

Rights of a Trust Beneficiary's Creditors Under the Uniform Trust Code

Kevin D. Millard

Prepared for the ABA Section of Real Property, Trust & Estate Law Spring Symposium 2008

© 2008. All rights reserved.

Part One—Introduction...	1
1. Background on the Uniform Trust Code...	1
2. Organization of this Outline...	2
Part Two—UTC Provisions Affecting the Rights of Beneficiaries' Creditors..	3
3. Section 501—Creditor Rights in the Absence of a Spendthrift Provision..	3
4. Section 502—Spendthrift Protection..	5
5. Section 503—Spendthrift Exception Creditors...	6
6. Section 504—Discretionary Trusts..	9
7. Section 505—Self-Settled Trusts and Powers of Withdrawal..	14
8. Section 506—Mandatory Versus Discretionary Distributions and Overdue Distributions..	18
Part Three—Criticisms of the UTC Creditor Rights Provisions..	19
9. Background..	19
10. Does the UTC Give Creditors Greater Rights than they Had at Common Law?	20
11. Elimination of the Distinction Between Support and Discretionary Trusts..	23
12. Supplemental Needs Trusts and Special Needs Trusts..	34
13. Claims of Creditors in the Bankruptcy of a Trust Beneficiary..	38
14. Treatment of Trusts in Connection with Divorce...	40
15. The Argument that Creating a Trust in a UTC Jurisdiction is Malpractice...	40
16. Conclusion...	41

Part One—Introduction.

1. Background on the Uniform Trust Code.

1.1 The Uniform Trust Code¹ was approved by the National Conference of Commissioners on Uniform State Laws (NCCUSL) on August 3, 2000, and by the House of Delegates of the American Bar Association at its mid-year meeting in February, 2001. The UTC was amended in 2001, 2003, 2004, and 2005.²

1.2 At the time this outline is prepared, the UTC has been enacted in 20 jurisdictions (Alabama, Arkansas, the District of Columbia, Florida, Kansas, Maine, Missouri, Nebraska, New Hampshire, New Mexico, North Carolina, North Dakota, Ohio,

¹ UNIFORM TRUST CODE (2000) [hereinafter UTC].

² NCCUSL Drafts and Final Acts, University of Pennsylvania Law School, <http://www.law.upenn.edu/bll/archives/ulc/ulc.htm#uta>, visited March 13, 2008.

Oregon, Pennsylvania, South Carolina, Tennessee, Utah, Virginia, and Wyoming)³, and has been introduced in three other jurisdictions (Connecticut, Massachusetts, and Oklahoma).⁴

- 1.3 The provisions of the UTC concerning the rights of a trust beneficiary's creditors are contained mainly in article 5 of the UTC.
- 1.4 That issue—the rights of a beneficiary's creditors—has been one of four “hot button” issues in states considering the enactment of the UTC.⁵ Existing non-UTC American law on the rights of trust beneficiary creditors is highly diverse.⁶ As Prof. David M. English, the Reporter for the UTC, points out, the spendthrift trust is an American invention (England, where the trust was born, does not recognize spendthrift trusts), and the lack of a common English heritage for spendthrift protection may explain this diversity of United States law on creditor rights.⁷ In any event, the enactments of the UTC have reflected the existing diversity—the tendency is to modify the uniform provisions to conform them to prior, existing law and practice in the enacting jurisdiction.⁸

2. **Organization of this Outline.**

- 2.1 This outline first summarizes the UTC provisions on the rights of beneficiaries' creditors, the extent to which those provisions codify or modify the common law of trusts, and notes some of the modifications that have been made to the UTC in the enacting jurisdictions.

³ Uniform Trust Code Legislative Fact Sheet, National Conference of Commissioners on Uniform State Laws, http://nccusl.org/Update/uniformact_factsheets/uniformacts-fs-utc2000.asp, visited March 13, 2008.

⁴ UTCProject.org, enactments, <http://www.utcproject.org/utc/DesktopDefault.aspx?tabindex=2&tabid=50>, visited March 13, 2008.

⁵ David M. English, *Hot Button Issues Under the Uniform Trust Code*, American College of Trust and Estate Counsel 2007 Annual Meeting, Symposium 1 (2007). The other “hot button” issues are the settlor's power to consent to the beneficiaries' request to terminate an irrevocable trust, the court's power to remove the trustee, and the trustee's duty to inform and report to the beneficiaries. *Id.*

⁶ *Id.* at 5.

⁷ *Id.*

⁸ *Id.* See S. Alan Medlin, *The Impact of Significant Substantive Provisions of the South Carolina Trust Code*, 57 S.C. LAW REV. 137, 177 (Autumn 2007) (“The SCTC [South Carolina Trust Code] eliminates much, if not all, of the controversial UTC provisions—generally retaining, with some refinement, pre-SCTC South Carolina law.”); Suzanne Brown Walsh *et al.*, *What Is the Status of Creditors Under the Uniform Trust Code?*, 32 ESTATE PLANNING 29, 31 (“many states make changes to conform the UTC to their current law.”).

- (A) It should be kept in mind that, because of the diversity of state law on this subject, the “common law” on these issues may be “difficult to pin down.”⁹
- (B) In addition, case law on trusts is sparse in some jurisdictions. In fact, the original impetus for the UTC came from less-populated states with little trust law that wanted a code to fill the gaps in their common law. In those states, the courts and lawyers frequently look to the treatises by Scott¹⁰ and Bogert,¹¹ the Restatement (Second) of Trusts, and, more recently, to the still-in-process Restatement (Third) of Trusts when issues arise that have not previously been dealt with by case law.¹²
- 2.2 The outline next addresses some of the criticisms that have been leveled against the UTC and the responses to those criticisms.
- 2.3 Appendix A provides the reader with the text of the UTC provisions on the rights of beneficiaries’ creditors.
- 2.4 Appendix B summarizes the changes that have been made in the UTC provisions on creditors’ rights by the enacting jurisdictions.

Part Two—UTC Provisions Affecting the Rights of Beneficiaries’ Creditors.

3. Section 501—Creditor Rights in the Absence of a Spendthrift Provision.

- 3.1 Under UTC § 501, creditors may reach a beneficiary’s interest in the trust “[t]o the extent [the] beneficiary’s interest is not subject to a spendthrift provision.”¹³

⁹ Alan Newman, *Spendthrift and Discretionary Trusts: Alive and well Under the Uniform Trust Code*, 40 REAL PROP. PROB. TR. J. 567, 568 note 2 (Fall 2005).

¹⁰ AUSTIN WAKEMAN SCOTT & WILLIAM FRANKLIN FRATCHER, *THE LAW OF TRUSTS* (4th ed. 1987).

¹¹ GEORGE GLEASON BOGERT & GEORGE TAYLOR BOGERT, *THE LAW OF TRUSTS AND TRUSTEES* (rev. 2d ed. 1977).

¹² David M. English, *The New Mexico Uniform Trust Code*, 34 N.M. L REV. 1 (Winter 2004).

¹³ UTC § 501.

- (A) This language recognizes that a spendthrift provision may apply to the interests of some beneficiaries and not to the interests of other beneficiaries.¹⁴
- (B) The language also recognizes that the spendthrift provision may apply to part but not all of a beneficiary's interest; for example, the spendthrift provision may apply to a beneficiary's interest in income but not principal.¹⁵
- 3.2 To the extent spendthrift protection does not apply to a beneficiary's interest, "the court may authorize a creditor or assignee of the beneficiary to reach the beneficiary's interest by attachment of present or future distributions to or for the benefit of the beneficiary or other means."¹⁶
- 3.3 Note that this section does not authorize the creditor to reach the trust property; it is the beneficiary's interest in the trust, not the trust property, that is reachable by creditors.
- 3.4 In addition, in recognition of the fact that a proceeding against a beneficiary's trust interest in equitable in nature, section 501 expressly provides that "[t]he court may limit the award to such relief as is appropriate under the circumstances."¹⁷
- 3.5 This provision is in accord with the common law.¹⁸
- 3.6 In their enactments of the UTC:¹⁹
- (A) Maine modified section 501 to omit the language allowing a creditor to attach distributions made for the benefit of, rather than to, the beneficiary; and

¹⁴ UTC § 501 comment.

¹⁵ *Id.*

¹⁶ UTC § 501.

¹⁷ *Id.* See UTC § 501 comment.

¹⁸ RESTATEMENT (THIRD) OF TRUSTS § 56; RESTATEMENT (SECOND) OF TRUSTS § 147.

¹⁹ See Appendix B.

(B) Ohio omitted section 501 entirely.

4. **Section 502—Spendthrift Protection.**

4.1 Section 502 expressly makes spendthrift provisions valid and enforceable. The beneficiary of a spendthrift trust may not transfer the beneficiary's interest, and, subject to the provisions on exception creditors, described below, the beneficiary's creditors "may not reach the interest or a distribution by the trustee before its receipt by the beneficiary."²⁰ This is consistent with the common law.²¹

4.2 Under this provision, if a trustee makes a distribution to a third party for the benefit of the beneficiary, a creditor of the beneficiary may not reach the distribution because it was never received by the beneficiary.²²

4.3 A valid spendthrift provision must prohibit both voluntary and involuntary transfers of the beneficiary's interest.²³ That is, a provision that purports to prevent creditors from reaching a beneficiary's interest while allowing the beneficiary to transfer the interest voluntarily is not a valid spendthrift provision under the UTC.

(A) This is also consistent with the common law.²⁴

(B) In their enactments of the UTC, Kansas, Missouri, North Dakota, and Wyoming allow spendthrift provisions that restrains either the voluntary or involuntary transfer of the beneficiary's interest.²⁵ The Ohio version of the

²⁰ UTC § 502(c).

²¹ RESTATEMENT (THIRD) OF TRUSTS § 58(1); RESTATEMENT (SECOND) OF TRUSTS §§ 152-53.

²² *See Newman, supra* note 9, at 570.

²³ UTC § 502(a).

²⁴ RESTATEMENT (THIRD) OF TRUSTS § 58 cmt. b(2) ("A spendthrift trust is one that restrains both voluntary and involuntary alienation."); RESTATEMENT (SECOND) OF TRUSTS §§ 152(1) (a spendthrift trust is one in which "it is provided that his interest shall not be transferable by him *and* shall not be subject to the claims of his creditors") (Emphasis added).

²⁵ *See Appendix B*; KAN. STAT. ANN. § 58a-103(15) (defining "spendthrift provision" to be a trust term that restrains either the voluntary or involuntary transfer of the beneficiary's interest).

UTC allows a trust to restrain involuntary transfers but to allow voluntary transfers with the consent of a trustee who is not the beneficiary.²⁶

- (C) Note that even in a state the adopts the UTC without modification, the settlor may effectively give a beneficiary of a spendthrift trust the power to assign the beneficiary's interest by giving the beneficiary a power of appointment.

4.4 The UTC makes it easy to create spendthrift protection. It is sufficient for the trust simply to say that it is a spendthrift trust or to use words "of similar import."²⁷ This too is consistent with the common law.²⁸

5. **Section 503—Spendthrift Exception Creditors.**

5.1 Section 503 of the UTC creates three categories of exception creditors against whom spendthrift protection is not enforceable.

- (A) The first category of exception creditor is the beneficiary's spouse, child, or former spouse but only if he or she has a court order or judgement against the beneficiary for support or maintenance.²⁹

- (1) This exception is consistent with the majority rule³⁰ and both the Second and Third Restatements.³¹

²⁶ See Appendix B.

²⁷ UTC § 502(b).

²⁸ RESTATEMENT (THIRD) OF TRUSTS § 58 cmt. b(3); RESTATEMENT (SECOND) OF TRUSTS §§ 152 cmt. c.

²⁹ UTC § 503(b)(1).

³⁰ Robert T. Danforth, *Article Five of the UTC and the Future of Creditors' Rights in Trusts*, 27 CARDOZO L. REV. 2551, 2570 (April 2006) [hereinafter Danforth, *Article Five*].

³¹ RESTATEMENT (SECOND) OF TRUSTS § 157(a) (1959); RESTATEMENT (THIRD) OF TRUSTS § 59(a) (1999).

(2) Note that the exception is limited to orders or judgments for support or maintenance and therefore does not apply to the division of property in a beneficiary's divorce.³²

(B) The second category of exception creditor is "a judgment creditor who has provided services for the protection of a beneficiary's interest in the trust,"³³ such as a lawyer who represented the beneficiary in litigation concerning the trust.

(C) The third category of exception creditor is the state or federal government, but only "to the extent a statute of this State or federal law so provides."³⁴

5.2 An exception creditor may, despite an otherwise enforceable spendthrift provision, obtain an order "attaching present or future distributions to or for the benefit of the beneficiary."³⁵ Note that an exception creditor does not automatically have any right to reach trust property:

Only those distributions that would otherwise have been made by the trustee (such as a mandatory distribution of income or principal, or a discretionary distribution of income or principal that the trustee has otherwise decided to make) may be the subject of a court order directing them to be paid to the exception creditor. Thus, for example, if the trust is a discretionary trust, and the trustee determines in its discretion not to make a distribution, in most cases a creditor would be unable to force a distribution in satisfaction of its claim.³⁶

5.3 In recognition of the fact that a proceeding against a beneficiary's trust interest is equitable in nature, "[t]he court may limit the award to such relief as is appropriate under the circumstances."³⁷

³² See section 14 of this outline. For a general discussion of the treatment of trusts in divorce property divisions see Marc A. Chorney, *Interests in Trust in Divorce: What the Settlor Giveth the Divorce Court May Taketh Away*, 40TH ANN. HECKERLING INST. EST. PLAN Chapter 16 (2006).

³³ UTC § 503(b)(2).

³⁴ UTC § 503(b)(3).

³⁵ UTC § 503(c).

³⁶ Danforth, *Article Five*, *supra* note 30, at 2570-71.

³⁷ *Id.*

- 5.4 The concept of exception creditors is nothing new.³⁸ Indeed, the idea that there might be creditors who, on public policy grounds, are not barred by a spendthrift provision was reflected in the leading case on the validity of spendthrift provisions, which was decided in 1882: “The founder of this trust was the absolute owner of his property. He had the entire right to dispose of it . . . with such restrictions or limitations, not repugnant to law, as he saw fit to impose. . . . His intentions ought to be carried out, *unless they are against public policy.*”³⁹
- 5.5 Under the UTC, unlike the Restatements, a provider of necessities to the beneficiary is not an exception creditor.⁴⁰
- 5.6 The UTC also does not include tort claimants as exception creditors. The Restatements do not expressly create an exception for tort creditors, but indicate that public policy might support such an exception.⁴¹ A 1997 Mississippi case acknowledged an exception for tort creditors,⁴² but the case was promptly overturned legislatively.⁴³ Others cases have refused to recognize an exception for tort creditors.⁴⁴
- 5.7 A number of states that have enacted the UTC have modified section 503:⁴⁵

³⁸ Mary Louise Fellows & Gregory S. Alexander, *Forty Years of Codification of Estates and Trusts Law: Lessons for the Next Generation*, 40 GA. L. REV. 1049, 1073 (Summer 2006) (“UTC § 503 sets out the four traditional common law exceptions to the rule that a settlor can prevent creditors from reaching the interests of a trust beneficiary.” [Counting spouses and children as separate exception creditors.]).

³⁹ *Broadway Nat’l Bank v. Adams*, 133 Mass. 170, 174 (Mass. 1882) (emphasis added).

⁴⁰ See RESTATEMENT (SECOND) OF TRUSTS § 157(b) (1959); RESTATEMENT (THIRD) OF TRUSTS § 59(b) (1999).

⁴¹ RESTATEMENT (SECOND) OF TRUSTS § 157 cmt. a (“The interest of the beneficiary of a spendthrift trust or a trust for support may be reached in cases other than those herein enumerated, if considerations of public policy so require. Thus it is possible that a person who has a claim in tort against the beneficiary of a spendthrift trust may be able to reach his interest under the trust.”); RESTATEMENT (THIRD) OF TRUSTS § 59 cmt. a(2) (“the exceptions to spendthrift immunity stated in this Section are not exclusive. Special circumstances or evolving policy may justify recognition of other exceptions . . .”).

⁴² *Sligh v. First Nat. Bank*, 704 So. 2d 1020 (Miss. 1997).

⁴³ MISS. CODE ANN. § 91-9-503.

⁴⁴ See *Duvall v. McGee*, 826 A.2d 416 (Md. App. 2003); *Scheffel v. Krueger*, 782 A.2d 410 (N.H. 2001).

⁴⁵ See Appendix B.

- (A) Arkansas, Kansas,⁴⁶ and Oregon omit section 503 entirely, so that there are no exception creditors in those states. Maine replaced the text of section 503 with a statement to the effect that there are no exception creditors.
- (B) Tennessee omits as exception creditors both children and spouses, as well as judgment creditors who provided services for the protection of a beneficiary's interest.
- (C) Ohio excludes former spouses, but not current spouses, as exception creditors, and also limits the exception to trusts allowing distributions for the beneficiary's support or providing mandatory distributions.
- (D) New Hampshire modified the exception for spouses to limit it to a judgment or court order that "expressly specifies the alimony amount attributable to the most basic food, shelter, and medical needs of the spouse or former spouse."
- (E) The District of Columbia, North Carolina, South Carolina, Utah, Virginia, and Wyoming retain the exception for a child's claim for support but exclude spouses and former spouses as exception creditors.

6. Section 504—Discretionary Trusts.

- 6.1 The general rule under the UTC is that a beneficiary's creditors may not reach an interest in a discretionary trust:

whether or not a trust contains a spendthrift provision, a creditor of a beneficiary may not compel a distribution that is subject to the trustee's discretion, even if:

- (1) the discretion is expressed in the form of a standard of distribution; or
- (2) the trustee has abused the discretion.⁴⁷

⁴⁶ This is likely a change in Kansas law. David M. English, *The Kansas Uniform Trust Code*, 51 KAN. L. REV. 311, 334 (February 2003) ("This likely represents a change in Kansas law. While the Kansas courts have not ruled specifically on whether exceptions to a spendthrift provision exist, such exceptions are well-established in the Restatement [Second], on which the Kansas courts have traditionally relied.") (footnote omitted).

⁴⁷ UTC § 504(c).

- 6.2 As discussed below, this general rule is subject to an exception for certain claims of spouses and children.
- 6.3 Under traditional analysis, a beneficiary's creditor could not reach a discretionary trust because of the nature of the beneficiary's interest. Because the trustee had discretion to make or withhold distributions, and the beneficiary could not force the trustee to exercise its discretion to make a distribution, the beneficiary's creditor, standing in the beneficiary's shoes, was no better off and also could not force distributions from the trust.⁴⁸ Several points should be noted about this traditional analysis:
- (A) Protection from the beneficiary's creditors was greatest if the trustee had broad discretion. The best protection was provided by a purely discretionary trust, and especially if the trust included language of "extended discretion" such as "the trustee may distribute to the beneficiary so much of the trust property as the trustee, *in its sole discretion*, may determine."
 - (B) A trust that gave the trustee discretion but also included a standard for making distributions (such as the tax-motivated "ascertainable standard" of health, education, maintenance, and support⁴⁹) was somewhere in between a trust with mandatory distributions and a purely discretionary trust.
 - (C) If the trust was characterized as a "support trust," such as a trust from which the trustee was required to make distributions for the beneficiary's support, creditors whose claims were based on having provided support to the beneficiary could reach the trust⁵⁰ but other creditors could not.⁵¹
 - (D) The theory that a creditor could not reach the trust because the creditor stood in the shoes of the beneficiary and the beneficiary could not force distributions from the trust was flawed, because no matter how broadly

⁴⁸ RESTATEMENT (SECOND) OF TRUSTS § 155(1) and cmt. b ("the 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.").

⁴⁹ INTERNAL REVENUE CODE OF 1986, as amended [hereinafter IRC] § 2041(b)(1)(A).

⁵⁰ RESTATEMENT (SECOND) OF TRUSTS § 157(b).

⁵¹ RESTATEMENT (SECOND) OF TRUSTS § 154.

worded the trustee's discretion was, it was always subject to review by a court for abuse.⁵²

- 6.4 The UTC decouples the rights of a beneficiary's creditors from the beneficiary's power to enforce the trust.
- (A) Under UTC § 504(b), quoted above, creditors (other than exception creditors, discussed below) are simply prohibited from reaching the trust regardless of whether the trust is purely discretionary or imposes a standard for distributions, and even if the trustee has abused its discretion.
 - (B) At the same time, section 504 expressly provides that it "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."⁵³
 - (C) Much of the criticism of the UTC's handling of creditor rights stems from a failure to appreciate this decoupling of creditor rights and the beneficiary's power to enforce the trust.
- 6.5 The UTC also, for purposes of creditor rights but not for purposes of the beneficiary's power to enforce the trust, eliminates the traditional distinction between discretionary and support trusts.
- (A) All trusts in which the trustee has discretion over whether to make distributions are treated as discretionary trusts for purposes of creditor rights, regardless of whether they are purely discretionary or impose a standard.
 - (B) Whether a trust is purely discretionary or includes a standard, and the breadth of the trustee's discretion, will continue to be relevant for purposes of the beneficiary's right to enforce the trust, but are not relevant for purposes of determining the rights of the beneficiary's creditors, other than exception creditors as discussed below.

6.6 Discretionary trust exception creditors.

⁵² Danforth, *Article Five*, *supra* note 30, at 2581 ("An essential principle of the common law of trusts is that a trustee's exercise of discretion is always subject to judicial review, no matter how broadly the trustee's discretion may be described.") (footnote omitted); RESTATEMENT (THIRD) OF TRUSTS § 50 cmt. c; RESTATEMENT (SECOND) OF TRUSTS § 187 cmt. k; BOGERT, *supra* note 11, § 560.

⁵³ UTC § 504(d).

- (A) The UTC creates an exception to the general rule that creditors may not reach a beneficiary's interest in a discretionary trust. The exception applies if all of these conditions are present:
- (1) The creditor is a spouse (or former spouse) or child of the beneficiary;
 - (2) The spouse or child has a judgment or court order;
 - (3) The judgement or court order is for support or maintenance of the spouse or child; and
 - (4) The trustee either has not complied with a standard for distribution or has abused its discretion.⁵⁴
- (B) Even where the exception applies, it does not give the spouse or child unrestricted access to the trust; rather, the court is to order the trustee to pay to the spouse or child "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."⁵⁵

6.7 There is considerable case law support for an exception for child support and alimony if the trust is a support trust, but little authority for such an exception if the trust is a purely discretionary trust.⁵⁶

6.8 Most of the states that have enacted the UTC have modified section 504.⁵⁷ For example:

- (A) The District of Columbia, Oregon, and Kansas omit section 504 entirely.
- (B) Arkansas, Florida, Maine, Missouri, Tennessee, and Wyoming omit subsection (c), thus eliminating all exception creditors in the context of a discretionary trust.

⁵⁴ UTC § 504(c).

⁵⁵ UTC § 504(c)(2).

⁵⁶ Danforth, *Article Five*, *supra* note 30, at 2578.

⁵⁷ *See* Appendix B.

- (C) North Carolina, South Carolina, Virginia, and Wyoming limit the exception to support claims of children, excluding claims of spouses and former spouses.
- (D) New Hampshire modified the exception for spouses to limit it to a judgment or court order that “expressly specifies the alimony amount attributable to the most basic food, shelter, and medical needs of the spouse or former spouse.”
- (E) Ohio allows the settlor to avoid the exception for claims of a child or spouse by explicitly providing in the trust that the beneficiary’s child or spouse, or both, may not benefit from the trust. Ohio also added to its trust code the concept of a “wholly discretionary trust,” which is a trust that grants the trustee extended discretion and does not include any standards for distributions, over which the beneficiary does not have a withdrawal power, and of which the beneficiary is not a trustee.⁵⁸ No creditors may reach a beneficiary’s interest in a wholly discretionary trust, nor any distribution from a wholly discretionary trust before it is received by the beneficiary.⁵⁹

6.9 A 2004 amendment to the UTC added a provision to address a potential tax problem. Trusts, such as credit-shelter or by-pass trusts, are frequently drafted to make a beneficiary the trustee. To prevent the inclusion of the trust property in the beneficiary-trustee’s gross estate for federal estate tax purposes, the trustee’s discretion to make distributions “is limited by an ascertainable standard relating to the health education, support, or maintenance”⁶⁰ of the beneficiary-trustee. A comment to the Restatement (Third) of Trusts § 60 provides that the creditors of a beneficiary who is also a trustee may reach the beneficiary’s interest in the trust.⁶¹ The original UTC did not specifically address this issue. Because the common law of trusts supplements the UTC,⁶² subsection 504(e) was added to the UTC to prevent the Restatement comment from applying in a UTC state. Under that subsection, the creditors of a beneficiary-trustee may not reach the beneficiary-

⁵⁸ ORC § 5801.01(Y).

⁵⁹ ORC § 5805.03.

⁶⁰ IRC § 2041(b)(1)(A).

⁶¹ RESTATEMENT (THIRD) OF TRUSTS § 60 cmt. g (2003).

⁶² UTC § 106.

trustee's interest, nor compel distribution to the beneficiary-trustee, if the trustee's discretion is limited by an ascertainable standard.⁶³ The term "ascertainable standard" is defined to have the same meaning that it does for federal transfer tax purposes.⁶⁴

7. **Section 505—Self-Settled Trusts and Powers of Withdrawal.**

7.1 The UTC follows the general rules concerning the rights of creditors of a settlor who retains a beneficial interest in the trust, or the power to revoke the trust, and rejects the approach of the states that have enacted self-settled asset protection trust legislation.

- (A) During the lifetime of the settlor of a revocable trust, the settlor's creditors may reach the trust property.⁶⁵ At common law, a creditor could not reach a power of revocation,⁶⁶ but the modern rule is to the contrary.⁶⁷ In the vast majority of revocable trusts, the settlor retains a beneficial interest in the trust that can be reached by his or her creditors, so that it does not matter whether creditors could independently reach the power of revocation.
- (B) The creditors of the settlor of an irrevocable trust who is also a trust beneficiary may reach the maximum amount that could be distributed to the settlor-beneficiary.⁶⁸ This is the common law rule.⁶⁹ Although this rule

⁶³ UTC § 504(e).

⁶⁴ UTC § 103(2).

⁶⁵ UTC § 505(a)(1).

⁶⁶ RESTATEMENT (SECOND) OF TRUSTS § 330 cmt. o ("Unless it is otherwise provided by statute a power of revocation reserved by the settlor cannot be reached by his creditors. . . . they cannot compel him to revoke the trust for their benefit.").

⁶⁷ RESTATEMENT (THIRD) OF TRUSTS § 25 cmt. e ("property held in [a revocable] trust is subject to the claims of creditors of the settlor or of the deceased settlor's estate if the same property belonging to the settlor or the estate would be subject to the claims of the creditors, taking account of homestead rights and other exemptions.").

⁶⁸ UTC § 505(a)(2).

⁶⁹ RESTATEMENT (SECOND) OF TRUSTS § 156; RESTATEMENT (THIRD) OF TRUSTS § 60 cmt. f.

has received criticism in the recent past,⁷⁰ it remains the majority rule for now, but the trend in recent years has been to legislatively authorize self-settled asset protection trusts.⁷¹

(C) At the death of the settlor of a revocable trust, the remaining trust property is subject to “claims of the settlor’s creditors, costs of administration of the settlor’s estate, the expenses of the settlor’s funeral and disposal of remains, and [statutory allowances] to a surviving spouse and children”⁷² but only to the extent that the probate estate is insufficient to meet those obligations and subject to the settlor’s right to direct the source of payments.⁷³

7.2 Despite the UTC’s rejection of self-settled asset protection trusts, the UTC is not inherently incompatible with that concept, and a few of the states that have adopted the UTC also recognize self-settled asset protection trusts.⁷⁴

7.3 These rules for self-settled trusts apply to a limited extent to the holder of a power of withdrawal over a trust created by a third party.

(A) Holding a power of withdrawal over trust property is functionally equivalent to being the settlor of a revocable trust of the property subject to the power. Therefore, the UTC treats the power-holder as if he or she were the settlor of a revocable trust—that is, property that the power-holder could withdraw is subject to the claims of the power-holder’s creditors.⁷⁵

⁷⁰ See Adam J. Hirsch, *Fear Not the Asset Protection Trust*, 27 CARDOZO L. REV. 2685 (April 2006); Jeffrey A. Schoenblum, *In Search of a Unifying Principle for Article V of the Uniform Trust Code: A Response to Professor Danforth*, 27 CARDOZO L. REV. 2609 (April 2006); Robert T. Danforth, *Rethinking the Law of Creditors’ Rights in Trusts*, 53 HASTINGS L.J. 287 (2002).

⁷¹ See Richard W. Nenko, *Planning With Domestic Asset-Protection Trusts: Part I*, 40 REAL PROP. PROB. TR. J. 263 (Summer 2005); Richard W. Nenko, *Planning With Domestic Asset-Protection Trusts: Part II*, 40 REAL PROP. PROB. TR. J. 477 (Fall 2005)

⁷² UTC § 505(a)(3).

⁷³ *Id.*

⁷⁴ See MO. REV. STAT. 456.1-505(3) (2005); UTAH CODE ANN. 25-6-14 (amended 2003 & 2004).

⁷⁵ UTC § 505(b)(1).

- (B) If the power of withdrawal is one that lapses, such as a Crummey⁷⁶ withdrawal power, then this treatment applies while the power remains exercisable, but when the power lapses, the power-holder continues to be treated as the settlor only to the extent that the value of the property as to which the power lapsed exceeded a certain amount.⁷⁷ That amount is the greater of:
- (1) The amount that can lapse without being treated as a release of a general power of appointment for federal transfer tax purposes—the greater of \$5,000 or 5% of the value of the property out of which an exercise of the power could have been satisfied;⁷⁸ or
 - (2) The amount of the gift tax annual exclusion (currently \$12,000).⁷⁹
- (C) As a result, if a trust contains Crummey powers that do not exceed these limits, then the trust property will be subject to the power-holders' creditors while the powers remain exercisable, but not after the powers lapse. Because Crummey powers typically lapse at the end of a relatively short time period, such as 30 days, it will be difficult (but not impossible) as a practical matter for a creditor to reach the trust property. If the trust uses “hanging” powers, on the other hand, the amount of the power that hangs and remains exercisable will remain exposed to the creditors of the power-holder until the hanging portion lapses.

7.4 It is difficult to say whether this treatment of the holder of a power of withdrawal as the settlor of the trust is consistent with the common law, because non-UTC law on this point is not uniform.⁸⁰ There is some case law that a presently exercisable but unexercised general power of appointment may not be reached by

⁷⁶ See *Crummey v. Commissioner*, 397 F.2d 82 (9th Cir. 1968).

⁷⁷ UTC § 505(b)(2).

⁷⁸ IRC §§ 2041(b)(2) and 2514(e).

⁷⁹ IRC § 2503(b).

⁸⁰ Newman, *supra* note 9, at 591-92.

creditors,⁸¹ but the Restatement (Third) of Trusts⁸² and federal bankruptcy law⁸³ are to the contrary.

7.5 Several enacting states have modified UTC section 505(b) concerning powers of withdrawal.⁸⁴ For example:

(A) Under the Wyoming UTC, the holder of a power of withdrawal ceases to be treated as the settlor with respect to property subject to the power when the power lapses, is released, or is waived, regardless of the amount subject to the power.

(B) The North Carolina UTC provides that the lapse, release, or waiver of a power of withdrawal does not cause the power-holder to be treated as a settlor of the trust.

8. **Section 506—Mandatory Versus Discretionary Distributions and Overdue Distributions.**

8.1 As discussed above, a creditor (other than an exception creditor) of a beneficiary of a spendthrift trust may not reach a distribution until it is actually received by the beneficiary.⁸⁵ The UTC prevents a trustee from collaborating with a beneficiary to avoid a creditor by withholding a mandatory distribution. The creditor can reach a mandatory distribution if it has not been made “within a reasonable time after the designated distribution date.”⁸⁶

8.2 The term “mandatory distribution” is defined to mean a distribution (of income or principal) “which the trustee is required to make to a beneficiary under the terms of the trust, including a distribution upon termination of the trust.”⁸⁷ The term expressly does not include “a distribution subject to the exercise of the trustee’s discretion even if (1) the discretion is expressed in the form of a standard of

⁸¹ See *Univ. Nat’l Bank v. Rhoadarmer*, 827 P.2d 561 (Colo. App. 1991).

⁸² RESTATEMENT (THIRD) OF TRUSTS § 56 cmt. b.

⁸³ See 11 U.S.C.S. § 541(a) and (b).

⁸⁴ See Appendix B.

⁸⁵ UTC § 502(c).

⁸⁶ UTC § 505(b).

⁸⁷ UTC § 505(a).

distribution, or (2) the terms of the trust authorizing a distribution couple language of discretion with language of direction.”⁸⁸

- 8.3 The comment to section 505 notes that trusts sometimes “couple language of discretion with language of direction”⁸⁹:

An example of such a provision is “my trustees shall, in their absolute discretion, distribute such amounts as are necessary for the beneficiary’s support.” Despite the presence of the imperative “shall,” the provision is discretionary, not mandatory. For a more elaborate example of such a discretionary “shall” provision, see Marsman. Nasca, 573 N.E. 2d 1025 (Mass. Ct. App. 1991).⁹⁰

- 8.4 Lawyers frequently and habitually use “shall” to mean different things, one of which is “may,”⁹¹ and the UTC comment simply recognizes this common drafting problem.

- 8.5 Common law rule.

- (A) This provision of the UTC is in accord with the Restatement (Third) of Trusts.⁹²
- (B) The Restatement (Second) of Trusts supports the concept that delayed distributions of principal may be reached⁹³ but does not seem to support

⁸⁸ *Id.*

⁸⁹ UTC § 505 cmt.

⁹⁰ *Id.*

⁹¹ BRYAN A. GARNER, A DICTIONARY OF MODERN LEGAL USAGE 939-42 (2d ed. 1995) (“courts in virtually every English-speaking jurisdiction have held—by necessity—that *shall* means *may* in some contexts and vice versa.”) (emphasis in original.)

⁹² RESTATEMENT (THIRD) OF TRUSTS § 58 cmt. d.

⁹³ RESTATEMENT (SECOND) OF TRUSTS § 153(2) and cmt. c. (“If a beneficiary is entitled to have the principal paid or conveyed to him immediately or at any time he may call for it, a restraint on alienation of his interest is invalid.”).

the concept that delayed distributions of income may be reached.⁹⁴ There is little case law.⁹⁵

- (C) In any event, it seems hard to justify a distinction between overdue income and principal distributions, and the rule of the Restatement (Third) of Trusts and the UTC makes sense on policy grounds.

Part Three—Criticisms of the UTC Creditor Rights Provisions.

9. Background.

9.1 The UTC, and especially its provisions on the rights of beneficiaries' creditors, have come under sharp attack from a small but vociferous group of practitioners.⁹⁶ The critics take the position that the UTC dramatically reduces the creditor protection traditionally available to spendthrift and discretionary trusts.

9.2 The responses to these critics have been equally sharp and have been unusually caustic for writing on an academic subject.⁹⁷ For example:

- (A) “Many of the criticisms are based on misinterpretations of the UTC, a disregard of pertinent UTC provisions, or a misunderstanding of existing law.”⁹⁸
- (B) “[T]he primary criticisms appeared in a three part diatribe published in late 2004”⁹⁹

⁹⁴ RESTATEMENT (SECOND) OF TRUSTS § 152 cmt. h (“A spendthrift trust protects income which has been received by the trustee but has not been paid by him to the beneficiary.”).

⁹⁵ RESTATEMENT (THIRD) OF TRUSTS § 58 cmt. d.

⁹⁶ See Mark Merric & Steven J. Oshins, *Effect of the UTC on the Asset Protection of Spendthrift Trusts*, 31 EST. PLAN. 375 (2004); Mark Merric & Steven J. Oshins, *UTC May Reduce the Asset Protection of Non-Self-Settled Trusts*, 31 EST. PLAN. 411 (2004); Mark Merric & Steven J. Oshins, *How Will Asset Protection of Spendthrift Trusts Be Affected by the UTC?*, 31 EST. PLAN. 478, (2004) [hereinafter Merric & Oshins, *Spendthrift Trusts*]; Mark Merric *et al.*, *Malpractice Issues and the Uniform Trust Code*, 31 EST. PLAN. 586 (2004) [hereinafter Merric, *Malpractice*]; Mark Merric & Douglas W. Stein, *A Threat to All SNTs*, 143 TR. & EST. 38 (2004); Mark Merric *et al.*, *The Uniform Trust Code: A Divorce Attorney's Dream*, J. PRAC. EST. PLAN., Oct.-Nov. 2004.

⁹⁷ Danforth, *Article Five*, *supra* note 30, at 2552-53 (“Article Five of the UTC—concerning creditors’ rights—has generated a veritable war of words . . .”).

⁹⁸ Walsh *et al.*, *supra* note 8, at 31.

⁹⁹ John K. Eason, *Policy, Logic, and Persuasion in the Evolving Realm of Trust Asset Protection*, 27 CARDOZO L. REV. 2621,2638 (April 2006).

- (C) “Mr. Merric’s article contains numerous unsupported statements, mischaracterizations and misinformation about the UTC and about American trust law in general.”¹⁰⁰
- (D) “Several articles take the position that the Uniform Trust Code reduces the asset protection benefits of trusts. The authors’ arguments are based on misinterpretations of the Uniform Trust Code and case law, and can safely be ignored.”¹⁰¹

9.3 Some of the criticisms of the UTC creditor rights provisions have already been addressed. This section of the outline expands on that discussion.

10. **Does the UTC Give Creditors Greater Rights than they Had at Common Law?**

10.1 The critics argue that the UTC weakens traditional spendthrift protection by giving creditors greater rights than they had at common law and by recognizing exception creditors. The critics assert that “[w]hile exception creditors had no claim against a discretionary trust under common law, all exception creditors would be allowed to directly attach the assets of a discretionary trust under the UTC”¹⁰²

10.2 This assertion is incorrect:

an exception creditor’s remedies [under the UTC] are quite limited. . . . [T]he exception creditor’s remedy is to attach the beneficiary’s interest, not the assets of the trust. Moreover, if the beneficiary’s interest is discretionary, except in the rare case in which a child or spouse is able to establish an abuse of discretion under section 504(c), if the trustee in its discretion withholds distributions to the debtor beneficiary, then the creditor will be entitled to nothing.¹⁰³

¹⁰⁰ Danforth, *Article Five*, *supra* note 30, at 2552 (footnote omitted).

¹⁰¹ Keith A. Herman, *Asset Protection under the New Missouri Uniform Trust Code*, 62 J. Mo. B. 196, 196 (July/August, 2006) (footnote omitted).

¹⁰² Merric & Oshins, *Spendthrift Trusts*, *supra* note 96, at 484.

¹⁰³ Danforth, *Article Five*, *supra* note 30, at 2571-72 (footnote omitted).

- 10.3 The critics seem to believe that by codifying the list of exception creditors, the legislature will be encouraged to expand the list.¹⁰⁴
- (A) This is a strikingly peculiar argument.
 - (B) Consideration of which, if any, creditors should be included in the list of exception creditors will of necessity be one of the considerations when a state enacts the UTC.
 - (C) The experience in the states that have enacted the UTC shows that legislatures are in fact inclined to restrict, or even eliminate, rather than expand, the list of exception creditors.¹⁰⁵
 - (D) If a state legislature proposes to expand its state's list of exception creditors in the future, there is no reason to believe that the proposal would be subject to any less scrutiny than the UTC is now receiving in states where it is introduced. And, of course, a state legislature may add to its list of exception creditors regardless of whether the UTC is in effect in that state.
- 10.4 The critics also believe that the list of exception creditors in a UTC state may be expanded by the court.¹⁰⁶ On this point the critics are simply wrong. The UTC provides that a creditor may not reach a beneficiary's interest or a distribution "except as otherwise provided in this [article]."¹⁰⁷ Consequently, section 503's list of exception creditors is exclusive and may be expanded only by the legislature, not by the courts.¹⁰⁸

¹⁰⁴ Merric & Oshins, *Spendthrift Trusts*, *supra* note 96, at 484.

¹⁰⁵ *See* Appendix B.

¹⁰⁶ Merric & Oshins, *Spendthrift Trusts*, *supra* note 96, at 484 ("future exception creditors may now be added both judicially and legislatively").

¹⁰⁷ UTC § 502(c). *Compare* RESTATEMENT (THIRD) OF TRUSTS § 59 cmt. a(2) ("The exceptions to spendthrift immunity stated in this Section are not exclusive. Special circumstances or evolving policy may justify recognition of other exceptions . . .").

¹⁰⁸ *See* *Sheffel v. Krueger*, 782 A.2d 410, 412 (N.H. 2001) (refusing to create a judicial exception to spendthrift protection for tort creditors, because "Where the legislature has made specific exemptions, we must presume no others were intended."); William H. Lyons & John M. Gradwohl, *Discretionary Trusts, Support Trusts, Discretionary Support Trusts, Spendthrift Trusts, and Special Needs Trusts Under the Nebraska Uniform Trust Code*, 86 NEB. L. REV. 231, 271 (2007) ("once a state has adopted a statute dealing with such exceptions, addition of exceptions will have to come from the legislature."); Eason, *supra* note 99, at 2651; Danforth, *Article Five*, *supra* note 30, at 2573.

10.5 For discretionary trusts, the UTC may strengthen creditor protection in one respect and may weaken it in another.

(A) An exception creditor may reach a discretionary trust only if the trustee “has not complied with a standard of distribution or has abused a discretion.”¹⁰⁹ Just as it is extremely difficult for a beneficiary to force a distribution from a discretionary trust on the ground that the trustee has abused its discretion, it will be extremely difficult for a creditor of the beneficiary to succeed in establishing an abuse of discretion.¹¹⁰

(B) The UTC weakens creditor protection in some states by including the spouse and child exception creditor provision:

Although there is substantial case law supporting the proposition that a child, spouse, or former spouse may compel distributions from a trust for the support of the beneficiary, there is only modest support for the proposition that such a claimant can compel distributions from a wholly discretionary trust. Thus, states adopting section 504(c) may be changing their law in this respect.¹¹¹

(C) That was the result in Nebraska: the Nebraska UTC “clearly changes the prior Nebraska rule that creditors of a beneficiary of a pure discretionary trust could not reach the beneficiary’s interest in the trust for any reason.”¹¹²

(D) This is of course a public policy issue with which some states adopting the UTC will agree and others will not.¹¹³ Even in states that retain the exception, it will still be very difficult, as noted above, for an exception

¹⁰⁹ UTC § 504(c).

¹¹⁰ Danforth, *Article Five*, *supra* note 30, at 2577.

¹¹¹ Danforth, *Article Five*, *supra* note 30, at 2578 (footnotes omitted). See Newman, *supra* note 9, at 589.

¹¹² Lyons & Gradwohl, *supra* note 108, at 256.

¹¹³ *Id.* (“the Nebraska UTC position is consistent with the majority rule in other states and, like the similar change in the law of spendthrift trusts, reflects a proper public policy balance between a person’s marital obligations and a settlor’s interest in protecting a beneficiary from claims of creditors.”); Eason, *supra* note 99 at 2643 (“the UTC position simply represents a logical implementation of a public policy choice favoring a class of dependent creditors over a settlor’s protective intentions.”).

creditor of a beneficiary of a discretionary trust to prove an abuse of discretion.

11. Elimination of the Distinction Between Support and Discretionary Trusts.

11.1 The *Second Restatement* drew a distinction between support trusts and discretionary trusts.

- (A) Under the rule of the *Second Restatement*, a discretionary trust may not be reached by the beneficiary's creditors:

Except as stated in § 156 [concerning self-settled trusts], if by the terms of a trust it is provided that the trustee shall pay to or apply for a beneficiary only so much of the income and principal or either as the trustee in his uncontrolled discretion shall see fit to pay or apply, a transferee or creditor of the beneficiary cannot compel the trustee to pay any part of the income or principal.¹¹⁴

- (B) The reason for this rule was that “the 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.”¹¹⁵

- (C) In general, a support trust also could not be reached by the beneficiary's creditors:

Except as stated in §§ 156 [concerning self-settled trusts] and 157 [concerning exception creditors], if by the terms of a trust it is provided that the trustee shall pay or apply only so much of the income and principal or either as is necessary for the education or support of the beneficiary, the beneficiary cannot transfer his interest and his creditors cannot reach it.¹¹⁶

¹¹⁴ RESTATEMENT (SECOND) OF TRUSTS § 155.

¹¹⁵ *Id.* cmt. b.

¹¹⁶ RESTATEMENT (SECOND) OF TRUSTS § 154.

- (D) A support trust could be reached, however, by exception creditors.¹¹⁷ The Second Restatement recognized four classes of exception creditor: claims by the beneficiary's wife or child for support, claims for necessities provided to the beneficiary, claims for services or materials furnished to the beneficiary to protect the beneficiary's interest in the trust, and government claims.¹¹⁸

11.2 Both discretionary and support trusts give the trustee some degree of discretion in making distributions, and the discretion is expressed in a myriad of ways.

- (A) A trust may appear to be a nondiscretionary support trust, for example, a trust in which "trustee shall distribute to the beneficiary as much of the net income and principal of the trust as is necessary for the beneficiary's support." Even in a trust like this, however, the trustee has some degree of discretion because the trustee must decide as a practical matter what items constitute support of the beneficiary.
- (B) A trust may expressly give the trustee discretion but require that the discretion be exercised according to a standard, such as, "the trustee may distribute to the beneficiary as much of the net income and principal of the trust as the trustee, in its discretion, determines advisable for the beneficiary's health, education, maintenance, and support."
- (C) Or the discretion may be subject to no standard, such as "the trustee may distribute to the beneficiary as much of the net income and principal of the trust as the trustee determines advisable in the trustee's discretion."
- (D) Sometimes, the grant of discretion is accompanied by language that expands the scope of the discretion, often referred to as language of "extended discretion."
 - (1) Language of extended discretion may be used along with a standard, such as "the trustee may distribute to the beneficiary as much of the net income and principal of the trust as the trustee determines advisable, in the trustee's *sole and absolute discretion*, for the beneficiary's health, education, maintenance, and support."
 - (2) Or language of extended discretion may be added to a grant of discretion that is not subject to a standard: "the trustee may

¹¹⁷ *Id.* § 157.

¹¹⁸ *Id.*

distribute to the beneficiary as much of the net income and principal of the trust as the trustee determines advisable in the trustee's *sole, absolute, and uncontrolled discretion.*"

11.3 Putting aside the issue of when and why one might want to allow a trustee to exercise discretion and, if so, how broad that discretion should be, what is the standard by which a court should evaluate a trustee's exercise of discretion? Does it matter whether the grant of discretion is accompanied by language of extended discretion? When and how will a court interfere with a trustee's exercise of discretion? The answers to these questions are not as clear as one might think. "It is an open question . . . whether in the face [of] a broad grant of discretionary authority the reasonableness of a trustee's actions may be the subject of judicial second-guessing."¹¹⁹

(A) There does seem to be consensus that a reasonableness standard applies to a trustee's actions if the trustee has discretion concerning distributions but the grant of discretion is not accompanied by language of extended discretion.

(B) The courts generally will not interfere with a trustee's exercise of discretion. As stated in the *Second Restatement*, "[w]here discretion is conferred upon the trustee with respect to the exercise of a power, its exercise is not subject to control by the court, except to prevent an abuse by the trustee of his discretion."¹²⁰ The language of the *Third Restatement* is similar: "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."¹²¹

(C) Despite this language indicating a high degree of deference to the trustee, if there is no language of extended discretion, the courts will step in to prevent a trustee from acting unreasonably.

(1) Under the *Second Restatement*:

If discretion is conferred upon the trustee in the exercise of a power, the court will not interfere

¹¹⁹ CHARLES E. ROUNDS, JR., *LORING A TRUSTEE'S HANDBOOK* § 3.5.3.2(a) (2007 ed.) (footnote omitted).

¹²⁰ *RESTATEMENT (SECOND) OF TRUSTS* § 187 (1959).

¹²¹ *RESTATEMENT (THIRD) OF TRUSTS* § 50(1) (2003).

unless the trustee in exercising or failing to exercise the power acts dishonestly, or with an improper even though not a dishonest motive, or fails to use his judgment, *or acts beyond the bounds of a reasonable judgment.*¹²²

- (2) And under the *Third Restatement*: “A court will not interfere with a trustee’s exercise of a discretionary power when that exercise is *reasonable* and not based on an improper interpretation of the terms of the trust.”¹²³

11.4 The picture becomes murky when the terms of the trust include language of extended discretion.

- (A) Scott takes the position that the trustee may be relieved of the duty to act reasonably by using language of extended discretion.¹²⁴ But even if the trustee need not be reasonable, the trustee is still subject to some judicial review. The courts will not interfere “if [the trustee] acts in good faith and does not act capriciously,”¹²⁵ but the court will interfere “where he acts dishonestly or in bad faith, or where he acts from an improper motive.”¹²⁶
- (B) The *Second Restatement*, for which Scott was the reporter, not surprisingly expresses the same view:

The mere fact that the trustee is given discretion does not authorize him to act beyond the bounds of a reasonable judgment. The settlor may, however, manifest an intention that the trustee’s judgment need not be exercised reasonably, even where there is a standard by which the reasonableness of the trustee’s conduct can be judged. This may be indicated by a provision in the trust instrument that the trustee shall have “absolute” or “unlimited” or “uncontrolled” discretion. These words are not interpreted literally but are ordinarily construed as merely dispensing

¹²² RESTATEMENT (SECOND) OF TRUSTS § 187 cmt. e (1959). Emphasis added.

¹²³ RESTATEMENT (THIRD) OF TRUSTS § 50 cmt. b (2003). Emphasis added.

¹²⁴ SCOTT ON TRUSTS § 187.2.

¹²⁵ *Id.*

¹²⁶ *Id.* Footnote omitted.

with the standard of reasonableness. In such a case the mere fact that the trustee has acted beyond the bounds of a reasonable judgment is not a sufficient ground for interposition by the court, so long as the trustee acts in a state of mind in which it was contemplated by the settlor that he would act. But the court will interfere if the trustee acts in a state of mind not contemplated by the settlor. Thus, the trustee will not be permitted to act dishonestly, or from some motive other than the accomplishment of the purposes of the trust, or ordinarily to act arbitrarily without an exercise of his judgment.¹²⁷

- (C) Bogert, the author of the other major treatise on trust law, disagrees with Scott, concluding after reviewing the cases that “[t]he authorities do not appear to support the Restatement position that there is no requirement of reasonableness in the exercise of a power granted in the trustee’s absolute discretion.”¹²⁸ In contrast to Scott’s position, Bogert concludes that:

a standard of reasonableness has been applied by the courts in judging the exercise of a discretionary power (whether simple or absolute), a standard implied from the settlor’s intent and the purposes expressed in the trust instrument. With respect to court review of discretionary powers, this standard is consistent with the standard of care and skill of a prudent man and is based upon established fiduciary standards and principles.¹²⁹

- (D) The Third Restatement is more consistent with Bogert than with Scott:

Cases . . . are difficult to find, involving extended discretion relating to distribution of income or principal, in which courts have approved what actually appears to be unreasonable conduct.¹³⁰

11.5 Because there are so many ways to express the discretion granted to a trustee, case law that attempts to categorize trusts as either discretionary trusts or support trusts

¹²⁷ Restatement (Second) of Trusts § 187 cmt. j.

¹²⁸ G. BOGERT AND G. BOGERT, THE LAW OF TRUSTS AND TRUSTEES § 560 (2d ed. 1983).

¹²⁹ *Id.* at 32 (Supp. 2004) (footnotes omitted).

¹³⁰ RESTATEMENT (THIRD) OF TRUSTS, Reporter’s notes on § 50 cmt. c (2003).

is diverse and conflicting, and the Third Restatement has abandoned the distinction in the context of the rights of a beneficiary's creditors.¹³¹

11.6 The UTC similarly abandons the discretionary/support trust distinction in the context of creditor's rights, and the UTC critics argue that doing so weakens creditor protection. The critics' argument is flawed, however, both because:

- (A) The argument fails to recognize that, except for claims of exception creditors, the UTC decouples a creditor's ability to reach a trust from the beneficiary's power to enforce the trust; and
- (B) For exception creditors, the UTC does not change the common law standards that will apply in evaluating a trustee's exercise of discretion.

11.7 Creditors Other than Exception Creditors.

- (A) In fact, the elimination of the discretionary/support trust distinction actually increases protection from claims of creditors other than exception creditors.¹³²
- (B) Under traditional theory, a creditor who had supplied necessities to the beneficiary of a support trust could recover from the trust.¹³³ The UTC treats a trust where the trustee's discretion is expressed in the form of a standard of distribution as a discretionary trust,¹³⁴ and a creditor (other than an exception creditor) cannot reach such a trust even if the trustee has not complied with the standard or has abused its discretion.¹³⁵ The fact that the *beneficiary* might be able to compel a distribution is irrelevant to the creditor's claim.¹³⁶

¹³¹ RESTATEMENT (THIRD) OF TRUSTS § 60, cmt. a.

¹³² Eason, *supra* note 99, at 2642 ("The UTC . . . provides clarification and certainty on the issue of creditors' rights in such [discretionary] trusts. That certainty appears to work to the distinct disadvantage of creditors, particularly with regard to discretionary trusts that are other than 'purely' discretionary.") (footnote omitted).

¹³³ RESTATEMENT (SECOND) OF TRUSTS § 157(b).

¹³⁴ UTC § 504(b); *see* UTC § 506(a).

¹³⁵ UTC § 504(b).

¹³⁶ *See* Newman, *supra* note 9, at 600 ("section 504(b) extends to support trusts the protection discretionary trusts have traditionally afforded against creditors of beneficiaries seeking to compel distributions they can reach. In this way, the UTC enhances asset protection planning with trusts."); Danforth, *Article Five, supra* note

- (1) By treating distributions subject to a standard as discretionary, the UTC eliminates the argument that a creditor may stand in the shoes of the beneficiary to force a distribution.¹³⁷
- (2) And by decoupling the creditor's rights from the beneficiary's power to enforce the trust, the UTC eliminates any argument that a creditor who is not an exception creditor may stand in the shoes of the beneficiary of a discretionary trust to argue that the trustee has abused its discretion.¹³⁸

11.8 Exception Creditors.

- (A) Under UTC section 504(c), exception creditors do, in a sense, stand in the shoes of the beneficiary, because if a child or spouse with a court order for child support or maintenance can show that the trustee has not complied with a standard or has abused its discretion, then the court is to order a distribution to satisfy the child support or maintenance award, "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."¹³⁹
- (B) The UTC critics point to UTC sections 504(d) and 814(a) to argue that the UTC gives trust beneficiaries' greater rights to force distributions than they had at common law and, therefore, that exception creditors who stand in the shoes of the beneficiary have greater rights than they had at common law.
 - (1) Section 504(d) says that section 504 "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."¹⁴⁰ Section 504(d) does not grant any rights to a beneficiary—it merely says that the restrictions on creditor's rights

30, at 2576-77.

¹³⁷ Danforth, *Article Five*, *supra* note 30, at 2576.

¹³⁸ Danforth, *Article Five*, *supra* note 30, at 2576-77; Walsh *et al.*, *supra* note 8, at 31.

¹³⁹ UTC § 504(c)(2).

¹⁴⁰ UTC § 504(d).

set out in the rest of section 504 do not limit the beneficiary's power to enforce the trust.¹⁴¹

- (2) At the heart of the critics' argument is UTC section 814(a), which 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.¹⁴²

- (C) The critics argue that at common law, a trustee who had extended discretion (that is, the trust used words such as "uncontrolled," "sole," or "absolute" discretion) could not act in bad faith but was not required to act in good faith. That is, they argue that lack of bad faith is a lesser standard than good faith, and that by requiring good faith on the part of the trustee, the UTC is increasing the rights of beneficiaries and, therefore, of exception creditors under UTC section 504(c).

- (1) The bad faith standard, according to the critics,¹⁴³ is exemplified by the opinion of the Colorado Supreme Court in *In re Marriage of Jones*.¹⁴⁴ *Jones* was a divorce case in which the issue was not whether the trustee had properly exercised its discretion, but whether the beneficiary's interest in the trust was property for purposes of the property division in the divorce. The court said that the beneficiary could not force any action by the trustee to make distributions where the trustee had "uncontrolled discretion," "unless she could establish fraud or abuse of discretion,"¹⁴⁵ or unless the trustee "acts dishonestly or from an improper motive, or

¹⁴¹ See Newman, *supra* note 9, at 602; Danforth, *Article Five*, *supra* note 30, at 2579-80.

¹⁴² UTC § 814(a).

¹⁴³ Merric & Oshins, *Spendthrift Trusts*, *supra* note 96 at 479, note 1.

¹⁴⁴ *In re Marriage of Jones*, 812 P.2d 1152 (Colo. 1991).

¹⁴⁵ *Id.* at 1156.

fails to use his judgment,”¹⁴⁶ or unless the trustee “performs dishonestly or does not act at all.”¹⁴⁷ The result in *Jones* may be correct, but the analysis of discretionary trusts is unhelpful when applied to the actual exercise of a trustee’s discretion. The opinion characterizes the beneficiary’s interest as an “expectancy” not rising to the level of a property interest.¹⁴⁸ Although a beneficiary of a discretionary trust, especially one that uses language of extended discretion, may accurately be said to have only an expectancy in receiving distributions from the trust, that does not mean that the beneficiary has no property interest. Under traditional theory, the beneficiary is still the equitable owner of the trust property,¹⁴⁹ and the trustee is still a fiduciary, owing to the beneficiary the fundamental duties of a trustee, including the duties of loyalty and impartiality and the duty to account to the beneficiary.¹⁵⁰ Thus, the language in *Jones* to the effect that the beneficiary has no property interest in the trust is best read to mean that the beneficiary’s interest was too attenuated to be considered property *for purposes of the divorce statutes*, but is no more than dicta with respect to the standard for evaluating a trustee’s actual exercise of discretion.

- (2) This is demonstrated by other pertinent Colorado law that is contrary to the dicta in *Jones*.
 - (a) *Marshall v. Grauberger*¹⁵¹ involved a property settlement in connection with a divorce. The agreement awarded some shares of the husband’s company to the wife immediately, plus an additional 500,000 shares “to be transferred to her within five years, during which time the husband maintained all powers over the stock. He could sell the

¹⁴⁶ *Id.*, quoting 2 A. SCOTT ON TRUSTS § 128.3.

¹⁴⁷ *In re Marriage of Jones*, 812 P.2d 1152, 1156 (Colo. 1991).

¹⁴⁸ *Id.* at 1156-57.

¹⁴⁹ 2 A. SCOTT ON TRUSTS § 130 (“The beneficiary of a trust has a property interest in the subject matter of the trust. He has a form of ownership.”).

¹⁵⁰ *Id.* §§ 169-185.

¹⁵¹ *Marshall v. Grauberger*, 796 P.2d 34 (Colo. App. 1990).

shares at any time within the five-year period,¹⁵² and a sale was to be within the husband's sole discretion.¹⁵³ Before the five years were up, the husband sold the remaining stock in his name but did not sell the stock earmarked for the ex-wife. The stock declined in value after the sale, and the ex-wife sued for breach of fiduciary duty. The court held that the husband was trustee of the 500,000 shares for the wife: "The use of the word 'trust' is not necessary to establish a legally sufficient trust. . . . We agree with the trial court that here a fiduciary duty owed by husband to his wife was 'created by his undertaking' to hold title to or to sell wife's 500,000 shares during a maximum period of 5 years."¹⁵⁴ The court then concluded that "husband had the obligation as a fiduciary to exercise reasonable care and skill in his administration of the trust,"¹⁵⁵ and "to operate within the bounds of prudent judgment, reasonableness, and equity,"¹⁵⁶ and that reasonableness was an external standard.¹⁵⁷ The court in *Marshall v. Grauberger* thus imposed a reasonableness standard on a trustee with extended discretion. A reasonableness standard is a more stringent standard than good faith or lack of bad faith, regardless of whether one views good faith and lack of bad faith as separate standards or simply different ways of expressing the same standard.

- (b) *In re Estate of McCart*,¹⁵⁸ a Colorado Court of Appeals case decided one year after *Jones*, involved a trustee-remainder beneficiary who reduced distributions to the decedent-settlor's husband after the husband remarried. Although the trustee had "sole discretion" as to distributions, the court

¹⁵² *Id.* at 35.

¹⁵³ *Id.* at 36.

¹⁵⁴ *Id.*

¹⁵⁵ *Id.* at 36-37.

¹⁵⁶ *Id.* at 37.

¹⁵⁷ *Id.*

¹⁵⁸ *In re Estate of McCart*, 847 P.2d 184 (Colo. App. 1992).

held that he had “abused his discretion and acted arbitrarily and capriciously,”¹⁵⁹ “acted with improper motives and with a clear conflict of interest,”¹⁶⁰ and was “in breach of his fiduciary responsibilities to act with the *utmost good faith and fairness* toward the beneficiary.”¹⁶¹

(c) In addition, Colorado has a statute that requires a trustee to act vreasonably in exercising any of its powers,¹⁶² and as noted above, a reasonableness standard is a more stringent standard than a good faith or lack of bad faith standard.

(D) In the end, the argument over whether good faith is something more than lack of bad faith:

place[s] too much emphasis on the language in some cases indicating that a trustee may not act in “bad faith.” Court decisions vary considerably in their formulations of the standards of conduct for trustees; the formulations differ from case to case not so much because courts intend to express substantively different standards, but rather because the facts of a specific controversy cause one court to emphasize certain aspects of the standard over others.

...

The critics’ assertion that a standard requiring “good faith” is different from—and, more specifically, is more onerous than—a standard prohibiting “bad faith” has no basis in the law.¹⁶³

¹⁵⁹ *Id.* at 186.

¹⁶⁰ *Id.*

¹⁶¹ *Id.* Emphasis added.

¹⁶² C.R.S. § 15-1-804(1) (“*In the exercise of any of his powers, whether derived from this part 8 [of title 15, Article 1] or from any other source, a fiduciary has a duty to act reasonably and equitably with due regard for his obligations and responsibilities toward the interests of beneficiaries and creditors, the estate or trust involved, and the purposes thereof and with due regard for the manner in which men of prudence, discretion, and intelligence would act in the management of the property of another.*”) (emphasis added).

¹⁶³ Danforth, *Article Five*, *supra* note 30, at 2582. See Newman, *supra* note 9, at 604-606; Eason, *supra* note 99, at 2640 (“the UTC’s pronouncement that a trustee must exercise discretion in good faith does not change the common law, even with respect to the ‘purest’ discretionary trusts.”) (footnote omitted); Walsh *et al.*,

- (E) Under the UTC, a spouse or child with an order or judgement for support against a beneficiary of a discretionary trust, including a trust that would previously have been characterized as a support trust, will have the opportunity to show that the trustee has not complied with a standard or has abused its discretion, and, if the spouse or child is successful in that difficult task, then the court is to order a distribution to satisfy the child support or maintenance award, “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.”¹⁶⁴ The UTC does not, however, change the legal standard of review by which the court is to determine whether the trustee has complied with a distribution standard or abused its discretion.

12. Supplemental Needs Trusts and Special Needs Trusts.

- 12.1 Critics argue that the UTC weakens the effectiveness of supplemental needs trusts and special needs trusts.
- (A) Self-settled special needs trusts must comply with the applicable federal law to be effective.¹⁶⁵ Those trusts are not asset-protection trusts and do not need to be to achieve their purpose. The UTC will not change that and will not affect those trusts.¹⁶⁶
- (B) The critics argue that the UTC may cause a third-party settled supplemental needs trust to become an available resource for purposes of determining whether the beneficiary qualifies for benefits. The critics base this argument on the UTC’s elimination of the distinction between support and discretionary trusts, because the case law on third-party SNTs often categorizes trusts as support trusts that are an available resource or discretionary trusts that are not. But the real question is not the label put on the trust but the beneficiary’s rights in the trust:

While cases often explain that the assets of support trusts are disqualifying available resources while those of

supra note 8, at 32.

¹⁶⁴ UTC § 504(c)(2).

¹⁶⁵ Newman, *supra* note 9, at 619.

¹⁶⁶ *Id.* Walsh *et al.*, *supra* note 8, at 34-35.

discretionary trusts are not, the underlying rationale for making that classification determinative of whether the trust assets are actually available to the beneficiary is that the beneficiary may compel distributions for support from a support trust but not from a discretionary trust. While the UTC does not classify trusts as ‘support’ or ‘discretionary,’ it does not change existing law on the question of whether a beneficiary of a third party created trust may compel a distribution and thus does not affect whether the trust assets will be disqualifying available resources for public benefits eligibility purposes.¹⁶⁷

- (1) If the trust expressly limits distributions to providing for the beneficiary’s supplemental needs, it is not an available resource and the UTC does nothing to change that result.¹⁶⁸
- (2) A discretionary trust with no support standards should also not be an available resource, and again the UTC will not change this result.¹⁶⁹
- (3) The case law on trusts that give the trustee discretion but use a support standard is diverse.¹⁷⁰ The UTC, however, should not adversely affect how these discretionary support trusts are treated by the courts, because the UTC treats support trusts as discretionary trusts and does not increase the beneficiary’s right to compel trust distributions.¹⁷¹ For example, “because it eliminates the concept of the discretionary support trust, the Nebraska UTC should prevent a Nebraska court from finding that a beneficiary’s interest in such a trust is an ‘available’ asset for purposes of qualification for Medicaid or SSI.”¹⁷²

¹⁶⁷ Newman, *supra* note 9, at 620 (footnotes omitted); Richard E. Davis & Stanley C. Kent, *The Impact of the Uniform Trust Code on Special Needs Trusts*, NAELA J. 235, 244-53 (2005).

¹⁶⁸ Newman, *supra* note 9, at 621-22.

¹⁶⁹ Newman, *supra* note 9, at 624-25.

¹⁷⁰ CLIFTON B. KRUSE, JR., *THIRD-PARTY AND SELF-CREATED TRUSTS—PLANNING FOR THE ELDERLY AND DISABLED CLIENT* (3d ed. 2002).

¹⁷¹ Newman, *supra* note 9, at 623-24; Davis & Kent, *supra* note 167, at 244-53.

¹⁷² Lyons & Gradwohl, *supra* note 108, at 272 (footnote omitted).

- (4) The comment to section 814 refers to the position taken by the *Third Restatement* that a trustee should exercise its discretion so as to preserve public benefits for the beneficiary:

distilling the results of scores of cases, the Restatement (Third) of Trusts concludes that there is a presumption that the ‘trustee’s discretion should be exercised in a manner that will avoid either disqualifying the beneficiary for other benefits or expending trust funds for purposes for which public funds would otherwise be available.’ Restatement (Third) of Trusts Section 50 cmt. e & Reporter’s Notes (Tentative Draft No. 2, 1999).¹⁷³

- (5) The inclusion of this reference in the comment may, if anything, help prevent discretionary support trusts from being treated as available resources.¹⁷⁴

- (C) The critics also argue that the UTC makes it too easy for the government to make itself an exception creditor and that doing so will allow the government to reach the property of a supplemental needs or special needs trust:

it may be only a matter of time before the state or federal government is able to convince the state legislators to add them as an exception creditor. At this time, a state or federal governmental agency would be able to recover from all trusts in a UTC state, including third-party discretionary Medicaid or special needs trusts.¹⁷⁵

- (D) This argument is puzzling in several respects. Under UTC section 503, the government is an exception creditor only “to the extent a statute of this State or federal law so provides.”¹⁷⁶ The critics seem to be saying that excluding the government as an automatic exception creditor will somehow prompt state legislators to enact a future statute to make the

¹⁷³ UTC § 814 cmt.

¹⁷⁴ Newman, *supra* note 9, at 637.

¹⁷⁵ Merric & Oshins, *Spendthrift Trusts*, *supra* note 96, at 484.

¹⁷⁶ UTC § 503(b)(3).

government an exception creditor. But the policy decision of whether the state should be an exception creditor will presumably be made by a legislature in connection with the enactment of the UTC.

- (E) Moreover, regardless of whether a state adopts the UTC, the state legislature is free to create an exception to spendthrift protection for government claims.
- (F) And so far as claims of the federal government are concerned, the critics' argument fails to appreciate the relationship between state and federal law:

No matter what the UTC says, and no matter how the UTC may subsequently be modified by a state legislature, the federal government is not dependent on state law if it chooses to recover from spendthrift trusts. If the federal government wishes to be treated as an exception creditor, a federal statute or a decision favorable to the government by a federal court will suffice.¹⁷⁷

- (G) Further, government agencies that pay needs-based benefits are rarely creditors of the trust beneficiary during the beneficiary's lifetime. The government can recover from certain types of special needs trusts after the beneficiary's death, but that is dictated by federal law and the extent of creditor protection provided or not provided by the trust during the beneficiary's lifetime, either under the UTC or in a non-UTC state, is irrelevant to that result.¹⁷⁸

13. **Claims of Creditors in the Bankruptcy of a Trust Beneficiary.**

13.1 The UTC should have no effect on the treatment of trusts in bankruptcy.

- (A) Federal bankruptcy law provides that “[a] restriction on the transfer of a beneficial interest of the debtor in a trust that is enforceable under applicable nonbankruptcy law is enforceable in a case under this title.”¹⁷⁹

¹⁷⁷ Danforth, *Article Five*, *supra* note 30, at 2572; see Walsh *et al.*, *supra* note 8, at 33 (“the federal government already has the power to preempt the states to reach the interest of beneficiaries of spendthrift trusts to satisfy claims [owed to] to the United States”).

¹⁷⁸ Danforth, *Article Five*, *supra* note 30, at 2572-73; Davis & Kent, *supra* note 167, at 237-44.

¹⁷⁹ 11 U.S.C.S. § 541(c)(2).

- (B) Consequently, a trust that is a valid spendthrift trust under state law will not become part of the bankrupt's estate, and because the UTC validates spendthrift trusts, it should have no effect on this result.
- (C) In the rare case in which a trust does not include a spendthrift provision, the beneficiary's interest may still be protected in bankruptcy if the interest is subject to the trustee's discretion, and, as a result, the beneficiary cannot compel distributions.¹⁸⁰ Because the UTC does not change whether beneficiaries may compel distributions, it should also have no effect on how a discretionary trust without a spendthrift provision will be treated in bankruptcy.¹⁸¹

13.2 The critics argue that the UTC invites changes to federal bankruptcy law that would expose all trusts to creditors:

What if the federal Bankruptcy Code one day references the UTC exception creditor list? . . . The federal Bankruptcy Code could take advantage of this loophole by enacting a statute such as, "the Federal Bankruptcy Trustee is an exception creditor pursuant to section 503(c) of any State that has adopted this provision of the Uniform Trust Code."

All a creditor need do is file an involuntary bankruptcy against the debtor, . . . and the creditor would have easy access to the trust assets. In essence, this would mean all judgment creditors—not just alimony, child support, necessary expenses of the creditor, federal claims, state claims and tort creditors—but anyone who had a debt greater than \$ 11,625 [citation omitted]. Should federal bankruptcy law ever allow recovery against a trust in a UTC state, there is virtually no asset protection provided by a spendthrift provision.¹⁸²

13.3 UTC section 503(c), cited in the preceding quotation, makes the *government* an exception creditor to the extent that a state or federal statute so provides.¹⁸³ The critics' argument makes the leap of logic that a bankruptcy trustee, who is a

¹⁸⁰ Newman, *supra* note 9, at 633-34.

¹⁸¹ *Id.*

¹⁸² Merric & Oshins, *Spendthrift Trusts*, *supra* note 96, at 484-85.

¹⁸³ UTC § 503(c).

fiduciary for the creditors in a bankruptcy proceeding, would be considered a governmental agency for purposes of UTC section 503(c).¹⁸⁴

- 13.4 Moreover, enactment of the UTC is irrelevant to whether the federal government may change federal law to subject trusts to creditor claims in bankruptcy. Such a federal law would preempt state law, including the UTC, some other trust code, or state common law.¹⁸⁵
- 13.5 Additionally, it is silly to suggest that federal bankruptcy law would single out states that have adopted the UTC and subject trusts created in those states, but not trusts created in other states, to creditor claims in bankruptcy.¹⁸⁶

14. **Treatment of Trusts in Connection with Divorce.**

- 14.1 The critics argue that the UTC will enhance the ability of a former spouse to reach trust assets to enforce a claim for alimony. That would be true in a state that previously did not have exceptions to spendthrift and discretionary trust protections for claims for alimony, and which adopted the UTC without change.¹⁸⁷ A number of the states that have adopted the UTC have eliminated former spouses as exception creditors, probably to conform their versions of the UTC either to the state's prior law or, in states that did not have case law on this issue, to conform their versions of the UTC to practitioners' conceptions of what pre-existing law was. If a state already recognized former spouses as exception creditors, adoption of the UTC would not increase former spouses' rights.
- 14.2 The critics also argue that the UTC will make a beneficiary's interest in a trust an asset that may be divided in a divorce proceeding, or an interest that may be considered in dividing other assets, or an interest that the court may consider in awarding child support or alimony. These arguments are based on the theory that the UTC increases a beneficiary's ability to force a distribution from a trust, an argument that is incorrect for the reasons discussed above.¹⁸⁸

¹⁸⁴ Danforth, *Article Five*, *supra* note 30, at 2574.

¹⁸⁵ Danforth, *Article Five*, *supra* note 30, at 2574.

¹⁸⁶ Danforth, *Article Five*, *supra* note 30, at 2574.

¹⁸⁷ *See* Newman, *supra* note 9, at 626-27.

¹⁸⁸ *See* section 11 of this outline; Newman, *supra* note 9, at 627-32; Walsh *et al.*, *supra* note 8, at 36-

14.3 All of these issues concerning trusts in divorce are governed by state domestic relations law, which varies considerably among the states.¹⁸⁹ The UTC should not affect how trusts are treated in divorce.¹⁹⁰

15. **The Argument that Creating a Trust in a UTC Jurisdiction is Malpractice.**

15.1 The critics argue that a lawyer who drafts a trust subject to the law of a UTC jurisdiction may commit malpractice if he or she does not advise the client that the UTC increases a trust's exposure to creditor claims.¹⁹¹

15.2 This argument is based on the incorrect conclusion that the UTC does in fact increase exposure to creditor claims.¹⁹²

15.3 Further, whether a lawyer commits malpractice depends on whether the lawyer has failed to satisfy the standard of practice in his or her particular jurisdiction.¹⁹³

15.4 Lawyers in the 20 jurisdictions that have adopted the UTC who continue to practice in their home states and to create trusts under their home state's law are not committing malpractice. Rather, the malpractice argument seems to be only a scare tactic used by the critics to attempt to prevent the adoption of the UTC. (A tactic that has been largely unsuccessful.)

16. **Conclusion.** All in all, the critics' arguments that the UTC weakens traditional spendthrift and discretionary trust protection have been largely ineffective and have failed to convince lawyers in the jurisdictions that have enacted the UTC. For example:

16.1 "Contrary to the often shrill voices of the relatively few critics of the UTC, the Nebraska UTC does not diminish appropriate protection of trust property and beneficiaries from the claims of creditors."¹⁹⁴

¹⁸⁹ See Chorney, *supra* note 32.

¹⁹⁰ See Danforth, *Article Five, supra* note 30, at 2591-92.

¹⁹¹ Merric, *Malpractice, supra* note 96, at 586.

¹⁹² See section 11 of this outline; Walsh *et al., supra* note 8, at 37.

¹⁹³ RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS § 52 cmt. b ("The professional community whose practices and standards are relevant in applying this duty of competence is ordinarily that of lawyers undertaking similar matters in the relevant jurisdiction (typically, a state).").

¹⁹⁴ Lyons & Gradwohl, *supra* note 108, at 278.

16.2 “The UTC provisions on spendthrift rules and creditors’ rights, adopted in Virginia with a few variations, essentially preserve current Virginia statutory and case law concerning these issues.”¹⁹⁵

¹⁹⁵ John E. Donaldson & Robert T. Danforth, *The Virginia Uniform Trust Code*, 40 U. RICH. L. REV. 325, 363 (2005).