ACTEC Law Journal

Volume 39 | Number 1 Article 6

3-1-2013

Protecting Your Clients' Assets from Their Future Ex-Sons and Daughters-in-Law: The Impact of Evolving Trust Laws on Alimony Awards

Christopher J. Roman

Protecting Your Clients' Assets from Their Future Ex-Sons and Daughters-in-Law: The Impact of Evolving Trust Laws on Alimony Awards

Christopher J. Roman, Villanova Law School

First Place Winner of the Mary Moers Wenig Student Writing Competition (2013)

Since the dawn of modern estate planning, parents have sought to keep wealth "in the family" and protected from the reach of their descendants' creditors. To achieve this objective, estate planners have often implemented discretionary trusts to shield beneficiaries' assets from their own misjudgments. For the modern parent, with nearly fifty percent of first marriages ending in divorce,[1] the most threatening creditor has become a future ex-son or ex-daughter-in-law.

As we continue through this era with a high rate of divorce and an increasing number of children becoming beneficiaries of trusts from past generations, the confluence of these two factors has created a tension between trust law and matrimonial law that has become the subject of an increasing number of cases across the county. This tension has pushed trust law and matrimonial law to evolve in tandem as more and more divorce cases involve a trust for the benefit of one of the parties. A critical issue in these divorces becomes whether potential distributions to the beneficiary-spouse after the divorce should be included as a source of income for the purposes of calculating alimony. This issue gives rise to the following dilemma for the court: since the court cannot determine whether the future distributions will be made, can the court presume that distributions will be made or, alternatively, can the court compel the trustee of the trust to make distributions to the beneficiary to ensure that the alimony obligation is satisfied?

The evolution of the law with respect to these issues is highlighted in a recent Supreme Court of New Jersey decision, *Tannen v. Tannen*,[2] which examines whether a court can compel future distributions from a discretionary trust and, thereby, include those distributions as a source

---

1 *See* Casey E. Copen, Ph.D., et. al., *First Marriages in the United States: Data From the 2006–2010 National Survey of Family Growth*, National Health Statistics Reports, No. 49 at 9 (March 22, 2012)("The probability of a first marriage reaching its 20th anniversary was 52% for women and 56% for men in 2006–2010").

2 Tannen v. Tannen, 31 A.3d 621 (N.J. 2011).

of income for the beneficiary-spouse in calculating alimony. The *Tannen* case is not the first of its kind to address these issues as state courts in Iowa, Colorado and Massachusetts, among others, have also been challenged over the past two decades to decide these cases that cross the line between matrimonial law and trust law.[3] However, as the most recent decision analyzing whether potential distributions from a discretionary trust may be included in the alimony calculation, the *Tannen* case reveals some of the most compelling arguments that have been entered on behalf of the non-beneficiary spouse. The most impressionable of which is the non-beneficiary spouse's argument that the court should adopt the relevant sections of the Restatement (Third) of Trusts (the "Restatement (Third)").[4] The non-beneficiary spouse in *Tannen* argued that the Restatement (Third) expands the rights of the beneficiary-spouse to compel distributions from discretionary trusts and, thereby, the rights of the non-beneficiary spouse to claim that potential future distributions from the trust should be included in the alimony calculation.[5] Although the court in *Tannen* declined to adopt the relevant sections of the Restatement (Third), the court's analysis of the changes in the law that the Restatement (Third) sets forth, whether right or wrong, is instructive for estate planners on a national scale as it highlights the impact of the evolving principles of trust law in the context of a non-beneficiary spouse's claim for alimony in a divorce case.

The discussion of the decision in *Tannen* is also pertinent on a national scale because, on its surface, the case provides a fairly typical set of facts: wealthy parents establish a trust for the benefit of their daughter who later marries, has children, relies on the trust distributions to support her family, and then files for divorce from her husband. The *Tannen* case, as well as the other cases surveyed here, uncover a host of issues that can be raised with respect to discretionary trusts in the event of a beneficiary's divorce: the trust's standard of discretion; the number and identity of the trustees; and the history of trust distributions are such issues. The analysis of these issues could impact whether a court determines to impute potential future distributions from the discretionary trust to the beneficiary-spouse for the purposes of calculating alimony.

---

[3] *See, e.g., In re* Marriage of Rhinehart, 704 N.W.2d 677 (Iowa 2005); *In re* Marriage of Jones, 812 P.2d 1152 (Colo. 1991); D.L. v. G.L., 811 N.E.2d 1013 (Mass. App. Ct. 2004).

[4] RESTATEMENT (THIRD) OF TRUSTS (2003). The Restatement (Third) of Trusts is a treatise published in 2003 that is considered persuasive authority and purports to draw both on court decisions and statutes to provide a contemporary treatment of trust law.

[5] Tannen v. Tannen, 3 A.3d 1229, 1239-44 (N.J. Super. Ct. App. Div. 2010), *aff'd*, 31 A.3d 621 (N.J. 2011).

To examine the impact of evolving trust law on the beneficiary of a discretionary trust in the midst of a divorce, this article begins with a survey of cases to analyze the different standards of discretion that a grantor may vest in its trustee with respect to making distributions to beneficiaries. The article then discusses the potential impact of the Restatement (Third) on the rights of beneficiaries to compel distributions from a discretionary trust, and the corresponding rights of creditors to attach to the interest of the beneficiaries. Following the discussion of the Restatement (Third), this article provides an examination of *Tannen*, including the non-beneficiary spouse's claim to include potential future distributions from a discretionary trust for the beneficiary-spouse in the alimony calculation based on certain sections of the Restatement (Third). Finally, with the cases surveyed, the Restatement (Third) and *Tannen* in mind, this article proposes drafting and practical suggestions for estate planning attorneys aimed at protecting their clients' descendants from the future alimony claims of an ex-spouse.

I. Contrasting Standards of Discretion and Their Impact on Creditor Rights

A critical issue in determining whether potential future trust distributions are includable in an alimony calculation is the trust's standard of discretion. The standard of discretion in a trust sets forth the grantor's intention with respect to trust distributions. For the trustee, the standard of discretion defines the purposes for which the trustee can make distributions from the trust to the beneficiary and the amount of discretion vested in the trustee when determining whether and if distributions are appropriate.[6] For the beneficiary, the standard of discretion defines the beneficiary's rights to receive distributions, meaning whether the beneficiary can compel the trustee to make a distribution in the event that a trustee fails or declines to make a distribution on his own accord.

In the context of a divorce, the standard of discretion is of paramount importance because it not only defines the rights of the beneficiary to compel distributions from the trust, but also the rights of a beneficiary's creditors, including a soon-to-be ex-spouse, to compel distributions from the trust. This occurs because the rights of a creditor are dependent on the rights of the beneficiary.[7] A common expression of trust law provides that the creditor steps into the shoes of the benefici-

---

[6] *See* Roorda v. Roorda, 300 N.W. 294, 295 (Iowa 1941); *Tannen*, 3 A.3d at 1238, 1240.

[7] *See* Loeb v. Loeb, 301 N.E.2d 349, 356 (Ind. 1973) ("[T]he transferee or creditor cannot compel the trustee to pay anything to him because the beneficiary could not compel payment to himself or application for his own benefit.") (quoting Restatement (Second) of Trusts § 155(1) cmt. b (1959)).

ary when it seeks to attach to the beneficiary's interest in a discretionary trust.[8] As a result, if the beneficiary can compel a distribution from the trust, then the creditor can attach to the trust and compel a distribution; if the beneficiary cannot compel a distribution, then, likewise, the creditor cannot compel a distribution.[9]

For the purposes of this article, the trusts at issue are discretionary third-party irrevocable trusts – trusts that grantors establish for the benefit of individuals other than themselves that they cannot amend, but from which distributions are made subject to varying degrees of discretion vested in the trustees. In general, discretionary trusts vest the trustees with two alternative standards of discretion. One alternative is to draft the trust with a pure discretionary standard.[10] This type of standard might include vesting the trustee with the discretion to make distributions for "any or no purpose," which can be created with the following language: The trustee shall make such payment or application for any or no purpose, irrespective of cause or need, as the trustee, in his sole and absolute discretion, shall deem to be in the best interest of such beneficiary.[11] This type of discretionary trust is often referred to as a "pure discretionary trust."[12] Under this standard, the trustee is vested with the complete and uncontrolled discretion to make distributions of trust assets to the beneficiary. Because the beneficiary has no power over distributions from the trust, a creditor, likewise, is unlikely to have any power to compel distributions to satisfy a judgment.

In the alternative, the drafter of the trust may choose a more restrictive standard of discretion; for example, a "support" standard, which vests the trustee with the discretion to make distributions as the trustee deems necessary only for the beneficiary's "health, education, maintenance or support."[13] A trust that vests this standard of discretion

---

[8] Kevin D. Millard, *Rights of a Trust Beneficiary's Creditors Under the Uniform Trust Code*, 34 No. 2 ACTEC J. 58, 62 (2008).

[9] *See Id*.

[10] *See Tannen*, 3 A.3d at 1239 (citing RESTATEMENT (SECOND) OF TRUSTS §155(1) (1959)).

[11] *See* RESTATEMENT (SECOND) OF TRUSTS §155(1) (1959).

[12] *See Pack v. Osborne*, 881 N.E.2d 237, 243 (Ohio 2008) ("a trust that allows the the uncontrolled discretion to distribute income and principal as the principal determines, without a support standard, is a pure discretionary trust").

[13] *See Tannen*, 3 A.3d at 1239 (citing RESTATEMENT (SECOND) OF TRUSTS §128 cmt. e (1959)). This standard is commonly referred to as the "ascertainable standard" and is pulled directly from § 2041(b)(1)(A) of the Internal Revenue Code of 1986, as amended. *See* I.R.C. § 2041(b)(1)(A). The ascertainable standard is commonly implemented in trust agreements to achieve certain estate tax benefits which result from complying with § 2041.

in the trustee is commonly referred to as a "support trust."[14] Although a support standard vests considerable discretion in the trustee, a beneficiary typically can compel the trustee to make a distribution by showing that it is necessary for the beneficiary's support.[15] Likewise, certain creditors (including a former spouse) of the beneficiary may be able to enforce that right as well.[16]

A. Pure Discretionary Trusts

Traditionally, trusts that courts deem as pure discretionary trusts have been more likely to be excluded from the alimony calculation. A 1941 case before the Supreme Court of Iowa, *Roorda v. Roorda*, presents a simple set of facts that demonstrates the implications of a pure discretionary trust on a former spouse's claim for alimony from a trust of which her former husband was the beneficiary.[17] In *Roorda*, the plaintiff brought an action against both the estate of her former father-in-law and her former husband. She claimed that her former father-in-law conspired with her former husband to establish a trust upon the father-in-law's death for the benefit of the former husband.[18] She argued that the trust was established for the sole purpose of defeating her potential claim against the husband for the alimony and support payments to which she was entitled under her divorce decree.[19]

The trust her former father-in-law established for the benefit of her former husband contained the following standard of discretion: "[the trustee] shall pay over to [the beneficiary], the income from same and any part or all of the principal at such time or times as in the judgment of [the trustee] the payment of same will be to the best interests of [the beneficiary]."[20] The court interpreted this standard as a pure discretionary trust, meaning "the judgment of the trustee as to the best interests of the beneficiary shall determine payments of income as well as principal and that the making of payments from either or both sources is discretionary with the trustee."[21] Accordingly, the court affirmed the lower court's decision that "the trust assets in the hands of the trustee were

---

14 *See Tannen*, 3 A.3d at 1239; RESTATEMENT (SECOND) OF TRUSTS § 128 cmt. e (1959).

15 *See* RESTATEMENT (SECOND) OF TRUSTS § 154 cmt. b (1959).

16 *See* RESTATEMENT (SECOND) OF TRUSTS § 157 (1959); *see also* Dwight v. Dwight, 756 N.E.2d 17, 19, 22 (Mass. App. Ct. 2001); Coverston v. Kellog, 357 N.W.2d 705, 709 (Mich. Ct. App. 1984) (quoting Hurley v. Hurley, 309 N.W.2d 225, 227 (Mich. Ct. App. 1981).

17 Roorda v. Roorda, 300 N.W. 294 (Iowa 1941).

18 *Id.* at 294-95.

19 *Id.* at 295-96.

20 *Id.* at 295.

21 *Id.*

not subject to appropriation by [the former wife] because payments of income and principal to the beneficiary were entirely subject to the discretion of the trustee and the beneficiary had no present interest therein."[22]

This case illustrates the protections that a pure discretionary trust may offer even despite the father's expressed intent to protect his assets from the claims of his son's ex-wife. To the contrary, the court honored the father's testamentary intent to shield his assets from the claims of his former daughter-in-law because "a testator has the right to dispose of his estate as he desires."[23] With respect to this trust in particular, since the trustee was vested with total discretion over the trust assets, those assets were not available to the claims of the son's creditors, including his former wife.[24] In other words, since the son had no power to compel distributions from the trust, the court could not include potential distributions from the trust in the alimony calculation. As such, the wife could not attach to potential future distributions from the trust in order to receive the alimony and support payments to which she was entitled under the parties' divorce agreement.[25]

This case, which was decided in 1941, represents the more traditional view when a non-beneficiary spouse seeks an alimony award based upon the beneficiary-spouse's interest in a pure discretionary trust; namely, to exclude potential future distributions from the alimony calculation. The reason the non-beneficiary spouse cannot attach to the beneficiary-spouse's interest in the discretionary trust is that the beneficiary-spouse has no power to compel a distribution from a pure discretionary trust. In more recent cases, however, courts have held that potential future distributions from pure discretionary trusts may be included in an alimony calculation, particularly where there is a history of a consistent stream of distributions to the parties to support their marital lifestyle.[26]

An example of such a case is a 2004 Appeals Court of Massachusetts decision, *D.L. v. G.L.* In this case, the parties were involved in a divorce proceeding. The husband was a descendant of "a family whose wealth dates back for generations."[27] As a result of the family's estate planning, he was the beneficiary of seven trusts that in the aggregate held over $100 million, of which the husband's interest was valued at approximately $28 million. The issue presented to the court was, among

---

22 *Id*. at 295, 297.
23 *Id.* at 297.
24 *Id.* at 295.
25 *Id.* at 296-97.
26 *See, e.g.,* D.L. v. G.L., 811 N.E.2d 1013, 1024 (Mass. App. Ct. 2004).
27 *Id*. at 1018.

others, whether "the [trial court] erred . . . by awarding insufficient alimony and child support" to the wife.[28]

One of the larger trusts at issue, "The Children's Trust," vested the following standard of discretion in the trustee: "the disinterested trustees, in their uncontrolled discretion, shall pay to the [beneficiary] such amount or amounts from the net income and principal as the disinterested trustees, in their uncontrolled discretion, think advisable."[29] The court conducted a review of relevant existing case law in order to distinguish the "Children's Trust" – a pure discretionary trust – from trusts in other Massachusetts cases that vested their trustees with a support standard.[30] The court then analyzed the terms of the trust as well as the past history of distributions from the trust.

The court (i) acknowledged that payments to the beneficiaries, including the husband, were "to be made, if at all, in the uncontrolled discretion of the trustees;"[31] (ii) noted that there had never been a distribution from the principal of the trust in its 38 year existence and (iii) found the checks and balances system imposed upon the interested and disinterested trustees sufficient to ensure impartiality.[32] However, the court also emphasized that, over the past ten years, all of the income attributed to the husband's share of the trust had been distributed to him annually.[33] The court also focused on the fact that those distributions were made pursuant to the trustee's "standing instructions," which were instructions directing automatic annual distributions from the trust account to the husband until the trustee changed or cancelled those instructions.[34]

The appellate court held that the trial court "could" treat the husband's discretionary interest in the Children's Trust "as a stream of income for the payment of alimony and child support,"[35] emphasizing "at least, as here, where income from the trust has historically been distributed to the husband on a consistent basis."[36] Although the court suggests that the income from the trust could be excluded from the alimony calculation because it is a pure discretionary trust, it instead upheld the trial court's decision to include the income stream in the alimony calculation because the income from the trust had been distributed to the husband on a consistent, historical basis. In other words, the court

---

28 *Id.*
29 *Id.* at 1021 n.10.
30 *Id.* at 1022-24.
31 *Id.* at 1023.
32 *See id*.
33 *Id.* at 1021.
34 *Id.* at 1021-22.
35 *Id.* at 1024.
36 *Id.*

found that the trial court could assume that the stream of distributions from the trust to the husband would continue into the future based upon the historical pattern of distributions. As such, those future distributions from the trust could be considered a "stream of income" for the purposes of an alimony calculation.

This decision, however, conflicts with *Roorda.* While *D.L.* included potential future distributions from a discretionary trust in the alimony calculation because of the trust's history of distributions, *Roorda* excluded the potential income stream from the discretionary trust from the alimony calculation.[37] To distinguish cases like *Roorda,* the court in *D.L.* concluded that the consistent, historical pattern of income distributions to the husband that were made pursuant to the "standing instructions" would continue into the future.[38] Thus, the distributions of income created an income stream that could be included in the alimony calculation. The facts were simply too compelling for the court to ignore. It was readily apparent that these distributions would continue into the future and, in the court's opinion, it would be inequitable to the former wife to turn a blind eye to that fact.

B. Support Trusts

In contrast to a pure discretionary trust, a support trust is a discretionary trust that obligates the trustee to make distributions to the beneficiary for her support. In a support trust, the trustee could be required to distribute as much of the net income or principal as is necessary for the beneficiary's health, education, maintenance or support.[39] The operative word in this provision is "required." This language obligates the trustee to make distributions to the beneficiary for her support; thereby, removing the trustee's discretion over distributions necessary for the beneficiary's support.[40] Not only is the trustee's discretion over these distributions removed, but since the beneficiary of a support trust is entitled to receive these distributions, the beneficiary can compel distributions from the trustee of a support trust to the extent those distributions are necessary for her support.[41]

Because a support trust limits the trustee's discretion over distributions, a support trust is often in conflict with the grantor's intent in es-

---

37 *Id.*; *see* Roorda v. Roorda, 300 N.W. 294, 295, 297 (Iowa 1941).

38 *See D.L.*, 811 N.E.2d 1021-22, 1024.

39 *See* RESTATEMENT (SECOND) OF TRUSTS § 154 (1959); *see also* Tannen v. Tannen, 3 A.3d 1229, 1239 (NJ. Super. Ct. App. Div. 2010).

40 Though, as a practical matter, the trustee has discretion over the specific amount of a distribution that is necessary to "support" the beneficiary. *See* RESTATEMENT (SECOND) OF TRUSTS § 187 cmt. c (1959).

41 *See* RESTATEMENT (SECOND) OF TRUSTS § 128 cmt. e (1959); *Id.* § 187 cmt. e.

tablishing the trust, which is to establish a trust that will continue for generations under the guidance of a trustee acting in his own discretion. Despite this limitation, however, many estate planners implement the support standard as the default standard of discretion in their trust agreements. The reason for this use of the "health, education, maintenance and support" standard as the default standard in trust agreements is that these words are found in § 2041 of the Internal Revenue Code. In short, § 2041 provides that a beneficiary of a trust who is also a trustee of the trust is considered to have a general power of appointment over the trust unless his power to invade the trust is limited to distributions for his "health, education, support, or maintenance."[42] If a beneficiary has the power to invade the trust for amounts in excess of the amount necessary for his "health, education, support, or maintenance," then such beneficiary is deemed to have a general power of appointment, and the trust of which he is a beneficiary is included in his estate for estate tax purpose under § 2041.[43] In many cases, having a trust included in a beneficiary's estate defeats the purpose of the grantor establishing the trust in the first place. As a result, planners often use the support standard as the default standard in their documents because the Internal Revenue Code explicitly states that this standard does not vest a general power of appointment in the beneficiary. It is important to note, however, that it is the beneficiary as a trustee that cannot be vested with a general power of appointment. A co-trustee, for example, who does not have an interest in the trust may be vested with the power to make distributions to a beneficiary for any purpose without causing the trust to be included in the beneficiary's estate.

In addition to comporting with this "safe harbor" language of the Internal Revenue Code, there is another benefit to support trusts; specifically, that most creditors cannot compel distributions from a support trust even though the beneficiary has the power to compel distributions necessary for her support.[44] In other words, in the case of a support trust, the creditor does not step into the shoes of the beneficiary with respect to distributions from the trust for support. The public policy reason that creditors are not permitted to attach to distributions from a support trust is that the creditor would be attaching to funds earmarked for the beneficiary's support and, without those funds, the beneficiary may be left without the means to support himself.[45] However, in the case of a divorce, a line of cases exists that considers a former spouse as

---

42 I.R.C. § 2041(b)(1)(A).

43 *Id.* § 2041(a).

44 RESTATEMENT (SECOND) OF TRUSTS § 154 cmt. c (1959).

45 *See* Coverston v. Kellogg, 357 N.W.2d 705, 708 (Mich. Ct. App. 1984) (citing RESTATEMENT (SECOND) OF TRUSTS § 154 cmt. b (1959)).

an "exception creditor" who has certain rights to attach his or her former spouse's interest in a support trust.[46]

An example of such a case is *Dwight v. Dwight*.[47] In *Dwight*, the parties' separation agreement was incorporated into the terms of their divorce in 1990. The agreement contained a provision providing that the wife waived alimony unless and until the husband "receive[d] a substantial inheritance which increase[d] his income."[48] In 1992, the husband's parents established a support trust for his benefit with the following standard of discretion: the trustee shall pay the husband and his descendants "so much of the annual net income and principal of the trust property as the trustee may deem to be necessary or desirable for the support, comfort, maintenance, education or benefit of such beneficiary or beneficiaries."[49] The former wife filed a motion with the trial court to enforce the provision of the parties' separation agreement with respect to her husband receiving "a substantial inheritance" based on his interest in the trust his parents established for his benefit.[50] She claimed that the trust increased her former husband's income under the terms of the agreement and, thus, she should receive an alimony award based upon the potential distributions from the trust.[51] The trial court granted her motion, awarding monthly alimony.[52]

The former husband appealed the decision, arguing that his interest in the trust did not increase his income under the agreement because the trust's "payment of income and principal to him [was] not within his control but [was] wholly within the discretion of the trustee."[53] The husband also stressed that he had only received one distribution from the trust. The court, however, noted that despite the fact that the husband had only received one distribution from the trust, it was because he had directed the trustee not to make distributions to him and that, based upon the terms of the trust agreement, he "had access to additional funds if he needed or wanted them."[54] As such, the court upheld the trial court's determination to award alimony to the former wife because the trust represented a "substantial inheritance which 'increase[d]' [his] income."[55] Importantly, the court reasoned that the "slight uncertainty

---

46 *Coverston*, 357 N.W.2d at 709; *see also* RESTATEMENT (SECOND) OF TRUSTS § 157(a) (1959).

47 *See* Dwight v. Dwight, 756 N.E.2d 17 (Mass. App. Ct. 2001);.

48 *Id.* at 19.

49 *Id*. at 19-20.

50 *Id.* at 18-19.

51 *Id.*

52 *Id.* at 19.

53 *Id.* at 20-21.

54 *Id.*

55 *Id.* at 21.

of his access to income because of the discretion vested in the trustee . . . is not in these circumstances dispositive."[56]

This case demonstrates the risks of establishing a simple support trust for a child who may have exposure to an alimony obligation as a result of a divorce. In *Dwight,* the wife was successful in her request for alimony even though the husband's parents established the trust after the two parties divorced. Moreover, the trust had only made one distribution to the former husband. However, the reason the wife was successful in her claim that the husband received a "substantial inheritance which increase[d] his income[,]" is that the trustee of the trust at issue was not granted any discretion as to whether or not to make distributions from the trust for his support. Though the husband ordered the trustee not to make distributions, the trustee was obligated under the standard of discretion in the trust to make distributions to the husband for his support. In the eyes of the court, simply because the husband refused to receive distributions to which he was entitled did not demonstrate that he did not have access to the trust.[57] Stated a different way, it is the amount of discretion vested in the trustee that is determinative, not the amount or number of distributions that the beneficiary receives or requests.

II. The blending of discretionary and support trusts, and the resulting Restatement (Third)

Because of the trustee's limited discretion in support trusts as well as the rights of certain creditors to reach support trusts as *Dwight* demonstrates, estate planners typically include language of discretion in combination with language of support when drafting a discretionary trust; thus, blurring the line between the two types of discretionary trusts. An example of this blending of discretionary standards is as follows: The trustees may distribute to the beneficiary so much, all or none of the net income and principal of the trust as the trustees, *in their sole discretion*, deem necessary for beneficiary's health, education, maintenance or support. In contrast to a simple standard of support where the trustee is obligated to make distributions to the beneficiary for his support, a support standard blended with language of discretion vests the trustee with the discretion to determine whether distributions should be made to or for the beneficiary's support.[58]

---

56 *Id.*

57 *Id.* at 21.

58 A reasonableness standard is generally the only limitation to such a grant of discretion, meaning that so long as the trustee's determination to make or withhold a distribution is reasonable, courts will not interfere. *See* Restatement (Second) of Trusts § 187 cmt. e (1959).

With this blending of pure discretionary and support standards, courts are now faced with parsing out the terms of discretionary trusts to determine the rights of beneficiaries and creditors. In the case of divorcing spouses, this analysis is even more complex because courts may view the rights of a former spouse as an "exemption creditor" with rights different from the rights of a general creditor.[59] As a result of this complexity, the issue of whether a trust is purely discretionary or one of support has spurred a tremendous amount of litigation. The line between the two types of trusts has become so blurred that an additional term – the "hybrid trust" – has been created to define trusts that contain both discretionary language and support language, further confusing creditor rights with respect to discretionary trusts.[60]

Because hybrid trusts have generated such lengthy and costly litigation with results that many commentators view as arbitrary, recent model statutes and treatises have attempted to set forth new law that alters the existing law with respect to a creditor's right to attach a beneficiary's interest in a hybrid trust.[61] One of these treatises is the Restatement (Third), a treatise published in 2003 that purports to draw both on court decisions and statutes to provide a contemporary treatment of trust law. In the past, courts across the nation have been inclined to adopt the provisions of the prior Restatements of Trusts as accurate statements of law. However, the volumes of the Restatement (Third) that have been published intermittently over the past decade have not received the same wide-range acceptance.[62]

With respect to discretionary trusts, section 60 of the Restatement (Third) "departs significantly from prior Restatements" and abandons the distinction between discretionary trusts and support trusts with respect to creditor rights.[63] Instead of distinguishing between pure discretionary trusts and support trusts, section 60 defines support trusts as discretionary trusts with a standard; thus, eliminating the line of case law and prior Restatement positions with respect to creditor's rights to attach to support trusts. Specifically, by treating support trusts as discretionary trusts with a standard for the purposes of creditor rights, section 60 eliminates the prior Restatement's blanket prohibition of non-exception creditors – creditors other than a former spouse or child – from attaching to a beneficiary's interest in a support trust. In the prior Re-

---

59 *See* Coverston v. Kellogg, 357 N.W.2d 705, 709 (Mich. Ct. App. 1984).

60 *See* RESTATEMENT (THIRD) OF TRUSTS § 50 reporter's note on cmt. e (2003).

61 *See* Unif. Trust Code § 504(c) (2000). *See generally* RESTATEMENT (THIRD) OF TRUSTS §§ 50-60 (2003). See Millard, *supra* note 8, for a general background of creditor's rights under the Uniform Trust Code.

62 See Tannen, 3 A.3d at 1243.

63 RESTATEMENT (THIRD) OF TRUSTS § 60 reporter's note on cmt. a (2003).

statement, non-exemption creditors could not attach to a beneficiary's interest in a support trust because those funds were earmarked for the beneficiary's support.[64] Under section 60 of the Restatement (Third), however, a court may order payment from a support trust to a creditor after taking into account the beneficiary's "*actual* needs in maintaining a reasonable level of support, care, and education."[65] In other words, if the beneficiary is receiving support from other sources, then the court may order the trustee to make a distribution to the creditor because the distribution is not necessary for the beneficiary's actual support.

It is important to note that the non-exemption creditor would be compelling a distribution in excess of what the beneficiary himself could compel, as the beneficiary would not be able to compel a distribution if it was not necessary for his support. Because a non-exemption creditor could succeed in compelling a distribution in excess of the amount a beneficiary could compel from a support trust, section 60 of the Restatement (Third) eliminates the traditional view that a non-exception creditor of a beneficiary steps into the shoes of beneficiary and may only exercise those rights that the beneficiary may exercise.

With respect to exception creditors, such as a former spouse, the exception creditor arguably still stands in the shoes of the beneficiary when seeking to compel distributions from a support trust.[66] Whether the Restatement (Third) provides more expansive support for exemption creditors than prior Restatements for the inclusion of potential trust distributions in the alimony calculation is the subject of debate among commentators.[67] On the one hand, commentators argue that exception creditors, such as former spouses, hold the power to compel distributions from support trusts under common law and the Restatement (Second) of Trusts (the "Restatement (Second)").[68] These commentators argue that although section 60 may expand the rights of non-exception creditors, it does not alter the rights a former spouse held over a support trust under common law and the Restatement (Second).[69]

On the other hand, however, some commentators argue that although section 60 of the Restatement (Third) governs non-exception creditors' rights to discretionary trusts, a beneficiary's right to compel distributions from a discretionary trust is governed by section 50 of the

---

64 RESTATEMENT (SECOND) OF TRUSTS § 154 cmt. c (1959); *See* RESTATEMENT (SECOND) OF TRUSTS § 157 (1959).

65 RESTATEMENT (THIRD) OF TRUSTS § 60 cmt. c (2003) (emphasis added).

66 Millard, *supra* note 8, at 71.

67 *See id.* at 70.

68 *See id.* at 69, 71.

69 *See id.* at 71.

Restatement (Third).[70] These commentators argue that section 50 provides beneficiaries with greater power to compel distributions from a discretionary trust, which in turn provides greater rights to exception creditors to compel distributions from discretionary trusts.[71] This follows because a non-exception creditor, in the view of these commentators, stands in the shoes of the beneficiary when exerting their right to compel distributions.

This debate recently played out in the background of the appellate court's analysis of the facts presented in a recent case by the Supreme Court of New Jersey, *Tannen v. Tannen*.[72] Although the court sided with the latter group of commentators in stating that the non-beneficiary spouse likely had greater access to the trust at issue under the Restatement (Third), the court declined to adopt the Restatement (Third), relegating its analysis to dicta in the court's opinion.[73] The court's analysis, however, is of particular relevance to the impact of the evolving principles of trust law in the context of a discretionary trust in a divorce proceeding and helpful guidance for estate planners drafting trusts that may be the subject of divorce proceedings in the future.

III. *Tannen v. Tannen*: The Application of the Restatement (Third) to a Claim for Alimony from a Hybrid Trust

On its surface, the *Tannen* case presents an example of a "hybrid trust" that the court analyzes under both settled case law, the Restatement (Second) and the Restatement (Third) in order to determine whether the court should adopt the Restatement (Third) and the impact such an adoption would have on the outcome of the case. Because of the court's in-depth analysis of the issues presented, the case highlights not only the impact of the Restatement (Third) on existing trusts that may become the subject of a divorce, but also the issues going forward that estate planners must consider when drafting new trusts for their clients.

In *Tannen,* the Supreme Court of New Jersey affirmed the judgment of the Appellate Division in December 2011, based substantially on the reasons expressed in the Appellate Decision's written holding.[74] In the Appellate Division, Wendy Tannen (the "wife") appealed, among other things, a judgment of divorce entered by the trial court, which

---

70 *See* Gary R. Botwinick & Christopher J. Roman, *Maybe a Discretionary Trust isn't so Discretionary After All*, 202 N. J. L. J. 983, 983 (2010).

71 *Id*.

72 Tannen v. Tannen, 31 A.3d 621 (N.J. 2011), *aff'g* 3 A.3d 1229 (N.J. Super. Ct. App. Div. 2010).

73 *Tannen*, 3 A.3d at 1243.

74 *Tannen*, 31 A.3d at 621.

found that the income of a trust her parents' established for her benefit should be imputed to her for the purpose of calculating the alimony obligation of her husband.[75]

The trust at issue, the Wendy Tannen Trust, named the wife as the sole beneficiary and appointed her as co-trustee along with both of her parents.[76] The trust was a hybrid trust, employing a discretionary standard, subject to a "health, support, maintenance, education" standard of support.[77] The trust also contained language indicating that the wife could not "compel distributions of income and/or principal" as well as a typical "spendthrift" clause.[78]

The Appellate Division conducted a "review of the specific language" of the trust.[79] Based on the support standard, the wife's inability to compel distributions, and the spendthrift clause, the Appellate Division preliminarily found that the trust income was not an asset of the wife and, thereby, not imputable to her for the purposes of the alimony calculation.[80] However, the husband argued that according to section 50 of the Restatement (Third) the trust income stream was an asset belonging to the wife, and that the court could compel a distribution from the trust because the terms of the trust must be interpreted consistently with the evolving fiduciary obligations of trustees under the Restatement (Third).[81]

Although no reported New Jersey Appellate Division or Supreme Court case had relied upon section 50 of the Restatement (Third), the Appellate Division acknowledged that the Restatement (Third) reflected a change to existing law in that "a beneficiary of a discretionary trust has an enforceable interest in the benefits of the trust, even if the trustees are accorded the broadest discretion."[82] In contrast, under current law, New Jersey courts have "repeatedly recognized the broad discretion accorded trustees of a discretionary trust, and thereby, implicitly the limits upon a beneficiary's ability to compel a specific exercise of the trustee's discretion."[83]

By juxtaposing these two conflicting outcomes, the court identified that the Restatement (Third)'s abandonment of the distinction between discretionary trusts and support trusts increased not only the beneficiary's power to compel distributions of discretionary trusts, but also the

---

75 *See Tannen*, 3 A.3d at 1232.
76 *Id.* at 1233.
77 *See id.* at 1233.
78 *Id.* at 1233-34 (emphasis omitted).
79 *Id.* at 1238.
80 *See id.* at 1239.
81 *See Tannen,* 3 A.3d at 1239.
82 *Id.* at 1241.
83 *Id.* at 1240.

power of a soon-to-be ex-spouse to compel a distribution.[84] To further distinguish the two outcomes, the court noted that unlike the limited rights of a discretionary beneficiary recognized by the prior Restatement, under the Restatement (Third), "the benefits to which [Wendy] is entitled . . . depend on the terms of the discretion, including the proper construction of any accompanying standards."[85] The court determined that the import of this analysis is that the wife had a greater ability to enforce her rights to the benefits of the trust and, thereby, her soon-to-be ex-husband could also enforce her rights to the trust. It would then follow that potential future distributions from the trust should be included in the alimony calculation because the trust was an asset owned by the wife under state law.

After reaching this conclusion that the Restatement (Third) would result in a substantial change in the law, the Appellate Division declined to adopt section 50 of the Restatement (Third).[86] Instead, the court held that the trust income was not imputable to the wife for the purpose of alimony calculations and, in conclusion, noted that a determination to adopt the Restatement (Third) "would be more appropriately made by our Supreme Court."[87]

Accordingly, the Appellate Division held that the wife's "beneficial interest in the [Wendy Tannen Trust] was not an asset held by her" for purposes of the New Jersey alimony statute.[88] Therefore, the Court determined no income from the Wendy Tannen Trust should have been imputed to the wife in determining her husband's alimony obligation.[89] On December 8, 2011, the Supreme Court affirmed the Appellate Division's decision, declining to adopt section 50 of the Restatement (Third).

IV. Going Forward, Protecting the Beneficiaries of Discretionary Trusts from Potential Alimony Claims

Under the court's analysis in *Tannen*, the paramount issue in the case is whether the court should adopt the Restatement (Third) even though it presents a significant change from well-settled case law with respect to a beneficiary's right to compel distributions from a discretionary trust. While both the Appellate Division and Supreme Court of New Jersey declined to adopt the Restatement (Third) and, thereby, declined to provide the beneficiary-spouse in *Tannen* with, in the opinion

84 *See id.* at 1241.

85 *Id.* at 1242 (quoting Restatement (Third) of Trusts § 50(2) (2010)) (internal quotation marks omitted).

86 *Id.* at 1243.

87 *Id.*

88 *Id.* at 1243-44 (internal quotation marks omitted).

89 *Id.* at 1244.

of the Appellate Division, greater rights to compel distributions from the trust, the court did provide future non-beneficiary spouses in other states with a roadmap to argue that the Restatement (Third) applies in the context of an alimony claim. In particular, *Tannen* serves as a roadmap to argue that distributions from a discretionary trust should be included in the alimony calculation to a non-beneficiary spouse in states where (i) the Restatement (Third) has been adopted; (ii) the Restatement (Third) has not yet been considered or (iii) the Uniform Trust Code, which includes provisions similar to the Restatement (Third), has been adopted.[90]

Despite the expansion of a beneficiary's power to compel distributions from discretionary trusts in the Restatement (Third), a pure discretionary standard remains the best protection from the claim of an exception creditor, including a soon-to-be ex-spouse. Though the Restatement (Third) confirms that a "creditor of a trust beneficiary cannot compel the trustee to make discretionary distributions if the beneficiary personally could not do so," the Restatement (Third) also notes that "[i]t is rare . . . that the beneficiary's circumstances, the terms of the discretionary power, and the purposes of the trust leave the beneficiary so powerless."[91] In other words, the Restatement (Third) suggests that it is rare that a beneficiary would have no power at all to compel a distribution from a discretionary trust. However, as the *Roorda* case demonstrates, a discretionary trust with a pure discretionary standard may fit into that rare circumstance where the beneficiary is so powerless[92] – a positive result for a beneficiary involved in a divorce where the non-beneficiary is claiming alimony based on potential trust distributions after the divorce.

For estate planners, when drafting a pure discretionary standard for a trust, they must be careful not to inject any support language that will limit the trustee's absolute discretion over distribution decisions. The objective for the estate planner is to draft a standard of discretion broad enough to shield the trustee's distribution decisions from creditors while at the same limit the breadth of the standard of discretion for other estate planning purposes, such as limiting estate tax liability or the grantor's personal preference as to distributions. With that objective in mind, however, the estate planner must be aware that each injection of

---

90 See Unif. Trust Code § 504 (2010).

91 RESTATEMENT (THIRD) OF TRUSTS § 60 cmt. e (2003).

92 *See* Roorda v. Roorda, 300 N.W. 294, 295 (Iowa 1941) ("It has been frequently said of trusts of this nature that the right of the cestui que trust against the trustee, to recover the property, is the measure of the rights of the creditor as against the property in the hands of the trustee. Measured by this test it appears that in this case the cestui has no interest in the income or principal of the trust which may be subjected to his debts.") (citation omitted).

support language that limits the breadth of the standard of discretion can increase the potential for an alimony award based on future trust distributions.

An example of a contemporary pure discretionary standard that could protect the beneficiary-spouse from the non-beneficiary spouse's claim under the Restatement (Third) is the standard in *D.L.*[93] The trust in *D.L.* included the following language: "the disinterested trustees, in their uncontrolled discretion, shall pay to the [beneficiary] such amount or amounts from the net income and principal as the disinterested trustees, in their uncontrolled discretion, think advisable."[94] Although this standard of discretion did not insulate the trust from the claims of the non-beneficiary spouse, it failed because of the historical pattern of consistent distributions from the trust, not the trust's standard of discretion and the resulting power of the beneficiary-spouse to compel distributions. The court acknowledged inasmuch, finding that "the [beneficiary] does not have a present, enforceable right to use the principal of the trust . . . [r]ather, payments from principal to the beneficiaries are to be made, if at all, in the uncontrolled discretion of the trustees."[95]

In other words, the court determined that the beneficiary spouse had no power to compel distributions from the trust because the discretion over distributions was vested solely in the trustees. For the purposes of a beneficiary spouse defending a claim for alimony under the Restatement (Third), this conclusion would be an extremely important factor in demonstrating that the beneficiary spouse was "powerless" – in the words of the Restatement (Third) – over distribution decisions.[96]

Standards of pure discretion similar to those included in the trust in *D.L.* could be successful despite the Restatement (Third) for two reasons. First, the phrase "in their uncontrolled discretion," which is inserted twice into the *D.L.* standard of discretion, as well as other phrases of similar import, are commonly referred to as language of extended discretion and provide the trustees with an added layer of protection over distribution decisions.[97] With respect to language of extended discretion, at common law, a court could interfere with a trustee's distribution decision if the trustee acted unreasonably.[98] However, under section 187 of the Restatement (Second), when adjectives like

---

93 *See* D.L. v. G.L., 811 N.E.2d 1013, 1023 (Mass. App. Ct. 2004) (finding that discretionary trusts by their peculiar nature must be examined closely in order to determine if parties' interests are too remote or speculative for them to have power over distribution).

94 *Id.* at 1021 n.10.

95 *Id.* at 1023 (internal quotations omitted).

96 RESTATEMENT (THIRD) OF TRUSTS § 60, cmt. e (2003).

97 *D.L.*, 811 N.E.2d at 1021 n.10; *see also* Millard, *supra* note 8, at 71.

98 *See* Millard, *supra* note 8, at 69-70.

"sole," "absolute," "uncontrolled" and other words of extended discretion are included in the standard of discretion, courts were to dispense with the reasonableness standard and instead review distribution decisions under a less stringent standard – an abuse of discretion standard.[99]

Section 50 of the Restatement (Third) seems to remain consistent with the Restatement (Second) and the related line of cases: "a discretionary power conferred upon the trustee to determine the benefits of a trust beneficiary is subject to judicial control only to prevent misinterpretation or abuse of the discretion by the trustee." However, the comments to section 50 interchangeably refer to an abuse of power standard, a bad faith standard and a reasonableness standard.[100] This interchanging of standards in the comments suggests that the Restatement (Third) may apply a more stringent standard than the Restatement (Second) to the review of distribution decisions even as to standards with language of extended discretion. Nevertheless, including language of extended discretion in a pure discretionary trust provides the beneficiary with the best argument when faced with the Restatement (Third) and will make it more difficult for a court to conclude that the beneficiary has the power to compel distributions.

The second reason a standard of discretion similar to the one in *D.L.* may succeed in shielding future distributions from the trust in the alimony calculation is its use of a disinterested trustee as a check and balance to a beneficiary serving as trustee.[101] The check and balance system, particularly in light of section 60 of the Restatement (Third), would buttress the beneficiary's argument that he cannot compel distributions from the trust. By appointing a disinterested trustee, the argument that the beneficiary, as trustee, has sole control over discretionary distributions is obviated.

If instead of incorporating a disinterested trustee, the beneficiary was the sole trustee and held sole control over the distributions, the court may see the discretionary aspect of the standard as a sham because the beneficiary would be controlling the distributions. In the context of an alimony claim, the beneficiary-spouse would have difficulty arguing that she cannot compel future distributions from the trust when she, herself, is the sole trustee. The argument becomes tenuous under those circumstances. However, if a disinterested trustee is appointed as co-trustee with the beneficiary or as the sole trustee, the disinterested trustee's decision whether or not to make distributions would be reviewed under the traditional standards of review. If the trustee is truly disinterested, there would be little substance to the argument that the

---

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

100 RESTATEMENT (THIRD) OF TRUSTS § 50 cmt. b (2003).

101 *See D.L.*, 811 N.E.2d at 1023.

beneficiary has the power to compel distributions because she, herself, is the trustee.

Though prior Restatements have not addressed the situation where the beneficiary is the sole trustee of a discretionary trust, comment g of section 60 of the Restatement (Third) includes relevant language not included in the prior Restatement. Comment g provides that when "a beneficiary is trustee of the discretionary trust, with authority to determine his or her own benefits[,] . . . creditors are able to reach from time to time the maximum amount the trustee-beneficiary can properly take."[102] Comment g, however, provides an exception: "if the discretionary power is held jointly with another person who, in exercising the discretionary authority, has fiduciary duties to other beneficiaries of the trust."[103] Accordingly, comment g emphasizes the importance of appointing a disinterested trustee to either serve alone or as a buffer between the interested trustee and distribution decisions. Though no reported decision has cited to comment g in the context of an alimony claim, its presence should give planners pause when appointing the beneficiary of a discretionary trust as sole trustee. The more prudent course would be to appoint a disinterested trustee alone or, if the grantor prefers to involve the beneficiary in the administration of the trust, a disinterested trustee to serve as co-trustee of the trust with the beneficiary.

Appointing a disinterested trustee and including a pure discretionary standard with language of extended discretion will provide a beneficiary-spouse with a strong argument against future trust distributions being included in the alimony calculation. However, even the best designed discretionary trust is susceptible to an alimony claim if the trustees engaged in a consistent pattern of distributions to the beneficiary during his or her marriage which the beneficiary relies upon to support the marital lifestyle. Under such circumstances, the beneficiary's argument to the court that distributions from the trust will not continue into the future becomes difficult to defend. In cases where the beneficiary makes this argument despite consistent, historical distributions, judges are troubled by the inequity that would arise if the beneficiary were able to exclude these distributions from the alimony calculation. The perceived inequity arises from the fact that both spouses relied upon the distributions as a source of income during the marriage, but only one will benefit from the distributions after the divorce.

D.L. and *Tannen* are two cases that demonstrate the way in which a court may struggle with consistent, historical distributions from a discretionary trust despite its terms. In *D.L.*, the trust at issue vested complete discretion in the trustee over distributions from the trust, yet the

---

102 RESTATEMENT (THIRD) OF TRUSTS § 60 cmt. g (2003).

103 *Id.*

non-beneficiary spouse was successful in including the distributions from the trust in the alimony calculation.[104] The reason for her success was the consistent, historical patterns of distributions that flowed from the trust to support the parties' lifestyle during the marriage.[105] The historical distributions from the trust in *D.L.* weighed heavily against the beneficiary-spouse – even though the terms of the trust did not – because the spouses were receiving consistent distributions from the trust pursuant to "standing instructions."[106] Under these instructions, each year, on the same date, the same distribution was made from the trust to the beneficiary without the requirement of an explicit request from the beneficiary or an explicit determination from the trustee that a distribution was appropriate.

The *Tannen* case provides a similar example. After the court in *Tannen* set forth a detailed and thorough analysis of the Restatement (Third) and relevant New Jersey case law on the issue of including potential future distributions from a discretionary trust in the alimony calculation, the court included two paragraphs at the end of its analysis that demonstrates the court's struggle with its perceived inequity of not including these distributions in the alimony calculation. In the first of these two paragraphs, the court states the following:

> We held above that the judge improperly imputed income from the [trust] to [the wife] and also improperly ordered distributions of that income by the trust. *We hasten to add*, however, that in determining what [the wife's] 'actual need' is to maintain her lifestyle post-divorce, . . . the judge must consider the historical record of payments made by the [trust] on [the wife's] behalf.[107]

As the court's use of the phrase "hasten to add" demonstrates, historical distributions from a discretionary trust may trouble a court and create a pause in its analysis of the alimony award despite even strong conclusion regarding the terms of the trust. The historical distributions appeal to the judge's sense of equity in a divorce. In the paragraph following the above language, the court refers the trust's distributions to the wife that were relied upon by the parties to support their marital lifestyle and, specifically, their ability to reside in and maintain an extravagant home. The appellate court concluded that a judge "should not

---

104 D.L. v. G.L. 811 N.E.2d 1013, 1023-24 (Mass. App. Ct. 2004)

105 *Id.* at 1024

106 *Id.* at 1021-22.

107 Tannen v. Tannen, 3 A.3d 1229, 1246 (N.J. Super. Ct. App. Div. 2010) (emphasis added).

turn a blind eye to this reality. To do so would clearly result in a windfall to [the wife] and be entirely inequitable to plaintiff."[108]

As these two cases demonstrate, consistent, historical distributions from a discretionary trust to a beneficiary during his or her marriage complicates the alimony issue for the court. The court's analysis turns from an analysis of the terms of the trust to the equities of not including future distributions from the trust in the alimony complication. For the estate planner establishing a trust, it is important to advise the beneficiaries and trustees that standing instructions for distributions similar to those in *D.L.*, and consistent distributions to pay for the property taxes and maintenance of principal residence as in *Tannen*, should be avoided. These two cases illustrate the issues that arise if even the most protective discretionary trust has made distributions to support the marital lifestyle of the parties in a consistent manner.

V. Conclusion

Because of the high divorce rate in this country and the expanding use of trusts, trust law and divorce law have increasingly converged in the courtroom. Of particular importance to parents who are establishing these trusts for their children is whether or not distributions from these trusts will be included in the alimony calculation in the event a child divorces. Traditionally, pure discretionary trusts have successfully protected the beneficiary spouse from a former spouse seeking to include the stream of income from a discretionary trust in the alimony calculation. However, estate planners typically include language of discretion and support in their trusts, creating hybrid trusts, which some courts have determined as includable in the alimony calculation. Moreover, the Restatement (Third), as analyzed in the *Tannen* case, may enhance the non-beneficiary spouse's alimony claim against a beneficiary of a hybrid trust.

With these evolving trends in trust law in the context of divorce law, estate planners must be cognizant of additional protections they may be able to implement in their trust agreements to protect beneficiaries. First, a pure discretionary standard has been the most successful in shielding a discretionary trust from inclusion in an alimony calculation. Second, the use of a disinterested trustee lends support to the argument that a beneficiary has no power to compel distributions. Finally, avoiding standing instructions and other consistent, historical patterns of distributions provides the non-beneficiary spouse with one less argu-

108 *Id.*

ment that future distributions are certain to be made. With these suggestions in mind, estate planners can better protect their clients' beneficiaries from the evolving laws of trusts and divorce.