ACTEC

McPherson Building
901 15th Street, NW, Suite 525
Washington, DC 20005
(202) 684-8460 Fax (202) 684-8459
www.actec.org

The American College of Trust and Estate Counsel

Please Address Reply to:

Executive Director
DEBORAH O. MCKINNON

February 22, 2017

U.S. Office of Government Ethics
1201 New York Ave NW, Suite #500
Washington, DC 20005

Via Electronic Mail: usoge@oge.gov

Attention: Request for Input on Discretionary Trusts

Dear Ladies and Gentlemen:

The American College of Trust and Estate Counsel ("ACTEC") is pleased to submit the enclosed comments in response to the following question posed by OGE in a Notice published in the Federal Register on January 3, 2017, 82 Fed. Reg. 122:

Are there any circumstances under which an eligible income beneficiary of a discretionary trust might, in the absence of a vested remainder interest, be able to compel the trust to make a distribution or payment?

ACTEC is a professional organization of approximately 2,600 lawyers from throughout the United States. Fellows of ACTEC are elected to membership by their peers on the basis of professional reputation and ability in the fields of trusts and estates and on the basis of having made substantial contributions to those fields through lecturing, writing, teaching, and bar activities. Fellows of ACTEC have extensive experience in providing advice to taxpayers on matters of federal taxes, with a focus on estate, gift, and GST tax planning, fiduciary income tax planning, and compliance. ACTEC offers technical comments about the law and its effective administration, but does not take positions on matters of policy or political objectives.

If you or your staff would like to discuss ACTEC's recommendations, please contact Beth Kaufman, chair of the Washington Affairs Committee, at 202-862-5062 or by email at bkaufman@capdale.com, or Leah Weatherspoon, ACTEC Communications Director, at (202) 688-0271, or by email at lweatherspoon@actec.org.

Respectfully submitted,

Cynda Ottaway

Cynda C. Ottaway
President

Enclosure: ACTEC Comments on Request for Input on Discretionary Trusts

REQUEST FOR INPUT ON DISCRETIONARY TRUSTS

ACTEC COMMENTS

Question Addressed

In a Notice published in the Federal Register on January 3, 2017, the Office of Government Ethics requested comments on the following question:

Are there any circumstances under which an eligible income beneficiary of a discretionary trust might, in the absence of a vested remainder interest, be able to compel the trust to make a distribution or payment?

Concise Answer

Under statutory provisions and judicial decisions of most United States jurisdictions, an income beneficiary of a discretionary trust may be able to demonstrate that the trustee breached fiduciary duties in not making a trust distribution to the beneficiary and therefore compel a distribution or payment.

Analysis – Majority Rule

The rights of a discretionary beneficiary of a trust are determined under state law. Thirty-one states and the District of Columbia have adopted statutes based on the Uniform Trust Code ("UTC"). More information about the Uniform Trust Code may be found at the Uniform Law Commission website, www.uniformlaws.org. Section 814 of the UTC provides that:

> 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.

Several states that have not adopted the Uniform Trust Code nonetheless have similar statutory provisions. For example, the Texas Trust Code in Section 13.029(a) provides, "Notwithstanding the breadth of discretion granted to a trustee in the terms of the trust, including the use of terms such 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." Maryland, in MD Code, Estates and Trusts, § 14.5-203, provides that "[a] discretionary power conferred on the trustee to determine the benefits of a beneficiary is subject to judicial control to prevent misinterpretation or abuse of the discretion of the trustee."

These types of provisions do not determine whether a discretionary trust beneficiary will actually be entitled to a distribution upon proof of the trustee's misconduct, but instead leave that decision up to the relevant state court. A court would consider not only the language of the particular instrument, but also the applicable state law, the family tree, all the circumstances of the family, the amount to be distributed, its intended use, what the settlor designed the trust to accomplish, etc. A court would consider the claims of a discretionary beneficiary on a case-by-case basis. Accordingly, a court may decide that failure of the trustee to make a payment or distribution is in violation of the trustee's duties and may compel the trustee to make a distribution or payment to the discretionary beneficiary.

Example

As an example, assume that the settlor of the trust granted the trustee discretion to distribute trust funds for a beneficiary's medical care. Subsequently, the beneficiary is in a serious car accident and the trustee decides not to make any distributions for the beneficiary's reasonable medical expenses. If the beneficiary sues the trustee, a court will examine the surrounding circumstances. Perhaps the court would find that the beneficiary has sufficient insurance or resources to cover the expenses. But if there is no basis justifiable within the terms and purposes of the trust for the refusal, a court may determine that the trustee is not acting within the scope of the settlor's intent and compel the trustee to make discretionary distributions for the beneficiary's medical expenses.

Analysis – Minority Rule

The laws of a few states make it unlikely that a discretionary trust beneficiary could compel a distribution. Nevada's laws are an example of this minority view. Nevada Revised Statute § 163.419 provides that "[a] beneficiary who has a discretionary interest in a trust does not have an enforceable right to a distribution from the trust, and a court may review a trustee's exercise of discretion concerning a discretionary interest only if the trustee acts dishonestly, with bad faith or willful misconduct." Thus, Nevada courts will not compel distributions, but they will consider removal and replacement of the trustee if the acting trustee is guilty of a breach of fiduciary duties that justify the trustee's removal. The beneficiary's only hope of redress would be that the replacement trustee will be more generous; however, the beneficiary still remains with no enforceable right to demand or compel a distribution.