Chicago Estate Planning Council

Do Trusts Really Create Trust Fund Babies?

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DO TRUSTS REALLY CREATE TRUST FUND BABIES?

I. The Dark Side of Wealth

A high school history class is taking a trip to Washington D.C. They will meet with one of the Senators from their state and tour the Capitol, the major monuments and the Smithsonian. It is a three-day, two-night trip and the students are told to bring carry-on suitcases for the flight. One student shows up at the gathering spot at the airport with a bag that is way too big for any overhead compartment. She also seems at a loss as to what to do in the security line. She does not know what items to put in the bins for the x-ray machine, and seems frightened by the prospect of the metal detector. A teacher asks her if this is her first time flying. "No," the student answers. "It's just my first time flying this way. My family always takes a private jet."

"Salvador Neme needed some help, and fast. The 22-year old Babson College junior was throwing a last-minute party at his Boston apartment and wanted to add a few special touches. So the undergrad rang his personal concierge. 'I had no idea where to start,' says Mr. Neme, who had decided that an authentic mariachi band would be just the thing for his Mexican Independence Day soiree. 'Mariachis are hard to find,' says the Mexico City native. No worries. For $300 a month, Mr. Neme has unlimited access to the seven full-time employees of Boston Collegiate Consulting Group, a local concierge company that helps today's moneyed students live like the privileged young swells of the Golden Age. . . . Although Mr. Neme declined to say what he spent on the 40-person affair, the concierge company says the tab ran into the thousands." From *Forget the Old College Try, Ring the Concierge*, Wall Street Journal (March 5, 2013).

As explained in the Wall Street Journal article, *A Hole in the Water You Fill With Money* (March 15, 2013), the book "Grand Ambition" follows the boat owning adventures of Doug Von Allmen, a self-made tycoon, and his wife Linda, as they conceived and built their 187-foot dreamboat. It "would weigh 400 tons and be propelled by two 3,384 horsepower Caterpillar engines costing $2 million each. Lady Linda would have four lavish decks, 10 bathrooms and 2 ½ miles of pipes and would cost $40 million. . . . Mr. Von Allmen and his wife alternately cajole and torment Lady Linda's patient yacht designer, Evan Marshall, with questions that may strike the reader as strictly the problems of the idle rich. Should the yacht have one built in garage or two for storing smaller craft? (Securing speedboats and wave runners on deck is viewed by the yachting community as déclassé and a sign that the owner can't *afford* a garage.) How will guests in the sky lounge be able to view underwater scenes sent from video cameras mounted beneath the yacht's hull? And what is the best way to air condition the *outdoor* decks during those sweltering Mediterranean cruises? . . . There is a scene toward the end of 'Grand Ambition' where the author accompanies Mr. Von Allmen on a tour of Lady Linda. The owner is in a rotten mood. As he glumly surveys each luxurious deck 'there is not a flicker of excitement.' He looks instead like a man staring down into a hole in the water that just swallowed a fortune."

A. These stories reflect the fears of many wealthy clients; that their children and grandchildren will be spoiled, lack basic life skills, live above their means, and fail to understand the prudent management of wealth. In short, they fear that their descendants will be "trust fund babies".

1. Trust fund baby – "a child of wealthy parents or other relatives who can rely on a trust fund rather than hard work for a living." http//dictionary. reference.com.

2. There are of course many other definitions. But regardless of the definition, the term is almost used as a pejorative.

3. The stories also illustrate that parents feed the problem, by leading privileged lives themselves, and engaging in irresponsible spending.

B. The ultimate result of unmotivated descendants who fail to properly manage their money is that the wealth created by the family patriarch or matriarch will be dissipated. The reality of this occurrence is reflected in the well-known phrase "shirtsleeves to shirtsleeves in three generations."

1. Studies support the anecdotal evidence of the phenomenon. In Williams and Preisser, <u>Preparing Heirs: Five Steps to a Successful Transition of Family Wealth and Values</u> (2003), the authors found that "70 percent of the families studied failed to sustain wealth across generations." *Ensuring Success in Wealth Transfers*, Kathleen Burns Kingsbury and James Grubman, <u>Investments & Wealth Monitor</u> (Sept/Oct 2010) (hereinafter *Ensuring Success*).

2. The article *Lost Inheritance*, from the March 7, 2013 edition of the Wall Street Journal tells the stories of several families who have experienced this dissipation of wealth. The article introduces Tom Rogerson, an executive with Wilmington Trust who works with affluent families on wealth-preservation strategies, and the "cruel irony" of his job. Tom Rogerson's great-grandfather was Charles Rogerson, a New England banking titan who helped build Boston Safe Deposit and Trust into a successful institution. Tom's father was a successful real-estate developer, but "[t]he problem was, he also developed some expensive hobbies . . ." that resulted in a "personal fleet of a dozen boats and small aircraft." When the real estate market collapsed in the mid-80's, the family fortune was lost and Rogerson's father was forced to sell off family belongings in a liquidation auction.

3. The article also mentions the descendants of Cornelius Vanderbilt, whose net worth was estimated to exceed $100 billion in today's dollars. "But by 1973, according to one biographer, a reunion of 120 Vanderbilt descendants included not a single millionaire." And Barbara Woolworth Hutton, who supposedly spent as much as $500 million in today's dollar

on art, jewelry and seven husbands, died "with a reported net worth of just $3,500."

C. A frequent question asked of estate planning attorneys and wealth professionals is what can we do in designing trusts and estate plans to prevent creating trust fund babies and lost inheritances. The inquiry begs the question of whether trusts cause the problems in the first place, and the question of whether a well-designed trust can ever provide a solution.

D. In fact, most experts who study and work in this area agree that trusts are definitely not the sole cause of trust fund babies and probably are not even a primary factor. The main culprits are choices in parenting, the broader family environment in which the child is raised, and how the child is prepared and educated to be a recipient of wealth.

E. Trusts do play a role, however. It may not be a direct role, but the structure of trusts and how they are administered can reinforce bad habits learned from family. Alternatively, they can be a tool in helping descendants on their journey to financial responsibility and success.

1. To help make trusts a positive force in the lives of beneficiaries, wealth professionals need to be able to educate the client about the standards to be used for determining what distributions are appropriate and the impact of various alternatives, as well as the practical application of those standards during the administration of a trust.

2. Wealth professionals also should be familiar with alternatives for trust grantors providing guidance to trustees and beneficiaries on the purposes of a trust, such as letters of wishes and incentive provisions, and the pros and cons of these alternatives.

3. Finally, trust grantors and family members need to understand the legal obligations of the trustee to provide information to, and account to, trust beneficiaries. In this regard, the emergence in state trust law of the concept of "silent" or "quiet" trusts provides a new alternative for grantors of trusts. But consider whether that alternative feeds exactly the type of family behavior that in fact creates trust fund babies.

II. Preparing the Next Generation for a Successful Transfer of Wealth

A. The Challenge of Raising Well-Adjusted Children in a Wealthy Family

1. Raising responsible children in an affluent setting is difficult. Admittedly, a large part of the population would have little sympathy for this observation, but it is true.

2. For many the motivation to succeed – to hold a good job, be financially responsible, and contribute to society – is driven by necessity. Most children figure out sooner or later that they must make a living and support themselves. "When security and affluence come too easily, the work ethic can be compromised." Aronoff & Ward, *Shirtsleeves to Shirtsleeves*, The Family Business Consulting Group (April 2005).

3. Thayer Willis is a member of the family that founded Georgia-Pacific Corporation. She observed:

   "The biggest curse of intergenerational wealth for me and many other people is the illusion that you don't have to do much with your life. You might want to and you might make the effort, but you don't have the same pressure to earn enough to live on. And that takes away a lot of incentive to find meaningful work." Willis, *Why Family Wealth Is A Curse*; Forbes http://www.forbes.com/sites/debrorahljacobs/2013/03/01/ why-family-wealth-is-a-curse.

4. Money also can lead to self-indulgence, and the expectation that you can always get what you want. Parents may be more indulgent and too protective, such that the children never experience adversity or failure.

   a. Matthew Wesley, who works with wealthy families and family offices on those issues, refers to this as the "silver spoon syndrome."

   b. In the article, *Forget the Old College Try, Ring the Concierge*, Hara Estroff Marano, author of a "A Nation of Wimps" and editor-at-large at Psychology Today, commented on concierge services, saying "Parents are 'breeding ineptitude' by allowing – and in some cases encouraging children to hand off those jobs…. Figuring out how to do laundry, cook a basic meal or even wait for a handyman 'are not crippling responsibilities' but rather 'minor life skills' that can prove useful…."

5. Professionals who work with wealthy families draw on interesting analogies to explain the challenges confronting wealthy families. Dr. David Lansky, of The Family Business Consulting Group, notes that children in wealthy families face emotional and family issues that are similar to those confronted by a child in a low-income family.

   a. A child in each case may suffer from a lack of direct parenting. A low-income child because it is a single-parent household or parents working multiple jobs; a wealthy child because the entrepreneurial parent is devoted entirely to his or her work, or because the parents are traveling among homes and relying on staff and boarding schools to raise children.

b. The children may share a similar sense of shame that they do not fit in with others and have to hide their circumstances.

6. Dr. James Grubman, a consultant to wealthy families, uses the immigrant analogy with the first and second generations in wealthy families. The parents who created the wealth, or were raised before their parents created the wealth, were raised in a middle class culture. They experienced hardship and financial challenges. Then they migrated to the land of wealth. Their children are natives to the land of wealth, and have no memory of the former land. They have known only financial comfort. Now the parents must raise them in this new land, and recognize that the process is different than it was for them. <u>See</u> Grubman, Jaffe and Whitaker, *Immigration to the Land of Wealth*, <u>Private Wealth Magazine</u>, 17 (Feb/March 2009).

7. The most difficult situation is one where the family members who are now parents themselves possess all the undesirable traits of spoiled wealthy trust beneficiaries. They lack financial acumen, do not work, have trouble living within their means, are narcissistic, and too busy living the good life to spend much time with their children. They outsource many parenting tasks to nannies, tutors and boarding schools. Matthew Wesley refers to this syndrome as the "silver dagger." It is the situation most likely to adversely affect the children and destroy the family wealth.

B. Overcoming the Challenges

1. Psychologists and consultants who work with wealthy families are in general agreement about the steps that should be taken to provide children of wealth with the opportunity to live fulfilling and successful lives.

2. This does not mean success is easily achieved. As every parent knows, there are no guarantees when it comes to raising children. Even the most diligent parents, ones who teach all the right moral and social lessons, and correctly balance nurturing and building self-reliance, sometimes fail.

3. The common theme for the right path is the necessity of preparing children for wealth and its responsibilities. Living with wealth successfully is a learned art. James Grubman uses a football analogy: a football quarterback prepares to throw a long pass downfield with the game on the line. He has been well-coached, has studied and practiced hard. The coach has drawn up the perfect play. But the receiver drops the ball – because no one bothered to train the receiver. Children must be trained to receive the wealth. *Ensuring Success*.

C. Communication

1. The first recommendation of most professionals is counter to the thinking of many parents. Parents often think they must hide their wealth from their children for fear that the children will lose all motivation once they know about it.

2. In fact, communication, open discussion of wealth, is the key. Children cannot learn to handle wealth if it is a taboo subject in the family.

   a. "Effective wealth transfer occurs when shared communication about the transfer and preparation of the beneficiary are integrated into the planning…. The main reasons for lack of success [in generational transfers of wealth] were lack of family communication and heir preparation." *Ensuring Success*.

   b. Dr. David Lansky observes that "fears that knowledge of forthcoming wealth will weaken initiative and will undermine the resolve of inheritors to pursue outside careers, leads to a lack of information and instruction on wealth management and financial responsibility." Lansky, *Managing the Psychological Impact of Inherited Wealth*, <u>The Family Business Advisor</u> (April 2012).

   c. In a white paper prepared by CTC Consulting, the author observes,

      "Open communication within and among generations is a cornerstone of successful generational planning. The challenge for many parents is when and how much to communicate to their children. People naturally fret about how much to tell their children about their wealth, but the reality is that children formulate opinions based on lifestyle. These opinions might be highly assumptive and a lack of communication could result in future misunderstandings and challenges." *Preparing the Next Generation*, CTC Consulting (Oct. 2011).

3. The last quote above emphasizes an important point. Children likely know much more than parents think. Their friends come over to the house and comment "wow, you live in a mansion." The child may hear comments from friends' parents. With the internet, children have much greater access to information about their parents' wealth. A child who googles his parents can find information about the family business, his parents' political and charitable contributions, and the value of their home. If there is a family foundation, its 990PF is available online.

4. This is one reason to start the conversation early. Another reason is emphasized by Dr. James Grubman, who notes that "money personalities are largely in place by age 14 and solidly entrenched by our 30s." *Ensuring Success*. If parents or grandparents want to delay serious

discussions and training until the child already is in his or her 40s, it is way too late.

D. Family Values and Wealth Stewardship

1. One of the lessons to communicate to children is the story of the family legacy and the shared values that exist.

2. For many families, this story involves a family business, possibly one that the family still owns. For many other families of wealth, it is philanthropy, and the strong family ethic of giving back, both in treasure and in time and talent.

3. The story of the family business, and the sacrifices made by the earlier generations, cannot start too early. They are readily translatable to the understanding of young children.

4. It is important for the wealth creator to be clear about his or her own motivations. While it may feel right for a client to simply explain to children that the reason he or she works – perhaps spending a large amount of time away from the children – is to provide for the family. But there is more to the story, which is important for children to hear. The client also should discuss motivations such as personal interests that led to a career path, enjoying the problem-solving or creativity that comes with the work, being able to make impactful charitable donations, creating and maintaining jobs for scores of employees, and being proud of his or her legacy. Without this important context, a child who inherits wealth and does not share the need to provide for family misses out on all of the other reasons to pursue a career or other outlet for meaningful self-expression.

5. The current values of a family may or may not include the value of working for pay. When the family has good role models for success in the workplace, they can use them. In some families, many of the family members are not in the workforce. Hopefully, though, they are involved in community or social causes, and those values can be demonstrated.

E. The Value of a Dollar

1. In a family that is living very well, it is a bit harder to provide lessons on living within ones means, and thinking about the costs of goods. Nevertheless, it can be done.

2. Dr. James Grubman uses the example of a parent shopping for a new car. The parent could sit down with a teenage child, discuss the models he or she is considering, and the cost. Instead of focusing on the extras available, discuss the cost not only of the purchase, but of maintenance, insurance and fuel. Let the child do some research for the parent. At the same time, if applicable, the parent can remind the child about what allows

them to purchase a car and (presumably) pay all cash – whether it's the parents' success or the generosity of past generations.

3. This of course all presupposes a parent who is willing to get involved. As alluded to earlier, if the parent is absent, and simply sends a family office employee to buy the car, the teaching opportunity is lost.

4. Sometimes, the role of grandparents is just as important as parents in teaching about wealth. Grandparents can send counterproductive messages, for example, if they take the grandchildren to the mall and let them all buy whatever they want. At the opposite end of the spectrum, a grandparent who was the primary wealth creator and who experienced hardships and challenges along the way, may be the best person to convey positive lessons about the family wealth.

F. How to Invest and Make Investment Decisions

1. A wealthy young adult easily could be the target of acquaintances and friends who want the person to fund business ideas or investment opportunities.

2. If the family has a family office, the child can hide behind the office investment staff. But it is even better if the child has received a sound financial education in analyzing and making investments and reviewing the performance of investment managers. He or she will feel more empowered.

3. Understanding investments also necessarily involves understanding the expense of investing and the impact of spending from the fund. The family can start by exposing the child to a smaller family trust and showing the history of investment return and distributions. A family foundation also is an excellent vehicle for lessons on investing and spending policy.

G. The Role of Trusts and Trustees

1. Trusts, and how they are administered, can reinforce the life lessons given to children of wealth, or they can be counter-productive.

2. Trustees and family advisors likely will be participants in the education process. As attorneys we often discuss trusts that are designed to help children on the "journey to independence." A trust might provide that the child can become a co-trustee at a certain age, with the expectation that the experienced trustee will begin to share the decision-making process with the child. The more experienced trustee probably will retain the tie-breaker authority for a period, and then it might shift to the child. The child then can become sole trustee at a certain age and possibly also receive part of the trust outright.

3. The following sections discuss alternative trust structures that families may find appealing. These materials also contain a discussion of distribution standards used in trusts.

4. For many clients, it is not possible to customize a trust to a great degree. It simply is not cost-effective. Such customization may not be necessary. For many families in the top 2% of income and net worth, but not in the top 0.10%, their wealth allows for a higher standard of living and certain luxuries, but it is not sufficient to allow anyone to live a life of idle leisure while being supported by a trust. A "health, support and education" standard or an additional "best interests" standard may be sufficient to reflect the intended level of generosity. For the upper levels of wealth, greater customization often is a worthy investment.

III. Distribution Standards and Other Important Guidance

A. When creating a trust, clients often ask about the meaning of various standards of distribution. What, for example, is the real difference between "support and maintenance" and "best interests and welfare" in terms of what access the beneficiaries will have to the trust assets? Or, what factors related to the beneficiary's other resources, lifestyle, etc. will the trustee take into account in making distributions?

1. Most attorneys have a standard procedure for addressing these issues and answering the client's questions. For instance, many clients have been told that "support and maintenance" allows the beneficiary to maintain his or her accustomed standard of living, whereas "best interests and welfare" could include distributions for luxury items -- a Mercedes Benz or a trip to Europe.

2. As mentioned, the brevity of focus on these issues is often necessary for very practical reasons -- many clients cannot afford to have the attorney spend hours exploring the client's goals and drafting unique, specific provisions governing distributions. However, some can afford, and indeed expect it. In these situations, trusts are likely to contain very customized distribution provisions.

3. Any decision regarding the appropriate distribution standard for a trust must take into account the transfer tax consequences of using the distribution standard. A trustee who has the discretionary power to distribute trust property to himself as a trust beneficiary possesses a general power of appointment unless the discretionary power is limited by an ascertainable standard related to his or her health, education, support or maintenance. IRC §§ 2041(b)(1)(A); 2514(c)(1).

a. Most draftspersons include provisions in trust documents to limit the distribution powers of a beneficiary/trustee to purposes that fall within an ascertainable standard. This is done directly, by specifically giving broader distribution powers only to an independent trustee, or indirectly, with a savings clause that provides that the powers of any trustee who also is a beneficiary are cut back to purposes that fall within the ascertainable standard.

b. Many states also have statutes that prevent a beneficiary/trustee from exercising discretionary distribution powers or cut back the powers to ascertainable purposes. The Uniform Trust Code provides that, with certain exceptions (including express contrary direction in the trust), "a person other than the settlor who is a beneficiary and trustee of a trust that confers on the trustee a power to make discretionary distributions to or for the trustee's personal benefit may exercise the power only in accordance with an ascertainable standard; . . " UTC Section 814(b)(1). The provision also states that a trustee may not exercise a discretionary distribution power to satisfy a personal legal obligation to support another. UTC Section 814(b)(2).

4. It is also important to note that depending on state law, certain discretionary standards may allow the trustee to modify an irrevocable trust – which is often referred to as "decanting." In Illinois, a trustee with "absolute discretion" may distribute part or all of the trust property to another irrevocable trust for the benefit of one, more than one, or all of the current beneficiaries of the original trust, and for the benefit of one, more than one, or all of the remainder beneficiaries of the original trust. For this purpose, "absolute discretion" is defined as the right to distribute principal that is not limited in any manner to or for the benefit of the trust beneficiaries, including, for example, purposes such as best interests, welfare, or happiness. A trustee that does not have "absolute discretion" only may distribute trust property to another irrevocable trust that has the same current beneficiaries and remainder beneficiaries. 760 ILCS 5/16.4.

B. The interpretation of terms which set out a standard of distribution, such as "best interests," "support" and "comfort," is governed by state law. Therefore, the meaning of a particular term may be more or less restrictive, depending on the law of the state that governs the interpretation of the instrument. See section VIII of this outline, which contains a more detailed discussion of the interpretation of various distribution standards.

C. In general, if the trustee's authority to make distributions is discretionary, and the trustee uses its judgment and makes a reasonable decision, a court will not disturb the trustee's decision to distribute or withhold trust assets unless there has been evidence of bad faith or an abuse of discretion. The Restatement (Third) of Trusts describes the trustee's powers and the court's oversight obligations as follows:

"§ 50. Enforcement And Construction Of Discretionary Interests

(1) A discretionary power conferred upon the trustee to determine the benefits of a trust beneficiary is subject to judicial control only to prevent misinterpretation or abuse of the discretion by the trustee.

(2) The benefits to which a beneficiary of a discretionary interest is entitled, and what may constitute an abuse of discretion by the trustee, depend on the terms of the discretion, including the proper construction of any accompanying standards, and on the settlor's purposes in granting the discretionary power and in creating the trust."

1. The commentary to the Restatement explains that a court will not interfere with a trustee's exercise of discretion merely because the court would have exercised the discretion differently. The court will act, however, to prevent an abuse of discretion. "What constitutes an abuse depends on the terms of the trust, as well as on basic fiduciary duties and principles. . . . Of particular importance are the purposes of the power and the standards . . . ." Restatement Third § 50, comment b.

2. The commentary states that intervention is appropriate to "rectify abuses resulting from bad faith or improper motive," to correct errors in interpretation, or to address a situation where the trustee failed to exercise his or her judgment or did so without inquiring into the relevant circumstances. Id.

3. If the trust defines the purposes for distributions ("health and support"), this limits the trustee's discretion and also gives the beneficiary more readily enforceable rights. A court has a specific standard to look to in determining if the trustee abused its discretion.

4. A broad or undefined standard ("the trustee may distribute trust income or principal to the beneficiary as the trustee determines to be advisable…") gives the trustee much freer rein to determine what is appropriate.

5. Regardless of the standard of distribution, it is usually wise to include additional guidance for the trustee in the trust agreement. Several fundamental categories of guidance are described below.

D. Unequal Distributions

1. Bogert states that where there are multiple current beneficiaries of a trust, and the trustee is not given discretion to make unequal distributions to those beneficiaries, there is a presumption that the beneficiaries should receive equal distributions from the trust. Bogert § 182. The presumption is based on the trustee's fiduciary duty to treat beneficiaries impartially.

2. The fact that the beneficiaries are in different financial circumstances may justify unequal distributions even absent specific authority.

3. If the client wishes to give the trustee the power to distribute unequal amounts to beneficiaries or to favor one group of beneficiaries over another, the trust agreement should specify that unequal distributions are permitted.

> **SAMPLE TRUST PROVISION:** The trustee may make unequal distributions to the descendants of the child or may at any time make a distribution to fewer than all of them, and shall have no duty to equalize those distributions.

4. As an alternative, the trust instrument may authorize unequal distributions, but provide that distributions for certain purposes, such as to start a business or for graduate education, will be treated as advancements.

> **SAMPLE TRUST PROVISION:** Any distribution (i) to a child for graduate or professional education, (ii) to permit a child to enter into or engage in a business or profession, (iii) to permit a child to make a downpayment on a personal residence, or (iv) to defray wedding expenses of a child, shall be charged as an interest-free advancement against the share, if any, distributable to that child or descendant of that child under [later provisions of the trust agreement].

E. Priority Among Beneficiaries

1. The Restatement Third of Trusts commentary states that "structure and terms of the interests may suggest a priority to be accorded various individuals or classes." The commentary adds that certain inferences can be identified even where the trust agreement does not specifically set priorities. For example, in a spray trust for spouse and descendants, a common inference to draw is that the spouse's needs should be accorded first priority. Similarly, it is reasonable to conclude that a child of the settlor has priority in a trust for the child and his or her descendants. See Restatement Third § 50, comment f.

2. It is best to specifically establish priorities among the beneficiaries in a trust benefiting multiple generations.

> **SAMPLE TRUST PROVISION:** My primary concern during the life of the child is for the child's health, support and education and the trustee need not consider the interest of any other beneficiary in making distributions to the child for those purposes under this paragraph.

SAMPLE TRUST PROVISION: My spouse shall be accorded clear first priority, and my children second priority (particularly those under age 25).

SAMPLE TRUST PROVISION: My primary concern during the period described in this paragraph is for the health, support and education of my children and the descendants of a deceased child of mine, rather than for the preservation of principal for ultimate distribution to my children or their descendants.

3. Priorities can be made more explicit by providing that all income is to be paid to one beneficiary except for the amount not required for the beneficiary's support, and that only the excess may be used for other beneficiaries.

SAMPLE TRUST PROVISION: Commencing with the death of the last to die of me and my spouse, the trustee shall pay all of the net income of the trust to my child during his or her life. Notwithstanding the foregoing, whenever the trustee may determine that the income of the trust is partially or wholly in excess of that required for my child's support and health needs, considering his or her standard of living at my death and all other income available from time to time for such purposes, then the trustee may in its discretion withhold part or all of such excess income. Income not paid to my child may be paid in whole or in part to any one or more of his or her children, living from time to time, in such equal or unequal proportions as the trustee determines to be desirable for the support, education, health needs and best interests of each of them. Income not paid out may in the discretion of the trustee be added to principal from time to time.

F. Consideration of the Beneficiary's Other Assets

1. At common law, the general presumption was that, unless the instrument expressly provides that the trustee may consider the beneficiary's other assets and income, the trustee may not consider those assets in determining what distributions are required for the support of the beneficiary. The beneficiary has the right to look first to the trust assets for his support. <u>See</u> Restatement (Second) of Trusts, § 128, comment e; <u>Nielsen v. Duyvejonck</u>, 236 N.E.2d 743, 747 (Ill. App. 1968); <u>Hart v. Connors</u>, 228 N.E.2d 273 (Ill. App. 1967); <u>Demitz' Estate</u>, 208 A.2d 280 (Pa. 1965); <u>Matter of Martin</u>, 269 N.Y. 305 (1936); <u>Godfrey v. Chandley</u>, 811 P.2d 1248 (Kan. 1991); <u>In re Bedell's Estate</u>, 92 N.Y.S.2d 70 (1949).

2. In many cases, this rule would be disadvantageous from both a tax and a fairness standpoint, and the trend seems to be moving away from it. The Restatement Third of Trusts states that the general rule, absent specific

direction to the contrary, is that the trustee has discretion to consider other resources. Restatement Third § 50, comment e.

3. In some states, if a gift to the beneficiary is conditioned on need -- for example if the trustee is directed to make distributions "for a beneficiary's support as it deems necessary" or "as the beneficiary needs" or "if there is an insufficiency" -- then the beneficiary's outside assets and income must be considered. See Boston Safe Deposit & Trust Company v. Boynton, 443 N.E.2d 1344 (Mass. App. 1983); Matter of Martin, 269 N.Y. 305 (1936); Matter of A. David Bernstein, NYLJ, December 7, 1988, p.26; Stempel v. Middletown Trust Co., 15 A.2d 305 (Conn. 1940); In re Tuthill's Will, 76 N.W.2d 499 (Minn. 1956); In re Martin's Will, 199 N.E. 491 (NY 1936); In re Seacrist's Estate, 66 A.2d 836 (Pa. 1949).

4. However, this is not a hard and fast rule, and in many cases the courts have not required the trustee to consider the beneficiary's other resources although the terms "as needed" or "necessary" were attached to the standard of distribution. See Cross v. Pharr, 221 S.W.2d 24 (Ark. 1949); Hamilton National Bank of Chattanooga, Tennessee v. Childers, 211 S.E.2d 723 (Ga. 1975); McClintock v. Smith, 29 N.W.2d 248 (Iowa 1947); Sibson v. First National Bank & Trust Co. of Paulsboro, 160 A.2d 76 (N.J. Super. 1960); In re Stern's Will, 228 N.Y.S.2d 90 (1962).

5. Some courts have found that where the trustee was directed to pay income and principal as needed for the support of the beneficiary, the beneficiary's other income, but not his other assets, should be considered. Peoples Bank & Trust Co. v. Shearin, 219 S.E.2d 299 (N.C. App. 1975); Sibson v. First National Bank & Trust Co. of Paulsboro, 165 A.2d 800 (N.J. Super. 1960).

6. Other courts have held that if the trustee is granted broad discretion in making distributions, the trustee is permitted to consider the beneficiary's other assets.

    a. In one case, a standard which authorized the trustee to make distributions of principal which she "in her sole discretion, determines necessary for the support and maintenance" of the beneficiary allowed the trustee to consider the beneficiary's other assets. The Pennsylvania Superior Court held that such a broad grant of discretion indicated that the trustee had the authority to withhold trust principal from a beneficiary with independent resources. In re Estate of Tahjian, 544 A.2d 67 (Pa. Super. 1988). Similarly, an Illinois appellate court held that where the "'trustee *may in the trustee's discretion* [distribute income and principal] as the trustee from time to time *deems necessary or advisable*' . . . confers upon the trustees unfettered discretion" that "necessarily includes the prerogative to consider all financial resources at [the

beneficiary's] disposal." [Emphasis added by court.] Stein v. Scott, 252 Ill.App.3d 611 N.E.2d 713 (1st Dist. 1993).

b. However, in a New York case involving similar language, the court held that the trustees should not require the beneficiary to use his personal assets for support before looking to the trust assets. In that case, the trustees were authorized to distribute as much of the trust income to the beneficiary as they in their sole discretion deemed advisable to supplement an annuity that the settlor gave to the beneficiary. Matter of Estate of McNab, 558 N.Y.S.2d 751 (1990).

7. If the settlor directs the trustee to consider the beneficiary's "other resources," there is still a question of which resources it may or must consider. In some circumstances, the settlor may want to specify whether the trustee is to consider only the beneficiary's liquid assets, or the beneficiary's entire estate, including non-liquid assets such as the beneficiary's home. Tax considerations also may be relevant.

a. The settlor may wish trust property which is not needed for the beneficiary's support to remain in trust for other beneficiaries, especially if the trust property will not be taxable in the beneficiary's estate.

b. For example, it may be desirable for the trustee of a credit shelter trust to consider the surviving spouse's marital trust and non-trust assets before making a distribution from the credit shelter trust, because those other assets will be included in the surviving spouse's gross estate, whereas the credit shelter trust assets will not.

8. The settlor may also want the trustee to consider the income tax consequences to the beneficiary if the beneficiary must liquidate his own assets to meet expenses and incur capital gains tax.

SAMPLE TRUST PROVISION: In determining whether to make discretionary distributions of net income or principal to a beneficiary, the trustee may consider such circumstances and factors as the trustee believes are relevant, including the other income and assets known to the trustee to be available to that beneficiary, including funds which might be made available by enforcement of the legal obligation of any person to furnish support or education, and the advisability of supplementing such income or assets, the tax consequences to the beneficiary of requiring the beneficiary to rely first on his or her own assets, and the tax consequences of any such distribution.

9. To give the trustee the maximum amount of flexibility in this matter, the settlor can authorize the trustee to consider a beneficiary's outside resources, but explicitly provide that those assets need not be considered. In one New York case, the court interpreted the following language in a marital trust: "In exercising this discretionary power [to invade principal], my corporate trustee may but need not consider any other resources of my said husband." The court found that the trustee could, but was not required to, consider the husband's other income and assets. Matter of Payson, NYLJ, June 20, 1989, p. 26.

10. For very wealthy families, this is another area where customized guidance often is helpful. For example, there may be certain older, long-term trusts in the family that pay mandatory income. The creator of a new trust may want to explicitly provide that the trustee should take that income into account before making additional distributions.

IV. More Specific Guidance to the Fiduciary

A. It often is not sufficient to simply define for a trustee or other fiduciary the purposes for which distributions can be made. For example, if the client's goal is to make the trust fund available in a manner that will not interfere with a beneficiary's development as a productive member of society, the trustee could be given authority to consider factors related to the beneficiary's personal development in determining whether to make distributions for the purposes set forth in the trust agreement.

B. At a minimum it is good practice to give the trustee discretion to consider the beneficiary's personal characteristics. A trustee generally cannot do this unless specifically authorized in the trust agreement because of the requirement to exercise discretionary powers impartially among the beneficiaries.

> **SAMPLE TRUST PROVISION:** In determining whether to make discretionary distributions of net income or principal to a beneficiary, the trustee may consider such circumstances and factors as the trustee believes are relevant, including the other income and assets known to the trustee to be available to the beneficiary and the advisability of supplementing such income or assets, the tax consequences of any such distribution, *and in the case of any descendant of mine, the character and habits of the beneficiary, the diligence, progress and aptitude of the beneficiary in acquiring an education and the ability of the beneficiary to handle money usefully and prudently and to assume the responsibilities of adult life and self-support*.

C. The trust agreement also can direct the trustee to obtain certain information from a beneficiary regarding finances, spending habits, or personal activities before authorizing a distribution to that beneficiary. In many cases this information is needed to apply the guidance that the trustee is directed to consider.

SAMPLE TRUST PROVISION: In determining whether to make discretionary distributions of net income or principal to a beneficiary, the trustee shall consider the other income and assets known to be available to the beneficiary [same provisions as above] . . . adult life and self-support, it being my intent that the failure of a beneficiary in any of these areas may, in the discretion of the trustee, constitute a reason for denying a distribution. In order to make these determinations, the trustee shall request any information it deems relevant from a beneficiary (and withhold a distribution if the beneficiary refuses to provide such information), including without limitation, the following:

1. A statement of the beneficiary's assets and liabilities, and the assets and liabilities of his or her spouse;

2. Copies of bank statements, cancelled checks, credit card statements or any related material that evidences the beneficiary's spending habits;

3. Evidence that the beneficiary is enrolled in school or employed and, for a beneficiary in school, copies of transcripts;

4. A beneficiary's employment history and authorization to contact and request employment information from the beneficiary's current employer;

5. A list of the beneficiary's place of residence for whatever period of time the trustee determines to be relevant;

6. Access to medical records, blood tests, or related medical information; and

7. Information concerning travel by the beneficiary and a copy of the beneficiary's passport.

D. The grantor can direct that the trustee should use the trust property for the purposes designated only as a last resort, if no other assets are available.

SAMPLE TRUST PROVISION: The primary purpose of the trust is to maintain a reserve fund to provide for the health, support and education of my descendants in situations in which all other assets and sources of income available to a descendant of mine are insufficient for those purposes.

E. A more common provision is one directing the trustee to make trust distributions sparingly so as to encourage self-sufficiency and avoid the development of unmotivated children or grandchildren who are content to live off their inheritance.

SAMPLE TRUST PROVISION: The primary purposes of the trust are (i) to provide for the health, support and education of the child for whom the trust is named, and (ii) to avoid use of the trust property in a manner that might impair the desire of the child or a descendant of the child to be self-sufficient. I intend for the trustee to distribute trust income and principal to the child or his or her descendants on a selective and considered basis, my concern being that the child or the child's descendants may receive too much rather than too little.

F. From time to time, practitioners and clients latch on to the idea of "incentive provisions" as a further step in using a trust to properly motivate a beneficiary.

1. Incentive provisions can take various forms but at the core of the concept is the use of trust property to encourage certain behavior or achievement by the trust beneficiaries or to reward beneficiaries for reaching certain benchmark goals.

2. An incentive provision can be quite simple, such as providing for a $10,000 distribution to a child or grandchild upon graduation from college or completion of his or her first year of full-time employment. Or, the trust agreement could provide that a beneficiary's trust will terminate and distribute its assets outright to the beneficiary only when the beneficiary provides evidence that he or she has accumulated a net worth of a set amount (for example, $1,000,000) on his or her own accord.

3. The incentive provisions also can be quite sophisticated and creative, such as providing a series of requirements that must be satisfied to receive distributions from the trust, or a special provision for rewarding descendants who achieve success.

SAMPLE TRUST PROVISION: In making distributions hereunder, the following provisions shall apply:

1. After a child of mine reaches the age of twenty-five years, no distribution of income or principal to that child for support in a given year may exceed in value twenty-five percent of the amount of income earned by that child and that child's spouse in that year from gainful employment. The decision of the trustee as to what constitutes gainful employment and the amount of income earned from that employment shall be conclusive, absent bad faith. This limitation shall not apply:

a. To a child who suffers from a physical or mental disability which the trustee determines, in the trustee's sole discretion, prevents the child from leading a self-sufficient life; or

b. To a child who, because of divorce or for any other reason, is a single parent with custody of dependent children under the age of fifteen years.

2. No distribution to assist a child of mine in the purchase of a personal residence may exceed the amount of the down payment contributed by that child from his or her funds, or, if applicable, by the child and his or her spouse from their own funds.

4. The foregoing sample trust provision is limited in detail. More expansive versions might address things like a maximum age (retirement age) after which the income provisions will not apply, or define other exceptions to the general provision.

5. A trust can be structured to assist a descendant who chooses to engage in a worthwhile occupation, such as teacher or social worker, and thereby forego the financial benefits that their talents otherwise would permit them to achieve. The trust could provide a financial security net that permits the descendant to pursue such a profession, by including language such as the following:

   SAMPLE TRUST PROVISION: In addition, if the grandchild is engaged in a profession which, in the trustee's sole discretion, the trustee deems to be a profession that I would consider as honorable and as resulting in some financial sacrifice to the grandchild, such as teaching, counseling, or a religious vocation, the trustee may distribute to the grandchild as much or all of the net income and principal of the trust named for the grandchild as the trustee deems to be necessary to provide the grandchild with sufficient financial security to permit the grandchild to remain in that profession, notwithstanding the more limited monetary compensation therefrom.

V. The Debate Over Using Trusts to Control Behavior

A. The Pros and Cons of Incentive Provisions

1. Incentive provisions can add specificity to the general guidance given to trustees, and can provide clearer evidence of the grantor's intent with respect to use of the trust property.

2. They can be inflexible, however, and they can intentionally or unintentionally favor some descendants over others. For example, employment and income related provisions can favor descendants who work full time outside the home even when the settlor may believe childrearing and homemaking are worthwhile pursuits.

3. The primary danger of incentive provisions is that they may require rewarding certain behavior that the settlor finds valuable, but which certainly is not the only honorable or worthwhile behavior to pursue. In some situations, this control from "beyond the grave" by the settlor will be resented by his or her descendants.

B. Family psychologists and consultants warn that guidance that is meant to limit access to a trust based on the beneficiary's behavior or success in leading a meaningful life (as defined by the trust settlor), if not accompanied by significant communication with and training of the beneficiary, can be counter-productive.

1. If the beneficiary has not been trained to receive the wealth, and has already developed bad spending and money management habits, the trust limitations are not likely to change those behaviors.

2. Moreover, significant limitations will probably interfere with the trustee's ability to work cooperatively with the beneficiary. The beneficiary probably will view the trust and the trustees negatively; that the trust is nothing more than a mechanism that his or her parents or grandparents left to control him or her, or to punish.

3. There has been a robust discussion in recent years about the impact of trust structures on beneficiaries, and what can be done to help trustees better understand the settlor's intentions and help beneficiaries lead better lives.

4. There is an underlying tension at work in this conversation.

a. The person creating the trust (often the person who created the wealth) may view the trust precisely as a way to exercise control, and a way to make a permanent system for carrying out his or her beliefs.

b. Attorneys reinforce this view by focusing on settlor intent and the ability of the settlor to dictate a system for how trust funds will be available.

c. Family psychologists and consultants often view this approach as counter-productive.

C. Some practitioners advocate including more settlor intent guidance in the trust agreement rather than less, but focusing on guidance that describes the settlor's values and principles. In Handler and Loathes, *The Case for Principle Trusts and Against Incentive Trusts*, Trusts & Estates (Oct. 2008), the authors suggest guidance that encourages the trustee to consider and reward certain desirable behaviors, such as:

1. Pursue an education at least through college;

2. Pursue gainful employment with a goal of becoming financially self-sufficient;

3. Be a law-abiding citizen;

4. Become a productive member of society, as exhibited by meaningful contributions to family, community and society;

5. Engage in entrepreneurial and/or creative activities;

6. Handle money intelligently and avoid wasteful spending;

7. Act with empathy, thoughtfulness, kindness and consideration toward others;

8. Develop healthy and meaningful relationships;

9. Make contributions of time and talent to charities; and

10. Maintain a healthy lifestyle, avoiding drugs and other harmful substances.

D. The authors advocate giving the trustee discretion to reward such behaviors rather than setting objective benchmarks that result in mandated distributions, as in some types of incentive trusts. Id. The guidance of course would be personalized to reflect the particular values and beliefs of the settlor.

E. Eileen Galo, Jon J. Gallo and James Grubman have contributed the idea of the Results-Oriented Trust Environment (ROTE) and a Financial Skills Trust (FST).

1. The concepts were presented in *The Use and Abuse of Incentive Trusts: Improvements and Alternatives*, 45th Annual Heckerling Institute on Estate Planning (2011), and are summarized in two columns in the Journal of Financial Planning in April, 2011.

2. The structure is based on behavioral studies that show that money is not an effective incentive for modifying cognitive skills, such as judgment or financial skills. The authors also contend that typical incentive provisions do nothing to help develop the beneficiaries sense of self-efficacy – "the belief in one's ability to succeed in life."

3. Instead, the authors advocate a type of trust that helps a beneficiary learn the skills that correlate with a beneficiary's ability to manage money responsibly, with a focus on the following skills:

a. The ability to live within one's means.

b. The ability to manage spending in order to save a portion of one's income.

c. The ability to understand and manage credit and debt, thereby avoiding excessive debt.

d. The ability to account for one's financial resources.

e. The ability to understand and manage the investment of one's assets; and

f. The ability to generate additional income through employment, if necessary.

4. This is accomplished by allowing the trustees to reward demonstrated abilities (but not mandating such rewards or punishing failure), and also using the trustees as mentors, to create opportunities to learn the skills.

5. An interesting question is when and how such a trust would be employed. As noted earlier, if the trust is first created for someone in their 40's or older, it may be too late. It certainly should not be a substitute for effective communication and training by parents and grandparents before the trust is created. It may be best used for future generations, as a mechanism to compliment the work of the parents of those future generations.

F. Another approach is to have the settlor provide guidance to the trustee outside the trust agreement, through a separate written set of instructions or general statement of the settlor's views and beliefs – a "Letter of Wishes."

1. The advice is meant in particular for trusts in which the trustee is granted broad discretion to make distributions, such as under as undefined standard like "as the trustee determines" or "best interests."

a. The advantage of such a standard is that is gives the trustee the greatest latitude to do what is appropriate in any given situation. In addition, because it is an undefined standard, the trustee should be less subject to claims by a beneficiary who does not agree with the trustee's distribution decisions.

b. It does, however, leave the trustee with little guidance about what the settlor wants or believes. The initial trustee may know the settlor personally, but future trustees may not, and therefore may have little or no knowledge about the settlor's intent. See Bove, *Letter of Wishes*, Trusts & Estates (Jan. 2006). As Bove points out, "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 would act." Id. (quoting Scott and Fratcher, The Law of Trusts, Section 187).

2. As suggested above, such guidance can be included in the trust agreement. The challenge is that, in many cases, the settlor is not prepared to provide such guidance at the time the trust is drafted, or the settlor may develop particular viewpoints after the trust has been in place for a while, for example because his or her children are older and the settlor now sees certain habits or values that he wishes to encourage or discourage.

3. Some settlors also like the idea of providing private guidance to a trustee, that the trustee does not have to share with the beneficiaries or others. Unfortunately, this idea, that the trustee has guidance that is not part of the trust agreement, yet the trustee is relying on it, creates a host of potential legal issues if a dispute later arises.

   a. The first issue is whether the trustee has an affirmative duty to disclose the letter to beneficiaries under the trustee's general duty to provide complete and accurate information about the trust to beneficiaries. The answer depends on whether a court would categorize the letter as part of the books and records of the trust.

   b. The next issue is whether the trustee can disclose the letter at an appropriate time, in particular as a defense for the actions taken by the trustee. If the letter is not binding on the trustee, and the issue relates to the actions of the trustee under unambiguous trust terms, then the letter would be extrinsic evidence that would not be relevant. If, on the other hand, there is an ambiguity and outside evidence of the settlor's intent is relevant, the letter would have evidentiary value.

4. If counsel is advising a trust settlor about a letter of wishes, he or she should recommend that the settlor address these questions of use and availability to the beneficiaries in the letter.

G. A somewhat different way to approach the question of providing guidance is the concept of an "ethical will." An ethical will is a written document designed to "transfer" a person's values, advice, life lessons and hopes and wishes for his or her family and loved ones.

1. It is not a legal document of course, and it can be in almost any form.

2. It is meant primarily for the person's family, not as guidance to trustees, although it certainly can serve that purpose too.

3. Hopefully no person would view an ethical will as a substitute for imparting life lessons directly to his or her children. Arguably, the main value of an ethical will is to inform future generations, who did not know the writer, but are benefiting from his or her wealth.

VI. The Trustee Duty to Disclose and the Alternative of Using a Silent Trust.

A. Trustee Duty to Disclose

1. These materials have alluded to the inevitable, eventual need to discuss family wealth with a younger generation because that child or grandchild will have to be told about the trust or trusts of which he or she is a beneficiary.

2. Parents or other family members who are resisting the start of the education process for the beneficiary will often ask "Why do we have to tell her [him] about the trust?"

3. The answer, of course, is that the trustee has a duty to disclose, a duty that is well-established in the common law.

4. Scott on Trusts, Section 173, summarizes the duty to provide information to beneficiaries as follows:

   "The trustee is under a duty to the beneficiaries to give them on their request at reasonable times complete and accurate information as to the administration of the trust. The beneficiaries are entitled to know what the trust property is and how the trustee has dealt with it. They are entitled to examine the trust property and the accounts and vouchers and other documents relating to the trust and its administration. Where a trust is created for several beneficiaries, each of them is entitled to information as to the trust. Where the trust is created in favor of successive beneficiaries, a beneficiary who has a future interest under the trust, as well as a beneficiary who is presently entitled to receive income, is entitled to such information, whether his interest is vested or contingent."

5. The duty is a fundamental element of the trust relationship. To be a trust, there must be a beneficiary, and the trust arguably cannot operate as such if the beneficiary has no knowledge of it and no ability to enforce his or her rights.

6. Disclosure also plays a role in fiduciary risk because, depending on state law, disclosure of information may commence the running of the statute of limitations for bringing an action against the trustee. A desire by the settlor for secrecy, or trust terms that restrict a trustee from disclosing information to beneficiaries, may increase the exposure of the trustee by preventing the trustee from starting the running of statutes of limitation.

7. A trust agreement that restricts a trustee's ability to disclose information also may prevent the trustee from taking advantage of risk management tools under the Uniform Trust Code (where enacted), which include:

   a. Entering into binding nonjudicial settlement agreements with trust beneficiaries.

   b. Shortening the statute of limitations on trust contests to 120 days.

   c. Limiting to 30 days a beneficiary's right to object to a terminating distribution.

   d. Obtaining beneficiary consents, releases, and ratifications.

e. Shortening the statute of limitations on claims against the trustee to 1 year.

8. The duty to furnish information about the trust and its administration is distinct from the duty to keep and render accounts.

9. While particular state law might provide that the two duties extend to the same beneficiaries, this is not necessarily always the case. In particular, general common law principles impose a duty on trustees to provide information to beneficiaries who request it that often is broader than the duty to formally account.

10. The distinction is evident in the Restatement (Second) of Trusts, which addresses the two duties separately.

    a. Section 173, quoted above, imposes a duty to furnish information to beneficiaries.

    b. Section 172 is entitled "Duty to Keep and Render Accounts" and provides "The trustee is under a duty to the beneficiary to keep and render clear and accurate accounts with respect to the administration of the trust."

B. Beneficiaries Entitled to Information.

1. Trustee's duty to disclose at common law is rarely subject to controversy, but to whom the duty is owed is a source of regular uncertainty and ongoing litigation.

2. It is this aspect of the common law where the duty to furnish information and the duty to account most often are mixed together and treated by some courts as interchangeable. This likely is the result of a couple of factors.

    a. A beneficiary rarely sues just to obtain selected pieces of information. Most cases that result in published opinions involve a beneficiary who is seeking a full accounting by a trustee. Therefore, most of the case law discusses the issue in this context.

    b. A court ruling that a particular class of beneficiary is not entitled to an accounting often is cited by later courts, without thoughtful analysis, for the proposition that the class of beneficiary is not entitled to any information. That later case then becomes precedent for further cases who cite the general proposition without making the distinction between the two duties (and, because the cases usually involve a request for an accounting, the distinction is not relevant to the facts of the case).

3. The general statements of the law quoted earlier do not distinguish between classes of beneficiaries in stating the trustee's duty to disclose. The case law does make distinctions.

   a. Current beneficiaries of income and principal always have the right, unless the trust agreement excludes some of them.

   b. Remainder beneficiaries with vested interests (subject to the extensive case law debate over what "vested" means) often have the right.

   c. The right of contingent beneficiaries to trust information is sometimes denied, or limited to situations where the beneficiary has made an adequate showing of need.

4. Bogert summarizes the state of the common law as follows:

   "There is some authority to the effect that in the absence of a contrary provision in the trust instrument or statute only current beneficiaries, those currently entitled to receive income or principal, are entitled to information from the trustee. Current beneficiaries would appear to include persons eligible to receive income or principal in the exercise of the trustee's discretion and may include remainder beneficiaries who have vested interests. This view is similar to one adopted by a majority of the states to the effect that only a beneficiary currently entitled to payment of trust income or principal may compel the trustee to render an account, although a contingent remainderman has standing to secure an account if he alleges and makes a case for mismanagement or waste of trust assets."

   Bogert, <u>The Law of Trusts and Trustees</u>, §961.

5. Illinois is among the states that appear to follow the rule that a contingent remainder beneficiary must make some showing before being entitled to information.

   a. One of the leading statements of that rule is in the context of the right of the beneficiary to maintain an action against the trustee. In <u>Barnhart v. Barnhart</u>, 114 N.E.2d 378, 388 (1953), the court stated:

      "We believe the better rule to be that while a contingent remainderman should not be denied the right to bring an action against the trustees regardless of circumstances and merely because his interest is remote and contingent, nevertheless, the scope of the right should be limited to that which is necessary to protect his possible eventual interest, i.e., the protection and preservation of the trust *res*. It should be afforded only where waste, mismanagement or dissipation of assets appear or can be shown."

b. Remote or contingent beneficiaries have been able to maintain suits on numerous occasions. See Bullis v. Dupage Trust Co., 391 N.E.2d 231 (Ill. App. 1979) (vested remainderman); Pinzino v. Vogel, 424 N.E.2d 371 (Ill. App. 1981) (default takers under general power of appointment).

c. In each of these cases, the beneficiary obviously was able to gain some information about the trustee's actions sufficient to raise a question of possible mismanagement. The case law does not help if a beneficiary knows of the trust but the trustee refuses to provide any information about its administration. Query though whether a trustee really is entitled to refuse to provide any information to a remainder beneficiary based on case law that addresses a beneficiary's right to sue for an accounting or an alleged breach of fiduciary duty.

6. Cases in some states have granted contingent beneficiaries an unequivocal right to seek information or enforce the trust. See, e.g. Gaynor v. Payne, 804 A.2d 170 (Conn. 2002) (representative of contingent remainder beneficiaries allowed to sue); Matter of Polson, 585 P.2d 840 (Wash. 1978) (statute allows any beneficiary to petition for an accounting and it was not necessary to allege waste and mismanagement).

C. Power of Settlor to Alter Duties.

1. State law will define the extent and scope of the trustee's duties. The governing principles may be defined in the common law, or, increasingly, by statute. The Uniform Trust Code model is becoming the most common form of statutory authority.

2. Under the Uniform Trust Code as well as the law of Illinois and most non-UTC states, the trust settlor has the right to alter the duty to disclose rules that otherwise would apply under state law. The Illinois Trusts and Trustees Act generally states that its provisions apply "to the extent that they are not inconsistent with the provisions of the instrument." 760 ILCS 5/3.

3. The common law supports settlor control of this question, but not without limits. Comment c. to the Restatement (Second) of Trusts states:

"*Terms of the trust*. Although the terms of the trust may regulate the amount of information which the trustee must give and the frequency with which it must be given, the beneficiary is always entitled to such information as is reasonably necessary to enable him to enforce his rights under the trust or to prevent or redress a breach of trust."

4. The primary limits at common law on the settlor's ability to control disclosure of information are:

a. The settlor cannot eliminate completely the trustee's obligation to account. The trustee must be answerable to someone; to allow otherwise destroys the nature of the trust relationship.

b. A limitation on the duty to disclose or duty to account will not be given effect in a particular instance if doing so is harmful to a particular beneficiary's interests.

(1) For example, a trust provision that allows the trustee to submit an accounting to a particular beneficiary, and that approval of that beneficiary will bind all beneficiaries, may not be given effect if the trustee and/or approving beneficiary are acting in bad faith as to the interests of other beneficiaries.

(2) Or, a provision allowing a trustee not to inform a current beneficiary of the existence of the trust might be deemed invalid.

(3) There is a great deal of uncertainty over this second category, in particular as it applies to minor or young adult beneficiaries whose parents also are beneficiaries of a trust. Many practitioners believe that an explicit direction from the trust settlor that directs the trustee not to inform a beneficiary of their interests until the beneficiary reaches a certain age should be enforceable.

5. In In re Malasky, 736 N.Y.S.2d 151 (2002), the court recognized that a trust settlor could limit the rights of beneficiaries to an accounting but stated that "any attempt to completely excuse the obligation of a trustee to account is void against public policy."

6. In Briggs v. Crowley, 224 N.E.2d 417 (Mass. 1967), the court stated "that the clauses in the trust instrument purporting to relieve the trustees of the duty imposed by law to account are invalid as against public policy in so far as they deprive the Probate Court of jurisdiction and the petitioner of her standing to maintain this proceeding." See also In re Estate of Wallich, 420 P.2d 40 (Utah 1966) (trust provision purporting to waive obligation of making any accounting held against public policy).

7. In In re McGuire Marital Trust, 660 N.W.2d 308 (Wis. 2003), the court upheld a provision that the trustees were required to account only to current beneficiaries. The court stated that the settlor had broad discretion to control the trust administration and that the settlor in this case clearly had intended to favor income beneficiaries over remainder beneficiaries. Therefore, it concluded that the settlor could limit the trustee's duty to

account and it denied a request by remainder beneficiaries to obtain copies of accountings.

8. Even where the trustee may have a legal right to deny accountings to certain beneficiaries based on the settlor's explicit intent as reflected in the trust agreement, the trustee should be conscious of the consequences separate and apart from any legal issues. In a longer term trust relationship, the beneficiaries who are denied information now someday will be the primary beneficiaries and likely will not have forgotten how the trustee treated them.

D. Silent Trusts

1. A "silent trust" or "quiet trust" is one in which the settlor overrides state law and directs the trustee not to inform certain beneficiaries of the existence of the trust, or the information about it that the trustee normally would have a duty to provide.

2. Advocates of the silent trust support it as another means of carrying out the settlor's intent. Proponents observe that a settlor should be able to engage in trust planning but still maintain confidentiality about their plan, including from certain trust beneficiaries. If a settlor can choose to exclude a child or grandchild from a trust, the settlor also should be able to include that person but not inform him or her.

3. It also is pointed out that limits on disclosure can be particularly appropriate for younger beneficiaries, who may not have the maturity or sufficiently formed values to properly deal with the information.

4. The ability of a trust settlor to alter the duties of the trustee under the laws of many states allows the settlor to create a silent trust. Illinois and California are two of the many states that implicitly allow silent trusts, through the general statutory provision that the trust settlor can override the provisions of the statute on providing accounts and information. Common law would determine the limits, if any, on that ability. See Appendix A for samples of the statutes on accounting and duty to inform from several states.

5. The UTC takes another approach. It specifically allows the settlor to negate the duty to disclose but only for beneficiaries who have not reached the age of twenty-five years. See Appendix A, UTC discussion, Default vs. Mandatory Rules for a more detailed discussion of the UTC provisions. Enacting states have taken a number of different approaches with this provision, from eliminating it entirely to broadening the scope of the non-disclosure rule.

6. A third approach is found in states such as Delaware, which expressly allow silent trusts and exculpate the trustee of such a trust to the maximum extent reasonable. Section 3303(a) of the Delaware statute provides:

"§ 3303 Effect of provisions of instrument

(a) Notwithstanding any other provision of this Code or other law, the terms of a governing instrument may expand, restrict, eliminate, or otherwise vary any laws of general application to fiduciaries, trusts and trust administration, including, but not limited to, any such laws pertaining to:

(1) The rights and interests of beneficiaries, including, but not limited to, the right to be informed of the beneficiary's interest for a period of time, as set forth in subsection (c) of this section;

. . .

(c) The terms of a governing instrument may expand, restrict, eliminate, or otherwise vary the right of a beneficiary to be informed of the beneficiary's interest in a trust for a period of time, including but not limited to:

(1) A period of time related to the age of a beneficiary;

(2) A period of time related to the lifetime of each trustor and/or spouse of a trustor;

(3) A period of time related to a term of years or specific date; and/or

(4) A period of time related to a specific event that is certain to occur.

(d) During any period of time that a governing instrument restricts or eliminates the right of a beneficiary to be informed of the beneficiary's interest in a trust, unless otherwise provided in the governing instrument, any designated representative (as defined in § 3339 of this title) then serving shall represent and bind such beneficiary for purposes of any judicial proceeding and for purposes of any nonjudicial matter, and shall have the authority to, and is a proper party to, initiate a proceeding relating to the trust before a court or administrative tribunal on behalf of any such beneficiary."

7. Delaware and a number of other states, including for example Florida, add the concept of an information delegate or "qualified representative" who is designated to receive information on behalf of the beneficiary. This arguably creates a mechanism for the trustee to manage risk and fulfill its

fiduciary duties. While the statute may help limit the liability of the trustee, it does so by shifting potential liability to the representative.

VII. Considerations in Drafting Trusts

A. None of the preceding discussion leaves practitioners with a clear guide for best practices in drafting trusts. And it should not. By definition each client representation is unique. What follows are some general considerations based on the client's family situation.

B. As noted earlier, for families who are in the top 2 to 3% of income and net worth, but not in the top 0.10%, it may not be necessary or cost-effective to highly customize trust terms for future generations.

1. Their wealth allows for a very nice lifestyle, but not for family members to truly live the life of idle rich.

2. The use of traditional distribution standards and standard guidance to trustee may be fine. The focus of a discussion on customized provisions should be on terms that allow for the child or grandchild to become involved in managing the trust property as a co-trustee or eventually a trustee.

3. The best way to address trust terms for grandchildren and future generations is to provide a standard default set of terms but give each child a power of appointment that will allow the child to evaluate what is best for their children and modify the trust terms appropriately.

C. If you agree that the goal in family wealth planning is to encourage family communication and education about wealth, then silent trusts do not contribute positively.

1. Standard trust terms will force the clients and their families to confront informing a trust beneficiary.

2. The attorney still must be sensitive to concerns that parents or grandparents might have about informing a beneficiary who is age eighteen. Many practitioners start with the idea of using spray trusts that allow for distributions to spouse and descendants or child and descendants. They are the most flexible form of trust to use. If the clients are concerned about young adults being told about the trust, then, instead of using a form of silent trust, consider not including young descendants as beneficiaries.

    a. The trust for the child could name only the child as a beneficiary during his or her life (or until disability). The child could have a lifetime power of appointment to descendants as a way to get funds to lower generations without making them beneficiaries.

b. Another alternative is a trust for the child and any descendant over a designated age (21, 25 or 30). The trust could be crafted so that distributions could be made directly to the child to cover education or health costs of the child's children when they are young.

3. Another approach is to layer trusts. The settlor could make each child the only beneficiary of his or her trust but create separate, smaller trusts for the grandchildren as well. A grandchild will learn about his or her trust at age 18, and it will be part of the education process for the grandchild. But the grandchild has no interest in, or right to information on the child's trust (or perhaps only gains an interest at a designated age).

D. Ages matter a great deal in crafting the estate plan.

1. A client whose children are young and who is concerned about the impact that trusts will have on the children's motivation and life goals is missing the point.

a. For the most part the child will have formed their own values and "money personalities" before he or she ever becomes aware of the trust.

b. The family's lifestyle and lessons from the parents will be the primary influence on the child's values.

2. If the children are adults and are appropriately successful and independent, the trust can be designed, as most are, to help make their lives better, to supplement their own resources, but not to let them immediately retire.

3. In any situation where a child already has problems, whether they are physical or mental disabilities or a clear inability to manage their financial life, the trust should be designed to address the child's needs and/or to provide special restrictions and instructions.

E. Ultra-high net worth families face the greatest challenges. It is for them that highly customized trusts are worth the investment.

1. The default still should be to emphasize communication and education as the key. Never let the clients believe that the trust terms will solve their problem.

2. The children and grandchildren in these families are much more likely to have a reasonably accurate understanding of the family's wealth. The idea of a silent trust that allows the family to put off disclosure of the trusts' existence seems especially misplaced in this circumstance.

3. An extremely restrictive trust also can be counter-productive. The child will be accustomed to a certain lifestyle, and trusts or inheritance may in

fact have helped support that lifestyle for the parents and for the child when he or she lived at home. It does not make sense to limit access to trusts by the child to such a degree that the child must create his or her own wealth to maintain their accustomed lifestyle.

4. This is exactly what some clients do want, however. If they make that choice in an informed manner, it is their right to do so. The estate planner must craft the estate plan to help carry out their intent.

5. The most challenging situation is where the family already is living an idle life, and spending recklessly. The parents are not working and not managing their wealth responsibly. The silver dagger syndrome, as described by consultant Matthew Wesley, already is well-entrenched. A trust never will solve the family's challenges.

   a. In these circumstances, there may be some unique customized terms to consider.

   b. For example, the trust could contain expanded authorization for the trustee to make expenditures directly for the benefit of the beneficiary rather than to the beneficiary. This gives the trustee greater ability to control how funds are spent.

   c. That authorization could include explicit direction to use funds for treatment for substance abuse or other disorders.

   d. Another option would be to go "old school" and have a large portion of the family wealth pass to a generation-skipping, income only per stirpes trust. All each generation will receive from the trust is income. The ability to pressure a trustee for other distributions is eliminated. A harsh approach, but it preserves the family wealth for future generations.

VIII. Particular Standards of Distribution – What Does the Language Mean?

A. "Support" and "maintenance"

1. The terms "support" and "maintenance" normally are construed as synonyms. See Restatement Third § 50, comment d(2). They encompass more than bare subsistence. Hartford-Connecticut Trust Co. v. Eaton, 36 F.2d 710 (2d Cir. 1929). These terms include the beneficiary's normal living expenses, such as housing, clothing, food, and medical care, depending on the standard of living enjoyed by the beneficiary during the settlor's or testator's life. In re Levinson's Will, 5 Misc. 2d 979, 162 N.Y.S.2d 287 (1957); Hill v. Comm'r, 88 F.2d 941 (8th Cir. 1937); Equitable Trust Co. v. Montgomery, 44 A.2d 420 (Del. Ch. 1945).

2. The commentary to the Restatement adds that living expenses normally would include things such as mortgage payments, property taxes, suitable health insurance or care, casualty insurance, and also items such as vacation expenses in accordance with past vacations. The Restatement suggests that a beneficiary should be able to continue past patterns of charitable and family giving; not that the trustee would cover these with distributions, but that the beneficiary should be able to make these expenditures without reduction of the support coming from the trust. Restatement Third § 50, comment d(2)

3. The extent to which the standard of living or lifestyle of the beneficiary should be taken into account also depends on the size of the trust fund, and whether it needs to be preserved for probably future needs of the beneficiary. See Restatement Third § 50, comment d(2). In other words, the beneficiary may need to accept a less extravagant lifestyle if he or she is dependent on a trust of more limited size as his or her primary source of support.

4. In many states, if a trustee may distribute principal for a beneficiary's support, the trustee also may distribute principal for the support of the beneficiary's spouse and children. The beneficiary's legal obligations of support are a part of his living expenses. See In re Sullivan, 12 N.W.2d 148 (Neb. 1943); Robinson v. Robinson, 173 Misc. 985, 19 N.Y.S.2d 44 (Surr. Ct. 1940); Seattle-First National Bank v. Crosby, 254 P.2d 732 (1953); Akers v. Fidelity & Columbian Trust Co., 234 S.W. 72 (1921).

   a. However, one court limited the permissible distributions to those for the support of the beneficiary alone, and not for the support of his wife and dependent children. Cavett v. Buck, 397 P.2d 901 (Okla. 1964).

   b. An Illinois appellate court recently addressed a case in which the trustee-beneficiary used trust property that was available for his "health, support and maintenance in reasonable comfort" to purchase a custom-built second home and title it in his current wife's name. In reversing a dismissal by the lower court in the trustee-beneficiary's favor, the court focused on whether this "extraordinary gift" to the new wife was authorized under the trust's distribution standard. The court remanded the case for further proceedings. Gwinn v. Gwinn, 60 N.E.3d 890, 2016 Ill.App.2d 150851 (2nd Dist. 2016).

   c. If the settlor wishes to allow the trustee to make distributions to spouses of the settlor's descendants, he or she should include a specific provision in the trust instrument.

SAMPLE TRUST PROVISION: In the trustee's sole and uncontrolled discretion, the trustee also may distribute income or principal to any individual who at any time was married to a descendant of mine in such amounts as the trustee, other than the distributee, deems necessary for the distributee's health and support in reasonable comfort in light of the distributee's role within the family of that descendant of mine.

B. "Comfort"

1. In some states, the term "comfort" is limited to an ascertainable standard related to the beneficiary's health and support. Estate of Vissering, 990 F.2d 578 (10th Cir. 1993); Pyle v. United States, 766 F.2d 1141 (7th Cir. 1985), cert. denied, 106 S.Ct. 1197 (1986) (under Illinois law, the word "comfort," when linked to "health," "support," and "maintenance," created an ascertainable standard).

2. In other states, the standard is broader than "support or maintenance," and encompasses a beneficiary's enjoyment, pleasure, happiness, satisfaction, or peace of mind.

3. The Restatement Third takes the position that the term "comfort", whether used separately ("support and comfort") or as a modifier ("comfortable support") adds nothing to the usual meaning of support for a beneficiary whose lifestyle already is comfortable. It may be meaningful if the beneficiary's lifestyle has been more modest. See Restatement Third § 50, comment d(2).

4. In applying this standard, one court allowed distributions to purchase an automobile to enable the beneficiary's daughter to visit the beneficiary because her visits "did much to ease the mind" of the beneficiary. In re Mirfield's Estate, 126 N.Y.S. 465 (Sur. Ct. 1953).

5. "Comfort" has also been construed as relating to the grantor's, rather than the beneficiary's, accustomed standard of living. The Mississippi Supreme Court ruled that the term "comfort" should be construed according to the grantor's understanding of the word, which could be discovered by looking at the grantor's standard of living. Gulf National Bank v. Sturtevant, 511 So. 2d 936 (Miss. 1987).

C. "Best interests" or "best interests and welfare"

1. Under these standards, the trustee may make distributions to allow the beneficiary to enjoy a higher standard of living, or to have certain selected luxuries, such as extensive travel or the purchase of luxury automobiles and jewelry.

2. The term "best interests" has been interpreted to allow distributions for more than the beneficiary's pecuniary interests. Best interests include peace of mind, as well as financial gain. Wiedenmanyer v. Johnson, 254 A.2d 534, aff'd, 259 A.2d 465 (1969). In light of the broad meaning of the term and the liberal attitude towards distributions that it encompasses, it may be appropriate to add some limitations to the standard, such as the italicized language below.

   SAMPLE TRUST PROVISION: The term "best interests" with respect to distributions to any beneficiary shall be construed to provide the beneficiary with the means to enjoy a comfortable lifestyle, including recreation, cultural pursuits, and travel, *but, in the case of a descendant of mine, shall not be construed so generously as to discourage the descendant from assuming the responsibilities of self-support*.

   SAMPLE TRUST PROVISION: The term "best interests" refers to all aspects of a beneficiary's happiness and well-being *within the context of reasonable personal and social conduct*, as determined in the absolute discretion of the trustee.

3. Although distributions are permissible for a wider variety of purposes under a best interests standard than under a standard of support, the beneficiary may be less able to compel the trustee to distribute trust assets since the beneficiary's best interests are less easily defined. In other words, the standard is less enforceable from a beneficiary's perspective and therefore grants the trustee greater latitude.

4. Some courts have held that if the trustee is authorized to distribute principal under a best interests or similar standard, then the trustee has the authority to distribute the entire trust principal to the beneficiary in a lump sum, provided that such a distribution is not an abuse of the trustee's discretion. See, e.g., Lees v. Howarth, 131 A.2d 229 (R.I. 1957). Therefore, if a best interests standard is used, but the settlor wants to preserve trust principal for the remaindermen, the trust instrument should contain language which expresses that intention.

   SAMPLE TRUST PROVISION: My primary concerns during the life of the child are to preserve trust principal for ultimate distribution to the child's descendants while at the same time reasonably providing for the health, support, education and best interests of the child.

5. If the settlor does want the trustee to have the power to distribute the entire trust principal to the beneficiary, the settlor could use the following provision:

SAMPLE TRUST PROVISION: If at any time the trustee believes that it would be in my child's best interests and determines that it is otherwise appropriate under the circumstances, it may in its absolute discretion distribute to him the entire principal of his trust and terminate his trust, without regard to the interests of remaindermen. My child shall have no right to require that the trustee make any distribution that is not subject to an ascertainable standard, and the trustee is expressly exonerated from all liability to my child and all other interested parties by reason of the exercise or non-exercise of its discretionary authority in such matters.

D. "Education"

1. In general, the term "education" includes college education, but does not include graduate level or professional education, unless specifically provided by the trust instrument. Bogert § 182; Murphy v. Morris, 141 S.W.2d 518 (Ark. 1940); Epstein v. Kuvin, 95 A.2d 753 (N.J. Super. 1953).

2. The term "college education" has been held to include the expenses of a high school education, since a high school education is normally required to prepare the beneficiary for college. Security Trust Co. v. Smith, 145 S.W.2d 512 (Ky. 1940).

SAMPLE TRUST PROVISION: The term "education" includes, but is not limited to, the expenses of private schooling at the elementary and secondary school level, college, graduate and professional schools, and specialized or vocational training.

SAMPLE TRUST PROVISION: The term "education" includes all expenses of public and private education at any level, such as tuition, room and board, books, fees, all desirable study materials, dues, reasonable allowance and travel to and from home, as well as graduate and professional education, and specialized or vocational training.

E. "Health"

1. The term "health" includes all routine medical care, medication, surgery and hospitalization, as well as expenditures for extended nursing care and mental health. It arguably is duplicative of support, because most states would find that reasonable health care expenses would be included within support.

2. Some commentators have suggested that the term "medical care" may be more limited than health, because it may not cover treatment for psychological or mental health problems or addictions, which have not been universally recognized as "medical" problems. See W. Franzen, W. Butler & E. McGee, "Discretionary Distributions," Trust Administration, p. 5-16 (Illinois Institute for Continuing Legal Education 2014).

SAMPLE TRUST PROVISION: The term "health" shall be construed liberally to include all forms of mental or physical health care, including, but not limited to, nursing or other extended care.

SAMPLE TRUST PROVISION: The term "health" includes all expenses of health care providers net of insurance benefits paid to or for the beneficiary, such as hospital charges, physician service fees, lab charges, ambulance, nursing care at any location, physical and psychological therapy, drugs and the like, health insurance premiums for a beneficiary, as well as all costs of an extended health care facility, including an entrance fee or endowment fee (whether refundable or not), interest free loan and other forms of capital charge, as well as monthly assessments and other periodic charges.

3. In some cases, the settlor may wish to express a preference for home health care over nursing home care, and specifically to authorize distributions for that purpose.

SAMPLE TRUST PROVISION: In making discretionary distributions for me or my spouse under this instrument, the trustee shall consider my strong desire that medical care, nursing care, and other types of care and assistance that are necessary for me or my spouse be provided to me or my spouse in the familiar environment of our home to the greatest extent practicable, without regard to the additional cost of such home care and assistance.

F. "Emergency"

1. The Restatement Third categorizes "emergency" as restrictive terminology, along with terms like "severe hardship" or "special need." Restatement Third § 50, comment d(4). Likewise, many courts interpret the term "emergency" as a very narrow and restrictive standard, which authorizes distributions only for the beneficiary's unusual and unforeseen expenses, and not for the beneficiary's routine or ordinary support and maintenance. See, e.g., Nardi v. United States, 385 F.2d 343 (7th Cir. 1967); Budd v. Commissioner, 49 T.C. 468 (1968).

2. Nevertheless, the IRS has taken the position on a number of occasions that the term does not create an ascertainable standard for federal estate and gift tax purposes.

   a. The IRS has privately ruled that a standard of "great emergencies which may arise in the lives and affairs of [the beneficiary], such as extra needed medical services or hospitalization" did not restrict distributions to emergencies relating to medical needs. The language "such as extra needed medical services or hospitalization" merely illustrated some of the types of

expenditures that would qualify as emergencies, but were not intended to be an exclusive list. The IRS noted that distributions could also be made for any "sudden or unexpected happenings," such as being stranded in a foreign country without funds to return home. Letter Ruling 8304009 (Oct. 25, 1982).

b. The IRS has also ruled that the phrase "any other emergency condition of any exigencies" did not constitute an ascertainable standard. Letter Ruling 9044081 (July 31, 1990).

c. However, in Letter Ruling 200028008 (July 14, 2000), the IRS gave a more favorable interpretation to the standard "proper care, support and maintenance, or in the event of any other accident, illness or other emergency." The IRS concluded that "emergency" must be limited to the types of emergencies itemized before the word "other" and therefore constituted an ascertainable standard. Similarly, in Letter Ruling 201039003 (June 25, 2010) the IRS concluded the power to distribute principal for the beneficiary's "reasonable care, maintenance or proper education, or on account of any illnesses, infirmity, or other like emergency" is limited by an ascertainable standard.

3. Several courts have rejected the IRS position and held that a standard of distribution related to "emergency" is an ascertainable standard for tax purposes. Estate of Sowell v. Commissioner, 708 F.2d 1564 (10th Cir. 1983), rev'g 74 T.C. 1001 (1980); Wahlfeld v. United States, 47 A.F.T.R.2d (P-H) ¶ 148,432, at 81-1565 (C.D. Ill. 1980); Hunter v. United States, 597 F. Supp. 1293 (W.D. Pa. 1984). In Hunter, the court stated that it could not envision an emergency that was not measurable in terms of the beneficiary's health or support.

4. To forestall the IRS's argument that the term emergency is not an ascertainable standard, the draftsperson may wish to specify the types of emergencies for which distributions are authorized: such as financial emergencies or only those related to health or maintenance.

SAMPLE TRUST PROVISION: The trustee shall distribute as much of the principal of the trust, even to the extent of exhausting principal, as the trustee from time to time determines to be required to meet the expenses of an illness or other emergency relating to the health, support and education of the child and his or her descendants.

G. "Happiness"

1. In contrast to "emergency", the use of the term "happiness" is considered expansive of the distribution power.

2. The Restatement Third states that the term suggests an intention that the trustee act generously and "without relatively objective limitation." Restatement Third § 50, comment d(3). It adds that the primary effect of the term is to immunize decisions from the challenge of remainder beneficiaries. At the same time, it does not create minimum entitlements for the current beneficiary, so the trustee still can legitimately decline requests. Id.

H. "Sole and absolute discretion" of the trustee

1. Under the older common law interpretation of this standard, the trustee may make distributions for any purpose or withhold funds from the beneficiary, as long as the trustee does not act in bad faith or arbitrarily. See In re Ledyard's Estate, 21 N.Y.S.2d 860 (1939); Estate of Zuckerman, NYLJ, January 29, 1990, p. 30. Where the trustee's discretion is "absolute" or "uncontrolled," a court will grant the trustee's decision even more deference. Bogert § 811.

2. More recent guidance suggests that the courts exercise more oversight, in light of the fundamental duty to act in a beneficiary's interests. The UTC provision is as follows:

> (a) 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.
>
> UTC Section 814 (a)

3. The commentary to Section 814 states that no grant of discretion to a trustee should be absolute.

4. Indeed, courts often impose a standard of reasonableness, even where the trustees are given "absolute and uncontrolled discretion" to invade principal.

   a. In one case, the beneficiaries of two $8 million trusts requested distributions of $145,000 and $150,000 in principal. The trustees refused the request because the money was not needed and the beneficiaries' planned use for the money was unlikely to be productive. Although the court found that the trustees had acted in good faith in refusing the request, the court found that the trustees should not have applied such considerations in determining whether or not to make the requested distribution, and directed the trustees to make the distribution. Matter of Stillman, 433 N.Y.S.2d 701 (1980).

b. In another case in which the trustees had the power to invade principal "as the trustees in their discretion shall deem proper," the court held that "even where the payment of principal rests in the uncontrolled discretion of the trustee, he must not in exercising his authority act dishonestly, or with an improper motive or fail to use his judgment or act beyond the bounds of reasonable judgment." Estate of Joseph P. Sanders, NYLJ, April 19, 1991, p. 25.

c. In a Connecticut case, a trustee was given authority to distribute as much of the income as it thought advisable in its absolute discretion. The court found that the trustee could withhold income from the beneficiaries as long as it acted in good faith and without abuse of discretion. Auchincloss v. City Bank Farmers Trust Co., 70 A.2d 105 (Conn. 1949).

d. The case law indicates that the use of the words "sole and absolute discretion" will not necessarily free the trustee completely from enforceable requests for distributions. If the settlor wants the trustee to have complete latitude and the beneficiaries to have no enforceable rights against the trustee, it may be necessary to be more explicit.

SAMPLE TRUST PROVISION: My child shall have no right to require that the trustee make any distribution, and the trustee is expressly exonerated from all liability to my child by reason of the exercise or non-exercise of its discretionary power.

e. It is possible that a state court might declare this broad a grant of discretion void as against public policy.

5. A trustee's power to make distributions in its sole discretion must be distinguished from a trustee's power, in its sole discretion, to make distributions pursuant to a particular standard, such as for the beneficiary's support. In one case, the trustee argued that his authority to make payments for "the comfortable maintenance, support and education [of the beneficiary] as he or it shall, in his or its sole discretion, deem advisable" authorized the trustee to withhold any payments to the beneficiary. The court disagreed, and found that the trustee's power was limited by the standard of "comfortable maintenance, support and education," and that the trustee had the duty to make distributions in accordance with that standard. Kolodney v. Kolodney, 503 A.2d 625 (Conn. App. 1986).

6. The Restatement Third provides the following illustration regarding the grant of uncontrolled discretion in the context of a defined standard:

> 3. Following S's death his previously revocable trust has been administered for nearly a decade by T Bank, which is directed to

pay income to S's widow, W, and also empowered to pay her "such additional amounts from the principal of the trust as the Trustee, in its sole and uncontrolled discretion, believes appropriate for W's comfortable support and care," with the remainder upon W's death to pass to S's then living issue. In response to requests by W, T Bank has begun to pay substantially increased amounts to her to enable her to accumulate funds from which she may aid C (her child by a prior marriage) in his plans to obtain control and expand the activities of X Co., of which C has been an officer and shareholder for a number of years. S's children petition the court to instruct T Bank that principal distributions for that purpose are improper and that it must recover amounts previously paid to W for that purpose. Nothing in relevant circumstances or in other terms of the trust indicates a broader purpose for the invasion power than the support-related (see Comment *d)* language quoted above. The court will issue the order requested by the remainder beneficiaries. Despite S's grant of extensive discretion, and without a finding of bad faith, T's judgment was not exercised in an appropriate state of mind, that is, for a purpose falling within the quoted standard.

Restatement Third § 50, comment c.

I. "Standard of living"

1. A distribution standard often refers to the beneficiary's standard of living. In most cases, it is not necessary to elaborate on this reference. However, if there is a concern about changing standards of living, the time to which the standard of living refers should be made clear.

    a. For example, it could refer to the standard of living when the instrument was drafted, when the instrument became effective (i.e., at the decedent's death in the case of the will), or when the beneficiary's interest vested.

    b. It may be especially important to provide guidance on standard of living in a very wealthy family. The standard of living may be quite opulent for the creator of the trust, but he or she recognizes that future generations cannot or should not be able to live that lifestyle, in particular at a younger age. This may be simply because the amounts available to descendants will be far less after reduction by estate taxes and division among multiple family members.

2. One case has stated that a direction in a will to distribute trust property for the beneficiary's "support or maintenance in accordance with her present standard of living" referred to the beneficiary's standard of living at the

time the will was executed, rather than at the decedent's death. Hart v. Connors, 228 N.E.2d 273, 275 (Ill. App. 1967).

3. In another case, however, the court found that the trustee's authority to invade principal to maintain the beneficiary's standard of living referred to the beneficiary's standard of living at the death of the testator. In re Golodetz' Will, 118 N.Y.S.2d 707 (N.Y. Sur. 1952).

4. If the beneficiary's standard of living substantially improves or is reduced between the time the instrument is drafted and the decedent's death, a standard of distribution tied to the beneficiary's standard of living may not carry out the settlor's intent.

SAMPLE TRUST PROVISION: The trustee shall distribute to my wife so much of the income and principal as it determines to be desirable for her comfortable support and reasonable health, considering our standard of living at my death and all other income currently available for such purposes.

IX. Conclusion

An experienced trusts and estates lawyer can draft a highly personalized trust with very specific provisions reflecting the settlor's intent and the trust purposes. The foregoing discussion should make it evident, however, that this is not the only service that the client may need. The trust professional should be prepared to engage clients in the discussion of how to prepare future generations for the wealth they may receive, and to refer them to other professionals who can assist with that process.

Appendix – State Statutes

Illinois

(760 ILCS 5/11) (from Ch. 17, par. 1681)

Sec. 11. Accounts.

(a) Every trustee at least annually shall furnish to the beneficiaries then entitled to receive or receiving the income from the trust estate, or if none, then those beneficiaries eligible to have the benefit of the income from the trust estate a current account showing the receipts, disbursements and inventory of the trust estate. A current account shall be binding on the beneficiaries receiving the account and on such beneficiaries' heirs and assigns unless an action against the trustee is instituted by the beneficiary or such beneficiary's heirs and assigns within 3 years from the date the current account is furnished.

(b) Every trustee shall on termination of the trust furnish to the beneficiaries then entitled to distribution of the trust estate a final account for the period from the date of the last current account to the date of distribution showing the inventory of the trust estate, the receipts, disbursements and distributions and shall make available to such beneficiaries copies of prior accounts not theretofore furnished. Such final accounting shall be binding on the beneficiaries receiving the same and all persons claiming by or through them, unless an action against the trustee is instituted by the beneficiary or person claiming by or through him or her within 3 years from the date the final account is furnished.

* * *

(e) If a beneficiary is under a legal disability, the account shall be provided to the representative of the estate of the beneficiary and shall be binding on the beneficiary and the beneficiary's estate unless an action against the trustee is instituted by the representative within 3 years from the date the account is furnished. If no representative for the estate of a beneficiary under legal disability has been appointed, the account shall be provided to a spouse, parent, adult child, or guardian of the person of the beneficiary and shall be binding on the beneficiary unless an action is instituted against the trustee by the spouse, parent, adult child, or guardian of the person to whom the account is furnished within 3 years from the date it is furnished.

(f) If the trustee is guilty of fraudulent concealment, notwithstanding subsection (a), (b), (c), (d) or (e), the beneficiary may bring the action within the time limit set forth in Section 13-215 of the Code of Civil Procedure.

(g) Receipt of an account by a beneficiary (or other person, as provided) is presumed if the trustee has procedures in place requiring the mailing or delivery of an account to the beneficiary (or other person, as provided). This presumption shall apply to the mailing or delivery of an account by electronic means or the provision of access to an account by electronic means so long as the beneficiary has agreed to receive such electronic delivery or access.

(Source: P.A. 92-222, eff. 8-2-01.)

California

ARTICLE 3. Trustee's Duty to Report Information and Account to Beneficiaries [16060 - 16069] (Article 3 enacted by Stats. 1990, Ch. 79.)

16060. The trustee has a duty to keep the beneficiaries of the trust reasonably informed of the trust and its administration.

16060.5. As used in this article, "terms of the trust" means the written trust instrument of an irrevocable trust or those provisions of a written trust instrument in effect at the settlor's death that describe or affect that portion of a trust that has become irrevocable at the death of the settlor. In addition, "terms of the trust" includes, but is not limited to, signatures, amendments, disclaimers, and any directions or instructions to the trustee that affect the disposition of the trust. "Terms of the trust" does not include documents which were intended to affect disposition only while the trust was revocable. If a trust has been completely restated, "terms of the trust" does not include trust instruments or amendments which are superseded by the last restatement before the settlor's death, but it does include amendments executed after the restatement. "Terms of the trust" also includes any document irrevocably exercising a power of appointment over the trust or over any portion of the trust which has become irrevocable.

16060.7. On the request of a beneficiary, the trustee shall provide the terms of the trust to the beneficiary unless the trustee is not required to provide the terms of the trust to the beneficiary in accordance with Section 16069.

16061. Except as provided in Section 16069, on reasonable request by a beneficiary, the trustee shall report to the beneficiary by providing requested information to the beneficiary relating to the administration of the trust relevant to the beneficiary's interest.

16061.5. (a) A trustee shall provide a true and complete copy of the terms of the irrevocable trust, or irrevocable portion of the trust, to each of the following:

(1) Any beneficiary of the trust who requests it, and to any heir of a deceased settlor who requests it, when a revocable trust or any portion of a revocable trust becomes irrevocable because of the death of one or more of the settlors of the trust, when a power of appointment is effective or lapses upon the death of a settlor under the circumstances described in paragraph (3) of subdivision (a) of Section 16061.7, or because, by the express terms of the trust, the trust becomes irrevocable within one year of the death of a settlor because of a contingency related to the death of one or more of the settlors of the trust.

(2) Any beneficiary of the trust who requests it, whenever there is a change of trustee of an irrevocable trust.

* * *

16061.7. (a) A trustee shall serve a notification by the trustee as described in this section in the following events:

(1) When a revocable trust or any portion thereof becomes irrevocable because of the death of one or more of the settlors of the trust, or because, by the express terms of the trust, the trust becomes irrevocable within one year of the death of a settlor because of a contingency related to the death of one or more of the settlors of the trust.

(2) Whenever there is a change of trustee of an irrevocable trust.

(3) Whenever a power of appointment retained by a settlor is effective or lapses upon death of the settlor with respect to an inter vivos trust which was, or was purported to be, irrevocable upon its creation. This paragraph shall not apply to a charitable remainder trust. For purposes of this paragraph, "charitable remainder trust" means a charitable remainder annuity trust or charitable remainder unitrust as defined in Section 664(d) of the Internal Revenue Code.

(4) The duty to serve the notification by the trustee pursuant to this subdivision is the duty of the continuing or successor trustee, and any one cotrustee may serve the notification.

* * *

(i) Any waiver by a settlor of the requirement of serving the notification by trustee required by this section is against public policy and shall be void.

(j) A trustee may serve a notification by trustee in the form required by this section on any person in addition to those on whom the notification by trustee is required to be served. A trustee is not liable to any person for serving or for not serving the notice on any person in addition to those on whom the notice is required to be served. A trustee is not required to serve a notification by trustee if the event that otherwise requires service of the notification by trustee occurs before January 1, 1998.

16061.8. No person upon whom the notification by the trustee is served pursuant to this chapter, whether the notice is served on him or her within or after the time period set forth in subdivision (f) of Section 16061.7, may bring an action to contest the trust more than 120 days from the date the notification by the trustee is served upon him or her, or 60 days from the day on which a copy of the terms of the trust is mailed or personally delivered to him or her during that 120-day period, whichever is later.

16061.9. (a) A trustee who fails to serve the notification by trustee as required by Section 16061.7 on a beneficiary shall be responsible for all damages, attorney's fees, and costs caused by the failure unless the trustee makes a reasonably diligent effort to comply with that section.

(b) A trustee who fails to serve the notification by trustee as required by Section 16061.7 on an heir who is not a beneficiary and whose identity is known to the trustee shall be responsible for all damages caused to the heir by the failure unless the trustee shows that the trustee made a reasonably diligent effort to comply with that section. For purposes of this subdivision, "reasonably diligent effort" means that the trustee has sent notice by first-class mail to the heir at the heir's last mailing address actually known to the trustee.

(c) A trustee, in exercising discretion with respect to the timing and nature of distributions of trust assets, may consider the fact that the period in which a beneficiary or heir could bring an action to contest the trust has not expired.

(Added by Stats. 2000, Ch. 34, Sec. 6. Effective January 1, 2001.)

16062. (a) Except as otherwise provided in this section and in Section 16064, the trustee shall account at least annually, at the termination of the trust, and upon a change of trustee, to each beneficiary to whom income or principal is required or authorized in the trustee's discretion to be currently distributed.

(b) A trustee of a living trust created by an instrument executed before July 1, 1987, is not subject to the duty to account provided by subdivision (a).

* * *

(e) Any limitation or waiver in a trust instrument of the obligation to account is against public policy and shall be void as to any sole trustee who is either of the following:

(1) A disqualified person as defined in former Section 21350.5 (as repealed by Chapter 620 of the Statutes of 2010).

(2) Described in subdivision (a) of Section 21380, but not described in Section 21382.

* * *

16064. The trustee is not required to account to a beneficiary as described in subdivision (a) of Section 16062, in any of the following circumstances:

(a) To the extent the trust instrument waives the account, except that no waiver described in subdivision (e) of Section 16062 shall be valid or enforceable. Regardless of a waiver of accounting in the trust instrument, upon a showing that it is reasonably likely that a material breach of the trust has occurred, the court may compel the trustee to account.

(b) As to a beneficiary who has waived in writing the right to an account. A waiver of rights under this subdivision may be withdrawn in writing at any time as to accounts for transactions occurring after the date of the written withdrawal. Regardless of a waiver of accounting by a beneficiary, upon a showing that is reasonably likely that a material breach of the trust has occurred, the court may compel the trustee to account.

(c) In any of the circumstances set forth in Section 16069.

16068. Any waiver by a settlor of the obligation of the trustee of either of the following is against public policy and shall be void:

(a) To provide the terms of the trust to the beneficiary as required by Sections 16060.7 and 16061.5.

(b) To provide requested information to the beneficiary as required by Section 16061.

16069. The trustee is not required to account to the beneficiary, provide the terms of the trust to a beneficiary, or provide requested information to the beneficiary pursuant to Section 16061, in any of the following circumstances:

(a) In the case of a beneficiary of a revocable trust, as provided in Section 15800, for the period when the trust may be revoked.

(b) If the beneficiary and the trustee are the same person.

(Added by Stats. 2010, Ch. 621, Sec. 9. Effective January 1, 2011.)

Florida

736.0306 Designated representative.—

(1) If specifically nominated in the trust instrument, one or more persons may be designated to represent and bind a beneficiary and receive any notice, information, accounting, or report. The trust instrument may also authorize any person or persons, other than a trustee of the trust, to designate one or more persons to represent and bind a beneficiary and receive any notice, information, accounting, or report.

(2) Except as otherwise provided in this code, a person designated, as provided in subsection (1) may not represent and bind a beneficiary while that person is serving as trustee.

(3) Except as otherwise provided in this code, a person designated, as provided in subsection (1) may not represent and bind another beneficiary if the person designated also is a beneficiary, unless:

(a) That person was named by the settlor; or

(b) That person is the beneficiary's spouse or a grandparent or descendant of a grandparent of the beneficiary or the beneficiary's spouse.

(4) No person designated, as provided in subsection (1), is liable to the beneficiary whose interests are represented, or to anyone claiming through that beneficiary, for any actions or omissions to act made in good faith.

History.—s. 3, ch. 2006-217; s. 4, ch. 2009-117.

736.0813 Duty to inform and account.—The trustee shall keep the qualified beneficiaries of the trust reasonably informed of the trust and its administration.

(1) The trustee's duty to inform and account includes, but is not limited to, the following:

(a) Within 60 days after acceptance of the trust, the trustee shall give notice to the qualified beneficiaries of the acceptance of the trust, the full name and address of the trustee, and that the fiduciary lawyer-client privilege in s. 90.5021 applies with respect to the trustee and any attorney employed by the trustee.

(b) Within 60 days after the date the trustee acquires knowledge of the creation of an irrevocable trust, or the date the trustee acquires knowledge that a formerly revocable trust has become irrevocable, whether by the death of the settlor or otherwise, the trustee shall give notice to the qualified beneficiaries of the trust's existence, the identity of the settlor or settlors, the right to request a copy of the trust instrument, the right to accountings under this section, and that the fiduciary lawyer-client privilege in s. 90.5021 applies with respect to the trustee and any attorney employed by the trustee.

(c) Upon reasonable request, the trustee shall provide a qualified beneficiary with a complete copy of the trust instrument.

(d) A trustee of an irrevocable trust shall provide a trust accounting, as set forth in s. 736.08135, from the date of the last accounting or, if none, from the date on which the trustee became accountable, to each qualified beneficiary at least annually and on termination of the trust or on change of the trustee.

(e) Upon reasonable request, the trustee shall provide a qualified beneficiary with relevant information about the assets and liabilities of the trust and the particulars relating to administration.

Paragraphs (a) and (b) do not apply to an irrevocable trust created before the effective date of this code, or to a revocable trust that becomes irrevocable before the effective date of this code. Paragraph (a) does not apply to a trustee who accepts a trusteeship before the effective date of this code.

(2) A qualified beneficiary may waive the trustee's duty to account under paragraph (1)(d). A qualified beneficiary may withdraw a waiver previously given. Waivers and withdrawals of prior waivers under this subsection must be in writing. Withdrawals of prior waivers are effective only with respect to accountings for future periods.

(3) The representation provisions of part III apply with respect to all rights of a qualified beneficiary under this section.

(4) As provided in s. 736.0603(1), the trustee's duties under this section extend only to the settlor while a trust is revocable.

(5) This section applies to trust accountings rendered for accounting periods beginning on or after July 1, 2007.

The Uniform Trust Code

1. The Uniform Trust Code ("UTC") imposes several distinct duties to provide information to beneficiaries, all of which are located in Section 813 (Duty to Inform and Report).

2. The concept of the "qualified beneficiary" is important to understanding Section 813. Section 103 of the UTC defines "qualified beneficiary" as a beneficiary who, on the date the beneficiary's qualification is determined:

   a. is a distributee or permissible distributee of trust income or principal;

   b. would be a distributee or permissible distributee of trust income or principal if the interests of the distributees described in subparagraph (a) terminated on that date without causing the trust to terminate; or

   c. would be a distributee or permissible distributee of trust income or principal if the trust terminated on that date.

3. UTC section 813 imposes several distinct duties on trustees:

   a. 813(a) (duty to keep reasonably informed):

      > "A trustee shall keep the qualified beneficiaries of the trust reasonably informed about the administration of the trust and of the material facts necessary for them to protect their interests."

   b. 813(a) (duty to respond to requests for information):

      > "Unless unreasonable under the circumstances, a trustee shall promptly respond to a beneficiary's request for information related to the administration of the trust."

   c. 813(b)(1) (duty to provide a copy of the trust instrument):

      > "A trustee…upon request of a beneficiary, shall promptly furnish to the beneficiary a copy of the trust instrument."

   d. 813(b)(2) (duty to notify of acceptance of trusteeship):

      > "A trustee…within 60 days after accepting a trusteeship, shall notify the qualified beneficiaries of the acceptance and of the trustee's name, address, and telephone number."

   e. 813(b)(3) (duty to notify of trust existence and beneficiary rights):

      > "A trustee…within 60 days after the date the trustee acquires knowledge of the creation of an irrevocable trust, or the date the trustee acquires knowledge that a formerly revocable trust has become irrevocable, whether by the death of the settlor or otherwise, shall notify the qualified

beneficiaries of the trust's existence, of the identity of the settlor or settlors, of the right to request a copy of the trust instrument, and of the right to a trustee's report as provided in subsection (c)."

f. 813(b)(4) (duty to notify of change in compensation):

"A trustee…shall notify the qualified beneficiaries in advance of any change in the method or rate of the trustee's compensation."

g. 813(c) (duty to provide reports):

"A trustee shall send to the distributees or permissible distributees of trust income or principal, and to other qualified or nonqualified beneficiaries who request it, at least annually and at the termination of the trust, a report of the trust property, liabilities, receipts, and disbursements, including the source and amount of the trustee's compensation, a listing of the trust assets and, if feasible, their respective market values. Upon a vacancy in a trusteeship, unless a cotrustee remains in office, a report must be sent to the qualified beneficiaries by the former trustee. A personal representative, [conservator], or [guardian] may send the qualified beneficiaries a report on behalf of a deceased or incapacitated trustee."

4. Under UTC section 813(d), a beneficiary may (a) waive the right to any information under section 813, and (b) withdraw a waiver previously given.

5. Under UTC section 813(e), subsections 813(b)(2) (notice of acceptance of trusteeship) and 813(b)(3) (notice of trust existence and beneficiary rights to request) do not apply to a trustee who accepts a trusteeship before the date the UTC is enacted, to an irrevocable trust created before date of enactment, or to a revocable trust that becomes irrevocable before the date of enactment.

6. The NCCUSL commentary to section 813 is extensive, and reflects the controversy and ongoing policy debate concerning the duty to disclose:

"The duty to keep the beneficiaries reasonably informed of the administration of the trust is a fundamental duty of a trustee… this section limits the duty to keep the beneficiaries informed to the qualified beneficiaries...The result of this limitation is that the information need not be furnished to beneficiaries with remote remainder interests unless they have made a request to the trustee…

. . . Subsection (a) also requires that the trustee promptly respond to the request of any beneficiary, whether qualified or not, for information related to the administration of the trust. Performance is excused only if compliance is unreasonable under the circumstances. Within the bounds of the reasonableness limit, this provision allows the beneficiary to determine what information is relevant to protect the beneficiary's interest. Should a beneficiary so request, subsection (b)(1) also requires the trustee to furnish the beneficiary with a

complete copy of the trust instrument and not merely with those portions the trustee deems relevant to the beneficiary's interest …

To enable beneficiaries to protect their interests effectively, it is essential that they know the identity of the trustee. Subsection (b)(2) requires that a trustee inform the qualified beneficiaries within 60 days of the trustee's acceptance of office and of the trustee's name, address and telephone number. Similar to the obligation imposed on a personal representative following admission of the will to probate, subsection (b)(3) requires the trustee of a revocable trust to inform the qualified beneficiaries of the trust's existence within 60 days after the settlor's death. These two duties can overlap. If the death of the settlor happens also to be the occasion for the appointment of a successor trustee, the new trustee of the formerly revocable trust would need to inform the qualified beneficiaries both of the trustee's acceptance and of the trust's existence.

7. Default vs. Mandatory Rules. Section 105 of the NCCUSL version of the UTC provides that the most of the UTC are default rules in the absence of provisions in the governing instrument. Section 105 includes optional provisions for enacting jurisdictions as to whether the disclosure provisions of the UTC may be overridden by the terms of the governing instrument:

"(a) Except as otherwise provided in the terms of the trust, this [Code] governs the duties and powers of a trustee, relations among trustees, and the rights and interests of a beneficiary.

(b) The terms of a trust prevail over any provision of this [Code] except…

[(8) the duty under Section 813(b)(2) and (3) to notify qualified beneficiaries of an irrevocable trust who have attained 25 years of age of the existence of the trust, of the identity of the trustee, and of their right to request trustee's reports;]

[(9) the duty under Section 813(a) to respond to the request of a [qualified] beneficiary of an irrevocable trust for trustee's reports and other information reasonably related to the administration of a trust;]"

Delaware

§ 3303 Effect of provisions of instrument [For application of this section, see 79 Del. Laws, c. 172, § 79; Del. Laws, c. 352, § 6; 80 Del. Laws, c. 89, § 2]

(a) Notwithstanding any other provision of this Code or other law, the terms of a governing instrument may expand, restrict, eliminate, or otherwise vary any laws of general application to fiduciaries, trusts and trust administration, including, but not limited to, any such laws pertaining to:

(1) The rights and interests of beneficiaries, including, but not limited to, the right to be informed of the beneficiary's interest for a period of time, as set forth in subsection (c) of this section;

(2) The grounds for removal of a fiduciary;

(3) The circumstances, if any, in which the fiduciary must diversify investments; and

(4) A fiduciary's powers, duties, standard of care, rights of indemnification and liability to persons whose interests arise from that instrument;

provided, however, that nothing contained in this section shall be construed to permit the exculpation or indemnification of a fiduciary for the fiduciary's own wilful misconduct or preclude a court of competent jurisdiction from removing a fiduciary on account of the fiduciary's wilful misconduct. The rule that statutes in derogation of the common law are to be strictly construed shall have no application to this section. It is the policy of this section to give maximum effect to the principle of freedom of disposition and to the enforceability of governing instruments.

(c) The terms of a governing instrument may expand, restrict, eliminate, or otherwise vary the right of a beneficiary to be informed of the beneficiary's interest in a trust for a period of time, including but not limited to:

(1) A period of time related to the age of a beneficiary;

(2) A period of time related to the lifetime of each trustor and/or spouse of a trustor;

(3) A period of time related to a term of years or specific date; and/or

(4) A period of time related to a specific event that is certain to occur.

(d) During any period of time that a governing instrument restricts or eliminates the right of a beneficiary to be informed of the beneficiary's interest in a trust, unless otherwise provided in the governing instrument, any designated representative (as defined in § 3339 of this title) then serving shall represent and bind such beneficiary for purposes of any judicial proceeding and for purposes of any nonjudicial matter, and shall have the authority to, and is a proper party to, initiate a proceeding relating to the trust before a court or administrative tribunal on behalf of any such beneficiary.

(e) For purposes of this section, "judicial proceeding" means any proceeding before a court or administrative tribunal, including but not limited to, a proceeding that involves a trust whether or not the administration of the trust is governed by the laws of this State, and "nonjudicial matter" includes, but is not limited to, the grant of consents, releases or ratifications pursuant to § 3588 of this title and the receipt of a report for purposes of measuring the limitation period described in § 3585 of this title.

§ 3339 Designated representatives of trusts [For application of this section, see 80 Del. Laws, c. 89, § 2]

(a) For purposes of this title, the term "designated representative" means a person who is authorized to act as a designated representative in the manner described in at least 1 of the following paragraphs of this subsection (a) and who delivers to the trustee such person's written acceptance of the office of designated representative. A person who is authorized to act as a designated representative in the manner described in this subsection:

(1) Is expressly appointed under the terms of a governing instrument as a designated representative or by reference to this section;

(2) Is authorized or directed under the terms of a governing instrument to represent or bind 1 or more beneficiaries in connection with a judicial proceeding or nonjudicial matter, as those terms are defined in § 3303(e) of this title;

(3) Is a person appointed by 1 or more persons who are expressly authorized under a governing instrument to appoint a person who is described in paragraph (a)(1) or (2) of this section;

(4) Is a person appointed by a beneficiary to act as a designated representative of such beneficiary; and/or

(5) Is a person appointed by the trustor to act as designated representative for 1 or more beneficiaries.

(b) A designated representative shall be presumed to be a fiduciary.

South Dakota

55-2-13. Notice to qualified beneficiaries of existence of trust--Written directions--Information to be provided to excluded fiduciaries. Notification to any qualified beneficiary under this section may be carried out personally, by mail, postage prepaid, addressed to the entity or individual's last known post office address, or electronically pursuant to the provisions of § 15-6-5(d), and on representatives of qualified beneficiaries pursuant to chapter 55-18.

For purposes of this section, the term, qualified beneficiary, means a beneficiary that is an entity then in existence or an individual who is twenty-one years of age or older and who, on the date the beneficiary's qualification is determined:

(1) Is a distributee or permissible distributee of trust income or principal;

(2) Would be a distributee or permissible distributee of trust income or principal if the interests of the distributees terminated on that date; or

(3) Would be a distributee or permissible distributee of trust income or principal if the trust terminated on that date. However, if the distributee is then unknown because a person holds a power to change the distributee, the trustee shall give notice only to the holder of the power.

Except as otherwise provided by the terms of a revocable trust, a trustee has no duty to notify the qualified beneficiaries of the trust's existence.

Except as otherwise provided by the terms of an irrevocable trust or otherwise directed in writing by the settlor, trust advisor, or trust protector, the trustee shall, within sixty days after the trustee has accepted trusteeship of the trust, or within sixty days after the date the trustee acquires knowledge that a formerly revocable trust has become irrevocable, notify the qualified beneficiaries of the trust's existence and of the right of the beneficiary to request a copy of the trust instrument pertaining to the beneficiary's interest in the trust.

Except as otherwise provided by the terms of an irrevocable trust or otherwise directed in writing by the settlor, trust advisor, or trust protector, a trustee of an irrevocable trust:

(1) Upon request of a qualified beneficiary, shall promptly furnish to the qualified beneficiary a copy of the trust instrument;

(2) If notification of the trust has not been accomplished pursuant to this section within sixty days after accepting a trusteeship, shall notify the qualified beneficiaries of the acceptance and of the trustee's name, address, and telephone number;

(3) Shall promptly respond to a qualified beneficiary's request for information related to the administration of the trust, unless the request is unreasonable under the circumstances.

The settlor, trust advisor, or trust protector, may, by the terms of the governing instrument, or in writing delivered to the trustee, expand, restrict, eliminate, or otherwise modify the rights of beneficiaries to information relating to a trust.

Written directions provided by the settlor, trust advisor, or trust protector as set forth in this section remain in effect until and unless the settlor, trust advisor, or trust protector revokes the written instructions or is incapacitated. Additionally, the written directions remain in effect only while the trust advisor or trust protector providing the written directions is serving as the current trust advisor or trust protector. Unless otherwise specifically provided in the written directions, upon the death or incapacity of a settlor who provided the written directions described in this section, the directions shall be deemed revoked. However, upon the death or incapacity of the settlor, a trust advisor or trust protector, if any, may further direct the trustee in writing pursuant to this section. Unless otherwise stated in the governing instrument, in the event of a conflict in direction, the direction of the settlor shall control.

A beneficiary may waive the right to the notice or information otherwise required to be furnished under this section and, with respect to future reports and other information, may withdraw a waiver previously given.

The change in the identity of a trustee, occurring as the result of a mere name change or a merger, consolidation, combination, or reorganization of a trustee, does not require notice.

If a fiduciary is bound by a duty of confidentiality with respect to a trust or its assets, a fiduciary may require that any beneficiary who is eligible to receive information pursuant to this section be bound by the duty of confidentiality that binds the trustee before receiving such information from the trustee.

A trust advisor, trust protector, or other fiduciary designated by the terms of the trust shall keep each excluded fiduciary designated by the terms of the trust reasonably informed about:

(1) The administration of the trust with respect to any specific duty or function being performed by the trust advisor, trust protector, or other fiduciary to the extent that the duty or function would normally be performed by the excluded fiduciary or to the extent that providing such information to the excluded fiduciary is reasonably necessary for the excluded fiduciary to perform its duties; and

(2) Any other material information that the excluded fiduciary would be required to disclose to the qualified beneficiaries under this section regardless of whether the terms of the trust relieve the excluded fiduciary from providing such information to qualified beneficiaries. Neither the performance nor the failure to perform of a trust advisor, trust protector, or other fiduciary designated by the terms of the trust as provided in this subdivision shall affect the limitation on the liability of the excluded fiduciary.

The provisions of this section are effective for trusts created after June 30, 2002, except as otherwise directed by the settlor, trust protector, trust advisor, or other fiduciary designated by the terms of the trust. For trusts created before July 1, 2002, a trustee has no duty at common law or otherwise to notify a qualified beneficiary of the trust's existence unless otherwise directed by the settlor.

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