CODE § 501 (2005).

¹⁵⁷ See UNIF. TRUST CODE § 504 cmt. (2005) (citing RESTATEMENT (THIRD) OF TRUSTS § 60, Reporter's Note to cmt. a (2003)).

¹⁵⁸ See UNIF. TRUST CODE §§ 501 and 504 (2005).

¹⁵⁹ The most important exception to the statement that the UTC does not address distribution issues is § 814(a), under which the trustee must exercise its discretion in good faith and in accordance with the terms and purposes of the trust and the interests of the beneficiaries, regardless of how broadly the settlor defines the trustee's discretion. See UNIF. TRUST CODE § 814(a) (2005). For a discussion of § 814(a), see *infra* sections VII and VIII. Sections 814(b) and (c) also address distributions, but do so to avoid adverse transfer tax consequences that could arise if a trustee whose discretion was not limited by an ascertainable standard related to health, education, maintenance, and support also was a beneficiary of the trust. See UNIF. TRUST CODE §§ 814(b) and (c) (2005).

¹⁶⁰ See UNIF. TRUST CODE § 106 (2005).

¹⁶¹ See, e.g., RESTATEMENT (THIRD) OF TRUSTS § 50 (2003).

¹⁶² See UNIF. TRUST CODE § 504 cmt. (2005) and RESTATEMENT (THIRD) OF TRUSTS § 60, Reporter's Note to cmt. a (2003).

¹⁶³ The Second Restatement narrowly defines "discretionary trust" and "support trust." A "discretionary trust" is one by the terms of which "it is provided that the trustee shall pay to or apply for a beneficiary only so much of the income and principal or either as the trustee in his uncontrolled discretion shall see fit to pay or apply." RESTATEMENT (SECOND) OF TRUSTS § 155(1) (2003). A "support trust" is one under which the trustee is required to "pay or apply only so much of the income and principal or either as is necessary for the education or support of the beneficiary...." RESTATEMENT (SECOND) OF TRUSTS § 154 (1959). As noted in the Third Restatement, the territory between discretionary and support trusts as so defined is "vast (yet much traveled)," but not covered by the Second Restatement. See RESTATEMENT (THIRD) OF TRUSTS § 60, Reporter's Note to cmt. a (2003).

¹⁶⁴ See *id.* See also Evelyn Ginsberg Abravanel, *Discretionary Support Trusts*, 68 IOWA L. REV. 273, 289 (1983). Whether such trusts should be classified as "discretionary trusts" or "support trusts" has been the subject of

The definitional distinctions between support and discretionary trusts are limpid. Provisions of particular trusts muddy these clear demarcations. When the provision is equivocal or adheres to principles common to both types of trusts, interpretative inconsistencies abound... The parties in the present case ask this court to wade into these murky waters without even a life jacket. Each side throws out, as an aid for interpretation, only the specific language of the trust provision that supports their particular contention despite the remaining language to the contrary... The equivocal nature of the provision is obvious. It blends a desire to ensure the basic support needs of a handicapped daughter with the control mechanism of trustee discretion designed to prevent wasteful depletion of the trust's assets. Any attempt by this court to hammer the language of this particular trust provision into one of these rigid categories would only breed further inconsistencies in the law.¹⁶⁵

Further, even if the terms of a trust mandate distributions for the beneficiary's support, the trustee nevertheless will be required to exercise discretion in deciding how to provide for the beneficiary's support.¹⁶⁶ Similarly, in the event of a serious support need of the beneficiary of a purely discretionary trust, the trustee might be required to make a discretionary distribution to meet the beneficiary's need.¹⁶⁷ For such reasons, the Third Restatement concludes "that there is a continuum of discretionary trusts, with the terms of distributive powers ranging from the most objective ... of standards (pure 'support') to the most open ended (for example, 'happiness') or vague ('benefit') of standards, or even with no standards manifested at all"¹⁶⁸

C. *What effect does the UTC's elimination of the distinction between discretionary and support trusts have on the protection a spendthrift provision provides?* None. Spendthrift protection applies without regard to whether a trust would have been a discretionary trust or a support trust under the Second Restatement rules.¹⁶⁹ Thus, most creditors of a beneficiary of a spendthrift trust may not reach either the beneficiary's interest or the trust assets prior to their receipt by the beneficiary regardless of whether the trust is purely discretionary (for example, "the trustee may at its absolute discretion make distributions of income and principal to or for the beneficiary"), mandatory for the beneficiary's support (for example, "the trustee shall distribute income and principal to provide for the beneficiary's support), or a hybrid of the two (for example, "the trustee may in its discretion make distributions of income and principal for the beneficiary's support").¹⁷⁰

much litigation in the public benefits qualification area. For a discussion of the issues raised and many of the cases, see CLIFTON B. KRUSE, JR., *THIRD PARTY AND SELF-CREATED TRUSTS - PLANNING FOR THE ELDERLY AND DISABLED CLIENT* (3d ed. 2002).

¹⁶⁵ *Strojek v. Hardin County Bd. of Supervisors*, 602 N.W.2d 566, 569 (Iowa Ct. App. 1999). See also *Lang v. Dept. of Public Welfare*, 528 A.2d 1335, 1344 (Pa. 1987) ("We believe such a rigid categorization [of trusts as support trusts or discretionary trusts] is unwarranted and ignores the intent of a settlor who includes both support and discretionary language in his trust instrument, by substituting mechanical rules for individual facts.").

¹⁶⁶ See, e.g., *Old Colony Trust Co. v. Rodd*, 254 N.E.2d 886 (Mass. 1970); *Baker v. Brown*, 15 N.E. 783 (Mass. 1888).

¹⁶⁷ See, e.g., *Morris v. Daiker*, 172 N.E. 540, 542 (Ohio Ct. App. 1929).

¹⁶⁸ RESTATEMENT (THIRD) OF TRUSTS § 60, Reporter's Note to cmt. a (2003).

¹⁶⁹ See UNIF. TRUST CODE § 502(c) (2005).

¹⁷⁰ For discussions of spendthrift exception creditors and the rights of a beneficiary's creditor when the trustee does not make mandatory distributions within a reasonable time after their due date, see *supra* sections II.C through

D. *What effect does the UTC's elimination of the distinction between discretionary and support trusts have on the protection afforded by the UTC's rule prohibiting most creditors from compelling discretionary distributions they can reach?* None. Subject to the narrow exception for a beneficiary's child, spouse, or former spouse with a judgment or court order for support,¹⁷¹ a beneficiary's creditor may not compel discretionary distributions it can reach regardless of whether the trust is purely discretionary, mandatory for the beneficiary's support, or a hybrid of the two.¹⁷² Thus, section 504(b) extends the protection discretionary trusts have traditionally afforded against creditors of beneficiaries compelling distributions they can reach to support trusts. In this regard, the UTC enhances asset protection planning with trusts.

E. *What effect does the UTC's elimination of the distinction between discretionary and support trusts have on the rights of creditors of a beneficiary if the trust's terms do not include a spendthrift provision, or if the instrument includes such a provision, but the creditor's claim is not barred by it?* In the rare case of a trust that is not subject to a spendthrift provision,¹⁷³ section 501 allows a beneficiary's creditor to reach the beneficiary's interest by attachment or other means¹⁷⁴ (but not by compelling discretionary distributions¹⁷⁵). If the terms of the trust include a spendthrift provision, but the creditor's claim is not barred by it,¹⁷⁶ the remedy provided to the exception creditor by section 503(c) is attachment of present or future distributions.¹⁷⁷ Neither section 501 nor section 503 distinguishes between trusts that are purely discretionary, mandatory for support, or a hybrid of the two. Similarly, no distinction is made by either section between claims of creditors that are based on having provided support to the beneficiary and other claims. Thus, if a trust is for the beneficiary's support and its terms do not include a spendthrift provision (or if the instrument includes a spendthrift provision but the creditor is an exception creditor), a creditor of a beneficiary whose claim is not based on having provided support to the beneficiary may attach, under section 501 or 503, future distributions the trustee chooses to make.¹⁷⁸ By contrast, under the Second Restatement, creditors who provided support to the beneficiary of a support trust may reach the beneficiary's interest,¹⁷⁹ but other creditors may not.¹⁸⁰ Consistent with its not distinguishing between discretionary and support

H and II.K, respectively. *See also infra* section VI.E for a discussion of the effect of the elimination of the distinction between discretionary and support trusts when the trust instrument includes a spendthrift provision, but the creditor's claim is not barred by it.

¹⁷¹ *See* UNIF. TRUST CODE § 504(c)(1) (2005).

¹⁷² *See* UNIF. TRUST CODE § 504(b) (2005).

¹⁷³ *See supra* note 100 and accompanying text.

¹⁷⁴ *See* UNIF. TRUST CODE § 501 (2005).

¹⁷⁵ *See* UNIF. TRUST CODE § 504(b) (2005).

¹⁷⁶ *See supra* sections II.C. through I.

¹⁷⁷ *See* UNIF. TRUST CODE § 503(c) (2005).

¹⁷⁸ Both §§ 501 and 503, however, authorize the court to limit the creditor's award "to such relief as is appropriate under the circumstances." *See* UNIF. TRUST CODE §§ 501 and 503(c) (2005).

¹⁷⁹ RESTATEMENT (SECOND) OF TRUSTS § 157(b) (1959). Generally, at common law, if a creditor of a beneficiary of a support trust provides support to the beneficiary, the creditor may recover directly from the trust if it would have been an abuse of discretion for the trustee not to have expended trust funds to have procured the goods or services for the beneficiary. IIA SCOTT & FRATCHER, *supra* note 3, at § 157.2.

¹⁸⁰ *See* RESTATEMENT (SECOND) OF TRUSTS § 154 (1959). Further,

the trustee is not liable to the...creditor [whose claim is not based on having provided support to the beneficiary] though the trustee pays to or applies for the beneficiary so much of the property as is necessary for his education or support, even though the

trusts, the Third Restatement allows creditors whose claims are not based on having provided support to a beneficiary to reach the beneficiary's interest in a non-spendthrift trust, without regard to whether the trust was for the beneficiary's support.¹⁸¹

VII. Subsection 814(a): May the Beneficiary Compel Discretionary Distributions?

The UTC provides little guidance with respect to the rights of beneficiaries and the duties of trustees with respect to discretionary distributions.¹⁸² Rather, discretionary distribution issues are left largely to case law of the jurisdiction whose law governs.¹⁸³

A. *Does the UTC increase the ability of the beneficiary of a discretionary trust to compel distributions? If so, does that increase the ability of creditors of the beneficiary to reach the beneficiary's interest or the trust's assets?* There are three initial points to make with respect to these questions. First, section 504(d) provides that section 504 (which generally prohibits a beneficiary's creditors from compelling discretionary distributions they can reach¹⁸⁴) does not limit the beneficiary's right to maintain an action against the trustee for abuse of discretion or failure to comply with a standard of distribution.¹⁸⁵ Section 504(d) does not grant the beneficiary a new right to compel distributions. Rather, it affirms that the right a beneficiary has to compel distributions when the trustee has abused its discretion or failed to comply with a standard of distribution¹⁸⁶ is not affected by the inability of his or her creditors to do so. Second, section 504(b) explicitly prohibits most creditors of a beneficiary from compelling discretionary distributions they can reach.¹⁸⁷ Because that prohibition applies without regard to whether the beneficiary may compel distributions,¹⁸⁸ the right, if any, the beneficiary may have to compel distributions has no effect on creditors' inability to do so. Third, if the terms of the trust include a valid spendthrift provision, most creditors may not reach the beneficiary's interest, or the trust assets before their receipt by the beneficiary from a distribution by the trustee, regardless of the

trustee...has been served with process in proceedings instituted by the creditor to reach the interest of the beneficiary.

Id. at cmt. c. *See also*, Robert R. Young and T. Lauer, Note, *Creditor's Rights in Support Trusts*, 1956 WASH. U.L.Q. 106 (1956).

¹⁸¹ *See* RESTATEMENT (THIRD) OF TRUSTS § 60 (2003). *See also* Goforth v. Gee, 975 S.W.2d 448 (Ky. 1998).

¹⁸² *See* UNIF. TRUST CODE §§ 504(d), 504 cmt., 814(a) & 814 cmt. (2005).

¹⁸³ *See* UNIF. TRUST CODE § 814(a) cmt. (2005).

¹⁸⁴ *See supra* section IV.

¹⁸⁵ *See* UNIF. TRUST CODE § 504(d) (2005).

¹⁸⁶ As noted by the Second Restatement, for example, "if the trustee is empowered to apply so much of the trust property as he may deem necessary for the support of the beneficiary," the court will override the trustee's decision if the amount the trustee applies is unreasonably high or low for the beneficiary's support. *See* RESTATEMENT (SECOND) OF TRUSTS § 187 cmt. i (1959).

¹⁸⁷ *See supra* section IV.

¹⁸⁸ *See* UNIF. TRUST CODE § 504(b) (2005). For a recent case acknowledging differences in the rights of creditors and beneficiaries to compel discretionary distributions, *see* Corcoran v. Dep't of Soc. Serv., 859 A.2d 533, 543 (Conn. 2004) ("The right of a creditor to reach the trust is not determinative of the right of the beneficiary to do so. It is possible for a trustee to be ordered to make payment to the beneficiary even when the creditor cannot similarly force payment from the trust."). *See also* RESTATEMENT (THIRD) OF TRUSTS § 60 cmt. e (2003) (discussed *supra* at note 103).

beneficiary's rights to compel discretionary distributions (or even if the beneficiary has a mandatory right to receive distributions).¹⁸⁹

These two questions also arise in connection with concerns that have been expressed about the effect of the UTC in the contexts of special or supplemental needs trusts, divorce, and bankruptcy, which are discussed in sections IX, X, and XI.

*B. Does subsection 814(a) give the beneficiary of a discretionary trust an enforceable property right to compel discretionary distributions?*¹⁹⁰ As a threshold matter, whether a beneficiary of a trust has a property interest in the trust's assets, or merely a personal right against the trustee with respect to its administration of the trust's assets, has long been the subject of debate.¹⁹¹ While there is not a consensus on this question, the prevalent view is that a trust beneficiary has a property interest in the trust's assets as well as rights against the trustee to enforce the proper administration of the trust.¹⁹² With respect to subsection 814(a), it provides:

Notwithstanding the breadth of discretion granted to a trustee in the terms of the trust, including the use of such terms as 'absolute,' 'sole,' or 'uncontrolled,' the trustee shall exercise a discretionary power in good faith and in accordance with the terms and purposes of the trust and the interests of the beneficiaries.¹⁹³

1. At common law, can a settlor literally give the trustee unlimited discretion? No. As stated in the Second Restatement:

¹⁸⁹ See UNIF. TRUST CODE §§ 502 and 503 (2005). For a discussion, see *supra* section II.

¹⁹⁰ For an argument to that effect, see Merric and Oshins, *supra* note 1, at 481.

¹⁹¹ See generally, BOGERT & BOGERT, *supra* note 97, at § 183; RESTATEMENT (THIRD) OF TRUSTS § 2, Reporter's Notes, general note (2003).

¹⁹² "[T]here is probably general agreement in the United States today that a trust involves a division of legal and equitable ownership..." RESTATEMENT (THIRD) OF TRUSTS § 2, Reporter's Notes, general note (2003). Similarly:

The nature of the beneficiary's rights would seem to be summarized by the statement that while the right of the beneficiary originally was solely in personam against the trustee, it has become increasingly a right in rem and is now substantially equivalent to equitable ownership of the trust res. The beneficiary, of course, also has rights in personam against the trustee.

BOGERT & BOGERT, *supra* note 97, at § 183 (footnotes omitted). For a discussion of statutes in a number of states under which interests in real property held in trust are held entirely by the trustee, with the beneficiary having no estate or interest in the trust's real property, see *id.* at §184 (concluding that "[m]ost of the decisions either contradict these statutes by holding that the beneficiary does have some kind of an estate or interest in the trust property, or the cases could have been decided as they were decided without any dependence on the statutes in question." In Louisiana, however, recent cases have held that a trust beneficiary has no ownership interest in trust property. See *David v. Katz*, 83 F. Supp. 2d 736 (E.D. La. 2000); *Read v. U.S.*, 169 F.3d 243 (5th Cir. 1999)).

¹⁹³ UNIF. TRUST CODE § 814(a) (2005). Prior to the 2005 amendments, the UTC's mandatory rules precluded the settlor from overriding "the duty of a trustee to act in good faith and in accordance with the purposes of the trust." UNIF. TRUST CODE § 105(b)(2) (2004). Because provisions of the UTC other than its mandatory rules do not apply if the settlor provides otherwise in the terms of the trust, § 105(b)(2) raised the question of whether the settlor could waive the § 814(a) requirements that the trustee exercise its discretion in accordance with the terms of the trust and the interests of the beneficiaries. See UNIF. TRUST CODE § 105(a) (2005). The 2005 amendments addressed this question by amending § 105(b)(2), which now tracks the language of § 814(a), making its standard of conduct for a trustee of a discretionary trust mandatory. See UNIF. TRUST CODE § 105(b)(2) (2005).

It is against public policy to permit the settlor to relieve the trustee of all accountability It is true that the powers conferred upon the transferee of property may be so extensive as to indicate an intention not to create a trust but to give the beneficial interest in the property to the transferee If, however, a trust is created, it is required by public policy that the trustee should be answerable to the courts, so far at least as the honesty of his conduct is concerned.¹⁹⁴

2. *Under non-UTC law, if the settlor purports to give the trustee absolute or uncontrolled discretion, under what circumstances will a court nevertheless review the trustee's exercise of its discretion?* There is no single, universally accepted common law statement of the minimum standard of conduct required of the trustee to avoid judicial interference when the terms of the trust purport to give the trustee unlimited discretion.¹⁹⁵ Rather, different language is used in cases, treatises, restatements, and commentators' analyses to describe the standard the trustee will be held to regardless of the extent of discretion the settlor grants the trustee.¹⁹⁶ It is doubtful that such different language reflects substantively different standards.¹⁹⁷

For example, the same subsection of Professor Scott's treatise describes the limits on the discretion of a trustee, who is relieved by the settlor of the otherwise applicable requirement to exercise its discretion reasonably, in different ways.¹⁹⁸ First, it provides that the trustee may act "beyond the bounds of a reasonable judgment, *if he acts in good faith and does not act capriciously.*"¹⁹⁹ Second, it also provides that if, "by the terms of the trust [the trustee] is not required to act reasonably, the court will interfere *where he acts dishonestly or in bad faith, or where he acts from an improper motive.*"²⁰⁰ There is no mention of these standards being substantively different. Furthermore, a different passage of the same treatise notes that the trustee's discretion can be enlarged by the use of such terms as "absolute," but that even then "the court will control his action *where he acts in bad faith.* The real question is whether it appears that the trustee is *acting in that state of mind in which it was contemplated by the settlor*

¹⁹⁴ RESTATEMENT (SECOND) OF TRUSTS § 187 cmt. k (1959). *See also* Stix v. Comm'r, 152 F.2d 562, 563 (2d Cir. 1945); McNeil v. McNeil, 798 A.2d 503, 509 (Del. 2002); Keating v. Keating, 165 N.W. 74 (Iowa 1917); Ponzelino v. Ponzelino, 26 N.W.2d 330 (Iowa 1947); Estate of Ralston, 37 P.2d 76 (Cal. 1934); John H. Langbein, *Mandatory Rules in the Law of Trusts*, 98 NW. U. L. REV. 1105, 1120, 1124 (2004).

¹⁹⁵ *See generally* BOGERT & BOGERT, *supra* note 97, at § 560 (Supp. 2004). If the terms of the trust do not include such extended discretion language as "absolute," "sole," or "uncontrolled," under the Second Restatement the trustee's exercise of its discretion will not be disturbed unless the trustee "acts dishonestly, or with an improper motive, or fails to use his judgment, or acts beyond the bounds of a reasonable judgment." RESTATEMENT (SECOND) OF TRUSTS § 187 cmt. e (1959).

¹⁹⁶ In Colorado, for example, the Supreme Court, en banc, citing and quoting from IIA SCOTT & FRATCHER, *supra* note 3, at § 128.3, stated that: "*If the settlor manifested an intention that the discretion of the trustee should be uncontrolled, the court will not interfere unless he acts dishonestly or from an improper motive, or fails to use his judgment.*" *In re* Marriage of Jones, 812 P.2d 1152, 1156 (Colo. 1991) (emphasis in original). By contrast, according to the court in a recent Florida case: "Although the trustee of the trust in the instant appeal has absolute discretion to pay out income and principal to the beneficiaries, he still must exercise good faith and be judicious in the administration of the trust." Friedman v. Friedman, 844 So. 2d 789 (Fl. Ct. App. 2003).

¹⁹⁷ As discussed *infra* at notes 2243-2323 and accompanying text, the primary issue with respect to the effect of extended discretion language is whether it relieves the trustee of the otherwise applicable obligation to exercise its discretion in an objectively reasonable manner.

¹⁹⁸ *See* IIA SCOTT & FRATCHER, *supra* note 3, at § 187.2.

¹⁹⁹ *Id.* (emphasis added).

²⁰⁰ *Id.* (emphasis added).

that he should act.”²⁰¹ As a final illustration, the Third Restatement provides that “[e]ven under the broadest grant of fiduciary discretion, a trustee must act *honestly and in a state of mind contemplated by the settlor*. Thus, the court will not permit the trustee to act in bad faith or for some purpose or motive other than to accomplish the purposes of the discretionary power.”²⁰²

3. *Is the requirement of subsection 814(a) that the trustee act in good faith, regardless of the extent of discretion the settlor grants the trustee, a change from the common law?*²⁰³ No. Cases from many jurisdictions explicitly acknowledge the requirement that trustees exercise discretion in good faith even if the trustee is granted extended discretion.²⁰⁴ Many other cases, however, do not explicitly acknowledge the trustee’s duty to act in good faith, but instead provide that the trustee’s exercise of its discretion will not be disturbed absent one or more of such factors as bad faith, dishonesty, an improper motive, or a failure to use the trustee’s judgment.²⁰⁵ The fact that such cases do not explicitly state that trustees must act in good faith, regardless of the breadth of their discretion, however, does not mean that the courts that decided them do not require good faith of the trustee.²⁰⁶

Rather, requiring that the trustee not act in bad faith, or dishonestly, or with an improper motive, or fail to act altogether is another way of expressing the fundamental fiduciary requirement that the trustee must act in good faith (or implicitly includes such a requirement).²⁰⁷ There is much evidence that is the case. For example, a court in a 1953 California case addressed the judicial review of a trustee’s exercise of discretion by stating that if:

the ‘sole discretion’ vested in and exercised by the trustees in this case...were exercised fraudulently, in bad faith or in an abuse of discretion, it is subject to...review. Whether good faith has been exercised, or whether fraud, bad faith or an abuse of discretion has been committed is always subject to consideration by the court upon appropriate allegations and proof.”²⁰⁸

²⁰¹ *Id.* at § 187 (emphasis added). See also *Practical Drafting* 7439 (October 2003) (observing that § 187 “preserve[es] the requirement of good faith” [emphasis added]).

²⁰² RESTATEMENT (THIRD) OF TRUSTS § 50 cmt. c (2003) (emphasis added).

²⁰³ For an argument to that effect, see Merric and Oshins, *supra* note 1, at 482.

²⁰⁴ See, e.g., *Friedman*, 844 So.2d 789; *O’Shaughnessy*, 517 N.W.2d 574; *Jacob v. Davis*, 738 A.2d 904 (Md. Ct. App. 1999); *NationsBank of Virginia, N.A. v. Estate of Grandy*, 450 S.E.2d 140 (Va. 1994); *In re Ternansky’s Estate*, 141 N.E.2d 189 (Ohio Ct. App. 1957); *Matter of Estate of Mayer*, 672 N.Y.S.2d 998 (N.Y. Sur. 1998).

²⁰⁵ See, e.g., *Marriage of Jones*, 812 P.2d 1152; *Goodwine v. Goodwine*, 819 N.E.2d 824 (Ind. Ct. App. 2004); *Jennings v. Murdock*, 553 P.2d 846 (Kan. 1976); *Amer. Cancer Soc., St. Louis Div. v. Hammerstein*, 631 S.W.2d 858 (Mo. Ct. App. 1981); *In re Goodman*, 790 N.Y.S.2d 837 (N.Y. Sur. 2005); *Finch v. Wachovia Bank & Trust Co., N.A.*, 577 S.E.2d 306 (N.C. Ct. App. 2003); *Robinson v. Kirbie*, 793 P.2d 315 (Okla. Ct. App. 1990).

²⁰⁶ Professor Bogert’s treatise states that two standards are used by courts in determining whether and to what extent they will review a trustee’s exercise of absolute and uncontrolled discretion. BOGERT & BOGERT, *supra* note 97, at § 560 (Supp. 2004). Under the first, judicial review occurs when the trustee acts in bad faith, dishonestly, or from a motive other than the accomplishment of the purposes of the trust. *Id.* Under the second, the trustee must also act reasonably. *Id.* In discussing the two standards, the treatise notes that “[t]here is agreement that a trustee must act in good faith...” *Id.*

²⁰⁷ As amended in 2005, the comment to § 814 provides: “The obligation of the trustee to act in good faith is a fundamental concept of fiduciary law although there are different ways that it can be expressed.” UNIF. TRUST CODE § 814 cmt. (2005).

²⁰⁸ *In re Ferrall’s Estate*, 258 P.2d 1009, 1013 (Cal. 1953). A District of Columbia court similarly has equated good faith with the absence of bad faith: “The transfer of the certificate of deposit cannot be deemed self-dealing when it is done in good faith for the benefit of the estate.... Since no bad faith by Michele Hagens was shown at

More recently, California adopted a statute that provides “[w]hen a trust instrument confers ‘absolute,’ ‘sole’ or ‘uncontrolled’ discretion, the trustee shall act in accordance with fiduciary principles and shall not act in bad faith or in disregard of the purposes of the trust.”²⁰⁹ A California court, in referring to that statute, noted that: “It is presumed that the trustee will act in good faith to effectuate the settlor’s intent.”²¹⁰ Moreover, in an Indiana case (involving a trustee who was not granted extended discretion) in which the court noted that “[t]he trust relationship involves the exercise of the utmost good faith on the part of the trustees,” it also stated that “[i]n the absence of bad faith, or an abuse or unreasonable exercise of discretion by the co-trustees,” it would not interfere with the trustee’s exercise of its discretion.²¹¹

Further, a year after the Colorado Supreme Court stated that if the settlor gives the trustee uncontrolled discretion, the court will not interfere with its exercise unless the trustee “acts dishonestly or from an improper motive, or fails to use his judgment,”²¹² a lower appellate court in Colorado decided a case in which a trustee with sole and absolute discretion over distributions also was a remainder beneficiary and thus had a conflict of interest with respect to his exercise of discretion.²¹³ In upholding the income beneficiary’s claim for increased distributions from the trust, the opinion characterized the trustee’s conduct as an abuse of discretion, arbitrary and capricious, improperly motivated, and a “breach of his fiduciary responsibilities to act with the utmost good faith and fairness toward the beneficiary.”²¹⁴

Cases from Minnesota also illustrate that a test focusing on such factors as the trustee’s motive in exercising its discretion does not mean good faith is not required. In Minnesota, the trustee’s obligation to exercise its discretion in good faith is explicit,²¹⁵ and the test of whether a

trial, the trial judge did not clearly err in approving the transaction.” *Jones v. Hagans*, 634 A.2d 1219, 1225 (D.C. 1993).

²⁰⁹ CAL. PROB. CODE § 16081(a) (West 1991).

²¹⁰ *Ventura Co. Dept. of Child Support Servs. v. Brown*, 11 Cal. Rptr. 3d 489, 499 (Cal. Ct. App. 2004).

²¹¹ *See Matter of Nathan Trust*, 618 N.E.2d 1343, 1346 (Ind. Ct. App. 1993), *vacated by Matter of Della Lustgarten Nathan Trust*, 638 N.E.2d 789 (Ind. 1994). The court’s opinion in a Wisconsin case, in which extended discretion language was not used, addresses judicial review of the trustee’s exercise of its discretion similarly:

So long as trustees act in good faith and from proper motives and within the bounds of a reasonable judgment under the terms and conditions of the trust, the court has no right to interfere. It is only when they act outside the bounds of a reasonable judgment, or are guilty of an abuse of discretion, or when they act dishonestly and improperly that the court may interfere.

In re Filzen’s Estate, 31 N.W.2d 520, 522 (Wis. 1948).

²¹² *Marriage of Jones*, 812 P.2d at 1156. Note that in *Jones*, the Colorado Supreme Court did not announce a single standard to be applied in Colorado in cases involving a challenge to the trustee’s exercise of discretion. In fact, the case did not even involve such a challenge, but instead decided whether a wife’s interest in a discretionary trust constituted property for purposes of division in a divorce. *Id.* In holding that it did not, the court described the circumstances under which a trustee’s exercise of discretion will be reviewed in four different ways: (i) “the beneficiary could not force the trustee to pay income or principal unless she could establish fraud or abuse of discretion,” *id.* at 1156; (ii) “[t]he beneficiary cannot obtain the assistance of the court to control the exercise of the trustee’s discretion except to prevent an abuse by the trustee of his discretionary power,” *id.*; (iii) “[i]f the settlor manifested an intention that the discretion of the trustee should be uncontrolled, the court will not interfere unless he acts dishonestly or from an improper motive, or fails to use his judgment,” *id.* (emphasis in original), and (iv) “the beneficiary of a discretionary trust has no contractual or enforceable right to income or principal from the trust, and cannot force any action by the trustee unless the trustee performs dishonestly or does not act at all.” *Id.*

²¹³ *See In re Estate of McCart*, 847 P.2d 184 (Colo. Ct. App. 1992).

²¹⁴ *Id.*

²¹⁵ *See, e.g., O’Shaughnessy*, 517 N.W.2d 574; *Norwest Bank Minn. North, N.A. v. Beckler*, 663 N.W.2d 571 (Minn. Ct. App. 2003).

trustee has abused its discretion looks to, among other things, the trustee's motive and whether the trustee acted with a conflict of interest.²¹⁶ Furthermore, a 1931 South Carolina case²¹⁷ requires trustees to exercise discretion "honestly and faithfully," and stated that "[a] plainly arbitrary, unreasonable, or fraudulent exercise" would have been actionable.²¹⁸ The opinion does not explicitly require trustees to act in good faith. A relatively recent South Carolina case, however, summarizes the holding in the earlier case as follows: "[W]here a trust gives a trustee discretionary authority, the trustee cannot exercise such discretion upon a mere whim and without accountability, but the trustee is limited by the primary purpose of the grant, and must act with good faith as to any discretion vested in him. Moreover, discretion vested in a trustee must be honestly and faithfully exercised."²¹⁹ Finally, in a Virginia case in which the court noted that the trustees had "uncontrolled judgment and discretion" over distributions, it described the circumstances under which the exercise of that discretion would be subject to judicial review as follows:

Generally, a trustee's discretion is broadly construed, but his actions must be an exercise of good faith and reasonable judgment to promote the trust's purpose. A trustee's exercise of discretion should not be overruled by a court unless the trustee has clearly abused the discretion granted him under the trust instrument or acted arbitrarily in such a way as to destroy the trust he is to maintain.²²⁰

4. *Are there any cases in which a court has ~~held~~ stated that the use of extended discretion language waives the trustee's obligation to act in good faith?* Yes, there is at least one. According to an intermediate appellate court in Tennessee, in dictum, the settlor may waive the requirement that the trustee act in good faith, apparently by describing the trustee's discretion with such language as "absolute," "unlimited," or "uncontrolled."²²¹ That dictum, however, appears to be based on the court's mistaken treatment of the trustee's obligation to act in good faith as the obligation to act reasonably: "The good faith requirement may be waived by the words of the trust but the words are interpreted narrowly. Words found to waive the reasonableness standard are 'absolute' or 'unlimited' or 'uncontrolled' discretion."²²² Requiring a trustee to act in good faith, however, is not the same as requiring it to act reasonably.²²³ As noted in Professor Scott's treatise, if the settlor relieves the trustee from the duty to act reasonably, the courts will not interfere with the trustee's exercise of discretion "if he acts in good faith and does not act capriciously."²²⁴

²¹⁶ See *In re Trusts A & B of Divine*, 672 N.W.2d 912 (Minn. Ct. App. 2001).

²¹⁷ *Lynch v. Lynch*, 159 S.E. 26 (S.C. 1931).

²¹⁸ *Id.* at 31.

²¹⁹ *Sarlin v. Sarlin*, 430 S.E.2d 530, 532 (S.C. Ct. App. 1993).

²²⁰ *Grandy*, 450 S.E.2d at 143.

²²¹ *Krug v. Krug*, 838 S.W.2d 197, 201 (Tenn. Ct. App. 1992). In *Krug*, a trustee was given the "sole discretion" to remove and replace a cotrustee; the court held that such language was not sufficient to waive the trustee's obligation to act in good faith. *Id.*

²²² *Id.*

²²³ In reviewing the exercise of the trustee's discretion in an Oregon case, the court stated: "There is no question of the trustee's good faith in making his decision to limit the payments as he did. The only question presented is the reasonableness of his judgment." *Rowe v. Rowe*, 347 P.2d 968, 974 (Or. 1959).

²²⁴ IIA SCOTT & FRATCHER, *supra* note 3, at § 187.2. See also JESSE DUKEMINIER ET. AL., WILLS, TRUSTS, AND ESTATES 540-41 (7th ed. 2005).

5. *Does subsection 814(a) impose a reasonableness requirement on the trustee's exercise of discretion?* Generally, if a standard by which the reasonableness of the trustee's exercise of discretion can be tested is included in the instrument, reasonableness is required.²²⁵ If the terms of the trust do not include such a standard, the Second Restatement implies that reasonableness therefore is not required.²²⁶ Further, under the Second Restatement, even if the terms of the trust include a standard against which the reasonableness of the trustee's exercise of its discretion can be judged, the trustee will not be required to exercise it reasonably if the settlor provides otherwise in the terms of the trust.²²⁷ The settlor may do so by using such language as "absolute," "unlimited," or "uncontrolled" in describing the trustee's discretion.²²⁸

It is not clear whether these rules of the Second Restatement apply under the UTC. Subsection 814(a) itself does not address the issue. As amended in 2005, the comment to section 814 provides, in part:

Subsection (a) requires a trustee exercise a discretionary power in good faith and in accordance with the terms and purposes of the trust and the interests of the beneficiaries. Similar to Restatement (Second) of Trusts Section 187 (1959), subsection (a) does not impose an obligation that a trustee's decision be within the bounds of a reasonable judgment, although 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. Restatement (Second) of Trusts Section 187 cmt. f (1959).²²⁹

This comment, with its references to the Second Restatement, arguably indicates that the Second Restatement's treatment of the reasonableness issue applies under subsection 814(a). However, the comment does not address the effect of extended discretion language on the trustee's obligation to exercise its discretion reasonably, nor does it cite the Second Restatement provision²³⁰ that does so. Further, as next discussed, some jurisdictions require reasonableness of the trustee in the exercise of its discretion even if extended discretion language is used in the instrument. Thus, by not addressing the issue, the UTC may be leaving its resolution to the common law and principles of equity of enacting jurisdictions.²³¹

6. *Under non-UTC law, is a trustee whose discretion is described with such language as "absolute," "sole," or "uncontrolled" required to exercise it reasonably?* As discussed in the preceding paragraph, under the Second Restatement the use of such language precludes a court from reviewing a discretionary decision of a trustee for reasonableness.²³²

²²⁵ See RESTATEMENT (SECOND) OF TRUSTS § 187 cmt. i (1959).

²²⁶ *Id.* "In such a case, however, the court will interpose if the trustee acts dishonestly, or from some improper motive." *Id.*

²²⁷ *Id.*

²²⁸ *Id.* cmt. j.

²²⁹ UNIF. TRUST CODE § 814 cmt. (2005). (Note that the citation to comment f to § 187 of the Second Restatement apparently should be to comment i to § 187.)

²³⁰ See RESTATEMENT (SECOND) OF TRUSTS § 187 cmt. j (1959).

²³¹ See UNIF. TRUST CODE § 106 (2005).

²³² The Third Restatement's discussion of this subject notes that many cases cite the Second Restatement rule that use of extended discretion language dispenses with the reasonableness standard, but observes: "Cases, however, are difficult to find, involving extended discretion relating to distribution of income or principal, in which courts

After a lengthy review of the cases on the subject, however, Professor Bogert's treatise concludes that "[t]he authorities do not appear to support the Restatement position that there is no requirement of reasonableness in the exercise of a power granted in the trustee's absolute discretion."²³³ Rather:

In addition to the commonly recognized factors used to determine whether there had been an abuse of discretion, a standard of reasonableness has been applied by the courts in judging the exercise of a discretionary power (whether simple or absolute), a standard implied from the settlor's intent and the purposes expressed in the trust instrument. With respect to court review of discretionary powers, this standard is consistent with the standard of care and skill of a prudent man and is based upon established fiduciary standards and principles.²³⁴

7. *Does the language in subsection 814(a) that requires the trustee not only to act in good faith, but also to exercise its discretion "in accordance with the terms and purposes of the trust and the interests of the beneficiaries" expand the scope of judicial review of a trustee's exercise of extended discretion?* According to a recent argument to that effect:

Section 814(a) illustrates the uncertainty that codifying the trust law may create. What do the words "and in accordance with the terms and purposes of the trust and the interests of the beneficiaries" mean? Do they create a stricter limit on the discretion that may be conferred upon a trustee than the common law test set forth in the above quotation from Scott?²³⁶ It seems likely that courts will use them to

have approved what actually appears to be unreasonable conduct." See RESTATEMENT (THIRD) OF TRUSTS § 50, Reporter's Notes to cmt. c (2003).

²³³ BOGERT & BOGERT, *supra* note 97, at § 560 (Supp. 2004).

²³⁴ *Id.* The analysis of Professors Dukeminier, Johanson, Lindgren, and Sitkoff reaches a similar conclusion:

What, then, are the limitations on the trustee's freedom when the trustee has "absolute and uncontrolled discretion?" Professor Scott argued for a subjective standard, emphasizing the trustee's "good faith" and proper motives and dispensing with the requirement of reasonableness. He suggested, and the Restatement for which he was the reporter adopted, a standard of whether the trustee has acted "in that state of mind in which it was contemplated by the settlor that he should act." Scott, *supra*, at 16; Restatement (Second) of Trusts §187, cmt. j (1959). Some courts, relying on the Restatement's good faith standard, declare that the trustee must not act arbitrarily or capriciously, seemingly bringing in a reasonableness test under the guise of other words. Other courts apply a reasonableness test even when the discretion is "absolute."...

In the final analysis, it appears that the difference between simple discretion and "absolute" discretion is one of degree and that the trustee's action must not only be in good faith but also to some extent reasonable, with more elasticity in the concept of reasonableness the greater the discretion given.

| DUKEMINIER ET. AL., *supra* note 223, at 540-41.

²³⁵ Note that "interests of the beneficiaries" is a defined term under the UTC. See UNIF. TRUST CODE § 103(8) (2005). It does not mean what the beneficiaries assert or the court determines to be in the beneficiaries' best interests. Rather, "interests of the beneficiaries" means "the beneficial interests provided in the terms of the trust." *Id.*

²³⁶ The earlier quotation from Scott referred to is:

The extent of the discretion may be enlarged by the use of qualifying adjectives or phrases such as "absolute" or "uncontrolled." Even the use of such terms, however,

do so in particular cases, yet their application to particular facts remains as hard to predict as that of the common law. Has anything been gained by codification?²³⁷

Subsection 814(a)'s requirement that the trustee exercise even extended discretion in accordance with the terms and purposes of the trust and the interests of the beneficiaries, however, is not new. Rather, it simply reflects the trustee's basic obligation with respect to the administration of the trust.²³⁸

A trustee's obligation to exercise its discretion in administering a trust in accordance with the purposes of the trust is expressly addressed by the Second Restatement: even a trustee with "absolute," "unlimited," or "uncontrolled" discretion may not exercise it "from some motive other than the accomplishment of the purposes of the trust."²³⁹ In a New York case, a testator who made substantial preresiduary charitable gifts left the residue of his estate in trust for his wife's benefit, stating his "paramount intention and wish that (my) wife shall have anything that she requires or may desire for her personal welfare and comfort."²⁴⁰ The testator named his wife as the primary income beneficiary of the trust and authorized the trustee to invade principal for her benefit "in its sole, absolute, and unimpeachable discretion."²⁴¹ In rejecting the widow's request for a principal distribution to make a charitable gift in memory of the testator, which the trustee was willing to grant, the court stated that allowing the distribution "would constitute a departure from the testamentary program fixed by the deceased."²⁴² Many other cases from many jurisdictions support subsection 814(a)'s requirement that the trustee exercise even extended discretion in accordance with the terms and purposes of the trust and the interests of the beneficiaries.²⁴³

does not give him unlimited discretion. A good deal depends upon whether there is any standard by which the trustee's conduct can be judged. Thus if he is directed to pay as much of the income and principal as is necessary for the support of a beneficiary, he can be compelled to pay at least the minimum amount which in the opinion of a reasonable man would be necessary. If, on the other hand, he is to pay a part of the principal to a beneficiary entitled to the income, if in his discretion he should deem it wise, the trustee's decision would normally be final, although as will be seen the court will control his action where he acts in bad faith. The real question is whether it appears that the trustee is acting in that state of mind in which it was contemplated by the settlor that he should act.

Richard Covey, ed. *Practical Drafting*, 7439 (October 2003) (quoting SCOTT AND FRATCHER, *supra* note 3, at § 187).

²³⁷ Richard Covey, ed. *Practical Drafting*, 7440 (October 2003).

²³⁸ The comment to § 814 addresses this language by noting that: "Consistent with the trustee's duty to administer the trust (see Section 801), the trustee's exercise must also be in accordance with the terms and purposes of the trust and the interests of the beneficiaries." UNIF. TRUST CODE § 814 cmt. (2005).

²³⁹ RESTATEMENT (SECOND) OF TRUSTS § 187 cmt. j (1959).

²⁴⁰ *In re May's Estate*, 112 N.Y.S.2d 847, 848 (N.Y. Sur. 1952).

²⁴¹ *Id.*

²⁴² *Id.* at 849.

²⁴³ See, e.g., *Conway v. Enemy*, 96 A.2d 221 (Conn. 1953); *In re Hansen's Estate*, 23 A.2d 886 (Pa. 1942); *The Conn. Bank & Trust Co. v. Hartford Hosp.*, 276 A.2d 792 (Conn. Sup. 1971); *In re Murray*, 45 A.2d 636 (Me. 1946); *Fine v. Cohen*, 623 N.E.2d 1134, 1139 (Mass. App. Ct. 1993); *Hammerstein*, 631 S.W.2d 858; *O'Shaughnessy*, 517 N.W.2d 574; *Taylor v. McClave*, 15 A.2d 213 (N.J. Ch. 1940); *Estate of Mayer*, 672 N.Y.S.2d 998. See also MONT. CODE ANN. § 72-34-130 (1989).

C. What, then, is the effect of the UTC on the rights of trust beneficiaries and the duties of trustees with respect to discretionary distributions? Subsection 814(a)'s formulation of the minimum standard of conduct required even of a trustee that is granted extended discretion codifies the common law and will-should not change the traditional analysis of whether a beneficiary of a given trust in a given situation is entitled to receive a distribution. After discussing subsection 814(a)'s requirement that trustees act in good faith and in accordance with the terms and purposes of the trust and the interests of the beneficiaries, the comment to section 814, as amended in 2005, explicitly states that it “does not otherwise address the obligations of a trustee to make distributions, leaving that issue to the caselaw.”²⁴⁴ Further, the UTC's elimination of the distinction between discretionary and support trusts²⁴⁵ is with respect to the rights of creditors of beneficiaries and “does not affect the rights of a beneficiary to compel a distribution.”²⁴⁶ Given that subsection 814(a) codifies the common law standards applicable to trustees in the exercise of discretionary powers and that the UTC explicitly provides that neither subsection 814(a), nor Article 5's elimination of the distinction between discretionary and support trusts, affects distribution rights and duties, the UTC should not affect the rights and duties of beneficiaries and trustees with respect to discretionary distributions.

VIII. Subsection 814(a): Is there a Better Alternative?

Many of the criticisms directed at the UTC's creditors' rights provisions are based, to a significant extent, on the argument that beneficiaries of discretionary trusts have enforceable rights under the UTC that are greater than they have under non-UTC trust law.²⁴⁷ That argument, in turn, is largely based on the claim that the standard of conduct required of a trustee in the exercise of its discretion under subsection 814(a) provides beneficiaries with significantly greater rights to compel discretionary distributions than they otherwise would have.²⁴⁸ This Article argues that subsection 814(a)'s statement of the standard to which trustees will be held in their exercise of discretionary powers, regardless of the breadth of discretion the settlor grants, does not effect a change in the common law, but is a codification of the traditional common law standard that is expressed differently than it is in some jurisdictions.²⁴⁹

If subsection 814(a) is simply one of multiple ways of expressing the traditional, common law standard to which trustees with discretionary powers are held, though, the question is raised whether a UTC enacting jurisdiction could substitute for subsection 814(a) an alternative formulation of the standard without effecting a substantive change. Subsection 814(a) provides:

Notwithstanding the breadth of discretion granted to a trustee in the terms of the trust, including the use of such terms as “absolute,” “sole,” or “uncontrolled,” the

²⁴⁴ UNIF. TRUST CODE § 814 cmt. (2005).

²⁴⁵ See *supra* section VI.

²⁴⁶ UNIF. TRUST CODE § 504 cmt. (2005).

²⁴⁷ See, e.g., Merric and Oshins, *supra* note 1, at 481.

²⁴⁸ *Id.*

²⁴⁹ See *supra* section VII.

trustee shall exercise a discretionary power in good faith and in accordance with the terms and purposes of the trust and the interests of the beneficiaries.²⁵⁰

An alternative standard, derived from a Colorado case,²⁵¹ is that if the trustee is granted extended discretion, through the use of such language as “sole and absolute,” the court will interfere with its exercise only if the trustee (i) acts dishonestly, (ii) acts with an improper motive, or (iii) fails to use his or her judgment.²⁵² This standard has been described by its proponents as a “bad faith” standard.²⁵³

Fundamental to the duties of a trustee is that it administer the trust in accordance with the trust’s terms to carry out the intention of the settlor. If a trustee makes a discretionary distribution that is not permitted by the terms of the trust, it has breached its duty, regardless of the breadth of its discretion, even if it (i) did not act dishonestly, (ii) was motivated by a desire to act in the best interests of the beneficiary, and (iii) exercised its judgment in making its discretionary decision. For example, if the instrument grants the trustee the “sole, absolute, and uncontrolled” discretion to make distributions for a beneficiary’s support for life, remainder to other beneficiaries, a trustee who makes a distribution to the current beneficiary to meet a non-support related emergency need has breached its duty to administer the trust in accordance with its terms. (Such a breach also could be described as a failure to administer the trust in accordance with the interests of the beneficiaries, as defined in the instrument, because the distribution effectively would have shifted trust benefits to the distributee beneficiary and away from other beneficiaries. Alternatively, the breach also could be characterized as a failure to administer the trust in accordance with the settlor’s purposes of providing for the support of the current beneficiary and otherwise preserving the trust assets for successive beneficiaries.)

Arguably, the bad faith standard described above would cover such a breach through its requirement that a trustee not act with an improper motive, as the distribution would have been motivated by a desire to further a purpose the settlor had not intended for the trust. If the trustee, however, was motivated by the desire to benefit the beneficiary – perhaps in a way the trustee believes the settlor would have done, if the settlor were living – labeling the conduct as improperly motivated is more problematic than simply finding it to be impermissible as not in accordance with the trust’s terms, its purposes, or the interests of its beneficiaries.

Similarly Again, if a trustee with absolute and uncontrolled discretion exercises its judgment, acts honestly, and is not improperly motivated, it nevertheless will have breached its duty if it misconstrues the instrument and makes a discretionary distribution, or engages in other conduct in administering the trust, which is not permitted by the trust’s terms. For example To further illustrate, if the trust’s beneficiaries are the settlor’s descendants and a child of the settlor has adopted an adult, the adoptee may or may not be a “descendant” of the settlor within the meaning of the trust instrument.²⁵⁴ If not, a trustee who exercises its discretion to make

²⁵⁰ UNIF. TRUST CODE § 814(a) (2005).

²⁵¹ *Marriage of Jones*, 812 P.2d at 1156 (quoting IIA SCOTT & FRATCHER, *supra* note 3, at § 128.3). Note, however, that *Jones* did not even involve a challenge to a trustee’s exercise of discretion and actually expressed the circumstances under which the trustee’s exercise of its uncontrolled discretion would be reviewed in four different ways. *See supra* note 2110.

²⁵² *See Merric and Oshins, supra* note 1, at 479.

²⁵³ *Id.*

²⁵⁴ In some states, an adopted individual is not treated as the child of the adopting parent, for purposes of construing another’s trust instrument, unless the adopted person lived while a minor as a regular member of the adopting parent’s household. *See, e.g.*, UNIF. PROBATE CODE § 2-705(c) (2003). Similarly, even a birth child who

distributions to the adoptee has breached its duty without regard to the breadth of its discretion, its honesty, its motive, or its exercise of its judgment.²⁵⁵ Accordingly, if a jurisdiction prefers the bad faith standard to affirmatively stating that trustees must act in good faith, it should build language into the bad faith standard similar to that of subsection 814(a) that requires trustees to administer trusts in accordance with their terms and purposes and the interests of the beneficiaries.²⁵⁶

With respect to whether (in addition to requiring trustees to exercise discretion in accordance with the terms and purposes of the trust and the interests of the beneficiaries) the standard is best stated as requiring good faith or prohibiting bad faith, there is much evidence that courts (and commentators) do not distinguish between the two, but use the terms interchangeably.²⁵⁷ From that perspective, little may be lost in using a bad faith, rather than a good faith, standard. However, because the very nature of the fiduciary relationship between a trustee and beneficiary requires, at a minimum, that the trustee act in good faith in administering the trust,²⁵⁸ the preferable alternative is to simply say so.²⁵⁹

has not been adopted by another may not be considered as a child of the natural parent for purposes of construing another's trust instrument, if the child did not live while a minor as a regular member of the natural parent's household. *See, e.g.*, UNIF. PROBATE CODE § 2-705(b) (2003).

²⁵⁵ For cases holding that trustees with extended discretion must administer their trusts in accordance with the settlor's purposes and the trust's terms, *see supra* notes [2398](#) and [2412](#).

²⁵⁶ A Missouri case is illustrative of combining a bad faith standard with an obligation that a trustee exercise its discretion in accordance with the terms and purposes of the trust and the interests of the beneficiaries. In reviewing a trustee's exercise of discretion to terminate a trust, the court stated the Missouri bad faith test that applies when the trust's terms do not include an objective standard against which the trustee's conduct can be judged:

When a testator vests sole discretion in a matter in the trustee and supplies no objective standards by which to evaluate the reasonableness of his conduct, a court must not interfere unless the trustee, in exercising his power, wilfully abuses his discretion or acts arbitrarily, fraudulently, dishonestly or with an improper motive.

Amer. Cancer Soc., St. Louis Div. v. Hammerstein, 631 S.W.2d 858, 863 (Mo. Ct. App. 1981). The same opinion also states, however: "Certainly, a grant of absolute discretion to a trustee is not a roving commission-the trustee must be guided by the interest of the beneficiary and must further trust purposes in the exercise of his power." *Id.* at 864.

²⁵⁷ *See supra* notes [1943-2189](#) and accompanying text.

²⁵⁸ Judge Cardozo's famous description of the trustee's duty of loyalty is instructive:

Many forms of conduct permissible in a work-a-day world for those acting at arm's length, are forbidden to those bound by fiduciary ties. A trustee is held to something stricter than the morals of the market place. Not honesty alone, but the punctilio of an honor the most sensitive, is then the standard of behaviour.

Meinhard v. Salmon, 164 N.E. 545, 546 (N.Y. 1928). While Judge Cardozo was addressing the duty of loyalty, rather than the trustee's obligation with respect to the exercise of extended discretion, the principle he describes is difficult to reconcile with the position that a trustee need not act in good faith, as long as it does not act in bad faith.

For a sampling of cases involving fiduciary relationships other than a trustee and beneficiary that acknowledge the fundamental obligation of a fiduciary to act in good faith, *see* *Moore v. Moore*, 599 S.E.2d 467, 472 (S.C. Ct. App. 2004) (partners); *Gedeon v. State Farm Mut. Auto. Ins. Co.*, 188 A.2d 320, 322 (Pa. 1963) (insurer that defends claims against an insured); *Johnson v. Provena St. Therese Medical Center*, 778 N.E.2d 298 (Ill. App. Ct. 2002) (personal representative and beneficiaries of an estate); *Hoopes v. Hammargren*, 725 P.2d 238, 242 (Nev. 1986) (physician and patient); *Burch v. Argus Properties, Inc.*, 92 Cal. App. 3d 128, 131, 154 Cal. Rptr. 485, 487 (Cal. Ct. App. 1979) (real estate broker and principal); *Paul v. North*, 380 P.2d 421, 428 (Kan. 1963) (parties who, by their concerted action, willingly and knowingly act for one another in such a manner as to impose mutual trust and confidence). Note also that good faith is required even in arm's length business dealings when the parties are not in a fiduciary relationship, *see, e.g.*, *Sheltry v. Unum Life Ins. Co. of America*, 247 F. Supp. 2d 169 (D. Conn. 2003), and is referenced in at least 50 different provisions of the Uniform Commercial Code. *See* Tory A. Wiegand,

IX. The UTC, Special and Supplemental Needs Trusts, and Public Benefits

Some UTC critics have argued that it will have a negative impact on beneficiaries of special and supplemental needs trusts (collectively, SNTs).²⁶⁰ This section of the Article discusses some of the principal reasons why that is not the case.²⁶¹

A. *What is the difference between a “special needs trust” and a “supplemental needs trust”?* Both refer to trusts intended to allow their beneficiaries to receive benefits from the trust without disqualifying them from also receiving public assistance for their support. While the terms are sometimes used interchangeably, many refer to trusts that are funded with the beneficiary’s own assets, including those to which the beneficiary is entitled under a personal injury award, as “special needs trusts,” and to trusts that are funded by third parties for a disabled beneficiary as “supplemental needs trusts.”²⁶² The eligibility rules vary considerably for SNTs funded with a person’s own assets and for those funded with assets of a third party.

B. *Will the UTC adversely affect the ability of beneficiaries of self-settled SNTs to qualify for public benefits?* No. Generally, under the Omnibus Budget Reconciliation Act of 1993 (the “Act,” or “OBRA 1993”), trusts that meet the Act’s requirements may be used by disabled persons to hold their own assets for their benefit, without disqualifying them from receiving public benefits.²⁶³ The most common such OBRA 1993 trust is the “pay-back” or “(d)(4)(A)” trust,²⁶⁴ the terms of which require the state to be repaid from the remaining trust assets at the beneficiary’s death an amount equal to the Medicaid benefits that were paid for the beneficiary’s medical care.²⁶⁵ Under OBRA 1993, the assets in such a trust are “insulat[ed]... from consideration by the Medicaid program so that public entitlement for medical care remains available to them.”²⁶⁶ The UTC will have no effect on that federally mandated result.²⁶⁷

C. *Will the UTC adversely affect the ability of beneficiaries of third-party created SNTs to qualify for public benefits?* No. Generally, public assistance for such purposes as medical and institutionalized care is limited to the needy, with consideration in determining

The Duty of Good Faith and Fair Dealing in Commercial Contracts in Massachusetts, 88 MASS. L. REV. 174, 178 (2004).

²⁵⁹ As discussed *supra* at note 2032 and accompanying text, many courts have expressly done just that.

²⁶⁰ See, e.g., Mark Merric and Douglas W. Stein, *A Threat to all SNTs*, TRUSTS & ESTATES 38 (Nov. 2004).

²⁶¹ For a more detailed analysis of the UTC and SNTs, see Richard E. Davis and Stanley C. Kent, *The Uniform Trust Code and Supplemental Needs Trusts*, 15 PROBATE LAW JOURNAL OF OHIO 53 (Jan./Feb. 2005). See also Richard E. Davis, *UTC is No Threat to SNTs*, TRUSTS & ESTATES 12 (Jan. 2005).

²⁶² See, e.g., Ian S. Oppenheim, *Guest Editor’s Message*, NAELA QUARTERLY 3 (Summer 2001).

²⁶³ See Pub. L. No. 103-66, tit. XIII, § 13562, 107 Stat. 312, 596-605 (1993) (codified at 42 U.S.C. § 1396p) (2004). See generally KRUSE, *supra* note 1623, at 11-13.

²⁶⁴ See 42 U.S.C. § 1396p(d)(4)(A) (2004).

²⁶⁵ See KRUSE, *supra* note 1632, at 12.

²⁶⁶ *Id.* at 11.

²⁶⁷ See Davis and Kent, *supra* note 26059, at 55-56.

eligibility given both to a person's income and his or her resources.²⁶⁸ If the assets of an SNT are treated as available to the beneficiary, he or she likely will not meet the resources test for public benefits qualification.²⁶⁹ "Available" for this purpose means "actually available."²⁷⁰ Many cases state that whether the assets of a third-party created trust are actually available to the beneficiary depends on whether the beneficiary may compel distributions for support.²⁷¹ While cases often state that the assets of support trusts are disqualifying available resources while those of discretionary trusts are not,²⁷² the underlying rationale for making that classification determinative of whether the trust assets are actually available to the beneficiary is that the beneficiary may compel distributions for support from a support trust but not from a discretionary trust.²⁷³ While the UTC does not classify trusts as "support" or "discretionary,"²⁷⁴ it does not change existing law on the question of whether a beneficiary of a third-party created trust may compel a distribution²⁷⁵ and thus does not affect whether such trusts will be disqualifying available resources for public benefits eligibility purposes.

Third-party created trusts that raise public benefits qualification issues take at least three forms: (i) the dispositive provisions specifically preclude the trustee from providing for the beneficiary's basic support, but instead authorize the trustee to provide for the beneficiary's supplemental needs;²⁷⁶ (ii) the dispositive provisions grant the trustee discretion to provide for the beneficiary's support;²⁷⁷ and (iii) the dispositive provisions grant the trustee discretion to make distributions to or for the benefit of the beneficiary without a support or supplemental needs standard.²⁷⁸

²⁶⁸ For an overview of Medicaid, the most significant source of public benefits for medical and institutionalized care of the needy, see Centers for Medicare & Medicaid Services, United States Department of Health and Human Services, *Medicaid: A Brief Summary*, available at <http://www.cms.hhs.gov/publications/overview-medicare-medicaid/default4.asp> (last visited April 25, 2005). See also Molly Mead Wood, *Medicaid Eligibility for Long-Term Care: The Basics*, 16 PREVENTIVE L. REP. 8 (1997) [with 2003 updates]; Barbara J. Collins, *Medicaid Eligibility and Coverage for Elderly and Disabled Clients: Overview and Update*, 12TH ANNUAL ELDER LAW INSTITUTE REPRESENTING THE ELDERLY CLIENT OF MODEST MEANS (P.L.I. N.Y. Practice Skills Course Handbook Series, No. F0-006P), June 2000, available at 75 PLI/NY 39, 41.

²⁶⁹ The limit on non-exempt assets a Medicaid recipient may have varies from state to state, but typically is \$2,000 for an individual and \$3,000 for a couple. LAWRENCE A. FROLIK AND ALISON MCCHRISTAL BARNES, ELDER LAW CASES AND MATERIALS 335 (3d ed. 2003). Exempt assets include a home, household items and personal effects, a car (subject to limitations), a burial plot and limited burial fund, and nominal life insurance policies. *Id.*

²⁷⁰ See 42 U.S.C. § 1396a(a)(17)(B) (1993); 20 C.F.R. §§ 416.120(c)(3) and 416.1201(a)(1) (2005); Department of Human Services and Programs Operation Manual System 01120.000. See also KRUSE, *supra* note 162, at 52-54; *Corcoran*, 859 A.2d 533; *Linser v. Office of Attorney Gen.*, 672 N.W.2d 643, 646 (N.D. 2003).

²⁷¹ See, e.g., *Corcoran*, 859 A.2d 533 (Conn. 2004); *Metz v. Ohio Dep't of Human Servs.*, 762 N.E.2d 1032, 1039 (Ohio Ct. App. 2001); *Tidrow v. Director, Mo. State Div. of Family Servs.*, 688 S.W.2d 9 (Mo. Ct. App. 1985). See also KRUSE, *supra* note 163, at 54 ("To the extent that trust income, resources, or both are limited in terms of beneficiaries' access to them, such income and trust resources are unavailable to the trusts' beneficiaries and are improperly considered by the state agencies charged with administering public entitlement funds.")

²⁷² See, e.g., *Eckes v. Richland Co. Soc. Servs.*, 621 N.W.2d 851, 855 (N.D. 2001); *In re Horton*, 668 N.W.2d 208 (Minn. Ct. App. 2003).

²⁷³ See *Eckes*, 621 N.W.2d at 855; *Horton*, 668 N.W.2d at 214.

²⁷⁴ See *supra* section VI.

²⁷⁵ See *supra* section VII.

²⁷⁶ See, e.g., *Carnahan v. Ohio Dep't of Human Servs.*, 743 N.E.2d 473 (Ohio Ct. App. 2000).

²⁷⁷ See, e.g., *Corcoran*, 859 A.2d 533.

²⁷⁸ See, e.g., *Simpson v. Kan. Dep't of Soc. and Rehab. Servs.*, 906 P.2d 174 (Kan. Ct. App. 1996). Such trusts are often preferred by planners because they provide considerably more flexibility than do trusts that limit distributions to providing for the beneficiary's supplemental needs.

With respect to third-party created trusts the terms of which explicitly allow distributions only for the beneficiary's supplemental needs, case law is clear and uniform that the assets of such trusts will not be considered in determining the beneficiary's eligibility for public benefits.²⁷⁹ Moreover, some states have codified that result.²⁸⁰ In short, "[d]iscretionary supplemental care trusts providing for the needs of beneficiaries not supplied by way of public benefits programs, created by nonbeneficiary settlors, appear to be legal, appropriate, and encouraged by both state common law and statutes."²⁸¹ For such trusts, the settlor's intent that the trust assets not be used for the beneficiary's support is clear, the beneficiary thus has no right to compel distributions for his or her support, and the trust's assets therefore are not available disqualifying resources of the beneficiary.²⁸²

The UTC will have no effect on that result. Its treatment of the duties and rights of the trustee and beneficiary with respect to discretionary distributions is limited to its codification of the traditional, common law requirement that a trustee exercise its discretion in good faith and in accordance with the terms and purposes of the trust and the interests of the beneficiaries.²⁸³ It does not otherwise address distribution issues, leaving them to case law.²⁸⁴ More specifically, a 2005 amendment to the comment to section 814 provides:

[W]hether the trustee has a duty in a given situation to make a distribution depends on the exact language used, whether the standard grants discretion and its breadth, whether this discretion is coupled with a standard, whether the beneficiary has other available resources, and, more broadly, the overriding purposes of the trust. For example, distilling the results of scores of cases, the Restatement (Third) of Trusts concludes that there is a presumption that the "trustee's discretion should be exercised in a manner that will avoid either

²⁷⁹ See KRUSE, *supra* note 1632, at 70-78. An Ohio case, *Young v. State Department of Human Services*, 668 N.E.2d 908 (Ohio 1996), was almost the exception, as three members of the Ohio Supreme Court dissented on the ground that such trusts violate public policy. Contrary to the dissent in *Young*, most courts that have considered the public policy implications of supplemental needs trusts have expressly found that such trusts do not violate public policy. See, e.g., *Hecker v. Stark Co. Soc. Serv. Bd.*, 527 N.W.2d 226 (N.D. 1994); *In re Leona Carlisle Trust*, 498 N.W.2d 260 (Minn. Ct. App. 1993); *In re Wright's Will*, 107 N.W.2d 146 (Wis. 1961).

²⁸⁰ See KRUSE, *supra* note 1632, at 78-82.

²⁸¹ *Id.* at 82.

²⁸² As the Connecticut Supreme Court recently stated,

[u]nder applicable federal law, only assets actually available to a medical assistance recipient may be considered by the state in determining eligibility for public assistance programs such as title XIX [medicaid].... A state may not, in administering the eligibility requirements of its public assistance program pursuant to title XIX ... presume the availability of assets not actually available...."

Corcoran, 859 A.2d at 545.

²⁸³ See UNIF. TRUST CODE § 814(a) (2005). See also *supra* section VII.

²⁸⁴ See UNIF. TRUST CODE § 814 cmt. (2005). Further, the UTC's elimination of the common law distinction between "support trusts" and "discretionary trusts" for creditors rights purposes

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.

UNIF. TRUST CODE § 504 cmt. (2005).

disqualifying the beneficiary for other benefits or expending trust funds for purposes for which public funds would otherwise be available.”²⁸⁵

Third-party created trusts under which the trustee is given the discretion to provide for the beneficiary’s support may or may not disqualify the beneficiary from receiving public assistance. If the settlor directs that the beneficiary’s support be provided from the trust, without granting the trustee discretion in that regard, the trust assets clearly will be available resources of the beneficiary for public benefits eligibility purposes.²⁸⁶ By contrast, a third-party created trust over which the trustee has broad discretion over distributions, without a support standard, will not be an available resource that will disqualify the beneficiary from public benefits.²⁸⁷ Considerably more difficult are cases in which the trustee is given discretion over distributions for the beneficiary’s support. In many such discretionary support trust cases, the trust assets have been held not available to the beneficiary for public benefits qualification purposes (or insulated from a state creditor seeking reimbursement for the costs of support it provided), while in many others the trust assets were treated as disqualifying available resources (or as subject to the state’s reimbursement claim).²⁸⁸

An important – indeed often determinative – factor in resolving such cases is the court’s analysis of whether the settlor intended the trust to provide for the beneficiary’s support, or whether the settlor intended that, if the beneficiary otherwise qualified for public support, the trust assets would not be available for that purpose.²⁸⁹ While the UTC affirms the importance of the settlor’s intent in a variety of contexts,²⁹⁰ it does not address how to interpret the terms of a trust to ascertain the settlor’s intent in such a case. As discussed above, however, in acknowledging that the rights and duties of the beneficiaries and trustee with respect to discretionary distributions depend on a variety of factors, including the purposes of the trust, the comment to section 814 quotes the Third Restatement presumption that the trustee’s discretion is to be exercised in such a way as to preserve the beneficiary’s eligibility for public benefits and not to expend trust funds for purposes for which public funds otherwise would be available.²⁹¹ As a result, and because (i) the UTC treats trusts for the support of beneficiaries as discretionary trusts,²⁹² (ii) the UTC does not treat discretionary trusts without support standards as support trusts,²⁹³ and (iii) the UTC does not enhance the ability of beneficiaries of discretionary trusts to compel distributions,²⁹⁴ the UTC should not have an adverse effect on the uncertain treatment of discretionary support trusts for public benefits eligibility purposes.²⁹⁵

²⁸⁵ UNIF. TRUST CODE § 814 cmt. (2005) (citing RESTATEMENT (THIRD) OF TRUSTS, § 50 cmt. e & Reporter’s Notes (Tentative Draft No. 2, 1999)).

²⁸⁶ See, e.g., *Nason v. Commw. of Penn.*, 520 A.2d 1223 (Pa. Commw. Ct. 1987). See also KRUSE, *supra* note 1632, at 51-52.

²⁸⁷ See, e.g., *Simpson*, 906 P.2d at 177-79.

²⁸⁸ A 2002 analysis of the results of 54 discretionary support trust cases reports that the trust assets were insulated from the state in 30 cases, and not insulated in 24. See KRUSE, *supra* note 1623, at 117-128.

²⁸⁹ See KRUSE, *supra* note 1632, at 55-58.

²⁹⁰ See, e.g., UNIF. TRUST CODE Prefatory Note (2005). Under § 105(a), the terms of the trust generally override conflicting provisions of the Code. UNIF. TRUST CODE § 105(a) (2005).

²⁹¹ See *supra* note 2843 and accompanying text.

²⁹² See *supra* notes 1543-1556 and accompanying text.

²⁹³ See *supra* notes 1576-1596 and accompanying text.

²⁹⁴ See *supra* section VII.

²⁹⁵ The planning lesson is clear:

Public benefits cases involving trusts in which the trustee is given broad discretion over distributions, without a support standard or language limiting distributions to the beneficiary's supplemental needs, are rare.²⁹⁶ In the all too common discretionary support trust cases, however, courts state that assets in discretionary trusts are considered as available resources of the beneficiary only to the extent of distributions actually made.²⁹⁷ Further, as previously noted, many cases in which the trustee is granted discretion over distributions have held such trusts not to be available resources of the beneficiaries even when a support standard also is included.²⁹⁸ It is thus clear that a purely discretionary trust, without a support standard (or language limiting distributions to providing for supplemental needs), will not be counted as an available resource of its beneficiary for public benefits eligibility purposes. For the reasons set forth in the discussion of discretionary support trusts, above,²⁹⁹ the UTC will have no effect on that result.

D. Under the UTC, would a public benefits provider be able to recover the costs of the support it provided to a beneficiary of a spendthrift trust from the trust's assets? No. As previously discussed, the UTC does include a necessities provider exception to spendthrift protection.³⁰⁰

E. Under the UTC, would a public benefits provider be able to recover the costs of the support it provided to a beneficiary of a discretionary trust by compelling discretionary distributions it could reach? No. Also as previously discussed, there is no exception for claims

[W]hen lawyers consider Medicaid eligibility, unless the settlor intends the trust to be used for the beneficiary's support, language that specifically authorizes the trustee to use the entrusted funds for support purposes is inappropriately written. Beneficiaries of such trusts who are eligible for public medical benefits may or may not be able to continue receiving public support for basic necessities through dispensing agencies while at the same time receiving discretionary payments from privately endowed trusts for other purposes. The discretionary trust corpus may be deemed available for basic living needs. The case law is not consistent. The discretionary support trust is, therefore, an unreliable method by which settlors can continue to provide for their beneficiaries' additional needs beyond basic necessities. The funds are at risk held in such trusts. The language encourages eager state agencies and their employees to attempt its indirect seizure. "Use it. Reapply (for funds) when it's gone" may be their message.

| KRUSE, *supra* note 1632, at 69 (footnotes omitted). The problems discretionary support trusts create for their beneficiaries who attempt to qualify or remain qualified for public assistance are serious, but they are neither created nor exacerbated by the UTC.

| ²⁹⁶ Mr. Kruse's 2002 comprehensive compilation and analysis of public benefits cases involving third-party created trusts characterizes only one—*Simpson*, 906 P.2d 174 (Kan. Ct. App. 1996)—as involving a trust the terms of which grant the trustee discretion over distributions, but do not include a support standard and do not limit distributions to the beneficiary's supplemental needs. See KRUSE, *supra* note 1623, at 117-28. Perhaps the scarcity of such cases is attributable to the fact that the assets of such trusts clearly are not available for public benefits qualification purposes and generally are not challenged by state agencies. For a case in which the trustee was granted the "absolute and uncontrolled" discretion over distributions, but with precatory language stating the settlor's "fond hope" that the trustee would provide for the beneficiaries' support, see *Zeoli v. Comm'r of Social Svc.*, 425 A.2d 553 (Conn. 1979) (holding trust assets were not disqualifying available resources).

| ²⁹⁷ See, e.g., *Linser*, 672 N.W.2d at 646-47.

| ²⁹⁸ See *supra* note 2867.

| ²⁹⁹ See *supra* notes 2845-2934 and accompanying text.

| ³⁰⁰ See *supra* notes 42-46 and accompanying text.

of the state or other necessities providers from the UTC's general prohibition against creditors of a beneficiary compelling discretionary distributions they can reach.³⁰¹

F. *If a state enacts a statute making it a spendthrift exception creditor,³⁰² would a beneficiary of an SNT who also is receiving Medicaid benefits be able to continue receiving benefits from the SNT?* Yes. Generally, the state's claim for Medicaid reimbursement, which does not arise until after the death of the survivor of the Medicaid recipient and his or her spouse, is to recover its costs from the recipient's estate.³⁰³ Accordingly, the state would not be a creditor of the Medicaid recipient during his or her life, and would thus not be able to attach distributions from the SNT, or otherwise reach it, regardless of whether the trust terms include a spendthrift provision or the state is a spendthrift exception creditor.

X. Divorce and the UTC

The UTC addresses divorce only in the context of the rights of a former spouse or child (with a judgment or court order for support or maintenance) of a beneficiary of a spendthrift or discretionary trust to alimony or child support.³⁰⁴ Its critics claim that it will have a variety of other adverse consequences to a beneficiary of a third-party created trust who divorces.³⁰⁵

A. *Under the UTC, if a beneficiary of a third-party created trust divorces, may his or her ex-spouse reach the beneficiary's interest in the trust to satisfy an alimony claim?* Yes, if certain conditions are met. As previously discussed, if the ex-spouse has a judgment or court order for support or maintenance, under the UTC a spendthrift provision will not protect the beneficiary's interest.³⁰⁶ In such a case, the ex-spouse's remedy is to attach present or future distributions to or for the benefit of the beneficiary, provided that the court may limit any such award "to such relief as is appropriate under the circumstances."³⁰⁷ If the trust provides for distributions to be at the trustee's discretion, the ex-spouse may compel distributions he or she can reach, but only if (i) he or she has a judgment or court order for support or maintenance and (ii) in not making the distribution, the trustee has not complied with a standard of distribution or has abused a discretion.³⁰⁸ In such a case, the UTC provides for the court to order the trustee to pay to the ex-spouse "such amount as is equitable under the circumstances but not more than the amount the trustee would have been required to distribute to or for the benefit of the beneficiary had the trustee complied with the standard or not abused the discretion."³⁰⁹ Also as previously

³⁰¹ See *supra* note 109 and accompanying text.

³⁰² See, e.g., KY. REV. STAT. ANN. § 381.180(6)(c) (Banks-Baldwin 1990).

³⁰³ See 42 U.S.C. § 1396p(b)(1) (1993). See also Davis and Kent, *supra* note 26059, at 58-59. For a case in which the "estate" subject to repayment of the state's claim was held to include the assets of a testamentary trust established for the recipient with the amount that he otherwise would have been entitled to receive as an elective share, see *Estate of DeMartino v. Division of Med. Assistance and Health*, 861 A.2d 138 (N.J. Super. 2004).

³⁰⁴ See UNIF. TRUST CODE §§ 503(b)(1) and 504(c)(1) (2005).

³⁰⁵ See, e.g., Mark Merric, Carl Stevens, and Jane Freeman, *The Uniform Trust Code: A Divorce Attorney's Dream*, ESTATE PLANNING 41 (CCH Oct.-Nov. 2004).

³⁰⁶ See UNIF. TRUST CODE § 503(b)(1) (2005). See also *supra* notes 27-29 and accompanying text.

³⁰⁷ UNIF. TRUST CODE § 503(c) (2005).

³⁰⁸ See UNIF. TRUST CODE § 504(c)(1) (2005).

³⁰⁹ UNIF. TRUST CODE § 504(c)(2) (2005).

discussed, there is much support for the UTC's treatment of an ex-spouse as a spendthrift exception creditor, but limited support for its allowing an ex-spouse to compel discretionary distributions.³¹⁰

B. Will the UTC affect whether a beneficiary's trust interest will be divisible in a divorce? The UTC does not address the division of property in a divorce. In most states, generally only "marital property"³¹¹ is subject to division.³¹² Because a divorcing spouse's interest in a third-party created trust generally will have been received by gift or inheritance, in most states it will be separate property that is not subject to division, without regard to the extent or nature of the beneficiary's interest in the trust.³¹³ In states in which separate property is divisible,³¹⁴ however, or in which the income from, or appreciation in, separate property is marital property (and thus divisible),³¹⁵ part or all of a beneficiary's interest in a trust may be divisible in a divorce,³¹⁶ regardless of whether the UTC has been enacted.

If under applicable state law part or all of a beneficiary's interest in a third-party created trust is not protected from division in divorce by virtue of it being separate property, its divisibility in a given case may depend on one or more of a multitude of factors, such as (i) whether the beneficiary's interest is in a trust created by another that is revocable by its still living settlor;³¹⁷ (ii) whether the beneficiary's interest is vested;³¹⁸ (iii) whether the beneficiary's

³¹⁰ See *supra* notes 28-29, and 117-118, and accompanying text.

³¹¹ The definition of "marital property" will vary by jurisdiction. By way of example, the Uniform Marriage and Divorce Act, as originally promulgated, defined "marital property" as "all property acquired by either spouse subsequent to the marriage" other than property (i) acquired by gift or inheritance, (ii) acquired in an exchange for separate property, (iii) acquired after a decree of legal separation, (iv) excluded by agreement, or (v) representing the increase in the value of property acquired before the marriage. UNIF. MARRIAGE AND DIVORCE ACT § 307 (1971) (amended 1973).

³¹² See BRETT R. TURNER, *EQUITABLE DISTRIBUTION OF PROPERTY* § 2.08 (2d ed. 1994).

³¹³ See TURNER, *supra* note 311, at § 6.28.

³¹⁴ In some states, all of a couple's assets, without regard to when or how acquired, are subject to division at divorce. See TURNER, *supra* note 311, at § 2.07. Further, in some of the states in which separate property generally is not divisible, it may be awarded to the other spouse if, for example, failure to make such an award will result in undue hardship. See TURNER, *supra* note 311, at § 8.12.

³¹⁵ See TURNER, *supra* note 311, at §§ 5.21 and 5.22.

³¹⁶ See, e.g., *Davidson v. Davidson*, 474 N.E.2d 1137 (Mass. App. Ct. 1985).

³¹⁷ See, e.g., *In re Marriage of Gorman*, 36 P.3d 211 (Colo. Ct. App. 2001) (holding that the beneficiary's vested interest in the trust, though subject to divestment by the settlor's revocation or amendment, was property subject to division.) Shortly after *Gorman* was decided, new legislation effectively overruled it. See COLO. REV. STAT. § 14-10-113(7)(b) (2004).

³¹⁸ For a case stating that only vested interests in trust are divisible, see *In re Marriage of Beadle*, 968 P.2d 698 (Mont. 1998). See also *McGinley v. McGinley*, 565 A.2d 1220 (Pa. Super. Ct. 1989). Whether an interest is vested, in the traditional property law sense, however, should not be determinative of its divisibility in divorce. For example, a gift "to my spouse, S, for life, remainder to my child, C, if C survives my spouse; if not to X" creates a contingent remainder in C, while a gift "to my spouse, S, for life, remainder to my child, C, provided that if C does not survive S, remainder to X" creates a vested remainder, subject to divestment, in C. See *DUKEMINIER ET. AL.*, *supra* note 223, at 627-28. Because there is no substantive difference in C's interest in the two examples, they should not be treated differently in a divorce. See also *Stern v. Stern*, 331 A.2d 257, 262 (N.J. 1975) ("[t]he concept of vesting should probably find no significant place in the developing law of equitable distribution."); *S.L. v. R.L.*, 774 N.E.2d 1179 (Mass. App. Ct. 2002), *rev. denied*, 780 N.E.2d 468 (2002) (beneficiary's remainder interest treated as divisible property despite being contingent on the beneficiary surviving her mother); TURNER, *supra* note 311, at § 6.28; Marc A. Chorney, *Interests in Trusts as Property in Dissolution of Marriage: Identification and Valuation*, 40 REAL PROP. PROB. & TRUST J. ___ (2005).

interest may be defeated by another's exercise of a power of appointment;³¹⁹ (iv) whether the beneficiary's interest may be eliminated by discretionary distributions to another beneficiary, or by another beneficiary's power to invade principal;³²⁰ (v) whether the beneficiary's interest is a remainder;³²¹ (vi) whether the beneficiary's interest is an income interest;³²² or (vii) whether the beneficiary's interest is subject to the discretion of the trustee and thus is treated as an expectancy, rather than as divisible property.³²³

While application of most of the factors listed in the preceding paragraph clearly would be unaffected by enactment of the UTC, critics argue that a beneficiary's discretionary interest in a trust would more likely be divisible under the UTC than under non-UTC law.³²⁴ A Colorado case, *Marriage of Jones*,³²⁵ is said to illustrate the protection the common law affords discretionary trust interests in divorce that would be lost by enactment of the UTC.³²⁶ *Jones* was a divorce proceeding involving a testamentary trust the wife's mother had created.³²⁷ The trustees – the testator's husband (the wife's father) and a bank – were granted the “uncontrolled discretion” to make distributions of income and principal as they determined necessary for the health, welfare, comfort, support, maintenance and education of the testator's husband, the wife, and the wife's descendants.³²⁸ Unless earlier terminated by discretionary distributions, the trust was to terminate, at the earliest, at the wife's death.³²⁹ The remainder beneficiaries were the wife's descendants, if any, or the testator's heirs.³³⁰ The court held that because the wife's receipt of distributions was subject to the “uncontrolled” discretion of the trustees, her interest in the trust was not property subject to division.³³¹

³¹⁹ See, e.g., *S.L.*, 774 N.E.2d 1179 (beneficiary's parent's power to appoint the trust estate to others precluded treating beneficiary's interest as property subject to division). See also Chorney, *supra* note 3167, at ___.

³²⁰ See, e.g., *In re Marriage of Balanson*, 25 P.3d 28 (Colo. 2001) (beneficiary's remainder interest was property subject to division despite her father, the income beneficiary and trustee, having the power to distribute principal to himself for his support, care, and maintenance); *Davidson*, 474 N.E.2d 1137 (beneficiary's remainder interest in a trust created by his father was divisible despite the trustee having the “uncontrolled discretion” to invade principal for his mother).

³²¹ “The general rule is...that the remainder interest in a trust constitutes *property* which can be divided upon divorce.” TURNER, *supra* note 3119, at § 6.28. However, “[a] small number of decisions hold that remainder interests are not *property*.” *Id.* at n.663.

³²² Compare *In re Marriage of Guinn*, 93 P.3d 568 (Colo. Ct. App. 2004) (mandatory income interest not treated as property subject to division), with *Fox v. Fox*, 626 N.W.2d 660 (N.D. 2001) (mandatory income interest was treated as property subject to division). See also *Marriage of Jones*, 812 P.2d 1152 (because beneficiary's interest in a discretionary trust was not property – marital or separate – income distributed to beneficiary at the trustee's discretion was a non-divisible gift); *Friebel v. Friebel*, 510 N.W.2d 767 (Wis. Ct. App. 1993).

³²³ See, e.g., *Marriage of Jones*, 812 P.2d 1152; *In re Rosenblum*, 602 P.2d 892 (Colo. Ct. App. 1979); *Hawkins v. Hawkins*, 526 A.2d 872 (Conn. Ct. App. 1987); *In re Eddy*, 569 N.E.2d 174 (Ill. Ct. App. 1991).

³²⁴ See Merric, Stevens, and Freeman, *supra* note 3034, at 47.

³²⁵ 812 P.2d 1152 (Colo. 1991).

³²⁶ See Merric, Stevens, and Freeman, *supra* note 3043, at 47.

³²⁷ *Marriage of Jones*, 812 P.2d at 1153.

³²⁸ *Id.*

³²⁹ *Id.*

³³⁰ *Id.*

³³¹ *Id.* at 1157. In Massachusetts, a divorcing spouse's interest in a discretionary trust may not be excluded from division:

[w]hile a judge is not necessarily precluded from including within the marital estate...a party's beneficial interest in a discretionary trust..., because of the peculiar nature of such a trust, the trust instrument and other relevant evidence must be examined closely to determine whether that party's interest is too remote or speculative to be so included.

D.L. v. G.L., 811 N.E.2d 1013, 1023 (Mass. App. Ct. 2004).

UTC critics argue that the UTC would change the result in cases like *Jones*.³³² The argument focuses on (i) the UTC's elimination of the distinction between discretionary and support trusts, (ii) the UTC's standard of review of the trustee's exercise of discretion, and (iii) the UTC's acknowledgment of the right of a beneficiary of a discretionary trust to sue to compel distributions if the trustee abuses its discretion or fails to comply with a standard for distribution.³³³ The rationale for the court's decision in *Jones* was that the wife had no right to receive current or future distributions; rather, distributions were to be made at the sole discretion of the trustee.³³⁴ The UTC's elimination of the distinction between discretionary and support trusts for purposes of sections 501 and 504, which does not affect the duties and rights of the trustee and the beneficiaries with respect to discretionary distributions,³³⁵ should have no effect on that analysis.³³⁶ Further, subsection 814(a)'s standard of judicial review for the exercise of discretion by a trustee is not substantively different from the four standards³³⁷ referred to in *Jones*,³³⁸ and thus also should not have affected its result. Finally, a beneficiary of a discretionary trust always has had the ability to bring an action to compel distributions for abuse of discretion or failure to comply with a standard of distribution.³³⁹ Thus, the UTC's statement in section 504(d) that the remainder of section 504 does not limit the beneficiary's rights in that regard also would have had no effect on the result in *Jones*.

C. *Will the UTC affect whether a beneficiary's interest in a discretionary trust, even if not divisible, will be considered in dividing the couple's property?* It should not. In making an equitable division of a divorcing couple's property, some states consider the spouses' economic circumstances.³⁴⁰ For example, in *Jones*, discussed above, the court held that the wife's discretionary interest in her mother's trust was not property subject to division, but was an economic circumstance to be considered in equitably dividing the couple's marital property.³⁴¹ Again based on the claim that the UTC creates expanded rights to distributions in beneficiaries of discretionary trusts, the argument has been made that a beneficiary's interest in a discretionary trust under the UTC will be more valuable than it otherwise would, thus adversely affecting the

³³² See Merric, Stevens, and Freeman, *supra* note 3034, at 47.

³³³ *Id.*

³³⁴ *Marriage of Jones*, 812 P.2d at 1156-57.

³³⁵ See UNIF. TRUST CODE § 504 cmt. (2005). See also *supra* section VI.

³³⁶ Note, however, that the discretionary trust in *Jones* included a support standard, and that in many jurisdictions, in litigation involving public benefits, discretionary support trusts have been held to create enforceable standards for distributions for support. See *supra* note 2876 and accompanying text.

³³⁷ See *supra* note 2110.

³³⁸ See *supra* section VII. Subsection 814(a) requires trustees to act in good faith and in accordance with the terms and purposes of the trust and the interests of the beneficiaries. UNIF. TRUST CODE § 814(a) (2005). As discussed *supra* at notes 2042-2189 and accompanying text, language like that used in *Jones* to describe the minimum standard of conduct required of a trustee with discretionary powers is another way of requiring that a trustee act in good faith. Furthermore, three of the four different formulations of the minimum standard of conduct described in *Jones* include requirements that the trustee not abuse its discretion or act from an improper motive. See *supra* note 2101. A trustee who does not exercise its discretion in accordance with the purposes of the trust or the interests of the beneficiaries (as described in the terms of the trust, see UNIF. TRUST CODE § 103(8) (2005)), presumably would have abused its discretion or acted from an improper motive.

³³⁹ See *supra* notes 1823-1845 and accompanying text.

³⁴⁰ See, e.g., COLO. REV. STAT. § 14-10-113(1)(c) (2004); MO. REV. STAT. § 452.330.1(1). See also *Athorne v. Athorne*, 128 A.2d 910 (N.H. 1957). The future financial needs of the spouses also is a factor that commonly is considered in equitably dividing a couple's property. See TURNER, *supra* note 3101, at § 8.08.

³⁴¹ *Marriage of Jones*, 812 P.2d at 1158.

beneficiary with respect to the division of property when the couple's economic circumstances are to be taken into consideration.³⁴² Because the UTC does not affect the duties and rights of the trustee and beneficiaries with respect to discretionary distributions,³⁴³ that should not be the case.

D. *Will the UTC affect whether a beneficiary's interest in a discretionary trust will be considered for purposes of awarding spousal maintenance or child support against the beneficiary?* Among the factors that may affect an award of spousal maintenance or child support in a divorce are the financial resources of the spouses.³⁴⁴ UTC critics also argue that a beneficiary of a discretionary trust in a UTC jurisdiction will, by virtue of the trust interest, have income imputed to the beneficiary for purposes of awarding spousal maintenance or child support against him or her.³⁴⁵ Again, the argument is based on the claim that beneficiaries of discretionary trusts under the UTC have expanded rights to compel distributions, and again, the response is that they do not.³⁴⁶

XI. Bankruptcy and the UTC

Another concern UTC critics have expressed is that it will have an adverse effect on trust beneficiaries who go through bankruptcy.³⁴⁷ Because (i) most trust instruments include spendthrift provisions,³⁴⁸ (ii) bankruptcy law respects spendthrift trusts that are effective under state law,³⁴⁹ and (iii) spendthrift trusts (with limited exceptions) are effective under the UTC,³⁵⁰

³⁴² See Merric, Stevens, and Freeman, *supra* note 3043, at 49.

³⁴³ See *supra* section VII.

³⁴⁴ See, e.g., UNIF. MARRIAGE AND DIVORCE ACT §§ 308 and 309 (1973).

³⁴⁵ See Merric, Stevens, and Freeman, *supra* note 3043, at 49-50. While not based on an imputation of income theory, a pre-UTC case held that although the discretionary nature of a beneficiary's interest in the principal of a trust protected it from being reached by his spouse, the discretionary interest could be considered in determining both alimony and the division of property. *Athorne*, 128 A.2d 910.

³⁴⁶ See *supra* section VII. The argument is also based on a recent Massachusetts case, *Dwight v. Dwight*, 756 N.E.2d 17 (Mass. App. Ct. 2001). See Merric, Stevens, and Freeman, *supra* note 303, at 50. *Dwight*, however, does not support that argument. In *Dwight*, which was not decided under the UTC, the spouses entered into a separation agreement under which the wife was expressly authorized to bring an action for alimony if, among other things, the husband received "a substantial inheritance which increases his income." *Id.* at 18-19. Thereafter, the husband's father died and left approximately \$435,000 to a discretionary support trust for the husband and his issue. *Id.* at 19-20. The appellate court first affirmed the trial court's determination that the gift, though left to the discretionary support trust for the husband and his issue, constituted a substantial inheritance within the meaning of the separation agreement. *Id.* at 20-21. Next, the court also affirmed the lower court's finding that the substantial inheritance increased the husband's income, even though only one \$7,000 distribution had been made to the husband from the trust over a several year period. *Id.* at 21. That finding, which was based on the fact that the husband had told the trustee that he did not want any income from the trust and on the broad purposes for which discretionary payments could be made to the husband, was determined by the appellate court not to be clearly erroneous. *Id.* The court also noted that under Massachusetts law, if the trustee had determined that the husband needed distributions from the trust, the trustee would have been under a duty to provide them. *Id.* n.5.

³⁴⁷ See, e.g., Merric and Oshins, *supra* note 1, at 484-85.

³⁴⁸ See *supra* note 100 and accompanying text.

³⁴⁹ See 11 U.S.C. § 541(c)(2) (1994).

³⁵⁰ See UNIF. TRUST CODE §§ 502 and 503 (2005).

the UTC should have little or no effect on beneficiaries of third-party created trusts in the bankruptcy context.

A. *Under the UTC, may creditors of a beneficiary of a spendthrift trust reach the beneficiary's interest in the trust through a bankruptcy proceeding?* Generally, no. Under the Bankruptcy Code, a trust interest that is not alienable under applicable state law does not become a part of the bankruptcy estate.³⁵¹ Under the UTC, a beneficiary's interest in a spendthrift trust is not alienable (except with respect to exception creditors).³⁵²

B. *If the terms of the trust do not include a spendthrift provision, would a bankrupt beneficiary's interest in a third-party created trust governed by the UTC become part of the bankruptcy estate?* Generally, a debtor's bankruptcy estate includes all interests in property, including equitable interests in trusts, owned by the debtor at the time of bankruptcy filing.³⁵³ The exception that protects spendthrift trusts, however, is not limited to trusts that include spendthrift provisions. Rather, the exception provides that: "A restriction on the transfer of a beneficial interest of the debtor in a trust that is enforceable under applicable nonbankruptcy law is enforceable in a case under this title."³⁵⁴ If a beneficiary's interest in a third-party created trust is subject to the trustee's discretion, including to make distributions for the beneficiary's support, the interest may be protected from becoming a part of the beneficiary's bankruptcy estate even if the terms of the trust do not include a spendthrift provision.³⁵⁵ Because decisions so holding are based on the beneficiaries of such trusts being unable to compel distributions,³⁵⁶ and because the UTC does not change the duties and rights of the trustee and beneficiaries with respect to discretionary distributions from third-party created trusts,³⁵⁷ the same protection in bankruptcy for discretionary interests in non-spendthrift trusts should be available under the UTC as is available under non-UTC law. Clearly, though, the simplest and safest course for obtaining protection in bankruptcy for a beneficiary's interest in a third-party created trust is to include a spendthrift provision in the instrument.

XII. Conclusion

Article 5 of the UTC, dealing with the rights of creditors of trust beneficiaries and settlors, and subsection 814(a), describing the standard to which trustees will be held in the exercise of discretion, regardless of its breadth, have raised a number concerns among some

³⁵¹ See 11 U.S.C. § 541(c)(2) (1994). For two recent cases under which this provision protected debtors' interests in spendthrift trusts, see *In re Wachter*, 314 B.R. 365 (E.D. Tenn. 2004) and *In re Spencer*, 306 B.R. 328 (C.D. Cal. 2004).

³⁵² See UNIF. TRUST CODE § 502(c) (2005).

³⁵³ See 11 U.S.C. § 541(a)(1) (1994).

³⁵⁴ 11 U.S.C. § 541(c)(2) (1994).

³⁵⁵ See, e.g., *In re Knight*, 164 B.R. 372 (Bankr. S.D. Fla. 1994); *In re Pechenec*, 59 B.R. 899 (D. Kan. 1986); *In re Britton*, 300 B.R. 155 (D. Conn. 2003). In dictum, however, in a case involving the denial of discharge to a debtor who did not meet the Bankruptcy Code's disclosure requirements, a bankruptcy court has stated that the protection afforded by § 541(c)(2) is limited to spendthrift trusts and is not available to discretionary trusts without spendthrift provisions. *In re Katz*, 203 B.R. 227 (Bankr. E.D. Pa. 1996).

³⁵⁶ See *Knight*, 164 B.R. at 376 n.2; *Pechenec*, 59 B.R. at 904-05; *Britton*, 300 B.R. at 158-59.

³⁵⁷ See *supra* section VII.

trusts and estates lawyers. A number of amendments to the UTC and its comments have been made since its promulgation in 2000 that address many of those concerns:

1. The definition of “power of withdrawal” in section 103(11) was amended to avoid a beneficiary/trustee, whose power to distribute for his or her own benefit is limited by an ascertainable standard, from being treated as a settlor of a revocable trust for creditors’ rights purposes under section 505(b)(1).³⁵⁸
2. Section 501, and its comment, were amended to make it clear that its broad remedies are available to a creditor only if the terms of the trust do not include a spendthrift provision, or the provision does not apply to a particular beneficiary’s interest.³⁵⁹
3. The comment to section 501 also was amended to (i) acknowledge that a beneficiary’s interest may be too indefinite or contingent for a creditor to reach, or may qualify for an exemption under the jurisdiction’s general creditor exemption statutes, (ii) delete a paragraph describing creditor remedies and procedures, and (iii) delete the reference to the beneficiary’s support needs in its discussion of the court’s ability to limit a creditor’s award as appropriate under the circumstances.³⁶⁰
4. Section 503 was amended to specify that the remedy under the UTC for a spendthrift exception creditor is limited to the attachment of present or future distributions to or for the benefit of the beneficiary,³⁶¹ and to authorize the court to limit a creditor’s award as appropriate under the circumstances.³⁶²
5. Section 504 was amended to clarify that most creditors of a beneficiary may not compel discretionary distributions even if the beneficiary/debtor is the trustee, if distributions for the beneficiary/trustee are limited by an ascertainable standard and the creditor otherwise may not reach the interest.³⁶³
6. The comment to section 504 was amended to clarify that section 504’s elimination of the distinction between discretionary and support trusts for creditors’ rights purposes does not affect the duties and rights of the trustee and beneficiary with respect to distributions.³⁶⁴
7. Section 506 was amended to add a narrow definition of a “mandatory distribution” from a trust that a creditor may reach if it is not made within a reasonable time after its designated distribution date.³⁶⁵

³⁵⁸ See UNIF. TRUST CODE § 103(11) (2005).

³⁵⁹ See UNIF. TRUST CODE § 501 and cmt. (2005).

³⁶⁰ Compare UNIF. TRUST CODE § 501 cmt. (2005) with UNIF. TRUST CODE § 501 cmt. (2004)

³⁶¹ See UNIF. TRUST CODE § 503(c) (2005).

³⁶² *Id.*

³⁶³ See UNIF. TRUST CODE § 504(e) (2005).

³⁶⁴ See UNIF. TRUST CODE § 504 cmt. (2005).

³⁶⁵ See UNIF. TRUST CODE § 506(a) (2005).

8. The comment to section 814 was amended to acknowledge that other than requiring trustees to exercise discretionary powers in good faith and in accordance with the terms and purposes of the trust and the interests of the beneficiaries, the UTC does not address the duties and rights of the trustee and beneficiaries with respect to discretionary distributions. Rather, the comment states that those duties and rights will continue to be governed by case law and such factors as the precise language used in the instrument, whether and if so the extent to which discretion is granted, whether a standard for distributions is provided, whether the beneficiary has other resources, and the overriding purposes of the trust.³⁶⁶

These amendments have improved the UTC and addressed many concerns that have been raised about its creditors' rights provisions. Generally, for third-party created spendthrift and discretionary trusts, the UTC provides as much or more protection to beneficiaries' interests than does the common law. By not recognizing an exception for the claims of necessities providers,³⁶⁷ narrowing the exception for government claimants,³⁶⁸ and codifying an exclusive list of exception creditors that bars tort claimant and other public policy exceptions,³⁶⁹ the UTC has strengthened spendthrift protection. Further, as a general rule, no creditor of a beneficiary, even one who has provided support to the beneficiary, may compel discretionary distributions it can reach.³⁷⁰ The only exception to that rule is for child and spousal support claimants, and their ability to compel discretionary distributions is dependent on (i) their having a judgment or court order for support or maintenance and (ii) the trustee's failure to make distributions being an abuse of discretion or a failure to comply with a standard for distributions.³⁷¹

The UTC will not increase the ability of beneficiaries of third-party created trusts to compel discretionary distributions.³⁷² Requiring a trustee to act in good faith and in accordance with the terms and purposes of the trust and the interests of the beneficiaries, as the UTC does in subsection 814(a), is a codification of the common law.³⁷³ The new comment to section 504 explicitly states that the UTC's elimination of the distinction between discretionary and support trusts for purposes of sections 501 and 504 has no effect on the rights and duties of the beneficiaries and the trustee with respect to distributions.³⁷⁴ Similarly, the new comment to section 814 explicitly provides that other than requiring the trustee to act in good faith and in accordance with the terms and purposes of the trust and the interests of the beneficiaries, subsection 814(a) does not address distribution issues, leaving them to caselaw, and affirms that those issues will continue to be dependent on such factors as whether the trustee is granted discretion, the extent of discretion granted, and whether the instrument includes a support or other standard.³⁷⁵

³⁶⁶ See UNIF. TRUST CODE § 814 cmt. (2005).

³⁶⁷ See UNIF. TRUST CODE § 503(b) (2005).

³⁶⁸ See *supra* notes 37-38 and accompanying text.

³⁶⁹ See UNIF. TRUST CODE §§ 502(c) and 503(b) (2005).

³⁷⁰ See UNIF. TRUST CODE § 504(b).

³⁷¹ See UNIF. TRUST CODE § 504(c)(1).

³⁷² See *supra* section VII.

³⁷³ See *supra* notes 20+2-2445 and accompanying text.

³⁷⁴ See UNIF. TRUST CODE § 504 cmt.

³⁷⁵ See UNIF. TRUST CODE § 814 cmt.

Qualification for public benefits of a beneficiary of a special or supplemental needs trust will not be adversely affected by the UTC.³⁷⁶ While beneficiaries of discretionary support trusts have been denied public benefits in many cases in non-UTC jurisdictions,³⁷⁷ the new comment to section 814 may help avoid that result by its reference to the Third Restatement's presumption that the trustee's discretion should not be exercised in such a way as to disqualify the beneficiary from such benefits or for purposes for which public funds otherwise are available.³⁷⁸ Further, from a planning perspective, the SNT discretionary support trust problem is easily avoided by drafting such trusts either as supplemental needs trusts or as discretionary trusts without support standards.

With respect to divorce, most or all of a beneficiary's interest in a third-party created trust will be protected separate property in most states.³⁷⁹ Because a beneficiary has no greater rights to receive distributions under the UTC than under non-UTC law,³⁸⁰ if the interest is discretionary it may also be protected from division on that ground under the UTC to the same extent as under non-UTC law.³⁸¹ Such a discretionary interest may be an economic circumstance that will affect the division of a couple's divisible assets and whether, and if so in what amount, a spousal maintenance or child support award will be issued.³⁸² That is the case under existing non-UTC law, and enactment of the UTC should not affect such divisions or awards one way or the other.

Finally, a beneficiary's interest in a discretionary, non-spendthrift trust may be protected in bankruptcy under the UTC to the same extent as under non-UTC law.³⁸³ The issue will rarely arise, however, as spendthrift provisions, which are routinely used in third-party created trusts, are effective to exclude a beneficiary's interest in a third-party created trust from his or her bankruptcy estate.³⁸⁴

In short, the UTC does not adversely affect the protections from creditors' claims that third-party created spendthrift and discretionary trusts have traditionally provided to their beneficiaries.

³⁷⁶ See *supra* section IX.

³⁷⁷ See *supra* note 2867 and accompanying text.

³⁷⁸ See UNIF. TRUST CODE § 814 cmt.

³⁷⁹ See *supra* notes 31009-3145 and accompanying text.

³⁸⁰ See *supra* section VII.

³⁸¹ See *supra* notes 3223-3378 and accompanying text.

³⁸² See *supra* notes 3398-3454 and accompanying text.

³⁸³ See *supra* notes 3542-3556 and accompanying text.

³⁸⁴ See 11 U.S.C. § 541(c)(2) (1994).