

## **Special Session IV-D**

### **How Much and When?**

### **A Panel Discussion on the Legal and Practical Considerations of the Exercise of Discretion**

#### ***Planning with Trusts Series***

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# HOW MUCH AND WHEN?

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# Substance Abuse

## FACTS:

- Charlie Spleen is the beneficiary of a trust created by his father which provides for mandatory income and discretionary principal if the trustee believes it is in his “best interests”.
- Lately, Charlie has been acting strange. He has ranted about having tiger blood and Adonis DNA. In the latest twist, he was recently picked up by the police, who found drugs in his car. Charlie denies that the drugs were his, claiming that they were left by an ex-girlfriend.
- The trustee is convinced that Charlie has a drug problem but has no actual medical proof.

## DISTRIBUTION STANDARD:

- Net income to Charlie. Principal as the trustee deems advisable for Charlie’s best interests.
- If my trustee reasonably believes that a beneficiary is abusing drugs or alcohol and that the resources of the trust, if distributed, would facilitate continued abuse, my trustee may establish a discretionary trust with all or any portion of the share which would otherwise be distributed to a beneficiary.

# Consideration of Other Resources

## FACTS:

- Mike Brady establishes a credit shelter trust for the benefit of his wife, Carol and two adult children, Greg and Peter.
- Carol makes annual requests to the trustee for all of the trust income to help cover her living expenses, and periodic requests for principal to reimburse her for amounts she provides to Greg and Peter for education expenses, auto insurance, and divorce-related expenses. Carol has modest other resources.
- Greg has a history of substance abuse, and refuses to seek full-time employment, because he thinks that his parents have a lifelong obligation to support him.

## DISTRIBUTION STANDARD:

- Net income to Carol, as the trustee deems advisable for her health, support and maintenance.
- Trustee can distribute to any one or more of Mike's children any of the net income not paid to Carol, as the trustee deems advisable for their health, support maintenance and education.
- Trust agreement authorizes, but does not require, the trustee to distribute principal to Carol and the children, if, in the trustee's sole and absolute discretion, it is needed for their health, support and maintenance.
- Trustee may, but need not, consider the beneficiaries' other resources, and has absolute discretion to exclude any or all of the beneficiaries, and to make unequal distributions among them.

# Beneficiary Circumstances and the Duty of Impartiality

## FACTS:

- \$2 million family trust for five adult siblings
- Beneficiary calls trust officer Friday afternoon
- Beneficiary is in jail and requests \$250 in bail so that he will not have to spend the weekend in jail

## DISTRIBUTION STANDARD:

- The trustee may pay so much or all of the income and principal of the Bypass Trust to and among my descendants from time to time living, in equal or unequal proportions, and at such times and in such manner, as the trustee deems necessary or advisable for their best interests, individually and as a group, considering the income of each of them from all sources known to the trustee.

# Hostility between Trustee and Beneficiaries

## FACTS:

- J. Howard Marcelle lived to the ripe old age of 98, leaving behind an estate worth \$10 million.
- At the age of 96, Howard married his private nurse, Anna Nicole Smythe, over the objection of his family. Anna was 66 years his junior.
- Howard's will left the bulk of his estate to a marital QTIP trust with Anna as the beneficiary during her lifetime. The remainder of his estate was left to his three children, who were each in their late 60s at the time of Howard's death. He named his son, Howard, Jr., as the sole trustee.
- The estate plan withstood a will contest much to the dismay of his children.
- You are now representing Howard, Jr. In your first conversation with Howard after the will contest, he says "I don't want to see that (&!^%\$) see a dime of my dad's estate. I promise you she is going to have to beg for every dollar."

## DISTRIBUTION STANDARD:

- Net income to Anna. Principal to Anna as the trustee deems advisable for her health, maintenance, and support in reasonable comfort.
- Trustee may, but need not, consider Anna's other resources.
- It is my intent that my trustee support Anna in her accustomed standard of living, and the trustee may exhaust the trust for her benefit during her lifetime.

# Distributions Related to a Personal Residence

## FACTS:

- George Jefferson establishes a testamentary trust for the benefit of his wife, Weezie, and George's descendants. George has one child, Lionel.
- One Weezie's death, the remaining trust property will be distributed to George's living issue, by right of representation.
- While George was living, he and Weezie had moved on up to a deluxe apartment in the sky, which they rented.
- Weezie requests a distribution that would allow her to purchase and furnish a new home in Brooklyn, so that she can live near Lionel and his children.

## DISTRIBUTION STANDARD:

- The trustee has sole and absolute discretion to distribute trust income and/or principal for the support and benefit of Weezie and any one or more of George's descendants, as the trustee deems desirable and in their best interests.
- Weezie is named as the "primary beneficiary" of the trust.

# Trust Funding Incompatible with Distribution Standard

## FACTS:

- \$14 million general power of appointment marital trust
- Surviving spouse and grantor led opulent lifestyle (multiple residences, extensive travel, art collection)

## DISTRIBUTION STANDARD:

- The trustee may pay to my wife such sums from principal as the trustee deems necessary to maintain her in her accustomed standard of living.



# Strangest Discretionary Requests

- Driver education training for a beneficiary who is legally blind
- \$1 Million to renovate a gentlemen's club
- Tuition expenses for circus/clown school



- Botox treatments
- Funds for loan repayment (felon owed to meth dealer)
- Bail money (beneficiary jailed for terrorist threats and kidnapping)
- Funds to prove paternity

# Keeping the Beneficiary on a Budget

## FACTS:

- Sally Spendthrift is the beneficiary of a marital QTIP Trust created by her deceased husband, Sam. The trust initially was funded with \$20M in liquid assets and residences in Florida, New York City, and South Hampton.
- At Sam's death, the carrying costs of the various properties were roughly \$450,000 a year. Sally insisted that none of them be sold.
- Sally's lifestyle was fairly extravagant. She was spending roughly \$100,000 per month on travel, club dues and plastic surgery at the time of Sam's death.
- After Sam's death, Big Bend Bank of Florida worked with Sally to come up with a budget. Big Bend requested information from Sally about her personal assets and had her provide a detailed analysis of her projected expenses. Big Bend and Sally agreed upon a budget of \$600,000 with distributions of \$50,000 per month. These distributions were in addition to the expenses of maintaining the residences.
- Five years have now passed since Sam's death. Volatility in the stock market and the distributions to Sally have depleted the liquid assets of the trust to \$13.5 million. Big Bend continues to make the previously budgeted and agreed upon distributions to Sally.

## DISTRIBUTION STANDARD:

- Net income to Sally. Principal as the trustee deems advisable for Sally's health, maintenance, and support in reasonable comfort.
- Trustee may, but need not, consider the beneficiaries' other resources.

# Distributions to Augment Surviving Spouse's Estate

## FACTS:

- Following Mr. Big's death, a trust, with a corporate trustee, is established for Mr. Big's wife, Carrie Bradshaw.
- In response to requests by Carrie, the trustee has begun to pay substantially increased amounts to her to enable her to accumulate funds from which she may assist Aiden, her child by a prior marriage, in his plans to obtain control and expand the activities of a furniture making company of which Alden has been an officer and shareholder for a number of years.
- On Carrie's death, the remaining trust property will pass to Mr. Big's descendants, who are not Carrie's descendants.

## DISTRIBUTION STANDARD:

- All income to Carrie.
- Principal to Carrie, in the trustee's sole and uncontrolled discretion, as the trustee believes appropriate for Carrie's comfortable support and care.

# Distributions to Facilitate Estate Planning

## FACTS:

- **\$26 million QTIP Marital Trust**
- **Recently funded - assets have high cost basis**
- **Trust assets will be included in her gross estate under IRC §2044 (b) (1) (A)**
- **Surviving spouse's attorney has proposed a large discretionary distribution to permit her to make gifts to the trust's remainder beneficiaries**
- **Surviving spouse has substantial separate property (marketable securities with low cost basis)**

## DISTRIBUTION STANDARD:

- **The trustee may distribute as much or all of the principal of the marital trust as it determines necessary for her best interests, considering her income and sources of support as it deems appropriate.**

# Creditor Problems

## FACTS:

- Donny Deepocketz lives a lavish lifestyle with multiple residences, yachts and fast cars.
- He is also a deadbeat dad. He owes his former spouse \$1,500,000 in back alimony and child support.
- He is completely supported by a \$20M trust established by his grandfather. Big Bend Bank serves as trustee.
- Big Bend makes frequent and regular distributions to Donny until Sally sues him to collect on the amounts due. Donny asks the Big Bend to begin paying his bills directly and to assist him in working out a plan to get him some cash until the lawsuit “goes away.”

## DISTRIBUTION STANDARD:

- Income and principal to or for the benefit of Donny as the trustee deems advisable for Donny’s best interests.

## SPENDTHRIFT PROVISION:

- No discretionary beneficiary of this trust, including but not limited to the settlor, shall have the power to anticipate, transfer, sell, assign or encumber any payment or distribution of either principal or income to be made under the provisions of this trust, and any anticipation, transfer, sale, assignment or encumbrance shall be void and of no effect whatsoever, and no distribution or payment shall be made by the trustee to any creditor, assignee, receiver, referee in bankruptcy, or trustee of any such discretionary beneficiary.

# Trustee's Duty to Act Reasonably

## FACTS:

- Following Uncle Phil's death, a trust is established for the benefit of his wife, Aunt Viv, and nephew, the Fresh Prince.
- The trustee thinks the Fresh Prince has a bad attitude and is a freeloader, having completely forgotten about his days of struggle on the playgrounds of West Philadelphia.
- As a matter of practice, the trustee refuses to consider any distribution requests from the Fresh Prince, even though Aunt Viv has significant resources of her own, and the trust estate is more than sufficient to meet all of Aunt Viv's needs and desires for her lifetime.

## DISTRIBUTION STANDARD:

- The trustee may distribute income and principal to Aunt Viv and the Fresh Prince, in the trustee's sole and absolute discretion.
- The trustee is authorized, but not required, to give primary consideration to Aunt Viv's needs and desires, and to give precedence to her needs and desires over those of the other current beneficiary and the remainder beneficiaries.

# Sustainability of Trust Distributions

## FACTS:

- \$150 million trust for one current beneficiary, one remainder beneficiary
- GST - Exempt
- Beneficiary is thrice divorced, married individual
- Beneficiary requests principal distributions to allow him to acquire custom-built yacht

## DISTRIBUTION STANDARD:

- The trustee shall pay to a beneficiary or use for his benefit so much or all of the income and principal of his trust as the trustee determines to be reasonably required, in addition to his other income from all sources known to the trustee, for his education and support in reasonable comfort.
- In addition the trustee may distribute to a beneficiary, for his use and benefit, any portion or all of the principal of his trust for his welfare or enjoyment...and the trustee need not consider the interests of any other beneficiary in doing so.

# Can a Trust Protector Save the Day?

## FACTS:

- Jack leaves the bulk of his estate in trust for his longtime spouse, Diane. He has three kids from a prior marriage. Diane is the trustee of the trust.
- Diane is using the trust in part to fund her small business where she designs and sell women's clothing. The kids do not like the principal invasions being made by Diane and file an action for an accounting.
- The trust contains a provision which authorizes that Diane, after Jack's death, to appoint a trust protector "to protect...the interests of the beneficiaries as the trust protector deems, in its sole and absolute discretion, to be in accordance with my intentions..." The trust protector is empowered to modify or amend the trust provisions to, inter alia: (1) "correct ambiguities that might otherwise require court construction"; or (2) "correct a drafting error that defeats my intent, as determined by the trust protector in its sole and absolute discretion..."
- After the lawsuit is filed, Diane appoints a trust protector who amends the trust to make it clear that the trustee is specifically authorized to make distributions to support Diane's clothing business.

## DISTRIBUTION STANDARD:

- Original language: Mandatory income. Principal as the trustee deems advisable for Diane's health, maintenance, support, and happiness.
- Modified language: Mandatory income. Principal as the trustee deems advisable for Diane's health, maintenance, support, and happiness. *The trustee is specifically authorized to make distributions to support Diane's clothing business.*



# Court's Interference with Trustee's Judgment

## FACTS:

- Adam Warlock's will establishes testamentary trusts for the benefit of his twin grandsons Rocket and Star-Lord, who are 19 years old.
- The grandsons' mother, Gamora Zen Whoberi Ben Titan, is the trustee of the trust.
- Each grandson has a 529 plan available to him.
- For the prior academic year, Star-Lord's college costs were fully paid by public benefits, and Rocket failed to complete the necessary applications for public college benefits and tuition assistance.
- Gamora refuses to exercise her discretion to pay for any of the college expenses of Rocket and Star-Lord, and also refuses to use trust funds to purchase an automobile for each of them.

## DISTRIBUTION STANDARD:

- The trustee must pay to or for the benefit of each grandson "so much of the net income and principal as the Trustee deems advisable in its sole discretion, not subject to judicial review, to provide for such grandson's maintenance, support, education, health and welfare, even to the point of exhausting the same."
- Trustee must distribute fractional distributions of principal and accumulated income when the beneficiaries reach the ages of 30, 32, and 35, at which time the trusts terminate.

# Balancing the Duty of Confidentiality and the Duty to Provide Information

## FACTS:

- \$45 million spray trust for three adult children
- **Beneficiary One:** Married parent of two children, starting non-profit, successful spouse
- **Beneficiary Two:** Married parent of one child, parenting full time, spouse is re-tooling
- **Beneficiary Three:** Single individual, running successful non-profit, limited income
- **Beneficiary One** requests trustee to cover all living expenses, to allow spouse to build up separate estate

## DISTRIBUTION STANDARD:

- The trustee may distribute principal to my children for their health, education, support and maintenance, after taking into account, to the extent of the trustee deems advisable, other income and financial resources reasonably available to such child.
- Any distributions to a child shall be charged, without interest, as advancements against the property set aside for that child on the termination of the trust.

# Trustee Hat vs. Parent Hat

## FACTS:

- Jack Arnold has one child, Kevin, who predeceases Jack.
- Jack dies shortly after Kevin. At the time, Kevin's surviving wife, Winnie, is living, as are Kevin and Winnie's minor children, Norma and Paul.
- Jack's trust provides that if Kevin isn't living at the time of Jack's death, Kevin's share of the remaining trust property will be held in a trust for the benefit of Kevin's children, until the youngest is 25. Winnie is the trustee of the children's trust.

## DISTRIBUTION STANDARD:

- The trustee may distribute trust income and principal to or for the benefit of Kevin's children as the trustee, in its sole and absolute discretion, determines, for the "health, support, maintenance, and education" of the children.
- The trust agreement is silent with respect to whether the trustee must consider the children's other resources in exercising its discretion.

# Limitations on the Trustee/Beneficiary

## FACTS:

- Following the untimely, tragic and unforgivable death of Dr. Derek Sheppard in a car accident, a trust is established for the benefit of his wife, Meredith Grey.
- Meredith is the sole trustee of the trust. Meredith is a busy surgeon, who knows nothing about managing money, accounting or fiduciary duties.
- The remainder beneficiaries are Derek's descendants, all of whom are issue by his prior marriage to Christina Yang.
- A few years after Derek's death, Derek's children challenge the extent of Meredith's principal invasion for her own benefit.

## DISTRIBUTION STANDARD:

- All income to Meredith.
- Principal to Meredith as the trustee, in its sole and absolute discretion, deems appropriate for Meredith's comfortable support.

# Distributions to Support Members of Beneficiary's Family

## FACTS:

- Upon Lonnie's death, a trust is created for the benefit of his wife, Joyce, and names Chief Hopper as trustee.
- Lonnie's intent in establishing the trust was to provide Joyce with her own money to spend, and to avoid taxes.
- Upon Joyce's death, half of the residue of the trust will be distributed to Lonnie's son, Will, and the other half will be distributed to Joyce's grandchildren in equal shares.
- When Joyce's grandchildren were minors, their parents were abducted into the Upside Down dimension, and have not been seen since. Joyce, through distributions from her trust, used 75% of the initial value of the trust assets for their graduate school education. Joyce also donated 10% of the value of the initial trust assets to the Hawkins National Laboratory, to fund research regarding the existence of parallel universes.

## DISTRIBUTION STANDARD:

- The trustee may principal to or for the benefit of Joyce for her health, support, or maintenance.