

## ADMINISTERING THE DISCRETIONARY TRUST

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By: David M. Repp

Atticus Finch always arrived at the office each morning promptly at 8:15 and would eat a muffin in the break room while glancing over the day's headlines in the newspaper. Today was different because it was Monday. "Triage Monday," he called it. That morning, the phone was already ringing as he stepped into his office. Atticus set his muffin down and answered. A woman caller disclosed that her husband had not filed their tax returns for seven years and wondered what the penalties might be. Atticus wondered what set of events must have occurred for them to suddenly realize, after seven years, that they needed to file their tax returns.

Atticus glanced at the clock on the lower right corner of his computer screen. "9:45 and I haven't billed a single minute," he uttered to himself. Thirty-three emails, two faxes, three meeting reminders and a half-finished bar association seminar article awaited Atticus's attention. A subtle rumble emerged from Atticus's stomach. No sooner had he reached for his muffin than the phone rang again. The caller ID listed a name he did not recognize, but the number was within the local calling area. He hesitated, but set the muffin back down and answered.

"Mr. Finch?"

**"Yes, may I help you?"**

"My husband passed away a couple years ago and left a big trust fund for me"

**"Uh, that's too bad, or I mean that's good to hear. Ah, so how may I help you?"**

"Well, I'm the trustee and I've been using the trust to pay for my living expenses. It says that I can use the trust for my health, education, maintenance and support, so just last month I booked a six month world cruise. My husband's kids haven't spoken to me since the funeral. When one of them found out about the vacation he blew a gasket. He says he is going to sue me. He says that I shouldn't be using any of my husband's trust money because I'm supposed to use all my other income first. Is that right? Can he do that? Oh, and by the way, the kid is a brat who has never worked a day in his life and thinks he is smarter than God. What do you think, . . . can you help me?"

**"Damn, I don't know a thing about trust administration."<sup>1</sup>**

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<sup>1</sup> My apologies to Harper Lee, author, "To Kill a Mockingbird" (1962).

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Note: This material is designed and intended for general informational purposes only, and is not intended, nor should it be construed or relied upon, as legal advice. Please consult with your attorney if specific legal information is desired.

## **I. INTRODUCTION**

### **A. What is a Discretionary Trust**

A discretionary trust is one in which the settler gives the trustee authority over the trust, for example, to use discretion in the timing and amount of income payments to the beneficiary.<sup>2</sup> Where discretionary powers granted to a trustee are so broad as to provide the trustee the authority to make full distribution, partial distribution or no distribution of income or corpus, courts generally, but not always, hold that a beneficiary or creditor of a beneficiary cannot compel the trustee to make distribution.<sup>3</sup> In this regard, the discretionary trust has the same, or broader, effect of a spendthrift trust provision, discussed, below. A pure discretionary trust would protect trust assets from the creditors of a beneficiary in situations that a spendthrift would not, such as necessities for beneficiaries<sup>4</sup> and the Internal Revenue Service.<sup>5</sup>

What would a pure discretionary trust look like? Perhaps it is the following:

my Trustee may pay (or not pay) to my wife such amounts  
of the income or principal of the Trust assets as my  
Trustee deems appropriate for her health, education,  
support and maintenance.

The language “may pay (or not pay)” certainly suggests that the minimal amount (the “floor”) that the trustee is required to pay to a beneficiary is zero. However, can the trustee pay an unlimited amount to a beneficiary? The answer is clearly no. The trustee is constrained by the ascertainable standards “health, education, support and maintenance.” Therefore, this is not a pure discretionary trust. A true discretionary trust would have no upper (a “ceiling”) or lower limit (a “floor”):

my Trustee may pay (or not pay) to my wife such amounts  
of the income or principal of the Trust assets as my  
Trustee deems appropriate.

This type of dispositive language is more akin to a power of appointment than a standard of distribution.<sup>6</sup> Such language could have negative asset protection and estate tax consequences if the wife were also the trustee.<sup>7</sup> The Restatement (Third) of Trusts distinguishes between a power

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<sup>2</sup> Bogert Trusts and Estates, § 228 (3d ed. 2007); Restatement (Third) of Trusts §§ 50, 60.

<sup>3</sup> Bogert Trusts and Estates, § 221 (3d ed. 2007); *In re Dodge's Estate*, 281 N.W.2d 447, 450 (Iowa 1979).

<sup>4</sup> *In re Dodge's Estate*, 281 N.W.2d 447 (Iowa 1979); Iowa Code § 633A.2302(3)(a) (2026).

<sup>5</sup> *In Re Orr*, 180 F.3d 656, 664 (5th Cir. 1999); *First Northwestern Trust Co. v. Internal Rev. Serv.* 622 F.2d 387, 393 (1980); TAM 200036045

<sup>6</sup> Although the pure discretionary trust language with no upper or lower limit is a power of appointment, such power granted to a trustee nevertheless contains certain restrictions that would not exist if the power were held by a person not a trustee. See **Extended Discretion – A Super Discretionary Standard**, discussed below.

<sup>7</sup> Iowa Code Section 633A.3105 (2026) (creditors may make claims on the assets of a general power of appointment holder); However, if a beneficiary who is a trustee only has power to distribute pursuant to an ascertainable standard

of appointment and a trustee's discretionary authority to distribute assets to himself or herself in that the latter is subject to a fiduciary obligation to the other beneficiaries whereas a power of appointment is not.<sup>8</sup>

## **B. Compared to a Support Trust**

A support trust exists where the grantor directs or mandates the trustee to make payments to the beneficiary for a beneficiary's support.<sup>9</sup> Absent a spendthrift provision, beneficiaries would be entitled to assign, transfer or sell their beneficial interests in the trust and their creditors could levy or foreclose on such interest.<sup>10</sup> Is there such a thing as a pure support trust? Determining what constitutes "support" requires a certain amount of judgment from the trustee.

## **C. Compared to a Spendthrift Trust**

A spendthrift trust is one in which, by direction of the settler or as a result of a statute, a trust beneficiary cannot alienate the right to payments, and the beneficiary's creditors may not subject the beneficiary's interest in the trust to the beneficiary's debts.<sup>11</sup> Every state in the United States has adopted or enacted some form of spendthrift trust provision, although the provisions are not uniform among the states.<sup>12</sup> In Iowa, the spendthrift trust was first cited in the 1907 Iowa Supreme Court case of *Olsen v. Youngerman*.<sup>13</sup> Spendthrift trusts are currently authorized under Iowa Code Section 633A.2302 (2026).

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the beneficiary-trustee is not considered a general power of appointment holder. IRC § 2041 (assets are includible in appointee's taxable estate). There are two ways to avoid inclusion of the trust assets in the estate of the trustee-wife. The first is to limit distributions to a fixed or ascertainable standard. Treas. Reg. §25.2511-1(g)(2); Iowa Code § 633A.4214(3)-(4). However, if the wife were to refrain from making a discretionary distribution to herself at a time when she had a need, there exists an argument that she has made a gift transfer to the remaining beneficiaries. RICHARD W. HARRIS, *Ascertainable Standard Restrictions on Trust Powers Under the Estate, Gift and Income Tax*, Vol. 50, NO. 3, Tax Lawyer. The second method to avoid negative gift and estate tax consequences to the wife is to require the consent of an adverse party prior to the wife's distribution to herself. In this case, a trustee's power of withdrawal to herself is not considered a general power of appointment causing the trust property to be included in the trustee's estate for estate tax purposes if the power of withdrawal is exercisable only in conjunction with a person having a substantial interest in the property subject to the power and which is adverse to the exercise of the power in favor of the trustee. IRC § 2041(b)(1)(C)(iii); IRC § 2514(c)(2); PLR 9030032.

<sup>8</sup> Restatement (Third) of Trusts § 50 General Comment (2003).

<sup>9</sup> *In re Dodge's Estate*, 281 N.W.2d 447, 451 (Iowa 1979).; *In re Barkema Trust*, 690 N.W.2d 50, 54 (Iowa 2004) (citing George Gleason Bogert & George Taylor Bogert, *THE LAW OF TRUSTS AND TRUSTEES* § 229 (2d ed. 1993)).

<sup>10</sup> Restatement (Third) of Trusts § 51 (2003). However, the assignee has only what the beneficiary had. Thus, if the trust were a pure discretionary trust, the assignee would only be entitled to distributions from the trust that the trustee decides he or she wants to make. Restatement (Third) of Trusts § 60 Comment (b) (2003).

<sup>11</sup> Bogert Trusts and Estates, § 221 (3d ed. 2007).

<sup>12</sup> See George Gleason Bogert & George Taylor Bogert, *The Law of Trusts and Trustees*, § 222 (2nd ed. 1992). Section 222 contains a summary of all the states' laws on spendthrift trust provisions.

<sup>13</sup> 136 Iowa 404, 113 N.W. 938 (1907). The *Olsen* case had nothing to do about the merits of the spendthrift provision in the trust. No creditors were involved and no assignment or transfer of a beneficial interest was addressed. At issue in *Olsen* was whether the trust could be terminated for the reason that it served no material

There is no particular form required for a spendthrift trust provision. However, Iowa Code Section 633A.2302 (2026) requires that in order for a trust to be a spendthrift trust, it must reference the term "spendthrift trust" or words of similar import. A spendthrift provision can be as simple as the following:

The interest of the beneficiary shall not be seized by creditors or said beneficiary or by anyone, by attachment, garnishment, execution or otherwise.<sup>14</sup>

Ultimately, in abuse of discretion cases, the court must determine the scope of discretion granted to the trustee by the settler in the trust instrument. The floor would be the absolute minimum that a trustee must provide to a beneficiary; the ceiling describes that absolute maximum amount that a trustee could distribute to a beneficiary. The focus of this article is to determine how courts define the floor and ceiling.

## **II. DISCRETIONARY TRUSTS IN IOWA**

### **A. Strojek and Barkema**

In *Strojek v. Hardin County Bd. of Supervisors*<sup>15</sup> the court was presented with the following dispositive provision of a trust:

"My trustee shall, from time to time, pay to or apply for the benefit of my daughter, Marie Helen Strojek, such sums from the income and principal as my trustee in the exercise of her sole discretion deems necessary or advisable, to provide for her proper care, support, maintenance and education." (Emphasis added.)<sup>16</sup>

The court noted that not all trust dispositive provisions can fit neatly in the category of either a support trust or discretionary trust.<sup>17</sup> It therefore devised a new category of trust called the "discretionary support" trust which it says is created when a grantor, like that in *Strojek*, combines explicit discretionary language with language that, in itself, would be deemed to be a pure support trust.

The *Strojek* court established the floor for distributions in discretionary support trusts as "[t]he minimal distributions a trustee must make in order to comport with the settlor's intent of

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purpose. The Iowa Supreme Court simply made an observation that the trust was a spendthrift trust and moved on with its analysis about the other issues of the case.

<sup>14</sup> *Emmet County Board of Supervisors v. Ridout*, 692 N.W.2d 821 (Iowa 2005)..

<sup>15</sup> 602 N.W.2d 566, 569 (Iowa App. 1999); see also the unreported case *In re the Matter of the Trust of Daniel J. McCabe*, Iowa Court of Appeals No. 2-677/01-1972 (Dec. 11, 2002) (involving a demand by a beneficiary for payment by the trustee of her nursing home costs).

<sup>16</sup> *Strojek v. Hardin County Bd. of Supervisors*, 602 N.W.2d 566, 568 (Iowa App. 1999).

<sup>17</sup> *Id.* at 569 (citing numerous contradictory rulings regarding seemingly similar dispositive provisions).

providing basic support.”<sup>18</sup> In other words, a trustee can be compelled by a beneficiary “to pay at least the minimum amount which in the opinion of a reasonable [person] would be necessary” to meet a support standard.<sup>19</sup> It also means that a beneficiary's interest can be reached by the beneficiary's creditor (but only for support or services the creditor provided to the beneficiary meeting the *Dodge* standard<sup>20</sup> and, as discussed in (iii), below, the Internal Revenue Service.

Once the court determined that the trust language was a form of a support trust, it applied the rationale of *In re Dodge*<sup>21</sup> to hold that the trust assets should be considered for purposes of determining Marie Strojek's eligibility for Hardin County benefits.

In *In re Barkema Trust*,<sup>22</sup> the Iowa Supreme Court was presented with the issue of whether the Department of Human Services had a valid claim for recovery of Medicaid benefits from a trustee of a trust for the benefit of the settlor's daughter, Lois. The trust dispositive provision was as follows:

"If possible, only the income from said share shall be used for Lois, however, if necessary for her proper support and maintenance, then the corpus of said trust may be invaded to the extent said trustees deem necessary."<sup>23</sup> (Emphasis added)

Unfortunately, the settlor of the trust did not provide who should take the remainder of the trust after Lois's death. Lois spent several years in a nursing home paid for by Medicaid<sup>24</sup> before passing away on April 14, 2003.

The Iowa Supreme Court said that due to Iowa Code Section 249A.5(2)(c) the Department of Human Services had the authority to seek recovery from any "*interest in trust*" that Lois may have had immediately before her death.<sup>25</sup> The court reasoned that Lois had an interest in trust only if she had a "legal ability to obtain [assets from the trust]."<sup>26</sup> The court applied the rationale

<sup>18</sup> *Strojek v. Hardin County Bd. of Supervisors*, 602 N.W.2d 566, 570 (Iowa App. 1999).

<sup>19</sup> *Id.*

<sup>20</sup> *In re Dodge's Estate*, 281 N.W.2d 447, 451 (Iowa 1979).

<sup>21</sup> 281 N.W.2d 447, 450 (Iowa 1979). *Dodge* says that a spendthrift trust provision is invalid as against a creditor of a beneficiary providing necessary goods or services to him or her, provided that: (1) the claim is for necessary goods or services, not officiously rendered, which the settlor intended to be provided the beneficiary by trust funds; and (2) the withholding of payment for the goods and services is not properly within the discretion granted the trustee by the instrument, before a creditor's claim may be enforced against the trustee of a support trust subject to a spendthrift clause.

<sup>22</sup> 690 N.W.2d 50 (Iowa 2004).

<sup>23</sup> *Id.* at 52.

<sup>24</sup> Apparently, the Department of Human Services never questioned whether the trust was an available resource to Lois for Medicaid eligibility purposes. *Id.* at 52-53.

<sup>25</sup> *Id.* at 55; *see also In re the Estate of Steffes*, No. 5-014/04-0601, 697 N.W.2d 128 (unpublished opinion) (Iowa Ct. App. 3/31/2005) (holding that a self-settled trust for a Medicaid applicant was an available resource to the applicant to be counted for purposes of determining eligibility).

<sup>26</sup> 690 N.W.2d at 55. (stating "[i]n order for an asset to be considered an actually available resource, an applicant must have a legal ability to obtain it") (citing *Hecker v. Stark County Soc. Serv. Bd.*, 527 N.W.2d 226, 237 (N.D. 1994).

of *Strojek* and concluded that the dispositive provision of the trust provided enough of a "support" standard to allow Lois to compel the trustee to invade the corpus for the trust and make distributions to her for her support. Therefore, she had an "interest in trust." Further, because the Department of Human Services provided "necessities" to Lois, the spendthrift clause of the trust did not apply.<sup>27</sup>

**B. Iowa Legislative Answer to *Strojek***

The Probate Section of the Iowa Bar Association had just about enough of the Iowa Supreme Court and the Iowa Court of Appeals. In 2004, it sponsored legislation intended to overrule the discretionary support trust concept and to lower the "floor" for discretionary distributions from such trusts to zero.<sup>28</sup> The result was the addition of section 633A.2301(4) (renumbered in 2008 as §633A.2305) and a new section 633A.4702 which the Probate Section believed would better protect trust assets from the creditors of its beneficiaries.

Section 633A.2305 provides as follows:

Whether or not a trust contains a spendthrift provision, a creditor or assignee of a beneficiary of a spendthrift trust shall not compel a distribution that is subject to the trustee's discretion if any of the following apply:

- a. The distribution is expressed in the form of a standard of distribution.
- b. The trustee has abused its discretion.

New Section 633A.4702 was added as follows

In the absence of clear and convincing evidence to the contrary, language in a governing instrument granting a trustee discretion to make or withhold a distribution shall prevail over any language in the governing instrument indicating that the beneficiary may have a legally enforceable right to distributions or indicating a standard for payments or distributions.

In essence, Iowa Code Section 633A.4702 purports to shift all interpretive close calls in favor of a discretionary trust status and set the floor for distributions back to zero. If a trustee had discretion to not make distributions, the beneficiary's interest in the trust is nothing and a creditor, such as Medicaid or the Iowa Department of Health and Human Services (formerly DHS), could not seek recovery from the trust (Effective July 1, 2023, the Iowa Department of

<sup>27</sup> *In re Dodge's Estate*, 281 N.W.2d 447 (Iowa 1979); Iowa Code § 633A.2302(3)(a) (2026).

<sup>28</sup> The *Strojek* court established the floor for distributions in discretionary support trusts as "[t]he minimal distributions a trustee must make in order to comport with the settlor's intent of providing basic support." *Strojek v. Hardin County Bd. of Supervisors*, 602 N.W.2d 566, 568 (Iowa App. 1999).

Human Services was consolidated into the Iowa Department of Health and Human Services. See, e.g., 2023 Iowa Acts ch. 19; Iowa Code § 598.34 (2026)).

Not to be outdone by the Iowa Probate Section, the Iowa Department of Human Services engineered a block by sponsoring legislation in 2008 that amended 633A.2301(4). The legislation recodified 633A.2301(4) as 633A.2305 and added a new subsection 2:

1. Whether or not a trust contains a spendthrift provision, a creditor or assignee of a beneficiary shall not compel a distribution that is subject to the trustee's discretion, even if any of the following occur:

a. The discretion is expressed in the form of a standard of distribution.

b. The trustee has abused its discretion.

2. This section shall not apply to a creditor of a beneficiary or to a creditor of a deceased beneficiary enforcing an interest in a trust, if any, given to a beneficiary by the trust instrument.

The Department of Human Services' defensive maneuver, that added subsection 2, neutralized the Probate Section's offense. However, Iowa Code Section 633A.4702 was not changed. The result of the 2008 legislative change (and non-change) was that the status of the *Strojek* "discretionary support" trust (and the "floor" for distributions) was now as unclear as ever.<sup>29</sup>

### **C. Gist**

In 2009, the Iowa Supreme Court decided the *Gist* case; the first case to address the discretionary support trust standard following the legislative changes to the Iowa Trust Code.<sup>30</sup> Elenore Gist was a beneficiary of her parent's testamentary trust that provided a very specific distribution provision that preferred Elenore over the remainder beneficiaries.<sup>31</sup>

<sup>29</sup> The 2008 legislation also enacted companion §§ 633A.2306 and 633A.2307: § 633A.2306 provides that a court shall neither order a trustee to exercise discretion nor order a payment that would inure to a beneficiary's creditor, but may order payment to a creditor of a beneficiary or deceased beneficiary "if the beneficiary has or had an interest in the trust"; and § 633A.2307 provides that a creditor may reach overdue mandatory distributions of all income or principal, a fraction or percentage of income or principal, or a specific dollar amount, while a distribution subject to a condition is not mandatory. Sections 633A.2305 and 633A.4702 remain unchanged in the current Code.

<sup>30</sup> *In re Estate of Elenore Gist*, 763 N.W.2d 561 (Iowa 2009).

<sup>31</sup> The full dispositive provision of *Gist* is as follows:

The trustee shall pay to Elenore for so long as she shall live at quarterly intervals, or more often the income from the trust assets or so much thereof as may be necessary to provide her with a reasonable standard of living, considering any other means of support or resources which she may have. If the income shall be insufficient to provide her with a reasonable standard of living the trustee may invade the principal or corpus of the trust assets. While provision is hereinafter made for the disposition of any trust assets which may remain at Elenore's death it shall not be an objective of this trust to preserve the trust estate intact for the remaindermen beneficiaries nor to deny Elenore a reasonable standard of living for the purpose of enhancing the value of the trust estate or even preserving it for the

The trustee shall pay to Elenore for so long as she shall live at quarterly intervals, or more often the income from the trust assets or so much thereof as may be necessary to provide her with a reasonable standard of living, considering any other means of support or resources which she may have. If the income shall be insufficient to provide her with a reasonable standard of living the trustee may invade the principal or corpus of the trust assets. (emphasis added)

The Iowa Supreme Court characterized the trust as a discretionary support trust based solely on common law analysis and, as a result, concluded that Elenore Gist had the power during her lifetime to compel the trustees to make payments to her for her support.

The Iowa Supreme Court tried to explain the fine distinction between a pure discretionary trust and a discretionary support trust (which it labels, “a support trust with standards”):

A settlor creates a pure support trust “[i]f a trustee is directed to pay or apply trust income or principal for the benefit of a named person, but only to the extent necessary to support him, and only when the disbursements will accomplish support.”

In contrast, a settlor creates a [discretionary trust with standards] if “the stated purpose of the trust is to furnish the beneficiary with support, and the trustee is directed to pay to the beneficiary whatever amount of trust income [or principal] the trustee deems necessary for his support.”

Generally, if the trust is a [discretionary trust with standards], the beneficiary has a right that the trustee pay him the amount which in the exercise of reasonable discretion is needed for his support; and the beneficiary can transfer this interest or his creditors may reach it, unless it is protected by a spendthrift clause.

The trust also had a spendthrift clause.

Because of the Iowa Supreme Court’s belief that the trust’s dispositive language vested Elenore Gist with the power to compel a distribution to her during her lifetime, it ruled that the Department of Human Services (“DHS”) also had the power to compel a distribution to repay it for necessary living expenses it paid on Elenore’s behalf despite the existence of the spendthrift clause.<sup>32</sup> The Iowa Supreme Court considered Iowa Code Section 633A.2301(4) (2005) (before

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benefit of the beneficiaries. The discretion of the trustees shall therefore extend to disbursing the whole of the trust estate for Elenore’s benefit during her lifetime but, if possible, the trustee shall make provision for her burial expenses.

Emphasis added.

<sup>32</sup> Because DHS provided “necessities” to Elenore Gist in the form of food, shelter and health care, the Iowa exception to spendthrift clauses applied and DHS was able to “step into the shoes” of Elenore Gist to demand a

amendment), but, apparently, only in the context of whether DHS's claim could override the spendthrift clause of the trust.

The Iowa Supreme Court may have been confused on this matter because the spendthrift clause had no bearing on whether Elenore Gist, and thus DHS, had an interest in the trust's assets.<sup>33</sup> The appellants' brief focused solely on the spendthrift clause and not on the discretionary/nondiscretionary nature of the trust. Further, the brief did not address new Section 633A.4702.<sup>34</sup> Thus, the Iowa Supreme Court may not have been made aware of the distinction between spendthrift trusts and discretionary trusts or the existence of 633A.4702. Why the attorneys for the *Gist* beneficiaries did not advocate for discretionary trust status by invoking 633A.4702 is unclear. Perhaps they knew they would lose; that the strong "support" language in the Gist dispositive provision of the trust would easily overcome the effect of 633A.4702 (which purports to only being a tie-breaker).

Even though the *Gist* court may have arrived at the right result, how it arrived at that result was not very satisfying. Even in light of the 2004 legislative changes, the Iowa Supreme Court still applied a *Strojek* analysis without even mentioning the new section 633A.4702 that was designed to overrule *Strojek*. The Court could have found that the dispositive language in the Gist trust was just a "support" trust, but it didn't. It could have said that the dispositive language overcame the presumption of discretionary trust status provided by section 633A.4702, but it didn't.

#### **D. Roth**

On December 22, 2010, the Court of Appeals decided the *Roth* case<sup>35</sup> which was one of the first cases to fully address new section 633A.4702. The dispositive language in Gilbert F. Roth's will was substantially similar to the language in *Strojek*.

|                 |         |
|-----------------|---------|
| Gilbert F. Roth | Strojek |
|-----------------|---------|

distribution from the trust for reimbursement. *In re Dodge's Estate*, 281 N.W.2d 447 (Iowa 1979); Iowa Code § 633A.2302(3)(a) (2026).

<sup>33</sup> *Id.*

<sup>34</sup> 633A.4702 provides as follows: In the absence of clear and convincing evidence to the contrary, language in a governing instrument granting a trustee discretion to make or withhold a distribution shall prevail over any language in the governing instrument indicating that the beneficiary may have a legally enforceable right to distributions or indicating a standard for payments or distributions. (emphasis added).

<sup>35</sup> *In the Matter of Estate of Roth*, 09-1947, 797 N.W.2d 131 unpublished (Iowa Ct. App. 12/22/2010); *see also In re Kinsel*, No. 08-1625, 780 N.W.2d 248 unpublished (Iowa Ct. App. 2/10/2010).

|                                                                                                                                                                                                                                                                                                       |                                                                                                                                                                                                                                                                                                                      |
|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <p>[T]he trustee shall pay to or for the benefit of my spouse so much of the income and principal of the trust in such manner and proportions as the trustee, in the trustee's sole discretion, deems necessary for the reasonable care, health, education, support and maintenance of my spouse.</p> | <p>My trust shall, from time to time, pay to or apply for the benefit of my daughter, Marie Helen Strojek, <u>such sums from the income and principal as my trustee in the exercise of her sole discretion deems necessary</u> or advisable, to provide for her proper care, support, maintenance and education.</p> |
|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|

Iowa Code Section 633A.4702 gives priority to discretionary language (and thus lowers the “floor” for distributions) *unless there is clear and convincing evidence to the contrary*. The Iowa Department of Human Services, in seeking recovery from Mr. Roth’s trust for Mrs. Roth’s nursing home care, astutely discovered a provision in an unrelated section of Mr. Roth’s will providing broad discretion to the executor to make certain tax elections but “keeping in mind my primary concern is the welfare of my spouse.” This was all the Court of Appeals needed for clear and convincing evidence that the testator intended to give a mandatory right of support from his trust despite appellants many arguments to the contrary.

In *Strojek*-like cases, the Iowa Department of Health and Human Services (formerly DHS) clearly has the edge. In the face of ambiguous language (like *Strojek*), an opponent must show that the testator intended to allow his or her trustee to withhold distributions to a beneficiary even for life-sustaining necessities. If a testator loved his or her beneficiaries enough to make them beneficiaries, it seems counterintuitive that a testator would want to withhold trust funds for such life-sustaining necessities (such as food, shelter or nursing home care).

Nevertheless, a knowledgeable attorney can draft a trust instrument that unambiguously and effectively expresses the testator’s intent to give full and complete discretion to a trustee to make or withhold distributions, even in light of a beneficiary’s dire need. It can be as simple as avoiding the word “shall” in the same context of any discretionary powers given to the trustee. Had Mr. Roth included the following dispositive language, the outcome may have been entirely different:

my Trustee may pay (or not pay) to my wife such amounts of the income or principal of the Trust assets as my Trustee deems appropriate for her health, education, support and maintenance.

The language “may pay (or not pay)” certainly suggests that the minimal amount (the “floor”) that the trustee is required to pay to a beneficiary is zero. This is very different than the language used in *Roth* and *Strojek*:

My trust shall, from time to time, pay to or apply for the benefit of my daughter, Marie Helen Strojek, such sums from the income and principal as my trustee in the exercise of her sole discretion deems necessary or advisable, to provide for her proper care, support, maintenance and education.

As discussed below, even the grant of the broadest discretion to the trustee may still impose an obligation on the trustee to make a distribution.<sup>36</sup> See, *Extended Discretion – A Super Discretionary Standard*.

### **III. ABUSE OF DISCRETION**

Even a discretionary trust does not give a trustee unfettered discretion to make or not make distributions to beneficiaries. Iowa Code Section 633A.4214 provides that “[a]bsent an abuse of discretion, a trustee’s exercise of discretion is not subject to control by a court.”<sup>37</sup> Thus, the trustee must not “abuse its discretion.”

#### **A. What Constitutes an Abuse of Discretion?**

What constitutes an abuse of discretion depends on the terms of the trust, as well as basic fiduciary duties and principles. Of particular importance are the *purposes* of the discretionary power and the *standards of distribution*, if any, applicable to a trustee’s exercise, and the *extent of the discretion* conferred upon the trustee. Relevant fiduciary principles include (i) the general duty to act, reasonably informed, with impartiality among the various beneficiaries and interests, and (ii) the duty to provide the beneficiaries with information concerning the trust and its administration.<sup>38</sup> These are all discussed in detail, below.

#### **B. Terms of the Trust.**

Many trusts incorporate the HEMS standard of distribution: the grant of discretionary power to the trustee to make distributions to beneficiaries for their *health, education, maintenance and support*. The terms “maintenance and support” mean a beneficiary’s accustomed standard of living or station in life at the time of the trust creation.<sup>39</sup> It would be unreasonable for a trustee to provide only bare essentials for a beneficiary incapable of self support who had enjoyed a relatively comfortable lifestyle.<sup>40</sup> Alternatively, it would be unreasonable for a trustee to make a distribution to a beneficiary for the sole purpose of enlarging the beneficiary’s personal estate or to enable the beneficiary to make extraordinary gifts.<sup>41</sup> A trustee is justified in making a distribution under circumstances between these two examples. For example, a distribution for regular mortgage payments, property taxes, suitable health insurance or care, existing programs of life and property insurance, and continuation of accustomed patterns of vacation and of charitable giving and family giving.<sup>42</sup> It may also be reasonable for a trustee to make

<sup>36</sup> The Iowa Court of Appeals in a 2022 decision strongly alluded to this in the context of a Medicaid claim against the assets of a trust. *In the Matter of the Riessen Trust*, No. 22-0048 (Ia. Ct. Apps. 2022) (citing *Bogert’s the Law of Trusts and Trustees* §228 (June 2022 Update)); See also *Gist*, 763 N.W. 2d at 565 (citing *Bogert’s* with approval).

<sup>37</sup> See also, Restatement (Third) of Trusts, § 87 (2007).

<sup>38</sup> Restatement (Third) of Trusts § 50, cmt b (2003).

<sup>39</sup> Restatement (Third) of Trusts § 50, cmt d(2) (2003).

<sup>40</sup> *Id.*

<sup>41</sup> *Id.*

<sup>42</sup> *Id.*

distributions for additional comforts or luxuries that are within the means of many individuals of like station in life, such as a special vacation of a type the beneficiary had never before taken.<sup>43</sup>

### **C. Fiduciary Duties and Principles.**

An abuse of discretion may result from the exercise of discretionary authority in bad faith or from improper motive.<sup>44</sup> Thus, a discretionary power is abused if a trustee acts dishonestly, such as when the trustee receives an improper inducement for exercising the power in question.<sup>45</sup> Similarly, an abuse of discretion occurs when a trustee acts from an improper, even though not dishonest, motive, such as when the act is undertaken in good faith but for a purpose other than to further the purposes of the trust or, more specifically, the purposes for which the power was granted.<sup>46</sup>

An abuse of discretion may result from the trustee's improper failure to exercise that judgment. An abuse of this type results if the trustee, arbitrarily or without knowledge of or inquiry into relevant circumstances, fails to exercise the discretion. This was the case in *In the Matter of the Estate of Manahan*, 125 N.W.2d 135 (Iowa 1963), where the trustees failed to inquire about a beneficiary's financial status before denying an application for a distribution. So also, the court will interpose where a trustee fails to exercise or otherwise abuses discretionary authority because of mistaken interpretation of the terms of the trust or power, or a misunderstanding of applicable fiduciary law. Similarly, an abuse of discretion occurs when a trustee, even in good faith, exercises a power in a manner that is inconsistent with the duty of loyalty or the duty of impartiality.<sup>47</sup>

1) *Duty of loyalty.* Iowa Code Section 633A.4202(1) provides that a trustee shall administer the trust solely in the interest of the beneficiaries. The Restatement (Third) of Trusts Section 78(1) provides similar language and elaborates on the scope of this provision. This restatement generally applies to conflict of interest transactions.

2) *Duty of impartiality.* The trustee has a duty to administer the trust in a manner that is impartial with respect to the various beneficiaries requiring that in distributing trust assets, the trustee gives due regard to the diverse interests of the beneficiaries.<sup>48</sup> Being impartial does not mean being equal.<sup>49</sup> Rather, the trustee must balance the interests of the beneficiaries in a manner that reflects their different needs.<sup>50</sup> This includes respecting any ascertainable preferences of the

<sup>43</sup> *Id.*

<sup>44</sup> Restatement (Third) of Trusts § 87, cmt c (2007).

<sup>45</sup> *Id.*

<sup>46</sup> *See, e.g.,* Restatement (Third) of Trusts § 50, cmt d(2) (stating that a discretionary power to make distributions for a beneficiary's "support" does not permit the trustee to make well-intentioned, even otherwise reasonable, distributions that are not support-related).

<sup>47</sup> Restatement (Third) of Trusts § 87, cmt c (2007).

<sup>48</sup> Restatement (Third) of Trusts § 79(1).

<sup>49</sup> *Id.*, cmt. b.

<sup>50</sup> *Id.*, cmt. c.

settlor for some beneficiaries over others.<sup>51</sup> In this regard, the Restatement (Third) of Trusts Section 50, cmt. f indicates that certain inferences may be made as a starting point. It says that the beneficiary's relationship to the settlor is relevant and that the settlor's spouse is favored over the settlor's children. The settlor's prior course of dealing may also be relevant. For example, if the settlor had a consistent pattern of making gifts (or not) to his children, the trustee would have to consider such prior gifting when making (or withholding) distributions. Other factors to consider are the beneficiaries' other resources, earning capacity and station in life, discussed in more detail, below.

3) *Duty to keep beneficiaries informed.* The trustee has a duty to keep the beneficiaries reasonably informed about the administration of the trust and the material facts necessary to protect their interests.<sup>52</sup> There is no guidance in Iowa law regarding the scope of this section. However, this is the same language used in Restatement (Third) of Trusts Section 82(1)(c). Under the Restatement, the trustee has a duty to advise the beneficiaries of information that the trustee may need or desire regarding the beneficiaries' circumstances, needs, resources, concerns or wishes along with a disclosure by the trustee of the bases upon which discretion will be exercised.<sup>53</sup> This is important information that the trustee must collect in order for it to satisfy its duty of impartiality, discussed above.<sup>54</sup> If a court determines that the trustee has not attempted to ascertain the support needs of the beneficiaries, then the trustee has breached its fiduciary duty of impartiality and the court will be free to substitute its judgment for that of the trustee during the period in question.

4) *A general standard of reasonableness.* Perhaps most of the litigation in which it is concluded that a trustee has committed an abuse of discretion involves a finding that the trustee, in exercising a power, has acted unreasonably—that is, beyond the bounds of a reasonable judgment. In some cases there is an objective standard by which the reasonableness of the trustee's conduct can be measured, but expressed standards are not necessary in order for a good-faith decision of a trustee to be found unreasonable; a court may apply what has sometimes been called “a general standard of reasonableness,” taking account of other terms and purposes of the trust. In either event, judicial intervention on the ground of abuse is called for, not because the court would have exercised the discretion differently, but because the trustee's decision is one that would not be accepted as reasonable by persons of prudence. Thus, a court may properly interpose if it finds that the trustee's conduct, in exercising a discretionary power, fails to satisfy the applicable standard of care, skill, and caution. For example, if discretionary power is conferred upon a designated trustee to appoint a successor or additional trustee, and the designated trustee appoints an unfit person, the court will remove the person so appointed.<sup>55</sup>

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<sup>51</sup> *Id.*

<sup>52</sup> Iowa Code § 633A.4213 (2026).

<sup>53</sup> Restatement (Third) of Trusts § 82, Cmt. d (2007).

<sup>54</sup> Restatement (Third) of Trusts § 50(e)(1) (stating “[t]he trustee has a duty to act in a reasonable manner in attempting to ascertain the beneficiary's needs”).

<sup>55</sup> Restatement (Third) of Trusts § 87, cmt c (2007).

The Iowa Supreme Court set the standard for abuse of discretion in *In re Clark*.<sup>56</sup> There, it said:

“In determining whether a trustee has abused his or her discretion in exercising or failing to exercise a power, we consider (1) the intended breadth of the trustee’s discretion under the trust instrument; (2) the purpose of the trust; (3) the nature of the power at issue; (4) “the existence . . . of an external standard by which the reasonableness of the trustee’s conduct can be judged” and the definiteness of that standard; (5) “the motives of the trustee in exercising or refraining from exercising the power”; and (6) whether the trustee has an interest in conflict with the beneficiaries’ interest.”

These factors were considered in the 2016 Court of Appeals case of *In the Matter of the Helene R. MacMasters Trust*.<sup>57</sup> There, a disabled beneficiary requested a distribution of \$300,000 for a new house that would be compatible for the beneficiary who was wheelchair-bound and had limited use of his arms. The trustee denied the request and the trial court ruled that such denial was an abuse of discretion because the trustee did not “diligently and timely investigate the needs of the beneficiary and property consider those needs.” The Court of Appeals reversed and noted that there was no “dishonesty or improper motive” upon the trustee. The Court of Appeals believed that it was not in a position to substitute its judgment over the judgment of the trustee in this case. The Court of Appeals also noted that the trustee was not required to investigate every request for a distribution:

“The district court faulted the trustee’s failure to investigate Riha’s finances, but we decline to put the onus on the trustee to investigate every request that comes before it. While an income beneficiary’s request for a new home is unusual, Riha’s request is perhaps a reasonable one, and he has now put forth some justification for it. However, it would be inefficient to require a trustee to spend resources investigating every proposal, particularly while placing no similar duty on the beneficiary to justify the request. We find no court that has imposed such a duty. We do not think it was misguided or an abuse of discretion to request financial information from Riha before making his requested distribution, absent language in the will prohibiting such practice.”

#### **D. Extended Discretion – A Super Discretionary Standard**

Although the discretionary character of a power of distribution does not ordinarily authorize the trustee to act beyond the bounds of reasonable judgment, a settlor may manifest an intention to grant the trustee greater than ordinary latitude in exercising discretionary judgment. Consider a true discretionary trust provision that would have no upper (a “ceiling”) or lower limit (a “floor”):

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<sup>56</sup> 154 N.W. 759, 760 (Iowa 1915).

<sup>57</sup> No. 15-2142 (Dec. 21, 2016).

my Trustee may pay (or not pay) to my wife such amounts of the income or principal of the Trust assets as my Trustee deems appropriate.<sup>58</sup>

How does such an intention affect the duty of the trustee and the role of the court?

It is contrary to sound policy, and a contradiction in terms, to permit the settlor to relieve a “trustee” of all accountability. Once it is determined that the authority over trust distributions is held in the role of trustee, words such as “absolute” or “unlimited” or “sole and uncontrolled” are not interpreted literally. Even under the broadest grant of fiduciary discretion, a trustee must act honestly and in a state of mind contemplated by the settlor. Thus, the court will not permit the trustee to act in bad faith or for some purpose or motive other than to accomplish the purposes of the discretionary power. Except as the power is for the trustee’s personal benefit, the court will also prevent the trustee from failing to act, either arbitrarily or from a misunderstanding of the trustee’s duty or authority.<sup>59</sup> Iowa has codified this principle in Iowa Code § 633A.4214(2).

Within these limits, it is a matter of interpretation to ascertain the degree to which the settlor’s use of language of extended (e.g., “absolute”) discretion manifests an intention to relieve the trustee of normal judicial supervision and control in the exercise of a discretionary power over trust distributions.

**Illustration 1.** Following S’s death his previously revocable trust has been administered for nearly a decade by T Bank, which is directed to pay income to S’s widow, W, and also empowered to pay her “such additional amounts from the principal of the trust as the Trustee, in its sole and uncontrolled discretion, believes appropriate for W’s comfortable support and care,” with the remainder upon W’s death to pass to S’s then living issue. In response to requests by W, T Bank has begun to pay substantially increased amounts to her to enable her to accumulate funds from which she may aid C (her child by a prior marriage) in his plans to obtain control and expand the activities of X Co., of which C has been an officer and shareholder for a number of years. S’s children petition the court to instruct T Bank that principal distributions for that purpose are improper and that it must recover amounts previously paid to W for that purpose. Nothing in relevant circumstances or in other terms of the trust indicates a broader purpose for the invasion power than the support-related language quoted above. The court will issue the order requested by the remainder beneficiaries. Despite S’s grant of extensive discretion, and without a finding of bad faith, T’s judgment was not

<sup>58</sup> The language is essentially a power of appointment if held by someone not in a fiduciary capacity. The Restatement (Third) of Trusts distinguishes between a power of appointment and a trustee’s discretionary authority to distribute assets to himself or herself in that the latter is subject to a fiduciary obligation to the other beneficiaries whereas a power of appointment is not. Restatement (Third) of Trusts § 50 General Comment (2003).

<sup>59</sup> Restatement (Third) of Trusts § 50 cmt. c.

exercised in an appropriate state of mind, that is, for a purpose falling within the quoted standard.<sup>60</sup>

Thus, if the grantor truly desires to provide the broadest discretion possible, the grantor should do one of two things: (1) grant a special power of appointment to a non-fiduciary, or (2) be extremely specific about the scope of the trustee's authority. Consider the following language:

Throughout my husband's lifetime my Co-Trustees may or may not make a distribution to my husband and my children. If the Co-Trustees decide to make a distribution the Co-Trustees shall not distribute an amount in excess of the amount necessary to satisfy the distributee's need for health, education, maintenance and support without taking into consideration the distributee's other income and resources. The Co-Trustees' discretion is broad and the Co-Trustees need not make a distribution even under the most dire of circumstances. Any such payments need not be equal between or among my husband and my children either as individuals or as separate groups. Any income not distributed shall be added to principal.

Extended discretion serves to discourage challenges by remainder beneficiaries to the generosity of trustees, as in Illustration 2. On the other hand, it may also make it difficult for a discretionary beneficiary to obtain judicial intervention when a trustee's judgments are highly conservative with regard to matters that fall within the settlor's authorized purposes. The overall tenor of the terms of a power may, however, in the context of the trust's more general purposes, lead to an interpretation granting the trustee ordinary discretion with respect to the benefits to which the discretionary beneficiary is minimally entitled (e.g., reasonable support), with the extended discretion applicable to the trustee's allowance of more. This "one-sided" liberalization of the discretionary authority, where a court finds the settlor's language was intended to assure generosity in favor of a life beneficiary, would thus tend to encumber the efforts of remainder beneficiaries who seek to challenge what might otherwise be excessively generous decisions by a trustee.

## **E. Standards**

The terms of trusts usually provide some standards or guidelines concerning the purposes the settlor has in mind in creating a discretionary interest. Reasonably definite or objective standards serve to assure a beneficiary some minimum level of benefits, even when other standards are included to grant broad latitude with respect to additional benefits.<sup>61</sup>

Sometimes trust terms express no standards or other clear guidance concerning the purposes of a discretionary power, or about the relative priority intended among the various beneficiaries. Even then a general standard of reasonableness, or at least of good-faith judgment, will apply to the trustee, based on the extent of the trustee's discretion, the various beneficial interests created,

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<sup>60</sup> *Id.*

<sup>61</sup> Restatement (Third) of Trusts § 50, cmt d.

the beneficiaries' circumstances and relationships to the settlor, and the general purposes of the trust.

The terms "support" and "maintenance" are normally construed as synonyms, even when this treats the terms as redundant. Probably the most common guides used in grants of discretion, these terms are sometimes accompanied by a reference to the beneficiary's accustomed standard of living or station in life. That level of intended support is normally implied from "support" or "maintenance" even without an express reference to the beneficiary's customary lifestyle. Whether this accustomed style is expressed or implied, a lower level of distributions may be justifiable if the trust estate is modest relative to the probable future needs of the beneficiary.

The accustomed manner of living for these purposes is ordinarily that enjoyed by the beneficiary at the time of the settlor's death or at the time an irrevocable trust is created. The distributions appropriate to that lifestyle not only increase to compensate for inflation but also may increase to meet subsequent increases in the beneficiary's needs resulting, for example, from deteriorating health or from added burdens appropriately assumed for the needs of another. Also, if a beneficiary becomes accustomed over time to a higher standard of living, that standard may become the appropriate standard of support if consistent with the trust's level of productivity and not inconsistent with an apparent priority among beneficiaries or other purpose of the settlor. Furthermore, distributions allowing the beneficiary an increased standard of living may be appropriate if, in light of the productivity of the trust estate, the eventual result would otherwise favor the remainder beneficiaries over the present beneficiary to a degree unlikely to have been intended by the settlor. "Productivity" for these purposes refers not only to trust income but also to a pattern of appreciation beyond maintenance of purchasing power, such as might result from a growth-oriented investment program.

During 2008, the Iowa Court of Appeals decided the *Windus* case, in an unpublished decision.<sup>62</sup> The *Windus* case involved three children who accused their mother of improper withdrawals from their father's trust. The three children were remainder beneficiaries and their mother was trustee with discretion to make principal payments to herself for her *health, education, support and maintenance*.<sup>63</sup> The sole issue before the Court of Appeal was whether the mother abused her discretion by making distributions to herself of more than \$110,000. The Iowa Court of Appeals believed it necessary to characterize the trust and deemed it a "discretionary support" trust, but it made no reference to Sections 633A.2301 (2005) or 633A.4702 (2005). However, the Iowa Court of Appeals ruling clearly did not require a determination of the trust's status as "discretionary" or "support" or anything in between. Instead, it held that the mother's distribution to herself of \$110,990.00 did not abuse her discretion to make distribution to herself

<sup>62</sup> *In re Family Trust of Keith Windus*, No. 07-2006, unpublished decision, 758 N.W.2d 840 (Iowa App. 2008).

<sup>63</sup> The dispositive provision of the trust provided that all the income was to go to the mother and the principal as follows: "my trustee shall pay to my spouse such sums from the principle as my trustee deems advisable for my spouse's health, education, support and maintenance."

for her support and maintenance and the court did not require her to exhaust her other resources before receiving such distribution.

#### **F. Other Resources of Beneficiaries**

The Restatement (Third) of Trusts Section 50(e) provides that the trustee should consider the other resources of a beneficiary but *has some discretion* in the matter.

The Restatement provides some qualifications to the general rule so stated. Where a beneficiary is entitled to payments from another trust created by the same settlor (e.g., nonmarital and marital deduction trusts for a surviving spouse), or as a part of coordinated estate planning with another (such as the settlor's spouse), required distributions from the other trust—and the purposes of both trusts—are to be taken into account by the trustee in deciding whether, in what amounts, and from which trust(s) discretionary payments are to be made. Restatement (Third) of Trusts § 50, cmt e.

Another qualification is that, to the extent and for as long as the discretionary interest is intended to provide for the support, education, or health care of a beneficiary (or group of beneficiaries) for periods during which a beneficiary probably was not expected to be self-supporting, the usual inference is that the trustee is not to deny or reduce payments for these purposes because of a beneficiary's personal resources. Restatement (Third) of Trusts § 50(e). Further, the Restatement suggests (without citation of specific judicial authority) that a trustee is entitled to take into account an unemployed or underemployed beneficiary's earning capacity (see below). Restatement (Third) of Trusts § 50(e)(5).

Iowa caselaw is a little vague on any governing standard. In *In re Tone's Estates*,<sup>64</sup> the Iowa Supreme Court held that it was proper for a trustee to consider a beneficiary's regular income and borrowing capacity as support for the trustee's *denial* of a request for a distribution to the beneficiary from the trust.

In *In the Matter of the Trust of McCabe*, No. 01-1972, unpublished decision (Iowa App. 2002); WL 31757533, a trustee of what the court labeled a discretionary support trust refused to distribute any funds to the beneficiary for the beneficiary's nursing home costs without first receiving a detailed accounting of the beneficiary's other assets and income. The court noted that the trust did not require the beneficiary to deplete her other income or assets first and therefore such documentation request was unnecessary.

During 2008, the Iowa Court of Appeals decided the *Windus* case, an unpublished decision. *In re Family Trust of Keith Windus*, No. 07-2006, unpublished decision, 758 N.W.2d 840 (Iowa App. 2008). The *Windus* case involved three children who accused their mother of improper withdrawals from their father's trust. The three children were remainder beneficiaries and their mother was trustee with discretion to make principal payments to herself for her *health*,

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<sup>64</sup> *In re Tone's Estates*, 39 N.W.2d 401 (1949).

*education, support and maintenance.*<sup>65</sup> The sole issue before the Court of Appeals was whether the mother abused her discretion by making distributions to herself of more than \$110,000. The Iowa Court of Appeals believed it necessary to characterize the trust and deemed it a “discretionary support” trust, but it made no reference to Sections 633A.2301 (2005) or 633A.4702 (2005). The court held that the mother’s distribution to herself of \$110,990.00 did not abuse her discretion to make distribution to herself for her support and maintenance and the court did not require her to exhaust her other resources before receiving such distribution.

#### **G. May the Trustee Take Into Consideration Whether a Beneficiary Is Unemployed Or Underemployed?**

The Restatement (Third) of Trusts § 50, cmt e(5) provides that this is a question that must be decided on a case-by-case basis absent some guidance from the settlor. Section 50, cmt. g, of Restatement (Third) of Trusts provides that a settlor’s “personal feelings” about a beneficiary is relevant along with whether it would have been “customary or would be natural for the settlor to provide for a beneficiary’s needs.” If a settlor was explicit in his or her desire that his or her children be self sufficient and not reliant upon others for their support, a trustee may be able to rely upon such facts (if they can be developed) to support a decision to make or not to make a discretionary distribution.

#### **H. Relationship of Beneficiary**

Relationship to the settlor is relevant and a settlor’s spouse is presumed to be at the top of the list of favored beneficiaries.<sup>66</sup> However, “favored status” (or status as a “primary” beneficiary) does not necessarily mean that a surviving spouse should receive principal and income payments greater than—or even equal to—the distributions made to others; nor does it mean either that the trustee *may not* withhold principal payments to him or her because of his or her other resources or that in considering and making distributions to the settlor’s descendants the trustee *must* take account of their independent resources. What a surviving spouse’s favored status does mean is that, in the absence of compelling considerations, the trustee is to give priority to providing what he or she needs, if anything, to continue his or her lifestyle and to have appropriate care and other suitable benefits. *Id.*

Following are other inferences set out in the Restatement:

—Relationship to the settlor is relevant, leading in the most common situations to an inference that the beneficiary at the top of a line of descendants is favored over his or her own issue, with the settlor’s spouse also so favored whether or not an ancestor of the others (e.g., settlor’s issue by prior marriage).

<sup>65</sup> The dispositive provision of the trust provided that all the income was to go to the mother and the principal as follows: “my trustee shall pay to my spouse such sums from the principle as my trustee deems advisable for my spouse’s health, education, support and maintenance.”

<sup>66</sup> Restatement (Third) of Trusts § 50, cmt f.

—Among multiple lines of descent (e.g., all of the settlor’s issue) there is an inference of priorities per stirpes, that is, that (i) the various lines are entitled to similar, impartial treatment, with disparities to be justified on a principled basis consistent with the trust purposes, and that (ii) the inference of favored status within a descending line begins with the person(s) at the top (e.g., the settlor’s child or the children of a deceased child).

—The preceding inference applies to the typical family trust for the support and education of minor or youthful beneficiaries following the death of one or both of their parents, with a preference for a common standard of living and similarity of opportunity to be balanced against usually modest funding and almost inevitably different beneficiary needs, capacities, and interests.

—Because these various situations do not involve “substantially separate and independent shares” for different lines of beneficiaries, it is presumed that differences in benefits received by remainder beneficiaries or their ancestors during the trust period are not later to be taken into account in determining shares upon subsequent distribution, or in dividing the original trust for continuation thereafter in separate shares or trusts for separate lines of issue.<sup>67</sup>

## **I. Trustee Conflict of Interest**

Frequently, a settlor will appoint a beneficiary as a trustee. This situation creates a conflict of interest between the trustee who is a beneficiary, and all the other beneficiaries of the trust. The Restatement provides that such conflicts are permissible, but the acts of the trustee are carefully scrutinized for abuse.<sup>68</sup> In such case, the court will not substitute its judgment for the trustee/beneficiary’s judgment merely because it would have exercised the discretion differently. It will, however, intervene if it finds that trustee/beneficiary has acted unreasonably, after considering in this situation not only such matters as the standards set out in the terms of the trust but also the fact that the settlor has trusted the trustee/beneficiary to serve as trustee with the fiduciary authority to determine the amounts of principal appropriate to his or her own comfortable support.<sup>69</sup> Iowa Code Section 633A.4214(3) provides that, unless the trust expressly provides otherwise, a non-settlor beneficiary-trustee may exercise a discretionary power to distribute to himself or herself only in accordance with an ascertainable standard relating to health, education, support, or maintenance within the meaning of IRC §§ 2041(b)(1)(A) or 2514(c)(1), and may not make discretionary distributions to satisfy the trustee’s personal legal support obligations. The limitation does not apply to marital-deduction trusts where the spouse is trustee, revocable trusts, or trusts under IRC § 2503(c). Section 633A.4214(4) allows the remaining unrestricted trustees or a court-appointed special fiduciary to exercise the power.

## **J. Recent Statutory Tools: Decanting and Directed Trusts**

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<sup>67</sup> *Id.*

<sup>68</sup> Restatement (Third) of Trusts, §§ 37, cmt. *f*, 50, cmt. *b*.

<sup>69</sup> *Id.*

## **1. Decanting.**

Decanting Generally. The term “decanting” generally refers to a process whereby a *trustee* exercises discretionary authority set forth in an existing trust instrument or by statute by distributing trust assets to a new trust for the benefit of one or more of the original beneficiaries or new beneficiaries. “Decanting” may also refer to a modification of a trust instrument carried out unilaterally by the trustee, having essentially the same result as previously described without actually moving trust corpus to a new trust.

Decanting can have many objectives. Minor administrative changes may be made by decanting; correction of errors; clarifying ambiguous language; or changing trust jurisdiction. More substantive changes can be made by decanting such as broadening distribution powers; add or remove beneficiaries; or create new powers of appointment.

Iowa’s Decanting Statute. Iowa adopted a decanting statute in 2020, codified at Iowa Code Section 633A.4215. It provides authority to the trustee to *either* transfer the assets of a trust to a new trust<sup>70</sup> or modify the existing trust.<sup>71</sup> If the trustee chooses to modify the existing trust, then the trustee must send a 20-day notice to the beneficiaries.<sup>72</sup> The trustee’s authority to transfer to a new trust does not require such notice; the trustee can exercise his, her or its authority in secret.

The trustee may only exercise a decanting right if the trustee otherwise has discretionary authority to make distributions to one or more beneficiaries.<sup>73</sup> If exercised, the trustee may not add to the class of beneficiaries entitled to a distribution, but the trustee can narrow the class by cutting or limiting them.<sup>74</sup> The trustee is even allowed to give a beneficiary super powers by the grant of a nonfiduciary special or general power of appointment.<sup>75</sup> With this decanting authority, the trustee has the authority to change the entire dynamic of the trust. But should he?

Fiduciary Liability to a Decanting Trustee. Just because a trustee can decant, doesn’t mean he should decant. Trustees with discretionary authority have fiduciary obligations to beneficiaries to exercise such discretion with prudence, skill and impartiality.<sup>76</sup> Iowa’s decanting statute is a little elusive whether it gives a trustee a free pass from liability for decanting. One part of the decanting statute says that the exercise of a decanting power is equivalent to the exercise of a special power of appointment.<sup>77</sup> Generally, a nontrustee power holder does not have fiduciary obligations.<sup>78</sup> A

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<sup>70</sup> Iowa Code §633A.4215(2) (2021).

<sup>71</sup> Iowa Code §633A.4215(2)(k) (2021).

<sup>72</sup> Iowa Code §633A.4215(2)(k) (2021) (stating “a modification in further trust pursuant to this paragraph shall require the trustee to notify all beneficiaries . . .”).

<sup>73</sup> Iowa Code §633A.4215(2) (2021).

<sup>74</sup> Iowa Code §633A.4215(2)(a) (2021).

<sup>75</sup> Iowa Code §633A.4215(2)(j) (2021).

<sup>76</sup> Iowa Code §§633A.4202; 4203; and 4205 (2021).

<sup>77</sup> Iowa Code §633A.4215(7) (2021).

<sup>78</sup> Restatement (Third) of Trusts, §75, comment d (stating “a power that is for the sole benefit of the person holding the power is not a fiduciary power”).

trustee holding a power of appointment generally does.<sup>79</sup> Nevertheless, the Iowa decanting statute imposes certain obligations on the trustee who decants:

[T]he trustee of the first trust shall determine whether the appointment is necessary or desirable after taking into account the purposes of the first trust, the terms and conditions of the second trust, and the consequences of the distribution.<sup>80</sup>

This part of the Iowa decanting statute certainly appears to impose obligations on the trustee.

There are few cases of fiduciary liability regarding decanting, but the ones that exist are illuminating. In *Hodges v. Johnson*,<sup>81</sup> a New Hampshire case, two irrevocable trusts were established in 2004 for the benefit of the settlor's wife, children, other descendants and step-children. The Trustees had a discretionary power to "distribute all or any portion of the net income and principal of the trust to any one or more of the group consisting of [the beneficiaries] and distributee trusts, in such amounts and at such times as the Trustee, in the Trustee's discretion, may determine." "Distributee trusts" were defined as any trust under the trust instruments or any other trust established by the settlor. A distributee trust could be for the benefit of one or more, "but not necessarily all," of the beneficiaries.

The trustees of the two irrevocable trusts signed documents effectively decanting the trusts' assets to new trusts. The governing instruments of the new trusts omitted the settlor's two step-children and one of his biological children from the definition of "descendants," effectively stripping their interests in the trusts. The decanting documents provided for the transfer of the assets of the original trusts to the new trusts upon the settlor's death, and so the assets of the original trusts were not transferred to the new trusts contemporaneously with the signing of the decanting documents. Both the trial court and the Supreme Court of New Hampshire treated the decantings as if they had occurred when decanting documents were executed and as if the failure promptly to transfer the assets didn't render the decantings invalid.

Under New Hampshire's decanting statute in effect when the decantings occurred, and now, if a trustee of a trust has the power to make discretionary distributions of principal to one or more beneficiaries, the trustee may decant the assets of that trust to another trust "for the benefit of one or more" of the beneficiaries of the original trust<sup>82</sup> (obviously implying that, at least in some circumstances, one or more beneficiaries of the original trust may be excluded as beneficiaries of the new trust).

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<sup>79</sup> Restatement (Third) of Prop., §17.1, comment g, "[i]n the case of a discretionary power of appointment . . . the donee may exercise the power arbitrarily as long as the exercise is within the scope of the power. In the case of a fiduciary distributive power, the fiduciary's exercise is subject to fiduciary obligations as provided in the Restatement (Third) of Trusts."

<sup>80</sup> Iowa Code §633A.4215(2) (2021).

<sup>81</sup> 177 A.3d 86 (N.H. 2017).

<sup>82</sup> N.H. Rev. Stat. § 564-B:4-418(a).

The trial court set aside the decantings and removed the Trustees. On appeal, the Supreme Court of New Hampshire held that, even though New Hampshire's decanting statute allowed the Trustees to eliminate beneficiaries, and even though the Trustees were permitted to distribute income and principal in their discretion, they were nevertheless subject to the duty of impartiality in carrying out the decanting. The New Hampshire Supreme Court stated that "a trustee, who makes unequal distributions among beneficiaries and/or eliminates a beneficiary's non-vested interest in an irrevocable trust through decanting, violates the statutory duty of impartiality . . . when the trustee fails to treat the beneficiaries 'equitably in light of the purposes and terms of the trust.'"<sup>83</sup> The Supreme Court of New Hampshire noted favorably the trial court's finding that, in decanting, the trustees failed to consider the interests of all of the beneficiaries, present or remainder, vested or contingent. Despite the seemingly plain language of New Hampshire's decanting statute, the New Hampshire Supreme Court opined it would be "difficult to imagine the factual scenario where the trustee would not violate its fiduciary duty of impartiality owed to that [eliminated] beneficiary."

The obvious learning from this New Hampshire case is any trustee wishing to exercise a decanting right should first protect itself by acquiring the consents of all beneficiaries in the same manner as in a modification or termination of a trust under Iowa Code Section 633A.2202 (2021). The sole difference is that the consent of the settlor would not seem to be necessary in a decanting. A trustee could also seek consent of a court prior to decanting.<sup>84</sup>

If a settlor wanted to prohibit a decanting, he or she can do so by inserting such desire into the trust document.<sup>85</sup>

## **2. Directed Trusts.**

In 2020, the Iowa legislature enacted Iowa Code sections 633A.4801 through 633A.4810 concerning trust directors and trust protectors. A trust director is typically held to fiduciary standards; a trust protector is typically not a fiduciary. Section 633A.4808 permits a distribution trust director to direct discretionary distributions, and under section 633A.4810 the distribution trust director's powers over discretionary distributions are exercised in the director's sole and absolute discretion in the best interests of the beneficiaries as a class and bind the trustee. Section 633A.4207(2) makes status depend on powers granted by the trust instrument, not the title given to the individual.

Also, Iowa Code section 633A.4206(1) provides that a trustee may not delegate to an agent or cotrustee responsibility for decisions on discretionary distributions.

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<sup>83</sup> Quoting the Uniform Trust Code § 803.

<sup>84</sup> Iowa Code §633A.4215(2) (2021).

<sup>85</sup> Iowa Code §633A.4215(2) (2021) (stating "[u]nless the terms of the governing instrument expressly provide otherwise . . .").