The Uniform Trust Code: A Continued Threat to SNTs, Even After Amendment

By Mark Merric, Douglas Stein, Carl Stevens, Eric Solem, Wayne Stewart and Mark Osborne

In Part One of this three-part series on special needs trusts under the Uniform Trust Code, Mark Merric, Douglas Stein, Carl Stevens, Eric Solem, Wayne Stewart and Mark Osborne continue the analysis of the effect of the U.T.C. on the historic common law interpretation of these trust vehicles as well as the tremendous drafting complications raised by these provisions.

An incredible number of positive comments regarding *The U.T.C.: A Threat to SNTs, The Uniform Trust Code*[1] have been received by its authors, Mark Merric and Doug Stein. As expected, there are differences of opinion voiced by some members of Uniform Trust Code (U.T.C.) committees.[2] Several U.T.C. committees have made modifications to the U.T.C. in an attempt to resolve some of the issues addressed in prior articles.[3] In fact, the National Conference of Commissioners on Uniform State Laws (NCCUSL) recently proposed changes that were finalized on February 18, 2005.[4] We are honored that many of changes made by NCCUSL's and state U.T.C. commissions attempt to resolve some of the issues that we raised. While these changes appear to be a step in the right direction, these modifications are simply insufficient to resolve the major problems created by the undefined "continuum of discretionary trusts."[5] The first part of this three-part article expands on two primary issues discussed in the first article: (1) the two-step process necessary to eliminate third-party special needs trusts (SNTs),[6] and (2) the availability of third-party SNT assets to governmental agencies thus rendering them ineligible for Medicaid and/or state governmental benefits. The second and third parts will review the limited effectiveness of various solutions proposed by various state U.T.C. committees and the NCCUSL, will explore related asset protection deficiencies and will ultimately conclude that Article 5 and §814(a) should be rewritten in their entirety.

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Background

Introduction and implementation of the U.T.C. has thus far proved to be more controversial than the Uniform Probate Code when it was first introduced. The controversy is exacerbated by the U.T.C.'s

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proclamation that the Restatement (Third) of Trusts ("Restatement Third") is the interpretive guide to the U.T.C.[7] Unlike preceding Restatements of Trusts, the Restatement Third adopts numerous minority positions, and occasionally even creates new law. The result is that in many well settled areas of trust law, the U.T.C. is not founded on the judicial wisdom of the majority of states refined over hundreds of years. Indeed, in some major areas, the U.T.C. and the Restatement Third are founded on shaky ground, which, at times, reflects nothing more than the U.T.C. drafting committee's opinion of what they would like the law to be. It is the authors' contention that this new view of trust law is ill-conceived. Further, in many areas, it is easer to draft a new trust code than to fix the sinking ship. As an analogy, the U.T.C. might be viewed as the Titanic—on the surface it appears solid and is touted as the greatest ship ever built. However, after scratching the surface, it is apparent that there are major holes in the underlying assumptions that it was built on. In this sense, cosmetic changes to patch these holes, no matter how well conceived, provide little help to save the sinking ship.

Key Areas of Disagreement

In this continuing debate, some proponents of the U.T.C. have misstated the concerns of others, relied on minority opinions as the current state of the law, and, at times, inaccurately cite cases to support their views. The following is a list of the key areas of disagreement[8]:

I. Proponents claim the state or federal government could eliminate SNTs with one act, and therefore, the "one big step–one little step" concern proposed by those wishing to retain the common law is irrelevant.

II. Proponents further claim that those who wish to retain the common law are concerned about the elimination of the "support trust."[9] The real issue is that the U.T.C. redefines the discretionary trust to be nothing more than a support trust under common law, thereby significantly weakening the asset protection of a common law discretionary trust.

III. Proponents claim that the U.T.C. does not codify a distinctly minority line of discretionary-support trust cases, sometimes referred to as the *Kreitzer* line of cases. However, the proponents then fail to provide any analysis of why it does not codify the available resource issue.

IV. Proponents claim that the critics do not understand the difference between the U.T.C. and the Restatement Third. As an extension of this, Proponents argue the U.T.C. reverses the distinctly minority opinion discretionary-support trust cases as related to distributions, rather than codifies it.

V. Without citing any authority, some proponents misstate the law and claim that Medicaid is not a creditor of a Medicaid applicant. This position lacks legal support. [10] This section as well as sections VI and VII will be discussed in Part 2 of this article.

VI. Proponents of the U.T.C. claim that allowing an exception creditor to attach at the trust level is not a reduction in the common law asset protection afforded many trusts. Proponents of the common law, however, point out, that the combination of the future addition of a governmental agency as a newly designated exception creditor and the trustee's inability to directly pay for a SNT beneficiary's expenses undermines the purpose of creating an SNT.

VII. Proponents claim that, under common law, an exception creditor may attach all present and future distributions at the trust level. While an accurate depiction of the law in a small number of states, this is contrary to the view of the vast majority of states.

I. The One Big Step–One Little Step Approach

The elimination of the discretionary-support dichotomy is the first, and by far the most significant, step of a two-step process that is necessary to eliminate third-party SNTs. The first step is adoption of the newly created "continuum of discretionary trusts" created by the U.T.C. and Restatement Third. The continuum involves a massive rewrite of American trust law by abolishing the discretionary-support distinction.[11] The second step is the enactment of legislation which makes states exception creditors ("exception creditor legislation").

Proponents of the U.T.C. dismiss the two-step approach as irrelevant, arguing, even without the adoption of the U.T.C., states and the federal government can make themselves exception creditors. This argument misses the mark. At common law, a discretionary SNT[12] relies on the inability of the beneficiary to force a distribution, because the beneficiary lacks

an enforceable right or a property interest.[13] This is the heart of the discretionary-support distinction. Since the common law SNT is a discretionary trust, the beneficiary does not have an available resource for a creditor to attach.[14] As discussed in our prior articles, however, the simple enactment of exception creditor legislation is insufficient because, under the newly created continuum of discretionary trusts, the beneficiaries of an SNT may have the ability to force a distribution, in an amount determined only by the court, pursuant to a distinctly minority line of discretionary support trust cases, sometimes referred to as the *Kreitzer*[15] line of cases.

Proponents of the U.T.C. also dismiss the two-step approach argument as irrelevant, because the federal government can pass a comprehensive amendment accomplishing both steps in one act. They contend that federal law automatically preempts state law. With this argument, the proponents of the U.T.C. have accepted a broadening of the authority of the federal government, which is not justified as a matter of policy and may well involve constitutional issues regarding due process, states' rights and impairment of contract, particularly since these provisions are made retroactive.[16] The U.T.C. concedes this undue expansion of power of the federal government in the official comments to U.T.C. §503(c) that states that "federal preemption guarantees that certain federal claims, such as claims by the Internal Revenue Service, may bypass a spendthrift provision no matter what this code might say." Under common law, a discretionary interest in trust is not a property interest under state law. Therefore federal preemption has not been applicable with respect to discretionary trusts.[17] Absent the U.T.C. creating a property interest in almost all, if not all, discretionary trust interests, not even the IRS with its expansive powers has been able to force a distribution from any common law discretionary trust.[18] After the U.T.C. concedes the Constitutional issues to the federal government, all that the federal government needs to do is make reference in any statute that it is an exception creditor under the U.T.C.

Even if the federal government could overcome the Constitutional and property interest issues under state law with one act, there are nonlegal practical issues involved. It is believed that a one-step approach where the federal government redefines a discretionary trust to be a property interest and then allows attachment and possibly judicial foreclosure of beneficial interests is highly unlikely to occur. Such a sweeping change in common law protection of the poor would not go unnoticed. Lobby groups, bar associations and handicapped persons would strongly oppose such legislation. In addition, an overhaul of established trust law is unprecedented. In sum this third point appears to be an area where opinion, not legal analysis, is the source of disagreement with some proponents of the U.T.C.

II. U.T.C. Redefines the Term "Discretionary Trust" to Be Subject to the Remedies of a Support Trust

Some U.T.C. proponents misstate the points of those expressing concerns when these U.T.C. proponents claim that opponents are concerned about the elimination of the support trust.[19] The real issue is that the U.T.C. eliminates the benefits of a common law discretionary trust by redefining it so that it resembles a support trust. Under the common law of the majority of states, a beneficiary of a discretionary trust had no right to force a distribution because of the high standard of judicial review. A judge could review the trustee's distribution decisions if the trustee (1) acted with an improper motive; (2) acted dishonestly; or (3) failed to act.[20] In essence, the beneficiary possessed no enforceable right to demand a distribution, holds only a mere expectancy,[21] and the interest is not considered a property interest.[22] There is no "good faith" or "reasonableness" standard of review for which a beneficiary could seek the aid of a court in forcing a distribution. In this respect, the U.T.C. eliminates the cornerstone of asset protection upon which the discretionary trust rests by abolishing the discretionary-support dichotomy and giving the beneficiary an enforceable right to demand a distribution. This is accomplished by having all trusts rest somewhere on the newly created continuum of discretionary trusts and subjecting all trusts to a good faith standard of judicial review. In this respect, the U.T.C.'s new definition of the term "discretionary trust" is a misnomer.

Some U.T.C. states have recognized this issue. For example, Ohio proposed U.T.C. §5801.03(24) which is a wholly discretionary trust (WDT) that makes a poor attempt at keeping the common law distinction of a discretionary-support trust. Further, both North Carolina and South Carolina U.T.C. committees rejected the continuum of discretionary trust.[23] Finally, Kansas and Oregon have omitted U.T.C.

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§504 in an attempt to retain the discretionary-support distinction. These state approaches, and why these approaches fall considerably short of the benefits currently under common law are discussed in detail in Part 3 of this article.

III. *Kreitzer* and the Discretionary Support Trust Line of Cases

When courts waver from the common law and hold that a beneficiary has an enforceable right to a distribution, both in the SNT context and in the divorce context,[24] beneficiaries meet with disastrous consequences. The result in the SNT context was that the beneficiary had an "available resource," and governmental benefits were either denied or the government recovered from the trust.[25] For example, in *Lackmann Est.*, the court found that a discretionary third-party SNT must distribute funds to the state to pay for the ward's care.[26] The court held that even though the trustee had the absolute and sole discretion to expend trust property for the proper care, support and maintenance of beneficiary, the court held the assets were available because the trustee's discretionary distribution power was limited by a "reasonableness standard."

Although this case has since been distinguished on its facts,[27] *Lackmann* remains good law. The California courts do not deny that the trustee must act reasonably but rather have tortured the law in an effort to obtain a more "just" result. For example, in *Hinckley*[28] and *Johnson*[29] the court held that because the grantor of the trust was a sister and not the ward's parent, the trust assets were protected. In point of fact, *Lackmann* may become the rationale of choice if the U.T.C. is adopted in its current form with §814(a) intact.

A. Changing the Standard of Review to an Enforceable Right or Property Interest

As noted above, under common law, a court could interfere with the trustee's "sole and absolute" discretion if the trustee abused his or her discretion by (1) acting dishonestly, (2) acting with an improper motive, or (3) failing to use his or her judgment.[30] A beneficiary had little, if any, standing to sue for a distribution or question the amount of a distribution, unless the beneficiary could prove one of the above factors. In almost all states, there was no reasonableness or good faith standard for a discretionary trust that used qualifying adjectives of the trustee's "absolute," "unlimited" or "uncontrolled" discretion.[31] Therefore, the beneficiary had an extremely high burden and virtually no enforceable right (*i.e.,* property interest).

The lack of an enforceable right is the cornerstone of the asset protection afforded by discretionary trusts. The principle is simple: "The beneficiary cannot obtain the assistance of the court to control the exercise of the trustee's discretion except to prevent an abuse by the trustee of his discretionary power. ..."[32] As a result, a creditor cannot compel the trustee to pay either a creditor or the beneficiary anything because the beneficiary cannot compel payment.[33] This is the difference, at common law, for the asset protection between a support trust and a discretionary trust. Unlike a discretionary trust, a support trust has a reasonableness judicial standard of review,[34] and a beneficiary can force a distribution pursuant to the standard. Further, a support trust relies on spendthrift protection, while a discretionary trust does not need to rely on spendthrift protection, even though spendthrift provisions are almost always included in such trusts.[35]

B. Erosion of Discretionary Trusts in Less Than a Handful of States

Discretionary trusts have withstood the test of time, and there has been little erosion of the protection they afford. However, the Ohio courts, beginning with *Krietzer,*[36] were the first courts to erode the protection provided by a discretionary trust. In *Kreitzer*, the Ohio Supreme Court held that a destitute beneficiary held an enforceable right to a distribution when a discretionary trust was coupled with any standard, regardless of whether or not the standard was capable of judicial interpretation. Once the beneficiary held the enforceable right to a distribution, the beneficiary had an "available resource," and, to the extent of the enforceable right, the governmental agency, as an exception creditor, could force a distribution in satisfaction of its claim. In the 1990s, Iowa and Pennsylvania, employing a slightly different analysis, followed Ohio's *Kreitzer* line of cases and held that when a discretionary trust is coupled with a standard, the beneficiary has an enforceable right to a distribution thus creating an available resource.[37] For purposes of this article, this distinctly minority line of cases is referred to as the "minority line of discretionary-support trust cases."

C. Creating an Available Resource

Proponents claim the minority line of discretionary-support trust cases will be overturned by the U.T.C. However, they confuse the issues of forcing a distribution and when a trust is an available resource.[38] There are two issues that must be addressed when discussing the minority line of discretionary-support trust cases[39]: (1) whether there an available resource; and (2) whether the governmental creditor may force a distribution in satisfaction of its claim. For any one of the following seven reasons, the authors believe the U.T.C. codifies the aberrational results found in Ohio, Iowa and, to a lesser extent, Pennsylvania, and forces the assets of an SNT, which does not include specific special needs language, to be an available resource:

1. The U.T.C. changes the judicial standard of review for a discretionary trust from the trustee (1) acting with an improper motive; (2) acting dishonestly; or (3) failing to act to a review standard of good faith.
2. The U.T.C. provides a beneficiary with the ability to force a distribution from a discretionary trust because of a change in the judicial review standard.
3. The U.T.C. allows an estranged spouse to force a distribution from a discretionary trust to satisfy a claim for child support or alimony.
4. The U.T.C. adopts the new undefined theory of a "continuum of discretionary trusts."
5. The U.T.C. references an article citing the reason for abolishing the discretionary-support distinction and this article states that a beneficiary of a discretionary trust may force a minimal distribution.
6. The U.T.C. looks to the Restatement Third for interpretation.
7. Recognition of the issue in the final amendments to the official comment under §814

U.T.C. proponents only attempt to address the "good faith" standard of review issue.[40] They provide no analysis regarding the other reasons why the U.T.C. has most likely created an enforceable right in almost all discretionary trust beneficiaries. Finally, on February 28, 2005, when NCCUSL issued its final 2004–2005 amendments, it attempted to plug the gaping holes with a mere comment but no significant change to the statutory language.

1. The U.T.C. "Good Faith" Standard of Judicial Review. Some proponents of the U.T.C. again misstate the position of those expressing concerns position when they claim the argument is that "good faith" and "bad faith" are synonymous. Under the U.T.C., the issue is where does the bright line rest? So planners may safely navigate the waters and draft trusts to achieve their clients' goals. What is the magical language that a planner should use to avoid the creation of an enforceable right? The proponents of the U.T.C. consistently fail to address this question.

In contrast, under the discretionary-support dichotomy, when the judicial standard of review is the trustee (1) acting dishonestly; (2) acting with an improper motive; or (3) failing to act, the courts have held that the beneficiary does not have an enforceable right thus, no available resource. So no one would misinterpret our article and then proceed to misstate our position like the proponents of the U.T.C. did[41]; in the two articles the proponents were criticizing, we specifically stated and continue to maintain that "courts define the term "bad faith" slightly differently and we used the above standard as our definition."[42] The reason we need to define "bad faith" is because courts use the term "good faith" and "bad faith" loosely. For example, Black's Law Dictionary (6th ed.) defines "good faith" as:

> an intangible and abstract quality with no technical meaning or statutory definition and it encompasses, among other things, an honest belief, the absence of malice and the absence of design to defraud or seek an unconscionable advantage, an individual's personal good faith is concept of his own mind and inner spirit and, therefore, may not conclusively be determined by his prostrations alone.[43]

Naturally, the above definition stressing no "technical meaning or statutory definition" leaves wide latitude for reasonable persons to disagree. In the SNT context, this becomes a major concern, because drafters must be certain not to create an enforceable right in a beneficiary that will be deemed an available resource. Further, drafting a discretionary dynasty trust to protect wealth or to protect an inheritance from an estranged spouse certainty is vital.[44] The issue is not whether "good faith" is synonymous with "bad faith" but rather whether courts use the nebulous definition of "good faith" to create an available resource in the SNT context or allow recovery by an exception creditor.[45] Rather than deal with the somewhat elusive or arbitrary definitions of "good faith" or "bad faith," both the first and second Restatement of Trusts defined

the judicial review standard for a discretionary trust with reference to specific actions or inactions of a trustee—the trustee (1) acts dishonestly; (2) acts with an improper motive; or (3) fails to act.[46]

When courts used the term "good faith" as the standard of judicial review, the nebulous standard resulted in some discretionary trusts becoming available resources, thereby allowing a governmental creditor to force a distribution.[47] The same does not appear to have happened when only the term "bad faith" was used by the court.[48] However, if the court used the terms "good faith" and "bad faith" synonymously, the result is often uncertain.[49] On the other hand, when courts use the standard judicial review standard of only (1) improper motive; (2) dishonesty; or (3) failure to act as defined in *Scotts* or *Boggerts*, it does not appear that trust assets are available to the beneficiary's creditors.[50] There is a "bright line" where the courts hold that a beneficiary does not have either (1) an enforceable right, or (2) a property interest. Therefore, the beneficiary of an SNT does not have an available resource under this common law definition when this judicial review standard is adopted.

There is extreme uncertainty in codifying trust law. The rules of statutory construction require that each word has meaning. Even the drafters of the U.T.C. are inconsistent in the use of the terms "good faith" and "bad faith." If the drafters meant for the terms to be synonymous, why did they use "good faith" under §§105(b)(1), 801, 814(a) and 1012 and the term "bad faith" under §§1002(b) and 1008(a)(1). Further, in some parts of the U.T.C., the term "good faith" refers to specific actions.[51] In other parts, the U.T.C. references to other bodies of law for a definition of "good faith."[52] Unfortunately, the use of the terms "good faith" and "bad faith" within the U.T.C. itself confirms BLACK'S LAW DICTIONARY's nebulous definition and our concern that a judge may interpret this term in almost any way he or she chooses.

The authors are not alone in expressing concerns when using a "good faith" standard of review. North Carolina has substituted the word "bad faith" as the review standard for all trusts.[53] Ohio, in its definition of a wholly discretionary trust, defines the review standard as the trustee (1) acting dishonestly; (2) acting with an improper purposes; (3) failing to act; or (4) acting in bad faith.[54] After over four years of study, the Colorado Uniform Trust Code committee concluded its official comments to the U.T.C. Part of the comment under §504 reads:

> Colorado courts have followed the *Restatement (Second)* position with respect to discretionary trusts. Our courts have held that neither the beneficiary nor a creditor of a beneficiary can compel exercise of discretion and that the interest of the beneficiary in a discretionary trust is not "property" but rather, a "mere expectancy. ... *This section [referring to U.T.C. Section 504] may be seen as an overruling of the Colorado Supreme Court in Jones, supra.* However, the Jones case left open the possiblility of interference if the trustee acts dishonestly, from an improper motive, or fails to use his judgment.[55]

Richard Covey and Dan Hastings[56] in PRACTICAL DRAFTING discussed the problem of the U.T.C. adopting this judicial standard of review, particularly as qualified by the words "in accordance with the terms and purposes of the trust and the interests of the beneficiaries." Their analysis in the October 2003 issue of PRACTICAL DRAFTING is quoted below, and their interpretive comments are italicized:

> Section 814(a) provides:
>
> Notwithstanding the breadth of discretion granted to a trustee in the terms of the trust, including the use of such terms as "absolute", "sole", or "uncontrolled", the 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.
>
> *Traditionally, the words "absolute" and "uncontrolled," absent an accompanying standard that would limit their effect, have been regarded as sufficient to dispense with a "reasonable man" test in evaluating a trustee's conduct, while preserving the requirement of good faith:*
>
> *Citing Scott on Trusts (Fratcher ed.) §187:*
>
> The extent of the discretion may be enlarged by the use of qualifying adjectives or phrases such as "absolute" or "uncontrolled." Even the use of such terms, however, does not give him unlimited discretion. A good deal depends upon whether there is any standard by which the trustee's conduct can be judged. Thus if he is directed to pay as much of the income and principal as is necessary for the support of a beneficiary, he can be

compelled to pay at least the minimum amount which in the opinion of a reasonable man would be necessary. If, on the other hand, he is to pay a part of the principal to a beneficiary entitled to the income, if in his discretion he should deem it wise, the trustee's decision would normally be final, although as will be seen the court will control his action where he acts in bad faith. The real question is whether it appears that the trustee is acting in that state of mind in which it was contemplated by the settlor that he should act. …

Section 814(a) illustrates the uncertainty that codifying the trust law may create. What do the words "and in accordance with the terms and purposes of the trust and the interests of the beneficiaries" mean? Do they create a stricter limit on the discretion that may be conferred upon a trustee than the common law test set forth in the above quotation from Scott? It seems likely that courts will use them to do so in particular cases, yet their application to particular facts remains as hard to predict as that of the common law. Has anything been gained by codification?[57]

In the April 2004 issue of PRACTICAL DRAFTING, Richard Covey and Dan Hastings again explained their conclusion regarding U.T.C. §814(a):

... we discussed Section 814(a), which provides that "[n]otwithstanding 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 trusts and the interests of the beneficiaries." We noted that the words following "good faith" arguably represent a tightening of the traditional formulation of the common law rule, and give the courts a new tool, of uncertain scope,[58] *with which to control trustee discretion.*[59]

We agree with Richard Covey and Dan Hastings that the words following "good faith" arguably give the court "a new tool, of uncertain scope, with which to control trustee discretion."[60] For example, the clause "in accordance with the terms and purposes of the trust and the interests of the beneficiaries" has little, if any, meaning. We also note that this problem is further magnified by the Iowa, Ohio, Connecticut and Pennsylvania cases.[61] A judge need not interpret the term "good faith" as reducing the discretionary trust threshold to that of "reasonableness" to create an available resource. Rather a judge need only find that the standard of review is something slightly less than the discretionary trust common law standard. This may result in the minority discretionary-support line of cases being a national problem instead of a localized one.

Due to the several factors that are involved in defining a discretionary trust, there are no cosmetic or simple solutions to fix this problem.[62] When discretionary-support distinction is arbitrarily eliminated, the statutory interpretation of over 100 years of case law is lost. As will be discussed in detail in Parts 2 and 3, oceans of ink need to be spilled to fix Article V and §814(a) in order to make it safe for planners create trusts.

2. Statutory Right That the Beneficiary Has a Right to Force a Distribution. U.T.C. §504, titled "discretionary trusts," appears to grant a beneficiary an enforceable right to a distribution. Under the "continuum of discretionary trust theory" all trusts are classified as discretionary thus, this section applies to all trusts.

U.T.C. §504(d) states:

This section does not limit the right of a beneficiary to maintain a judicial proceeding against a trustee for an abuse of discretion or failure to comply with a standard for distribution.

In this respect, the entirety of U.T.C. §504 directly conflicts with the common law definition of a discretionary trust, because under common law, a discretionary beneficiary does not have a right to force a distribution and holds nothing more than a mere expectancy. This may explain why Kansas deleted both §§503 and 504[63] and Oregon deleted §504 in an attempt to preserve common law discretionary trusts. If an SNT beneficiary has an enforceable right to a minimal distribution from a trust, such right will create an available resource and disqualify the SNT beneficiary from receiving governmental benefits.

3. Maintenance and Child Support Exception Is in Direct Conflict of Whether a Beneficiary Has an Enforceable Right. After the problems associated with U.T.C. §§814 and 504(d) were exposed, some proponents of the U.T.C. argued that §814(a) does not change the common law.[64] However, in direct conflict with this newly presented interpretation of the U.T.C.,

the proponents admit that an estranged spouse may force a distribution from a discretionary trust for child support or alimony. U.T.C. §504(c) reads:

> To the extent a trustee has not complied with a standard of distribution or has abused a discretion:
>
> 1) a distribution may be ordered by the court to satisfy a judgment or court order against the beneficiary for support or maintenance of the beneficiary's child, spouse, or former spouse; and
>
> 2) the court shall direct the trustee to pay to the child, spouse, or former spouse such amount as is equitable under the circumstances but not more than the amount the trustee would have been required to distribute to or for the benefit of the beneficiary had the trustee complied with the standard or not abused the discretion.

The statute and the U.T.C. proponents' statements appear to be contradictory. Under common law, a beneficiary of a discretionary trust could not force a distribution, because the beneficiary had no enforceable right and possessed a mere expectancy. Therefore, it was impossible for any exception creditor or the beneficiary to force a distribution. If the U.T.C. has not changed the beneficiary's rights to a distribution, then what is the underlying rational to permit an estranged spouse standing in the shoes of the beneficiary to force a distribution under U.T.C. §504(c)?

While the statute is clear on this point, the underlying rationale is vital when a court interprets the law. Simply stated, by changing the common law definition of a discretionary trust, the U.T.C. has modified the distribution standard for a discretionary trust and created an enforceable right. A court appears left with a paradox. If a beneficiary has an enforceable right for child support and alimony, is such a right also an available resource? The South Carolina U.T.C. committee recognized the internal conflict between the common law definition of a discretionary trust, and it attempted to carve out an exception for SNTs. Unfortunately, the underlying rationale for creating an exception for child and spousal support defeats the argument that the assets of a third-party SNT are not an available resource.

4. Adopting the Undefined Continuum of Discretionary Trusts. Further supporting the position that the U.T.C. has lowered the judicial standard of review for a discretionary trust and created a right for a beneficiary to force a distribution from a discretionary trust is the U.T.C.'s adoption of the undefined "continuum of discretionary trusts." Nowhere in the U.T.C. comments or in the RESTATEMENT THIRD is the continuum defined. The contours remain amorphous and the specific words necessary to create the type of trust a grantor wants remain uncertain. Is a discretionary trust with standards (either positive or negative) still a mere expectancy? How about a discretionary trust authorizing distributions for the beneficiary's health, education, support, maintenance, comfort, general welfare, happiness and joy? What about a discretionary trust with no standards? Is it safe? The RESTATEMENT THIRD greatly changes common law to the detriment of estate planning and special needs trusts. The U.T.C. does not specially address the issue. Rather, it appears to leans heavily in favor of adopting the RESTATEMENT THIRD's new position in law due to its specific references to the RESTATEMENT THIRD.[65] The numerous pitfalls created by eliminating the "bright line" common law test and replacing it with an undefined "facts and circumstances" test is beyond troubling. Certainty in result is vital to effectuating the grantor's intent.

5. Reference to a 1961 COLUMBIA LAW REVIEW Article. Since 1961, the Reporter for the RESTATEMENT (THIRD) OF TRUSTS has strongly disagreed with over 100 years of judicial wisdom regarding the discretionary-support dichotomy.[66] This law review article takes the position that the average estate planning attorney does not know whether or not he or she wished to create an enforceable right in a beneficiary when drafting a discretionary trust. Therefore, as the rule, not the exception, the Reporter assumes estate planners mistakenly draft discretionary trusts when they actually want the beneficiary to have an enforceable right or in essence a support trust. For this reason, the Reporter argues that when standards or guidelines are included in a discretionary trust, the RESTATEMENT SECOND's position that the terms "sole and absolute" discretion dispense with the standard of reasonableness should not be followed. Rather, a beneficiary should always have a right to at least a minimal distribution[67] and the amount of such distribution should be determined on a continuum of discretionary trusts. When interpreting the "good faith" standard for reviewing a trustee's discretion, the official comment under U.T.C. §814(a) specifically refers to this article. The comment also specifically references §50 of the RESTATEMENT THIRD, which also supports this minimal distribution view. So by reference, again it appears the U.T.C. has adopted

a position that creates a minimal distribution, if not more, in any trust that has a standard and possibly those that do not.

In over 44 years since this law review article was published, only four appellate cases cited it.[68] The last case cited was in 1973. Only one, or possibly two, case(s) appears to adopt the position of the article, which is a bright line test should not be used. In this respect, it is highly questionable whether the "continuum of discretionary trusts" is, as the proponents self-proclaim, "the modern theory" of creditor recovery or just a theory rejected by almost every appellate court.

6. Using the Restatement Third for Interpretation. The problems of the undefined continuum of discretionary trusts are exacerbated by using the Restatement Third as the handbook for interpreting the U.T.C. and possibly as a surrogate for substantive law.[69] The U.T.C. specifically abolishes the discretionary support dichotomy.[70] If a grantor's intention cannot be determined from the four corners of the trust, then there is no certainty regarding the interpretation of a trust under the U.T.C. Does this mean that all trusts must seek guidance from a court to determine where they lie on the continuum of discretionary trusts?

Under the Restatement Third, the answer appears to be a resounding "yes." The Restatement Third finds drawing bright lines between a discretionary and support trust to be "counterproductive, elusive (and a artificial) distinction."[71] It also describes any attempts to draw bright lines as "artificial and arbitrary and costly to society."[72] Therefore, the Restatement Third provides little, if any guidance, if it is possible to create a discretionary trust where a beneficiary would not have an enforceable right to a distribution.[73] Instead, the Restatement Third of Trusts requires costly litigation under an undefined "facts and circumstances" test.

Does this mean that all SNTs under the Restatement Third that do not have special needs or luxury language must now go to court? Again, the answer appears to be a resounding "yes." Does this mean that SNTs without any support standard are safe? There is no guaranty of this under the Restatement Third; in fact, the opposite may well be the case.[74] Is an SNT that has been drafted as a discretionary trust with a standard safe under the Restatement Third? The answer appears to be almost a definite "no," based on the Reporter comments and the Columbia Law Review article cited above. Does the U.T.C. change any of this? The answer to this question will be discussed in detail in Parts 2 and 3.

7. Recognition of the Issue in the Final Changes Issued February 18, 2005. First, while some proponents of the U.T.C. deny that any available resource issue existed under the U.T.C.,[75] the February 18, 2005, amendment to the official comments under §504 appears to acknowledge that, as originally drafted, there is, in fact, an available resource issue. Sadly, due to the magnitude of this apparent oversight, the proposed NCCUSL's fix remains ineffective and does not protect the vulnerable population who look to Medicaid to provide their necessary medical care.

Second, the February 18, 2005, NCCUSL amendment confirms our analysis of the nebulous use of the term "good faith" issue discussed above. In the comment to U.T.C. §814, the U.T.C. commentator notes by citations to *Scott* and the *In Re Ferrall's Estate* that the term "good faith" is used differently, depending on the context. However, rather than address the issue head on, the U.T.C. attempts to evade the question by adding the following comment: "Subsection (a) does not otherwise address the obligations of a trustee to make distributions, leaving that issue to case law."[76]

Third, this statement directly conflicts with the comments under §504 of the U.T.C. that states the discretionary-support dichotomy has been eliminated. Since the discretionary-support dichotomy has been eliminated, consequentially does this mean as a consequence that all case law that depended upon it is overturned? Alternatively, to what extent has each case been changed? The Uniform Trust Code provides virtually no answers to these questions.

Fourth, the amendments to the §814 comments are also internally inconsistent. Immediately after stating that distributions are left to case law, the amended comment then uses the newly created Restatement Third tests to determine the obligation of a trustee to make distributions. The comment states: "Under these standards, whether a trustee has a duty to make a distribution in a given situation to make a distribution depends on the exact language used, whether the standard grants discretion and its breadth, whether this discretion is coupled with a standard, whether the beneficiary has other available resources, and, more broadly, the overriding purposes of the trust." Regrettably, by this amended comment, the U.T.C. adopts the fundamental problem with the Restatement Third. Prior to the U.T.C. and the Restatement Third, estate planners within each state knew where the bright-line of "safe drafting" was so they could assure that they would not create an "enforceable" right. By admission in the amended comment, the U.T.C. replaces the

"bright-line" with a facts-and-circumstances test that is extremely amorphous. Within each state, there will be many inconsistent decisions based on relatively the same set of facts. There will also be many more inconsistent decisions between states. These inconsistent decisions must be reconciled. As mentioned in a previous article, "the proverbial yellow brick road is fragmented and crumbling. A future wave of litigation is required to define the contours of the U.T.C.'s new spectrum. In the interim, uncertainty and conflicting results will be the norm."[77]

Naturally, the question arises, has anything been accomplished by this NCCUSL amendment other than to note that there were, and most likely continues to be, many major flaws with the untested and newly created continuum of discretionary trusts? This issue will be more fully developed in Parts 2 and 3 of this article.

D. Synthesis

Any one of the following factors alone could easily result in a court holding that judicial review standard of a discretionary trust has created an enforceable right (*i.e.,* an available resource) under the U.T.C.: (1) the lowering of the judicial standard of review for a discretionary trust to "good faith," (2) the enforceable right under U.T.C. §504(d) of a beneficiary to demand a distribution, (3) the ability of an estranged spouse to force a distribution from a discretionary trust, (4) the adoption of the undefined continuum of discretionary trusts, (5) the reference to the 1961 COLUMBIA LAW REVIEW article as authority, (6) or the lack of guidance on how to interpret grantor's intent under the RESTATEMENT THIRD. However, all six of the above factors combined leave little question that most, if not all, beneficiaries of discretionary trusts have an enforceable right to force a distribution on their own behalf, and for many SNTs, the U.T.C. has codified the distinctly minority line of discretionary-support trust cases with respect to the available resource issue. In this sense, the question is not whether a beneficiary has an enforceable right to force a distribution, but rather how much and under what circumstances can a beneficiary of a discretionary trust force a distribution? In other words, do all beneficiaries of SNTs now have an available resource or is it limited to those SNTs that do not have "special needs" or "luxury" language? This issue will be discussed in detail in Parts 2 and 3 of this article.

IV. Forcing a Distribution

Ignoring the available resource issue, proponents of the U.T.C. claim that the U.T.C. strengthens protections for third-party SNTs by providing that initially a governmental creditor may not force a distribution to satisfy the claim.[78] While technically correct, it falls short of the analysis necessary to determine if the beneficiary is eligible for Medicaid or other governmental benefits. As noted above and in prior articles,[79] if a beneficiary's interest in an SNT is deemed an "available resource," the beneficiary may be denied governmental aid prior to accessing Medicaid or other governmental benefits. In this case, the entire issue of a governmental agency forcing a distribution is moot because the SNT beneficiary is not eligible for governmental aid in the first place.

Second, the authors now agree that the U.T.C., with the 2005 proposed changes which are responsive to a few of our comments, effectively resolves the issues we raised about the interplay of U.T.C. §§504 and 506. As noted above, U.T.C. §504 creates an enforceable right in almost all, if not all, discretionary trusts. Prior to the 2005 amendments, U.T.C. §506 allowed a creditor to attach an *undefined* overdue distribution. Relying on the RESTATEMENT THIRD for interpretation, the term "overdue" may easily be interpreted as any discretionary distribution based on the right that a beneficiary had to demand such a distribution. Without our suggested modification of this section, a governmental agency may well have been able to force a minimal distribution and create an available resource through U.T.C. §506. Therefore, the authors now agree the U.T.C., with the most recent amendments, overrules the minority line of discretionary-support cases with respect to only the distribution issue. However, the available resource issue remains because the test is not whether a creditor can force a distribution but whether the beneficiary can force a distribution.[80]

After addressing our concerns under §506, not only does the U.T.C. overrule the minority discretionary-support line of cases with respect to the distribution issue, it overrules the distribution as to all support trusts under common law. With rising state budgetary problems, once state agencies realize that they can no longer recover from any trust, how long will it be before the state legislator's create a statutory exception under U.T.C. §503(c)? U.T.C. §503(c) provides:

> (c) A spendthrift provision is unenforceable against a claim of this State or the United States to the extent a statute of this State or federal law so provides.

When the federal or state government creates an exception creditor so that governmental agencies may recover in U.T.C. states, the exception creditor status will now apply to all third-party SNTs—not just support trusts under common law. Further, the federal or state statute may specify that the governmental agency may force a distribution in addition to attaching all future distributions. Finally, this exception creditor status may be accomplished by mere reference within any other legislative bill.

Conclusion

In the areas of asset protection of beneficial interests, particularly as applied to SNTs, both the RESTATEMENT THIRD and the U.T.C. rewrite trust law on a scale unprecedented in trust law history. While proponents of the U.T.C. self-proclaim the unsupported position of the "continuum of discretionary" trusts as the modern view of trust law, this statement is not supported by case law. Rather, in over 44 years since the Reporter of the RESTATEMENT THIRD first espoused this theory, at the appellate level, it appears that only one and possibly two appellate cases have followed to any degree this new view of trust law. If this is the case, the "continuum of discretionary trusts" is not even an emerging trend, let alone the so called "modern view." Rather, the continuum of discretionary trusts is a view that has been rejected by the wisdom of almost every appellate court.

This theory may never have gained any acceptance because it is fundamentally flawed from an estate planning perspective. Estate planners need to have definite guidelines so they can draft trusts to achieve a client's goals, including a trust not being considered an available resource. Now that the many holes in the "continuum of discretionary trust" theory are beginning to be published, proponents of the U.T.C. are unable to answer the lynch pin question, what is the specific language that protects a beneficiary from having an enforceable right or an available resource under the U.T.C.? The answer under the RESTATEMENT THIRD is relatively simple: There are no bright lines where a planner can safely draft. The RESTATEMENT THIRD finds any such planning guidelines to be "arbitrary and artificial." The second part of the article will analyze whether some proponents of the U.T.C. have provided any better explanation than the RESTATEMENT THIRD.

As will be further discussed in Parts 2 and 3 of this article, it appears that building a new ship or completely overhauling the old ship seem to be the only alternatives with the U.T.C. On the one hand, should one decide to build a new trust code, one has concluded that it is not just the nuts and bolts of the ship that are defective, but it is the new trust philosophy espoused by the U.T.C. that is defective. On the other hand, should one try to overhaul the ship, one makes the assumption that the problems of poor design may be remedied. Attempting to keep the U.T.C. afloat just as it pertains to creditor rights requires a complete rewrite of Article V and §814(a). Cosmetic amendments or adding comments in an effort to correct the deficiencies in the U.T.C. may be analogized to attempting to use a band-aid to cover the hole in the Titanic. They simply fall drastically short of the task. Oceans of ink are necessary to fix the Article 5 and §814(a) of the U.T.C. For a review of how various state U.T.C. committees have attempted to band-aid, duct tape or overhaul the U.T.C., *see* Part 2 of our article in the August–September issue.

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1 Mark Merric and Douglas Stein, *The U.T.C. Threatens Special Needs Trusts,* TR. & EST., Nov. 2004, at X; Mark Merric and Steven Oshins, *The Effect of the U.T.C. on Spendthrift Trusts*, 31 ETPL 375 (Aug. 2004); Mark Merric and Steven Oshins, *U.T.C. May Reduce Asset Protection on Non-Self Settled Trusts,* 31 ETPL 411 (Sept. 2004); Mark Merric and Steven Oshins, *How Will Asset Protection of Spendthrift Trusts Be Affected by the U.T.C.,* 31 EPTL 478 (Oct. 2004); Mark Merric, Carl Stevens and Jane Freeman, *The Uniform Trust Code—A Divorce Attorney's Dream,* J. PRAC. EST. PLAN., Oct.–Nov. 2004, at 33; Mark Merric, Douglas Stein and Jane Freeman, *The Uniform Trust Code: A Continuum of Discretionary Trusts or a Continuum of Continuing Litigation?* J. PRAC. EST. PLAN., Dec.–Jan. 2005, at 33; Mark Merric, Gillen and Jane Freeman, *Malpractice Issues and the Uniform Trust Code,* 31 EPTL 586 (Dec. 2004); Mark Merric and Collins, *Can the Uniform Trust Code be Fixed?* LAWYERS WEEKLY—HECKERLING EDITION, Jan. 3, 2005; Mark Merric and Douglas Stein, *The U.T.C.: A Continuing Threat to Estate Planning* (a CCH interview), ESTATE PLANNING REVIEW, Jan. 21, 2005; Mark Merric and Douglas Stein, *The Uniform Trust Code and Asset Protection in Non-Self Settled Trusts,* STEVE LEIMBERG'S ASSET PROTECTION NEWSLETTER #53; and Mark Merric, Douglas Stein and Gillen, *The Effect of the U.T.C. on ILITs,* STEVE LEIMBERG'S ESTATE PLANNING NEWSLETTER #733 at *www. leimberg-services.com*, Leimberg Information Services, Inc. (LISI); Chapter 3 of the treatise ASSET PROTECTION STRATEGIES, VOLUME II, Alexander A. Bove, Jr., editor, Mark Merric Author, to be published by the American Bar Association. For more information about this book, please contact the American Bar Association at *www.ababooksorg/* or (800) 285-2221. To download a copy of any of these articles on the U.T.C., please go to *www.International-Counselor.com*, then to "Publications" then to "Articles."

2 Davis and Kent, *The Uniform Trust Code and Supplemental Needs Trusts*, PROBATE L. J. OF OHIO, Jan.–Feb. 2005; Walsh, Davis, Kent and Newman, *What is the Status of Creditors Under the Uniform Trust Code?* ESTATE PLANNING, Feb. 2005. Both of these articles criticize the first four articles listed above.

3 The proposed North Carolina, and South Carolina Uniform Trust Codes have made

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modifications to Article 5. Ohio has made a weak effort with its wholly discretionary trust. While Virginia has not made significant modifications to Article 5, it has attempted to address some third-party SNT issues by adding special needs protective provisions. Similar to the Ohio model, the Virginia model falls drastically short regarding the available resource issues discussed in this article. The Missouri U.T.C. has also met with the Missouri Elder Law Section to also attempt to deal with the many threats to SNTs created by the U.T.C.

[4] Based on the issues voiced by those expressing of the U.T.C., the following amendments have been made by NCCUSL:

a. U.T.C. §504(e) was added so that *any* creditor could not attach a sole trustee's interest. The ability for a creditor to attach a sole trustee's interest in a trust had no basis in common law.

b. The comment under U.T.C. §501 appeared to allow for the judicial foreclosure sale of current beneficial interests as well as remainder interests. Allowing the judicial foreclosure sale of current beneficial interests is a position that had virtually no legal support in common law. This comment has now been deleted. The U.T.C. committee has added language referring to both the RESTATEMENT THIRD and RESTATEMENT SECOND regarding the judicial foreclosure sale of remainder interests. Regrettably, the U.T.C. comment does not disclose that the RESTATEMENT THIRD has changed the strong presumption against the judicial foreclosure sale of a remainder interest to a presumption of a judicial foreclosure sale in favor of the creditor.

c. U.T.C. §503(c) was modified so that the only remedy granted to an "exception creditor" was the ability to attach present and future distributions. After this amendment, no longer may an exception creditor, such as an estranged spouse, force the judicial foreclosure sale of a beneficiary's interest. This is a major change to the Uniform Trust Code, and the NCCUSL U.T.C. committee should be complemented for making this responsive change.

d. U.T.C. §501 was modified and a comment added so that it was hopeful that a judge would not interpret U.T.C. §501 to mean that all creditors could attach at the trust level.

e. U.T.C. §506 was modified so that an "undefined distribution" would not include a distribution to any standard where the trustee had any discretion regarding the amount or timing of a distribution.

[5] *Supra* note 1.

[6] Reference to SNTs or SNT in this article refers to a third-party SNT unless the context dictates otherwise.

[7] U.T.C. Prefatory Note.

[8] Walsh, Davis, *et al., supra* note 2 regarding items I, III, IV, V, VI and VII.

[9] Clayton, *Uniform Trust Code 2005,* U.T.C. NOTES, Winter 2004, at 3.

[10] For further discussion, *see* our Letter to the Editor, TRUSTS AND ESTATES MAGAZINE, Feb. 2005. It can be found online at *www.International-Counselor.com*.

[11] Proponents of the U.T.C. and RESTATEMENT THIRD have self-proclaimed this as the "modern view" of trust law, implying anyone who does not agree with this new approach as not being up with modern times. As analyzed in this and many other articles, the term "modern" is probably an incredibly inaccurate way to describe this new legal theory.

[12] One which does not include special needs language or which prohibits distributions for certain purposes.

[13] For a detailed analysis of these issues, *see The Effect of the U.T.C. on Spendthrift Trusts and U.T.C. May Reduce Asset Protection on Non-Self Settled Trusts, supra* note 1.

[14] In New York, this type of trust is often referred to as an Escher trust.

[15] *See* note 25.

[16] As noted in *In Re Wilson*, BC DC Tex., 140 B.R. 400 (1992). "Spendthrift and similar protective trusts are not sustained out of consideration for the beneficiary; their justification is found in the right of the settlor to control his or her bounty and secure its application according to his or her pleasure." and "To allow the IRS to reach any part of the trust in question would frustrate Mrs. Huval's intentions and deprive the residual beneficiaries of what is rightfully theirs." But see*, S.L. Craft,* SCt, 2002-1 USTC ¶50,361, 535 US 274, 122 SCt 1414. In *Craft* the federal government was allowed to attach tenancy-by-entirety property contrary to Michigan state law. However, *Craft* may be distinguished from a discretionary trust interest under state law. In *Craft,* there is no question that the debtor held an interest in property. With a discretionary trust under common law the beneficiary holds no property interest under state law—until the U.T.C. created one.

[17] *W.E. Taylor,* DC Calif., 66-2 USTC ¶9522, 254 FSupp 752, stating "On the other hand, the Supreme Court has only recently reemphasized the importance of the role played by the states in creating and defining property interests; a federal tax lien cannot attach to property in which, under state law, the taxpayer has no property interest at all. Citing Aquilino v. United States, supra, SCt, 60-2 ustc ¶9538, 363 US at p. 513, n. 3, 80 SCt 1277.

[18] *U.S. v. O'Shaughnessy*, 517 N.W.2d 574 (Minn. 1994); *First Northwestern Trust Co. of South Dakota v. Internal Revenue Service,* CA-8, 622 F2d 387 (1980); *First of America Trust Co.,* DC Ill., 93-2 USTC ¶50,507 (where the income interest was a support trust, but the principal was a discretionary trust). At first blush, it looks like the RESTATEMENT (THIRD) OF TRUSTS, §60, Reporter comment e and e(1) made an incredible blunder when it states the IRS could recover from a discretionary trust in *S.D. Magavern*, CA-2, 77-1 USTC ¶9249, 550 F2d 797. The first thing to note is that *Magavern* is a support case under common law, and the federal government was an exception creditor. The second point to note is that the RESTATEMENT THIRD has redefined the term "discretionary trust" to mean all trusts including support trusts. Only when read in light of the new definition of a discretionary trust does this citation in the RESTATEMENT THIRD make any sense.

[19] Clayton, *supra* note 9.

[20] *In Re Jones*, 812 P.2d 1152 (Colo. 1991); *Ridgell v. Ridgell*, 960 S.W.2d 144 (Tex. App. 1997); *Kansas Dept. of Social and Rehabilitation Services*, 254 Kan. 467, 866 P.2d 1052 (1994); *Simpson v. State, Dept. of Social and Rehabilitation Services,* 21 Kan. App. 2d 680, 906 P.2d 174 (1995); *Wright v. Wright*, 2002 WL 1071934 (Iowa App. 2002)—not cited for publication. (However this is an excellent case of a psychotic child attempting to sue the parent trustees on a discretionary trust. Had the psychotic child had an enforceable right, the result would be more than problematic.); *First Nat. Bank of Maryland v. Department of Health and Mental Hygiene,* 284 Md. 720, 399 A.2d 891 (1979); *In re Tone's Estates*, 240 Iowa 1315, 39 N.W.2d 401 (1949); *Town of Randolph v. Roberts*, 346 Mass. 578, 195 N.E.2d 72 (1964); SCOTT ON TRUSTS, §187, at 15; GEORGE T. BOGERT, THE LAW OF TRUSTS AND TRUSTEES (2d ed. 1980, supp. through 2003). Section 560 of the supplement, at 183; RESTATEMENT (SECOND) TRUSTS, §187, at 409 (1959). In the proponents of the U.T.C.'s article, *What Is the Status of Creditors Under the Uniform Trust Code,* EST. PLAN. J., Feb. 2005, the proponents of the U.T.C. complain that only Jones was cited then there was a reference to Scotts and Bogerts. Some of the authors assumed that some of the proponents read the numerous cases cited by these publications regarding this well known common law issue.

[21] *O'Shaughnessy*, *supra* note 18; *Jones*, *supra* note 20; *In re Canfield's Estate,* 80 Cal. App. 2d 443, 181 P.2d 732 (1947).

[22] *Carlisle v. Carlisle,* 194 WL 592243 (Sup. Ct. Conn. 1994); *Lauricella v. Lauricella*, 409 Mass. 211, 565 N.E.2d 436 (1991); *supra* note 25. It should also be noted that a couple of these proponents also cite *In re Marriage of Jones,* out of context. *Davis, supra* note 2. They note that the *Jones* court held that the beneficiary had an "equitable interest" and imply that this is a property interest. What is not mentioned by some U.T.C. proponents is that *Jones* was a divorce case and the equitable discretionary interest was only to be used as one of the factors for an equitable division of marital property. What further is not mentioned by these U.T.C. proponents is

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that Colorado's position that a discretionary interest should be considered as an equitable factor in divorce is a distinctly minority position, possibly unique only to Colorado.

[23] Daniel Hicks and Andy Strauss of the North Carolina U.T.C. should be congratulated on their modifications to the pure U.T.C. The same congratulations should be extended to Daniel Collins of the South Carolina U.T.C. The authors are pleased that these committee members devoted huge amounts of time to learn many of the areas where the U.T.C. deviates from common law and attempt to remedy them. Yet, the authors still find the benefits of the common law of most states surpass these highly modified U.T.C. statutes.

[24] *The Uniform Trust Code—A Divorce Attorney's Dream, supra* note 1.

[25] **Ohio:** *Metz v. Ohio Dept. of Human Services*, 145 Ohio App. 3d 304, 762 N.E.2d 1032 (2001); *Bureau of Support in the Department of Mental Hygiene and Correction v. Kreitzer,* 16 Ohio St. 2d 147, 243 N.E.2d 83 (1968); *Matter of Gantz*, 1986 WL 12960; *Samson v. Bertok*, 1986 WL 14819 (the creditor did not recover because it was not a governmental claim); *Matter of Trust of Stum*, 1987 WL 26246; *Schierer v. Ostafin*, 1999 WL 493940 (the creditor did not recover because it was not a governmental claim). In the above SNT cases, the government was able to attach the beneficiary's interest and force a distribution pursuant to the standard.

Iowa: *Strojek v. Hardin County Board of Supervisors,* 602 N.W.2d 566 (Iowa App. 1999); *also see* the follow-up unpublished opinion where the Iowa Appellate Court expanded the definition of the distribution language as much broader than "basic needs." *Strojek v Hardin County Board of Supervisors,* 2002 WL 180377 (Iowa App. 2002); *Also see McCabe v. McKinnon,* 2002 WL 31757533 (Iowa App. 2002), an unpublished decision.

Pennsylvania: Using a slightly different analysis, Pennsylvania courts have generally held that if a discretionary support trust was for one beneficiary and such sole beneficiary was not receiving governmental benefits at the time of creating the trust, then the settlor intended that the principal of the trust as an available resource to the beneficiary. *Estate of Taylor v. Department of Public Welfare,* 825 A.2d 763 (Pa. 2003); *Shaak v. Pennsylvania Department of Public Welfare,* 747 A.2d 883 (Pa. 2000); *Estate of Rosenberg v. Department of Public Welfare,* 679 A.2d 767 (Pa. 1996); *Commonwealth Bank and Trust Co.,* 598 A.2d 1279 (Pa. 1991).

Connecticut: The Supreme Court concluded that when a discretionary trust was coupled with any standard, the trust was classified as a support trust. A support trust is by definition an available resource. *Corcoran v. Department of Social Services,* 271 Conn. 679, 859 A.2d 533 (2004).

[26] *Estate of Lackmann v. Department of Mental Health*, 156 Cal. App. 2d 674, 320 P.2d 186 (1958).

[27] *Estate of Johnson v. Department of Mental Health of the State of California*, 198 Cal. App. 2d 503 (1961); *Estate of Hinckley v. Department of Mental Health*, 195 Cal. App. 2d 164 (1961)

[28] *Id.*

[29] *Id.*

[30] *Supra* note 20.

[31] RESTATEMENT (SECOND) OF TRUSTS, §187, at 409 (1959); *also see* RESTATEMENT (SECOND) OF TRUSTS, §128, comment d. and note 25 above.

[32] *Jones*, supra note 20.

[33] RESTATEMENT (SECOND) OF TRUSTS, §155, comment b (1959).

[34] RESTATEMENT SECOND OF TRUSTS, §187, comments e. and i.

[35] SPERO, ASSET PROTECTION—LEGAL PLANNING AND STRATEGIES, §6.03(1).

[36] *Kreitzer, supra* note 25.

[37] *Supra* note 25.

[38] *Davis, supra* note 2.

[39] In an attempt to support their legal position that the U.T.C. does not codify *Kreitzer*, some proponents of the U.T.C. attempt to use an incredibly narrow holding for *Kreitzer*. Proponents argue that *Kreitzer* is limited to situations in which the state was creditor, where the trust beneficary resided in a state institution, where the trust had a support standard, and where the trust lacked a spendthrift provision. E-mail sent to Mark Merric from Ric Davis on February 10, 2005**.** First whether *Kreitzer* can be so narrowly construed is highly debatable. This is true because cases citing to *Kreitzer* in Ohio directly contradict such a narrow interpretation. *See* Ohio cases under note 25, *supra*. Second, it appears these proponents did not research or did not adequately research the *Kreitzer* file to find out if it really did or did not have a spendthrift clause in the six and one-half page will. The actual six and one-half page will created a trust with with a spendthrift provision. *See* Item Third, Paragraph B. of the Last Will and Testament of George L. Swallow. Third, as discussed in detail in this and the previous article, whether there is a spendthrift clause is irrelevant to the available resource issue as applied to a discretionary trust, because a discretionary trust does not rely on spendthrift protection. *See also* note 35, *supra*. Finally, when referring to the distinctly minority line of discretionary-support trust cases, we are referring to all of the cases in Ohio, Iowa and Pennsylvania. These cases are not limited by the above narrow reading.

[40] *Supra* note 2.

[41] *Walsh, supra* note 2. Also, in this article, these proponents divined and misrepresented the following statement which has never been articulated by those expressing concerns regarding the U.T.C.: "The critics' contention that the common law does not require the good faith of a trustee, no matter how broad the discretion of the trustee is simply wrong." This issue that has always been presented and is continued to be presented is when the U.T.C. abolishes the discretionary-support dichotomy that depends on two different standards of judicial review, what is the judicial review standard for a court? This begs the second question, what is the language under the U.T.C. that prevents a beneficiary from having an enforceable right or an available resource? As previously noted, proponents of the U.T.C. continue to avoid answering this fundamental question.

[42] *Supra* note 1.

[43] HENRY CAMPBELL BLACK, BLACK'S LAW DICTIONARY (1990). In fact, this edition of Black's dictionary defines "bad faith" as the opposite of "good faith."

[44] *The Uniform Trust Code: A Divorce Attorney's Dream, supra* note 1.

[45] For an analysis of terms used to prevent a creditor from recovering against a discretionary trust, *see In re Tone's Estates,* 39 N.W.2d 401 (Iowa 1949). This case cites the three leading secondary source materials (RESTATEMENT OF TRUSTS; AMERICAN JURISPRUDENCE; and CORPUS JURIS SECUNDUM). Two of these sources used improper motive, dishonesty and failure to act. One of them used bad faith. None of them used the term "good faith."

[46] RESTATEMENT OF TRUSTS, §187, comment j. (1935); RESTATEMENT (SECOND) OF TRUSTS, §187, comment j. (1959).

[47] *The U.T.C. Threatens Special Needs Trusts; The Effect of the U.T.C. on Spendthrift Trusts; U.T.C. May Reduce Asset Protection on Non-Self Settled Trusts, supra* note 1. Some U.T.C. proponents complain about our reliance on a handfull of cases that interpret the "good faith" standard with the standard of reasonableness. Walsh and Davis, *supra* note 2. However, their struggle to find support of their position that the good faith standard does not change anything, they incorrectly cite *In re Estate of McCart,* 847 P.2d 184 (Colo. App. 1992). This case is a classic discretionary trust case where the trustee did not make distributions to current discretionary beneficiary because the trustee was the remainder beneficiary and wanted the trust assets for himself. The Appellate Court noted: "The trial court specifically found and concluded that Goss had abused his discretion and acted arbitrarily and capriciously**.** The improper motives with a clear conflict of interest as trustee seeking to conserve the trust funds for himself and his heirs as remainderman under the trust, and also in breach of his fiduciary responsibilities to act with the utmost good faith and fairness toward a beneficiary."

These proponents quoted only the *"in breach of his fiduciary responsibilities to act with*

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the utmost good faith and fairness toward a beneficiary," and then they concluded that, because these words were used in combination with a discretionary trust, the review standard of "good faith" was the same as the discretionary common law standard. Despite these proponents careful selection of phrases to support their position, a cursory review of the case yields the opposite of their conclusion. *In re Estate of McCart* is nothing more than a classic discretionary trust case with the judicial review standard only for (1) acting dishonestly; (2) acting with an improper motive; or (3) failing to act.

48 Possibly without exception, when courts have used the term "bad faith" with no reference to "good faith," the courts have found that neither the beneficiary nor the creditor had an enforceable right. *SunTrust v. Children's Hospital,* 2003 WL 21085046 (Va. Cir. Ct. 2003); *In re Estate of McInery*, 289 Ill. App. 3d 589, 682 N.E.2d 284 (1997); *Simpson v. State, Dept. of Social and Rehabilitation Services*, supra note 20; *First Nat. Bank of Maryland v. Department of Health and Mental Hygiene, supra* note 20; *Town of Randolph v. Roberts*, *supra* note 20; *In re Maeder's Estate*, 329 N.Y.S.2d 663 (N.Y. Sup. 1972); *Greenwich Trust Co. v. Tyson*, 10 Conn. Supp. 147 (Conn. Super. 1941). According to Andy Strauss of the North Carolina U.T.C. committee, this was the primary reason why North Carolina chose the term "bad faith" over "good faith" as the judicial review standard under U.T.C. §814(a). Also, Scott on Trusts appendix cites the term "bad faith" and gives several references, but no mention is made of the term "good faith."

49 Unfortunately, the distinction between "good faith" and "bad faith" adopted by North Carolina and Ohio U.T.C. committees may be short lived. As noted by the proponents of the U.T.C. (Walsh, *supra* note 2), courts have combined the terms "good faith" and "bad faith," and these terms have been used synonymously. *In re Ferrall Estate,* 41 Cal. 2d 166, 258 P.2d 1009 (1953). *In re Ferrall*, holds the beneficiary of a discretionary trust coupled with a standard does not have an enforceable right under a good faith or bad faith standard. Therefore, a governmental agency was not allowed to force distributions from a discretionary trust coupled with a standard. On the other hand, the court in *In re Ventura County Dept. of Child Support Services v. Brown* authorized invasion of a discretionary trust coupled with a standard even though the court found that the debtor/beneficiary had no enforceable right. Again, holding that a creditor has greater rights than a trust beneficiary flies in the face of the common law definition of a common law discretionary trust but not the U.T.C. definition.

50 *Supra*, note 20.

51 U.T.C. §1013, official comment paragraph 4.

52 U.T.C. §1012, official comment thereunder.

53 Proposed N.C.S. §36C-5-814(a).

54 Proposed Ohio Statute §5808.14(a).

55 Colorado U.T.C. official comments. At the November 19, 2004, Colorado U.T.C. Committee, Stanton Kent, co-chair of the committee, stated that he had changed his position, and the U.T.C. did not overrule *In Re Jones*. Kent is one of the U.T.C. proponents criticizing the authors in two of his articles, *supra* note 2.

56 Covey and Hastings, Practical Drafting, Oct. 2003; Richard Covey is Senior Counsel at Carder, Ledyard & Milburn, LLP. Dan Hastings is counsel at Skadden, Arps, Meagher & Flom, LLP. Both are the primary drafters of Practical Drafting.

57 Covey and Hastings, *Recent Developments in Estate, Gift and Income Taxation—2004*, 39th Annual Heckerling Institute on Estate Planning, University of Miami School of Law, at 193–94.

58 For a detailed analysis of how "uncertain the scope" might be see Merric, Stein, and Berger, *The Uniform Trust Code: A Continuum of Discretionary Trusts or a Continuum of Continuing Litigation? supra* note 1.

59 Covey and Hastings, Practical Drafting, Apr. 2004.

60 *Id.*

61 *Supra* note 25.

62 Mark Merric and Douglas Stein, *The Effect of the U.T.C. on Spendthrift Trusts*, *supra* note 1; Mark Merric and Steven Oshins, *U.T.C. May Reduce Asset Protection on Non-Self Settled Trusts, supra* note 1; *also see* Part 2 of this article (forthcoming, June–July issue).

63 E-mail on ABA Listserv dated June 24, 2004, from Bob Redler.

64 Clayton, *supra* note 9.

65 *Comments Under U.T.C.* §§ *501 through 506 and 814(a)* reference directly to §50 in its entirety; §56, comment b; §58, comments b, c, d and e; and §60, comment a.

66 Halbach, *Problems of Discretion in Discretionary Trusts,* 61 Colum. L. Rev. 1425 (1961).

67 *Id.,* at 1428.

68 *In re Lykes' Estate,* 113 N.H. 282, 305 A.2d 684 (1973) (cited for the proposition differentiating between a direct invasion of principal by the wife in the paragraph 2.4 trusts and an indirect invasion through her consumption of income needed by the children which forces them to invade the corpus themselves*; First Nat. Bank & Trust Co. of Wyo. v. Finkbiner*, 416 P.2d 224 (Wyo. 1966); *U.S. v. Taylor*, *supra* note 17 (the court classified this trust as "primarily" a support trust; *In re Eckert's Trust*, 23 A.D.2d 32, 258 N.Y.S.2d 539 (1965) (cited for the proposition that a settlor of a spendthrift trust sometimes confides in the trustee discretion to terminate the trust when the beneficiary, in the opinion of the trustee, has attained a certain age and capacity to conserve and enjoy the trust principal).

69 *Supra* note 7.

70 U.T.C. §504. The comment states "[t]his section, similar to the Restatement, eliminates the distinction between discretionary and support trusts, unifying the rules for all trusts fiting within either of the former categories." *See* Restatment (Third) of Trusts, §60, Reporter's Notes to comment a (Tentative Draft No. 2, approved 1999).

71 Restatement (Third) of Trusts, §50, Reporter comment e, at 309.

72 Restatement (Third) of Trusts, §60, Reporter comment a., at 415.

73 Restatement (Third) of Trusts, §60, Reporter comment a., at 416, mentions a continuum of discretionary trusts from the most objective standards such as health, education, maintenance and support to one with no standards. However, it fails to define when, if ever, any trust on this continuum will not have an enforceable right.

74 Restatement (Third) of Trusts, §50, comment (d), provides that if a standard is omitted, the court will still apply a reasonableness or good-faith judgment "based on the extent of the trustee's discretion, the various beneficial interests created, the beneficiaries' circumstances and the relationships to the settlor, and the general purposes of the trust."

75 *Supra* note 2.

76 U.T.C. §504, Official Comment amended February 18, 2005.

77 *The Uniform Trust Code and Asset Protection in Non-Self Settled Trusts, supra* note 1.

78 Davis, s*upra* note 2; Clayton, *supra* note 9.

79 *Supra* note 1.

80 U.T.C. §504(d).

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