INCENTIVE TRUSTS AND PLANNING ACROSS GENERATIONS (WITH SAMPLE PROVISIONS)

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I. INTRODUCTION — BECAUSE MONEY DOESN'T COME WITH INSTRUCTIONS

In 1758, prior to the birth of our nation, Benjamin Franklin printed a short treatise entitled The Way to Wealth. One of the first, if not the first American book on personal finance, The Way to Wealth is the source of such famous aphorisms as "early to bed, and early to rise, makes a man healthy, wealthy and wise." Franklin translated his work into a book of picture riddles for children entitled The Art of Making Money Plenty, believing that it was never too early to begin learning the concepts of financial management.

The fact that our founding fathers struggled with the challenges associated with transitioning wealth to the next generation, with which difficulties we still find ourselves wrangling today, is not necessarily a comforting realization. Unfortunately, there is no one answer or simple way to educate the next generation or one magic transfer technique that fits all occasions.

We still live in a world where the failure of wealth transfer gives rise to clichés such as "shirtsleeves to shirtsleeves in three generations." The first generation creates the wealth. The second generation, often having experienced the struggles of their parents to earn and save, and generally under the watchful eye of the first generation, preserves the wealth. The third generation, having grown up knowing wealth and typically not having witnessed the obstacles overcome to create it, knows no better and dissipates the family wealth. The fourth generation is then left to start from scratch—from shirtsleeves to shirtsleeves. This dilemma is not just an American problem, however, as many cultures around the world have parallel metaphors.

The concept reflected by the shirtsleeves metaphor is not purely financial, however. John Adams is attributed widely with having said "I must study politics and war that my sons may have liberty to study mathematics and philosophy. My sons ought to study mathematics and philosophy, geography, natural history, naval architecture, navigation, commerce and agriculture in order to give their children a right to study painting, poetry, music, architecture, statuary, tapestry, and porcelain." With the change in financial fortune over the generations often comes a shifting of values, and Adams eloquently captured that sentiment.

There are numerous studies regarding family wealth transition that all reach the same conclusion: the senior generations, particularly the Baby Boomers, do not put enough thought and effort into planning for transition of wealth to succeeding generations. The reasons that individuals with wealth to pass on to their descendants fail to plan is unclear. Perhaps it is a discomfort with facing their own mortality, or perhaps they are frozen by paralysis of analysis when faced with difficult family dynamics? Regardless of

the reasons behind the inaction, the result generally is not positive, either emotionally or financially.

In order to successfully tackle stumbling blocks that prevent successful wealth transfer, it is useful to understand the societal forces affecting and legal issues restricting transition of family assets and values. Most of the drafting techniques considered and issues discussed are relevant to estate planning in the 21st century, regardless of the testator's net worth. Furthermore, the educational methods noted to help transmit values along with wealth are adaptable to varying net worth situations.

II. HISTORICAL DEVELOPMENT OF THE RIGHT TO BEQUEATH

A. Constitutional History

1. As a general rule, the laws dictating the rules for intergenerational wealth transfer are controlled by the states.
    a. Federal law does interact with state law in this arena, though, most often with respect to taxation of estates and trusts and distribution of trust income.
    b. There is significant variation from state to state, it is important to understand the applicable law of the governing jurisdiction, some of which is set forth by statute, but much of which stems from common law.
    c. In certain significant instances, however, the federal courts have set forth some important rules that provide a framework for testamentary disposition.
2. Historically, the laws of all civilized states recognized the absolute right of citizens to earnings, the enjoyment of property, and the disposition of property by will.[1]
    a. This right to pass property, both real and personal, has been part of the Anglo-American system since feudal times.
    b. Under King Henry II's reign, a man's goods were to be divided into three equal parts: one part to his heirs or lineal descendants, a second part to his wife, and the third part disposed of at the decedent's pleasure.[2]
3. The Supreme Court in 1896 stated that it knew of "no legal principle to prevent the legislature from taking away or limiting the right of testamentary disposition, or imposing such conditions upon its exercise as it may deem conducive to public good."[3]
    a. One hundred years later, however, the Supreme Court, in Hodel v. Irving, seemed to find that a constitutional right to bequeath property did exist.[4]
        i. Hodel involved seizure of tribal lands from estates of individual owners by Congressional Act.
        ii. In the early 1980s, members of the Oglala Sioux tribe brought suit seeking a declaratory judgment to hold the section of the Indian Land Consolidation Act (Act) unconstitutional on the grounds that it authorized seizure without the just compensation required by the Fifth Amendment.[5]
            (1) The Act stated, "No undivided fractional interest in any tract or trust or restricted land within a tribe's reservation or otherwise subjected to a tribe's jurisdiction shall descedent [sic] by intestacy or devise but shall escheat to that tribe if such interest represents 2 per centum or less of the total acreage in such tract and has earned to its owner less than $100 in the preceding year before it is due to escheat."[6]
            (2) The issue before the court was whether it was constitutional to prohibit passing de minimus amounts of Oglala Sioux Tribe land by intestate succession or devise and to instead force escheat to the tribe.[7]
    b. The Supreme Court noted that the right to "pass on property" has been a part of the legal system since feudal times and that the

attempted regulation amounted to the abrogation of the right to pass property.[8]

(1) "Moreover, [the] statute effectively abolishe[d] both devise and descent of these property interests…"[9]

(2) In affirming the Eighth Circuit's decision in *Irving v. Clark* the Supreme Court confirmed a constitutional right to pass property by devise and descent that is integral to today's successful transfer of intergenerational wealth.

B. The Influence of Society

1. The rules governing a testator's ability to place conditions on a gift at death are continually evolving.

   a. The law reacts to societal adjustments.

   b. Laws of different nations (and States) react at a different pace according to what the occupants of the political subdivision consider acceptable values.

   c. For example, consider the 2009 case involving Natal University College.[10]

      i. In the mid-1930s the testator, Sir Charles George Smith, drafted a will that left one-third of his estate in trust to fund the university education of European girls born of British South African or Dutch South African parents.

         (1) At the time his will was drafted, his intent was to assist poor white women who were financially disadvantaged and unlikely to attend college or university.

         (2) Sir Charles would not have focused on African women because at that time very few Africans, in general, attended college, let alone African women.

         (3) Unfortunately, Sir Charles could not foresee that today his bequest would not be seen as progressive, but rather as discriminatory and intended to preserve the privilege of the white women of South Africa.

      ii. Natal University College petitioned the court to have the trust modified to delete the terms "European," "British," and "Dutch South African" deleted.

         (1) The college relied on a provision of law that allows trust modification if, in the opinion of the court, the provision creates consequences the settlor could not anticipate and hinders the purpose of the trust, prejudices the interests of the beneficiaries, or runs contrary to public interest.

         (2) The court determined that to allow funds to be allocated to a specific population in a discriminatory manner was against public interest and granted the petition of the college.

III. A SURVEY OF CASE LAW REGARDING RESTRICTIVE BEQUESTS AND TRUST PROVISIONS

A. Posthumous Meddling or Valid Conditions?

1. Testators have tried to control from the grave since the beginning of time under the very basic rationale that it is their money and they should be able to dispose of it as they choose. For the most part, the U.S. courts have agreed with this principle.

2. In 1917, the Iowa Supreme Court was asked to determine whether a testator's provision vested his son with a fee simple absolute or with a defeasible fee.[11]

   a. The testator bequeathed one-half of his estate to his son on the condition that at the time of the son's death he was survived by living issue.[12] Upon the son's death, the son's wife challenged the condition and argued that the condition only applied should the son die during the life of the testator.[13]

   b. Rejecting the objection to the condition, the court stated: "[The testator] had the undoubted right to attach such condition to

his gift, and it would be difficult to indeed to express such intent in clearer or more explicit terms. The meaning being plain and the intent being lawful, there is no room left for controversy. It is not for the court to question or consider the absolute justice of the condition; its only function is to ascertain the testator's intent and give it effect."[14]

3. Courts will hold conditions in total restraint of marriage to be against public policy.[15]
    a. A partial restraint that limits, for example, a class of persons or the period of time in which marriage must occur, is more likely to be upheld.[16]
    b. In most instances, restriction of a beneficiary's marriage to persons of a designated faith generally is regarded as reasonable.[17]
    c. Further, courts will look to the testator's intent to determine whether a provision is a restraint of marriage.
        i. A New York testatrix included a provision in her will that precluded the sale of testatrix's residence until such time as all of the testatrix's children were married or left the residence and lived elsewhere, at which time the residence would be divided equally among the testatrix's children.[18]
        ii. The residence consisted of a store front on the bottom level, an apartment on the second level, and an apartment on the third level. The testatrix executed the will in 1983 when all four of her children were not married. After one of her son's divorce in 1993, he lived with the testatrix in the apartment on the second level and continued to live in said apartment even after the testatrix's death. Another one of testatrix's children lived with her family in the apartment on the third level and moved out shortly after the testatrix's passing. Due to the provision in the will, the residence could not be sold. Two of testatrix's children sued, alleging that the testratrix's will imposed conditions designed to discourage marriage in contravention of public policy.
        iii. The court found that the provision did not impose conditions designed to discourage marriage, even though the condition provides for a sale when all of the children live elsewhere, married or single. The court looked to the testatrix's intent and determined her intent was to provide all of her children with a secure place to reside while unmarried; thus, the court concluded, the provisions did not impose a condition calculated to discourage marriage or to induce divorce, but rather to provide for the support and maintenance of the testatrix's children. [19]

B. Religious Conditions on Marriage

1. A Massachusetts testator included a provision in his will that disincentivized his children from marrying outside the Jewish faith.[20] Should his children marry outside of the faith, all gifts would be revoked.
    a. His son married a woman who, at the time of their civil ceremony, was Roman Catholic.[21] Within months after the civil ceremony, the wife converted to Judaism and then participated in a rabbinical ceremony of marriage.[22]
    b. The court said that because the wife was not in any sense Jewish or Hebrew at the time of marriage, the son could not take under his father's will.[23] The court noted that the principal question in the case was not whether the testator used good judgment in including the provision in his will, but whether the testator was prevented from doing so by any rule of law.
2. Similarly, an Oregon court rejected the contention that a provision was against public policy because it prohibited a beneficiary from embracing the Roman Catholic faith or marrying a man of the Roman Catholic faith until she attained a certain age.[24]

a. The court noted that it was the prevailing rule that conditions in partial restraint of marriage were upheld if they did not unreasonably restrain a beneficiary's choice in spouse.[25]

b. In upholding the restriction, the court noted that the condition was temporary and there was a substantial pool of non Roman Catholic potential spouses.

3. In Clayton's Estate, testator sought to encourage his son's marriage to a Protestant and discourage his marriage to a Roman Catholic.[26] Should the son marry a Roman Catholic, he would receive income for life from a trust.[27] Should he marry a Protestant, he would receive income for life, and upon his death his surviving issue would take the principal of the trust.[28]

   a. Testator's son was married to a Catholic woman with whom he had children, and argued that the condition was religious discrimination.[29]

   b. The court found the son's argument flawed because it may have affected his choice of wife, but did not restrict his religious freedom. Although the court recognized the "bigotry and prejudice" of the conditions, the conditions were upheld as valid as a matter of law.[30]

4. One of the more extreme provisions upheld was one that required the beneficiary to marry a Jewish girl born of two Jewish parents within seven years after testator's death or the gift would go over to the State of Israel.[31]

   a. The Ohio court held the provision was constitutional, valid, and not contrary to public policy.

   b. In its decision to confirm this stringent condition, the court stated: *Whether this judgment was wise is not for this court to determine. But it is the duty of this court to honor the testator's intention within the limitations of law and of public policy. The prerogative granted to a testator by the laws of this state to dispose of his estate according to his conscience is entitled to as much judicial protection and enforcement as the prerogative of a beneficiary to receive an inheritance.*[32]

5. Similarly, the Illinois Supreme Court reversed the lower court's decision and refused to invalidate a clause that provided that any such descendant who married outside the Jewish faith or whose non-Jewish spouse did not convert to Judaism within one year of marriage would be "deemed deceased for all purposes."[33] The Illinois Supreme Court found that such a restriction clause does not violate public policy. The decedents "were free to distribute their bounty as they saw fit and to favor grandchildren of whose life choices they approved over other grandchildren who made choice of which they disapproved, so long as they did not convey a vested interest that was subject to divestment by a condition subsequent that tended to unreasonably restrict marriage or encourage divorce."[34]

6. Although more rare than cases like those cited above, there are cases where the courts draw a line when conditions are so narrow (whether by terms or circumstances) as to be unreasonable.

   a. One early example of a provision that was voided for this reason occurred in the mid-nineteenth century when a testator included a provision that required his daughter to remain a member of the Friends Society (Quakers).[35] After the death of the testator, the beneficiary married outside of the Society of Friends which ended her membership in the organization.

   b. A Virginia court held that it could not avoid the conclusion that the condition imposed by the bequest was an undue and unreasonable restraint on marriage and ought to be disregarded.[36] At the time the beneficiary was of marrying age, there were approximately five marriageable males in the Friends Society, which the court found imposed too significant a marital restraint.[37]

C. Conditions Inducing Divorce

1. Although some early courts had no problem with conditions that induced divorce (since it was

a legal act), the general rule today is that restrictions found to induce or encourage divorce will be held invalid as against public policy.

   a. Today, courts tend to investigate the intent of the testator.

   b. If a testator actually intended to induce divorce, the condition will be held void. If the testator's intention was economic, perhaps an effort to protect A from her husband's extravagant spending, then the condition will be upheld.[38]

2. In Winterland v. Winterland, the testator included a clause in his will that directed his son's share to be put in trust until his son's wife died or was separated from him for at least two years.[39]

   a. The son's family brought suit and alleged the clause promoted divorce and was contrary to good morals and public policy.[40]

      i. The court reasoned that in situations where a divorce was already pending, the condition did not induce divorce and was therefore valid.[41]

      ii. Where no separation had occurred, a provision dependent upon separation or divorce was null and void.[42]

   b. In this case, testator was attempting to encourage divorce, and the condition was held void.[43]

3. In Estate of Gerbing, the testator included a provision in her will that instructed the executor to deliver the principal of a trust to her son if his wife was deceased or they had been divorced for two years.[44]

   a. The son filed a petition with the court and alleged this provision was against public policy because it was an inducement to obtain a divorce.[45]

   b. The estate argued the testator's intent was to provide for her son's well-being.[46] The court disagreed that the testator's motive was really that innocent and held the condition void.[47]

D. Restraints on Remarriage

1. Generally speaking, a condition against the remarriage of a surviving spouse is valid.[48]

2. In Appleby v. Appleby's Estate, a husband and wife signed an antenuptial contract which provided that if the wife predeceased the husband, her estate passed to a specified charity upon remarriage of her surviving spouse.[49] This provision was also included in the wife's will, and upon her death the husband brought suit.[50]

   a. The surviving spouse challenged the antenuptial agreement and the will on the grounds that it was a restraint of marriage.[51]

   b. The court held that the general rule of contracts in restraint of marriage did not apply to second marriages.[52] Typically the contract was held void if it was for first-time marriages, but in second marriages there was no public policy argument to prevent a wife from withholding her estate to avoid supporting the second wife.[53]

3. In Lewis v. Johnson, the children of the decedent agreed to give their one-half of the estate to the widow in consideration for the widow's promise that if she remarried she would return the children's one-half of the estate.[54]

   a. The children filed suit when the widow remarried because she did not return their one-half of the estate.[55]

   b. The widow alleged the agreement was void because it was against public policy as a restraint on marriage.[56]

   c. In upholding a long line of cases supporting restraints against second marriages, the court affirmed the validity of the agreement.[57] The court found that it was reasonable to require repayment of the children's one-half of the estate upon the end of her status as a widow.[58]

E. Conditions Restraining Religious Practice

1. Courts generally uphold religious restraints on bequests that require the beneficiary to follow or

reject a certain religion. In fact, one study noted that from 1925 through the publication date in 1999, no state appellate court invalidated a testamentary religious restraint.[59]

2. In re Kempf's Will raises four strong arguments for the constitutionality of religious restraints in the context of the law of trusts and estates.[60]

    a. First, a restraint on religion in a donative transfer document presents no problem of establishment of any single form of religion.[61]

    b. Second, donative transfers are the acts of an individual, and constitutional guarantees of religious freedom are limitations on the power of government, not upon the right of an individual.[62]

    c. Third, since the beneficiary can reject the gift, the restraint is not coercive nor does it deny religious freedom.[63]

    d. Finally, the right of the testator to dispose of his property as he sees fit outweighs the religious restraint on the beneficiary.[64]

3. The Restatement (Second) of Property: Donative Transfers also ratifies the validity of religious conditions in disposition of estates.[65] The rationale behind allowing such conditions is that society is not concerned with the religious beliefs of individuals. Court decisions and the Restatement affirm the attempted religious promotion of the testator when the inducement takes the form of a religious restraint and is attached to a gift.[66]

4. In one of the very early American cases on this issue, a testator left trust income to his brother on the condition that within 12 months of testator's death, the brother must leave the Roman Catholic priesthood (should he be a priest at the time of death), disaffiliate from any and every order or society connected with the Roman Catholic Church, and refrain from forming any connection with the Church.[67]

    a. At the time of the testator's death, the brother was not a priest in the Roman Catholic Church, however, within several months of testator's death, the brother joined the Roman Catholic priesthood.[68]

    b. The court held that there was no room to question the right of the testator to attach certain conditions to receipt of his property.[69] And, no matter the prejudices or thoughts of the testator, the law recognizes the right of the testator to attach conditions to his property.[70]

5. In a 1906 case, a testatrix left her son a $1500 gift to be paid in fifteen annual payments on the condition that he attend regular church services at the local church "when not sick in bed, or prevented by accident or other unavoidable occurrence."[71]

    a. The son argued the condition was contrary to the constitutional provision that guaranteed every man religious freedom.[72]

    b. The court held the condition, noting that the son had the right to reject or accept the gift without restriction upon his will or coercion of his conscience.[73] Citing to Magee v. O'Neill[74], the court stated: The power of disposition is general. The power to give includes the right to withhold or to fix the terms of the gift, no matter how whimsical or capricious they may be, only provided they do not in any way violate the law.[75]

6. The Delaware courts tackled this issue in 1943 in the Fitzmaurice case.

    a. The testatrix included a condition that gave a beneficiary $10,000 if she lived up to and observed the teachings and faith of the Roman Catholic Church.[76]

    b. At trial, the beneficiary contended that a religious condition induced fraud and hypocrisy, and tended to replace real religious beliefs with a pretend belief.[77] The beneficiary asserted that inducement of a pretend religious belief was against the moral well-being of the state of Delaware and an invalid restriction on her religious freedom.[78] The court replied that an inducement to adopt a particular religious belief was not a denial

of religious freedom; the condition was valid and binding.[79]

7. In most jurisdictions, an attorney validly may include a gift conditioned on faith within testator's estate plan.
    a. To be safe, however, where the provision is one that might bring a challenge, it is advisable to provide for an alternative disposition in the event the condition is found to be invalid.
    b. It is also important to include a gift over should the condition not be satisfied.[80]

F. Effect of Invalidity of a Condition

1. As noted above, conditions on gifts generally are permissible as long as they are not illegal or against public policy.
2. When a gift is found invalid, how that invalidity is handled depends on whether it is a condition precedent or a condition subsequent. Given that the case law reflects that most courts cannot tell or explain the difference, it is a good idea to protect the integrity of a plan by including as much supporting guidance as possible.
    a. The courts often seem to focus on the grantor's intent behind the provision at issue, so it may be advisable to include a statement of grantor intent when including a condition that falls within the sensitive areas.
    b. For example, if the grantor of a trust provides that her daughter's income distribution will double if the daughter is not married, there is a possibility this provision could be voided as against public policy. If the trust contains a statement that the grantor does not desire that her daughter should divorce, but rather, the grantor wants the daughter to have increased income in the event of divorce because the daughter is a stay-at-home mother whose income will decrease if she is divorced, that purpose statement might offset the policy arguments.
3. When a strict condition is imposed on receipt of property, it is important to discuss with the testator what should happen if the condition is held void.
    a. Should the gift fail, or should the property pass to the beneficiary with no conditions?
    b. For example: *If the preceding provision is determined to be unenforceable by a court of law, I direct that the property passing to the trust for my daughter under Article V of this trust agreement shall instead be distributed to ABC Charity. Had I been aware that the preceding provision would not be allowed under the law, I would not have made any provision for my daughter under Article V.*
    c. Although there probably is no way to be completely certain whether such language will be honored, under the rules set forth in case law and in the Restatement of Trusts[81], it seems that such language is worthwhile. As belt and suspenders, inclusion of a no contest clause should be considered.

IV. DEFINING VALUES AND TRANSMITTING WEALTH

A. Understanding and Negotiating the Generation Gap

1. When drafting an estate plan, it is important to look not only at the personalities of our clients, but also at the traits of those who will be inheriting from the clients.
    a. While it is true that an estate planning attorney ultimately must do what the client wants, it is an important part of the attorney's job to help the client understand where there may be problems with the estate plan.
    b. Failing to consider how the beneficiaries might react to the estate plan or interact with the fiduciaries under the plan potentially leaves a gaping hole in the plan that will later be filled with conflict and litigation.
2. Understanding the beneficiaries of an estate plan, as well as their relationships with their parents and grandparents, necessitates a basic

understanding of the world in which the next generation is living.

a. In 2019, the "next generation" likely is a member of Generation X (born 1960-1979), Generation Y (born 1980-1994), or Generation Z (1995-2010).[82]

b. Baby Boomers (1946-1964) have probably reached a point in their lives where their values toward money are not going to change unless the Boomer makes a deliberate decision to re-make his or her life.

c. Generation X is a primary focus for current planners.

   i. This group encompasses what is known as the "MTV generation", and most grew up with personal computers in their homes.

   ii. Most Gen Xers learned to use the Internet in high school or during post-graduate education, and are comfortable with and willing to embrace new technologies.

   iii. In addition to leaps of technology, the social and political issues of this generation were defined by a rise in the divorce rate, an increased rate of mothers in the workplace, a work force requiring advanced academic credentials, and the end of the Cold War.

d. Members of Generation Y also are a major focus for planners, both as developing their own core estate plans and as beneficiaries of plans of previous generations.

   i. This generation is the biggest since the Baby Boomers, and approximately three times the size of Generation X.

   ii. The fluency with technology that they have known since birth has altered Gen Y's methods of communication and, some argue, their ability to communicate without their electronic intermediaries.[83]

      (1) Generation Y lives in a world where front doors are not left unlocked, homework and school pressures are ever-increasing, and a college degree is virtually a requirement to enter the workforce. Faster electronic communication is as much a necessity as a choice.

      (2) Like Gen Xers, the members of Gen Y are likely to take longer to move out of their parents' homes. Some commentators suggest this delay may be due to the continuation of increasing education requirements to access work force opportunities. Other commentators view it more as a failure to launch.[84]

e. Generation Z is now entering the picture as beneficiaries.

   i. Like Generation Y, members of Generation Z grew up during a time where they have been exposed to digital media likely from birth. As some commentators have noted, members of Generation Z are the "true digital natives."[85]

   ii. Generation Z is the most diverse and on track to be the most well-educated generation yet. With these characteristics, many Generation Zers tend to be more liberal. They are most likely (59%) to say gender options on forms should include options other than "man" or "woman." Along the same vein, the large majority of Generation Z agree that financial and child care responsibilities should be shared by both parents in a two-parent household.[86]

f. Despite the increased access to news and world events through electronic media and their facility with electronic media virtually starting in the crib, recent surveys of employers find that very few employers feel that the young people they encounter seeking employment have the basic skills needed to enter the workforce.[87]

   i. Some commentators on modern education feel that the schools have focused so much on self-esteem that they have allowed the generations now becoming

adults to pass through their childhood without learning basic life skills.[88]

ii. For example, Jump$tart Coalition's 2006 study found that high school seniors as a group would fail a basic test of financial literacy.

iii. If it is true that Gen X and Gen Y are less prepared with life skills, then those looking to prepare them to receive wealth may have an even more daunting task ahead of them than their ancestors.

B. Structuring the Plan and the Education

1. Determining the Amount of the Inheritance

a. The amount of the inheritance sets the stage for the entire planning structure, as it forces the testator to consider the goals of the wealth transfer.

i. Some testators want to leave every penny to their heirs.

ii. Other testators want to leave a safety net, but are concerned about creating trust fund babies. Warren Buffett, for example, widely known for his surprising 2006 announcement that he was leaving the bulk of his wealth to charity, expressed the opinion that leaving heirs too much money is akin to "a lifetime supply of food stamps just because they came out of the right womb."[89]

b. Many testators are concerned that the words of William Vanderbilt, grandson of Cornelius Vanderbilt, are true. He stated, "Inherited wealth is a real handicap to happiness. It is as certain a death to ambition as cocaine is to morality." On the flip side, other testators worry about the "legacy of ill will" that may result from not leaving an inheritance to heirs.

c. A 2006 report by Merrill Lynch and Capgemini found that 61 percent of high net worth individuals are over the age of 56.[90]

i. In the United States alone, it is estimated that $41 trillion will be transferred by 2053.

ii. The report also indicated that only two percent of the individuals were completely prepared to transfer wealth, and a staggering 39% were inadequately prepared.

2. Age and Education Considerations

a. Charles Collier, in his book *Wealth in Families*, recommends four strategies to start children on a path of financial education: set an example, provide guidance, allow consequences, and use mentors.[91]

b. It is important that parents (or grandparents) implement a financial education plan and tailor it to the needs of their children (or grandchildren). An effective financial education will lay the groundwork for a successful wealth transfer to future generations.

i. Ideally, parents should mirror the behavior they want to pass on to their children.

ii. Realistically, however, we cannot force our adult clients to change their behavior, and it can be difficult to say, "You are a spendthrift, so does it really surprise you that your child is, too?"

iii. As noted by author Charles Sykes, "If you can't handle dealing with your Resident Assistant or class schedule, then obviously your parents didn't actually raise you. You didn't grow up. Responsible parents prepare their children for navigating life on their own."[92]

3. Protecting the Inheritance

a. The divorce rate has increased significantly over the last few decades and now almost half of all marriages end in divorce,[93] and testators are expressing an increasing awareness of and concern regarding the potential loss of a beneficiary's property due to of divorce.

b. In most jurisdictions in the United States, a trust containing proper spendthrift provisions that was set up for the divorcing party by a third party (either through an inter vivos gift or upon death) will not be marital property subject to division in the event of a divorce.

i. If a beneficiary receives regular distributions, however, some courts will consider those distributions as income to the divorcing party for property settlement and support purposes.

ii. A 2009 survey published by the Family Law Quarterly notes that the following states do not distribute premarital property as part of a divorce settlement: Alabama, Arizona, Arkansas, California, Colorado, Delaware, District of Columbia, Florida, Georgia, Hawaii, Idaho, Illinois, Kentucky, Louisiana, Maine, Maryland, Michigan, Minnesota, Missouri, Nevada, New Jersey, New Mexico, New York, North Carolina, Ohio, Oklahoma, Pennsylvania, Rhode Island, South Carolina, Tennessee, Texas, Utah (property distribution limited to marital property by case law), West Virginia, and Wisconsin. 42 FAM. L.Q. 762. http://www.abanet.org/family/familylaw/flqwinter09_propertydivision.pdf.

iii. Transfers in trust avoid inadvertent commingling.

c. It is important to consider how "spouse" is defined in trust documents.

i. In some instances, a spouse will be included as a discretionary beneficiary of a trust, and there are many reasons to do so. For example, the grantor may want to care for a spouse if the beneficiary becomes disabled, pay health care expenses for the spouse, or provide for the spouse in the event of death of the beneficiary.

ii. For example: *As used herein, the term "spouse" shall mean the person to whom the beneficiary that is a descendant of the Grantor ("Designated Person") shall be "legally married" as of the date such determination is being made, or the person to whom such Designated Person was legally married at the date of death of such Designated Person. A person shall not be considered "legally married" if the person shall be either divorced or legally separated from such Designated Person. Any determination of whether a Designated Person has a spouse shall be made by the Trustee. Such determination shall be final and binding upon all persons and the Trustee shall incur no liability for any good faith determination. If at any time the person who initially qualified as a spouse shall be determined to no longer qualify, whether such person is designated generically or specifically by name in this Agreement, then, for the purposes of this Agreement, such person and all descendants of such person who are not descendants of the Grantor shall be considered to have died as of the date of such determination.*

iii. Although marriage equality is now the law of the land, a few people have determined that civil unions are a more fitting legal relationship for them. Additionally, many jurisdictions outside of the United States still do not allow same sex persons to marry. To include the possibility of these situations, consider an alternate definition to include civil unions and similar relationships: *As used herein, the term "spouse" shall mean the person to whom the beneficiary that is a descendant of the Grantor ("Designated Person") shall be "legally married" as of the date such determination is being made, or the person to whom such Designated Person was legally married at the date of death of such Designated Person. For purposes of this instrument, "legally married" shall include (a) civil unions, domestic partnerships and similar legal relationships valid under the laws of the state where made, and (b) a committed same-sex relationship specifically acknowledged in writing to the Trustee by the Designated Person when the Designated Person resides in a jurisdiction where legal marriage, civil unions, domestic partnerships or similar legal relationships are not permitted for same sex couples. A person shall not be considered "legally married" if the person shall be divorced or legally separated from such Designated Person. For purposes of this instrument, "divorce" shall include severance of a civil union, domestic partnership or similar legal relationship, and, in the case of a committed same-sex relationship acknowledged in writing by the Designated Person to*

the Trustee, a similar writing to the Trustee by the Designated Person revoking such status. Any determination of whether a Designated Person has a spouse shall be made by the Trustee. Such determination shall be final and binding upon all persons and the Trustee shall incur no liability for any good faith determination. If at any time the person who initially qualified as a spouse shall be determined to no longer qualify, whether such person is designated generically or specifically by name in this Agreement, then, for the purposes of this Agreement, such person and all descendants of such person who are not descendants of the Grantor shall be considered to have died as of the date of such determination.

iv. Alternate definition to provide cessation of spousal status upon initiation of divorce proceedings: *As used herein, the term "spouse" shall mean the person to whom the beneficiary that is a descendant of the Grantor ("Designated Person") shall be "legally married" as of the date such determination is being made, or the person to whom such Designated Person was legally married at the date of death of such Designated Person. For purposes of this instrument, "legally married" shall include (a) civil unions, domestic partnerships and similar legal relationships valid under the laws of the state where made, and (b) a committed same-sex relationship specifically acknowledged in writing to the Trustee by the Designated Person when the Designated Person resides in a jurisdiction where legal marriage, civil unions, domestic partnerships or similar legal relationships are not permitted for same sex couples. A Designated Person shall cease to be considered "legally married" upon the initiation of legal separation or divorce proceedings or, if formal proceedings are not required, then upon the occurrence of divorce (as defined in the following sentence). For purposes of this instrument, "divorce" shall include severance of a civil union, domestic partnership or similar legal relationship, and, in the case of a committed same-sex relationship acknowledged in writing by the Designated Person to the Trustee, a similar writing to the Trustee by the Designated Person revoking such status. Any determination of whether a Designated Person has a spouse shall be made by the Trustee. Such determination shall be final and binding upon all persons and the Trustee shall incur no liability for any good faith determination. If at any time the person who initially qualified as a spouse shall be determined to no longer qualify, whether such person is designated generically or specifically by name in this Agreement, then, for the purposes of this Agreement, such person and all descendants of such person who are not descendants of the Grantor shall be considered to have died as of the date of such determination.*

4. Encouraging the Beneficiary to Protect Himself

a. Many testators now are including in their estate plans a form of so-called incentive provision that encourages the beneficiaries to have a premarital agreement.

   i. Some grantors will take a stronger position and require their beneficiaries to have a premarital agreement in order to continue to receive distributions.

   ii. Incentive provisions must be used with thought and skill, however, because they truly may represent "bad psychology." If they are viewed as trying to control the child's life choices, incentive provisions may be more likely to produce rebellion than compliance.

b. Example to encourage premarital agreement: *If Betty and her fiancé execute a premarital agreement valid under the laws of Betty's state of residence at the time of her marriage, and the agreement addresses the treatment of her separate property and the division of marital property upon divorce, then the trustee shall distribute $40,000 to Betty on or before the date the wedding is solemnized.*

c. Example of a heavy-handed provision regarding premarital agreements: *At all times when the beneficiary is married, distributions of income and principal may only be made by the Trustee to the*

beneficiary if there is a legally valid and binding premarital agreement between the beneficiary and the beneficiary's spouse that is in writing and in full force and effect, and that specifically provides for the following [insert provisions that must be included in the premarital agreement].

d. Example of a middle road provision: *If the beneficiary and her fiancé execute a premarital agreement valid under the laws of the beneficiary's state of residence at the time of her marriage, which agreement addresses the treatment of her separate property and the division of marital property upon divorce, then the trustee shall distribute $ 40,000 to the beneficiary on or before the date the wedding is solemnized.*

V. INCENTIVE TRUSTS — SHOULD YOU OR SHOULD YOU NOT?

A. Definition and Use

"Incentive trust" is a phrase that broadly has come to define a trust instrument that places specific conditions on receipt of property, typically focused around education, employment or certain behaviors.

1. They may be structured either to encourage or discourage particular activities or behaviors.
2. Incentive provisions can be useful if the beneficiary is old enough when the provision is drafted to make it possible to understand that beneficiary's driving forces.
    a. Advisors, however, must be aware of the messages incentive provisions send, and should alert clients accordingly so clients properly reflect their values in their documents.
    b. Such provisions must be used with great care, because they truly may represent "bad psychology."
    c. An incentive provision that is viewed as trying to control the child's life choices may be more likely to produce rebellion than compliance.
3. Studies of financial incentives done over the last century reflect that these incentives may actually have mixed results.
    a. Several of the studies indicate that financial incentives actually achieve the opposite of the intended results, or a decrease in performance and effort.
    b. These studies do not say as a bright line that incentives do not work. Rather, they highlight the critical point when an incentive provision is to be used: the incentive must be at the right level and must be matched to the personality and motivators of the individual being incentivized.
    c. In short, incentives must be used thoughtfully and carefully.

B. Validity

1. As noted above, conditions generally are permissible for gifts in trust.
2. Prior to any decisions on the validity of incentive trusts there was Claflin v. Claflin. Claflin, an 1889 Massachusetts case, established the principle that trust restrictions cannot be set aside simply because a property interest exists.
    a. The testator, Wilbur F. Claflin included an article in his will that required his trustees to sell his personal estate and to then divide it into thirds to support his wife and children.[94]
        i. The proceeds for his son, Adelbert, were to be held in trust and distributed at age 21, 25, and the remainder at 30.[95]
        ii. Following Adelbert's twenty-first birthday, but prior to his twenty-fifth birthday, he brought suit to compel the trustees to pay him the remainder of his trust.[96] Adelbert argued that the provisions of the will postponing payment were void because his interest in the trust was vested and absolute.[97]
    b. The Massachusetts Supreme Court agreed that Adelbert's interest was vested and absolute, but also found that the directions of the

testator to his trustees were not against public policy or so inconsistent with Adelbert's property rights that the provisions should be given immediate effect.[98] The court remarked: *It cannot be said that these restrictions upon the plaintiff's possession and control of the property are altogether useless, for there is not the same danger that he will spend the property while it is in the hands of the trustees as there would be if it were in his own.*[99]

c. The bent of the American courts to enforce a testator's intent as demonstrated by the written restrictions of the document, so long as not contrary to public policy, has become known as the "Claflin doctrine."[100]

i. A trust or trust provision will fail if its intended "purpose or performance is unlawful or against public policy." [101]

ii. Even without an allegation that a provision is illegal or contrary to public policy, conditions that are ambiguous or impossible to satisfy will fail and the beneficiary generally will take as if the condition did not exist.

3. Issues with incentive provisions tend to fall into several primary categories. In drafting such clauses, therefore, it is important to avoid common pitfalls.

a. Ambiguities

i. Incentive provisions are one area where ambiguities seem to be somewhat common, perhaps because it is hard to structure the subjective judgment required of many such clauses.

ii. When drafting an incentive provision that requires a trustee to determine whether a condition has been met, it is important to provide as much guidance as possible. This can be done by setting objective criteria or by providing examples for a subjective judgment.

(1) Conditions like "proper education" and "good moral character" may be challenged as ambiguous without something more to offer guidance.

(2) An ambiguity exists only if the language at issue in the governing document is reasonably susceptible to multiple interpretations.[102]

(a) The determination as to whether multiple interpretations are reasonable typically is made after established principles of law are applied in an effort to clarify the uncertainty.[103]

(b) Whether or not a true ambiguity exists is a question of law.[104]

b. Impossible to Satisfy

i. Sometimes, testators include trust provisions that are impossible because of the attached condition or due to the circumstances of the case.

(1) Traditionally, if performance is impossible by operation of law, the condition is void and there is no forfeiture.[105] Additionally, if performance is impossible because of an act of God, the condition is void and there is no forfeiture.[106]

(2) If a situation becomes impossible after the time specified for completion, it does not excuse the nonperformance of the condition.[107]

(3) Conditions that are so vaguely described as to be impossible to effectuate are also inoperative.[108]

ii. In Jones v. Jones, a father believed that his two sons were "dissipated, wild and spendthrifts…"[109] Because of this assessment of his children, he conditioned their receipt of his land on a time period of twenty years, and following the twenty years if they were "capable of a prudent exercise, control and ownership of said real estate and no further danger shall exist" the real estate would vest in fee simple.[110] If to the contrary, the sons were engaged in drunkenness, gambling, or any other immoral activity that incapacitated the two, the land would never vest in fee simple.[111]

(1) The trustee petitioned the court for construction of the terms of the trust and contended that the sons were not entitled to the land if after twenty years they were

incompetent to manage the land, drunkards, or spendthrifts.[112]

(2) The sons argued that the conditions of the trust were void and the land vested in the two in fee simple.[113]

(3) The court held that the conditions imposed upon the two sons were so indefinite and uncertain that they were rendered impossible of performance.[114] The court stated that the testator made no plans to determine whether the conditions had been met, and to give the trustee that authority was to give him too much power.[115] Therefore, the conditions were void and the land was to vest in fee simple.[116]

C. Purpose Clauses

1. When incentives are used, the primary goal should be to ensure that intergenerational wealth transfer leaves a positive rather than a negative legacy.

   a. Incentive provisions create an easy road to bad psychology and should be used with great care.

   b. To create a positive legacy, understanding and accurately conveying the purpose of the trust is of the utmost importance.

      i. If, for example, the purpose of a trust is to encourage productivity, then what constitutes "productivity" must be very carefully defined.

         (1) Is productivity defined as the ability to support oneself, or is productivity defined as engaging in a meaningful career regardless of the salary?

         (2) Does volunteer work meet the definition of productivity?

         (3) Is the requirement met if a parent chooses to stay home and raise the children?

         (4) At what point in time can a beneficiary cease being "productive?"

         (5) What if the beneficiary becomes unable to be productive due to health reasons or inability to find employment?

         (6) Should the beneficiary be able to rely on his property interest for support during his retirement?

      ii. These questions are an example of how a simple word like "productivity," that seems easy to define can in fact have a great depth of subtle difference in interpretation. Without proper instruction, a trustee will not know what the settler meant by the use of the word "productivity."

   c. While many settlors feel that the trustee they have named knows what they would have wanted.

      i. Many jurisdictions permit opt-out of the rule against perpetuities, making it more likely that trusts will continue for many generations and increasing the odds that the personal connection between the settlor, trustee and beneficiaries will be lost somewhere down the line.

      ii. Also, as the law enabling beneficiaries to modify trust terms by agreement expands,[117] defining intent in the trust document arguably has become vital to preservation of a trust.

2. General Purpose Statements

a. A very general purpose statement may be helpful.

   i. For example: *My overall objective is that my children and their descendants become mature, responsible, self-sufficient, and productive adults. The trustee is authorized to make distributions that assist, encourage, or reward a beneficiary for his efforts to become a mature, responsible, self-sufficient, and productive person.*

   ii. On the other hand, a very general provision like the one above may land your trustee in a debate with the beneficiary over what

constitutes mature, responsible, self-sufficient, and productive.

b. The risk with narrowing parameters of the definition is creating inflexibility, however, adding to the provision above some additional guidance like the following may help reduce the likelihood for validity issues: *I define a productive adult as one who, for example, holds a steady job and earns sufficient salary to provide for his or her basic needs. I also view a productive adult as one in a supportive relationship who chooses to stay home to raise children while their spouse or life partner works to provide for the family's basic needs. These examples are intended to be instructive only, and the determination as to what is required to encourage a beneficiary to become a mature, responsible, self-sufficient and productive adult shall be in the trustee's sole and absolute discretion.*

3. Income Matching Distributions

a. Income matching can be helpful to beneficiaries who are working in positions that do not pay very well, but are personally rewarding to the settlor or the beneficiary.

   i. On the flip side, such provisions as frequently drafted send the message that the important value is earning a lot of money.

   ii. Such clauses, without more, may reward high-paid white-collar professionals more than altruistic professionals like teachers, public interest attorneys or government and military service employees.

b. If the value important to the settler is accumulation of wealth, than a straight-forward income matching provision will encourage that purposes.

   i. If the intention is to encourage a beneficiary to be productively employed in a satisfying career and to provide support, then a cap on matching or a fixed annual distribution with a "bonus" based on salary might more effectively achieve those goals.

   ii. In any event, income matching clauses should address the definition of earned income, the impact of a spouse's income, and the treatment of bonuses or commissions.[118] To avoid confusion, it also is a good idea to indicate whether the income matched is pre-tax or post-tax.

4. Philanthropic Pursuit

a. Some settlors may wish to reward a beneficiary who chooses to spend his time volunteering or doing charitable work that benefits the greater good of the community.

   i. A settlor might supplement the beneficiary's lifestyle with additional distributions, a nicer automobile than the beneficiary could afford otherwise, or other luxuries.

   ii. To encourage charitable involvement, a settlor might match charitable contributions made by the beneficiary up to a certain amount each year.

5. Childcare

a. Some settlors wish to assist the beneficiary who chooses to forego employment in order to be a stay-at-home parent.

b. The trick with a childcare provision is balancing the legitimate beneficiary with the manipulative beneficiary. Some settlors limit the monthly distribution to an amount equal to that of the beneficiary's employment prior to the decision to stay home and raise the children.

6. Education

a. Paying for a beneficiary's education encourages pursuit of education by removing cost as a barrier.

b. As educational options have expanded and more alternatives have become available even at the preschool level, some settlors have given education a very broad definition that is not limited to college, but also includes private secondary education, post-graduate education, and professional and vocational schools.

c. One pitfall with education incentive clauses is the perpetual student.

i. In addition to the beneficiary who will remain in school as long as possible to avoid become self-supporting, thought should be given to addressing the beneficiary who is not college material because of physical or mental disabilities or the beneficiary who will do the bare minimum to ensure funding.[119]

ii. The settlor should use purposeful language to ensure that his intent has the best chance of success.

7. Starting a Business

a. A settlor desiring to place value on entrepreneurial behavior might authorize a distribution to permit a beneficiary to start a business.

i. If the authority is for a small amount of seed money, the provision might be structured as a mandatory distribution once upon request of the beneficiary.

ii. If the thought is to fund a more substantial business endeavor or to fund the venture more fully, it is advisable for the settlor to set requirements that the beneficiary must satisfy in order to receive the funds.

(1) At a minimum, the beneficiary should be required to submit a reasonably viable business plan.

(2) Other criteria could mandate employment of a business consultant or partial funding by the beneficiary.

(3) These additional hurdles will not guarantee success but may help the beneficiary in his endeavor by providing guidance and support.

D. Treatment of Incentive Trusts by the Restatement (Third) of Trusts

1. The Restatement (Third) of Trusts establishes that if one of three conditions is present, the incentive provision is not enforceable.[120]

a. An incentive provision is invalid if it requires the beneficiary to commit a criminal or tortious act, violates the applicable rule against perpetuities, or is against public policy.

b. If one of these conditions is present, the validity of the entire trust can be cured if the provision can be modified or separated from other provisions without defeating the testator's intent.

2. The Restatement supports the concept that a provision generally is valid if it is aimed at preventing the receipt of a property interest because of a beneficiary's personal habit(s). The Restatement also takes the position that using these restraints in attempt to induce or eliminate personal habits is not against public policy.

E. Thoughtful Drafting of Incentives

1. When employing incentive provisions in trusts, therefore, it is important to consider the following questions

a. Can the trustee access the information necessary to implement the provision?

i. Will obtaining the information cause the trustee to pry into very personal aspects of the beneficiary's life?

ii. Will the trustee be able to force release of the information, and what will be involved in doing so?

b. Do the burdens to the beneficiary (and possibly the trustee) outweigh the benefits the settlor hopes the provision will create?

c. Is the measuring stick clearly defined or is it likely to lead to extended litigation if the beneficiary does not achieve the condition?

d. Can the beneficiary manipulate the provision to create an outcome that is contrary to the intent of the settlor?

2. It is critical to weigh all of the competing factors and make certain that the settlor's priorities and wishes are understood and clearly expressed.

a. It is important to help the settlor understand how and why the desired incentive provision may wreak havoc on the estate plan.

b. Unfortunately, if not used properly, the only legacy of incentive trusts may be ill will.

VI. RECOGNIZING THE ROLE OF POWERFUL EMOTIONS BEHIND PLANNING

A. Fear and Control Issues

1. Many of the techniques that are most tax effective in intergenerational wealth transfer require the client to relinquish control over his assets.

   a. Loss of complete control by the transferor is often a difficult pill to swallow.

   b. Reminding the client of what is likely to result with the wealth he has accumulated during his lifetime, that he has inherited and safeguarded for the family line, and/or the business he has worked hard to build can be an effective tool.

2. If keeping assets within the bloodline is a concern, placing assets in trust is the obvious choice.

   a. Not only can a trusted party be named as trustee, but generally the grantor can safely retain the right to remove and replace the trustee without triggering estate inclusion issues.[121]

   b. For example, a provision like the following might be included in an irrevocable trust established to benefit the settlor's descendants: *During the lifetime of the settlor, the settlor shall have the right, at any time and from time to time, to remove any trustee and appoint any person, corporation, or combination of persons or corporations as successor trustee, provided, however, that (a) any such person or corporation shall not be related or subordinate to the settlor (within the meaning of Section 672(c) of the Internal Revenue Code), (b) the settlor shall at no time be appointed as a trustee, and (c) the removed trustee shall continue to serve as trustee until a designated successor has agreed to act. The exercise of this power by the settlor shall be by an instrument in writing signed by the settlor and delivered to the trustee.*

3. Communication is important, though many settlors are unwilling to share the terms of their plan with their descendants.

   a. Incentive provisions and trusts become especially challenging if the settlor does not reveal his intentions to the family.

   b. If the settlor fails to discuss why he is utilizing incentive provisions and trusts, beneficiaries feel left out, ineffective, and non-trustworthy. The shock of learning that an inheritance is tied to specific behavior is not always pleasant and can lead to severe discord within the family.

B. Planning for Proper Tuition

1. Some individuals react to their fears by placing their wealth in trust until the children are fully grown and ready to handle it.

   a. Leaving money in trust and restricting the next generation to only income or regular small distributions, however, may preclude the members of the next generation from making their own mistakes and learning from them.

   b. The following are some ideas for consideration when drafting a trust agreement that will have children or grandchildren as future beneficiaries.

2. "Learning Sized" Distributions

a. Many trust agreements stagger a beneficiary's access to trust assets. Often, this access is granted in three tranches, starting around age 25 or 30.

   i. If a trust is worth a million dollars, is $333,000 too much for a "test run" with financial responsibility?

   ii. Consider giving the beneficiary a smaller amount at a younger age so they have some time to practice with money management and basic financial skills before the broader access rights take effect. For example: *Upon*

the beneficiary attaining age 21, the trustee shall distribute $100,000 to the beneficiary.

b. An annual or monthly allowance that the trustee has the authority to withhold if the beneficiary is a danger to himself can also be a good option.

   i. For a more "bright line" type of distribution, a low (2%) unitrust with access to the balance at retirement age (however defined by the settlor) is a good solution.

   ii. Of course, with a unitrust structure, the likely value of the trust principal must be considered to determine the appropriate level of annual distribution.

3. Withdrawal Rights In Lieu of Mandatory Distributions

a. Trust agreements often direct a trustee to distribute a portion of the trust to the beneficiary at certain ages or upon the occurrence of other triggering events.

   i. Instead of requiring distribution, why not simply grant the beneficiary a right to withdraw funds at those ages or triggering events?

   ii. Requiring the beneficiary to proactively request the funds is a low threshold step, but if a beneficiary cannot be responsible enough to write a letter to the trustee to request a distribution to which he is entitled, why force the trustee to write the beneficiary a check?

b. A withdrawal provision might read as follows: *Upon the beneficiary attaining age 25, the beneficiary shall have the right to direct distribution of no more than one-third of the assets of the trust. Such right must be exercised by a written direction signed by the beneficiary and delivered to the trustee.*

c. If granting withdrawal rights or requiring mandatory distributions, consider giving the trustee authority to hold back the funds or postpone distributions for good reasons. The language can be simple, as set forth in this example: *The trustee shall have the right to deny a withdrawal request if the trustee suspects the beneficiary is using or is addicted to a substance that might adversely impact the beneficiary's ability to manage, invest and conserve property.*

4. Annual "Allowance" With Emergency Invasion

a. Another concept that perhaps fits into the incentive trust mold but was designed to avoid the negative psychology of control is an "allowance trust".

   i. The concept behind the "allowance trust" is to give the beneficiary the feeling that the funds are his, that there are responsible management guidelines, but that a portion of the funds is there for the beneficiary's use each year.

   ii. The basic concept is a unitrust distribution cap each year and that an independent trustee works with the beneficiary to establish an annual budget. The trustee has discretion to invade principal if there are good reasons to do so, and those invasion guidelines will vary for each family's values and circumstances.

b. The following is a sample provision for the "allowance trust".

Support Distributions. The Trustee is authorized to distribute to the beneficiary for her support in each calendar year, as determined in the Trustee's discretion, an amount equal to the Unitrust Amount. The Unitrust Amount shall equal five percent (5%) of the average fair market value of the trust during the preceding three calendar years. The Unitrust Amount shall be determined in January of each calendar year by averaging the fair market value of the trust on the last business day of each of the three preceding calendar years (or as many calendar years as are available in the first few years of the trust), and then multiplying that result by five percent (5%). In the initial year of the trust, the Unitrust Amount shall be five percent (5%) of the initial funding value of the trust indicated to the Trustee by the Settlor, and [shall/shall not] be prorated.

Extraordinary Distributions. The independent Trustee is authorized to exceed the Unitrust Amount in any calendar year if the independent Trustee determines that one or more of the following conditions exists:

(a) A beneficiary, or a spouse or descendant of the a beneficiary, is suffering from a serious medical condition that requires unusual expenditures to provide for health care costs that are not covered by insurance;

(b) A beneficiary is unemployed, is actively seeking gainful employment, and requires additional support to maintain a reasonably comfortable lifestyle;

(c) A beneficiary is pursuing an undergraduate or post-graduate degree, is a full-time student, has not spent excessive time seeking higher education, and requires assistance with tuition, fees, books and ordinary support while in school; or

(d) The Unitrust Amount is insufficient to comply with the Settlor's intent to provide basic support to descendants while they establish their careers, to provide supplemental support to descendants who are self-supporting in order to make their lives more comfortable, and to provide for emergency needs of descendants.

Settlor's Intent. The Settlor intends that distributions will be made to a beneficiary under this Agreement only when the beneficiary submits a written request for a distribution. Ideally, the Settlor hopes that the Trustee will work with the beneficiary to establish a monthly budget within the Unitrust Amount and that the Trustee will make a monthly distribution to the beneficiary. In order to enable the Trustee to deal with unforeseen circumstances and emergency situations, and to address changes in the reasonable needs of a beneficiary, the Settlor has not restricted the Trustee to acting only within a specific distribution schedule.

c. Some commentators have expressed concern that incentive type provisions encourage the beneficiary to "game the system."

   i. While leaving the door open for expanded distributions beyond the unitrust amount may result in unethical behavior by the beneficiary in an attempt to get more money, the author does not believe that this type of provision is likely to produce behavior that did not already exist.

   ii. A dishonest person will act dishonestly. A greedy person will act greedily. A reasonably well-raised beneficiary given a bit of control with some positive guidance might just learn to make some great decisions.

5. The Educated Co-Trustee

a. Parents often mandate that a child becomes his own trust upon attaining a certain age.

   i. What virtues does achieving a particular age bestow that qualify a beneficiary to manage a trust estate?

   ii. Perhaps there is some expectation of a degree of life experience by a certain age, but there is nothing to predict whether that life experience will touch in any way on fiscal perspective.

b. If naming the child as a trustee, consider (a) requiring the child to elect to become a co-trustee starting at a specified age; and (b) permitting the child to become sole trustee only after a minimum time period during which such child actively participated as a co-trustee.

   i. Or, instead of a triggering age as the sole criteria, consider requiring the beneficiary to take a course in money management or have similar training.

   ii. The acting trustee or an independent third party could be given the discretion to determine whether the beneficiary has received the proper education to assume the role of a co-trustee.

   iii. None of these methods guarantees that the child will be a good, responsible or even competent trustee; however, why just hand over the keys as opposed to making the child demonstrate some responsibility?

c. Possible language might read: The primary beneficiary shall have the right to become a co-trustee of the trust upon the later of such beneficiary attaining the age of 25 years or completing a course of study in financial management. Whether the primary beneficiary has satisfied the requirement of completion of a course of study in financial management shall be determined in the sole discretion of [insert name].

Notes

1 U.S. v. Perkins, 163 U.S. 625, 627 (1896).

2 Id.

3 Id. at 628.

4 Hodel v. Irving, 481 U.S. 704, 716 (1987). Not all commentators, however, agree as to the reach of the Court's holding. "Although this case might be read as…an assertion of a constitutional right to bequeath, considerable doubt exists as to the case's reach and reasoning. There was no direct discussion of why the right to bequeath is a constitutionally protected right, and even if such a constitutionally protected right does exist, nothing in the Irving opinion warrants the conclusion that the right includes the freedom to impose testamentary restraints on transferees' conduct or, indeed, anything beyond the bare power to name successors in a will." Jeffrey G. Sherman, Posthumous Meddling: An Instrumentalist Theory of Testamentary Restraints on Conjugal and Religious Choices, 99 U. Ill. L. Rev. 1273, 1288-89 (1999).

5 Irving v. Clark, 758 F.2d 1260, 1262 (8th Cir. 1985).

6 Id.

7 Id. at 1261.

8 Hodel, supra, 481 U.S. at 716

9 Id. at 716.

10 Harry A. Joffe, A Question of Race, STEP Journal (October 2009).

11 Guilford v. Gardner, 162 N.W. 261, 263 (Iowa 1917).

12 Id.

13 Id.

14 Id. at 264.

15 E. LeFevre, Annotation, Validity of Provisions of Will or Deed Prohibiting, Penalizing, or Requiring Marriage to One of a Particular Religious Faith, 50 A.L.R.2d 740, *2 (2010).

16 Id.

17 Id.

18 In re Bonanno, 51 Misc. 3d 629 (NY Sur. Ct. 2016). "I direct that the said dwelling and premises be not sold during the time when any one of my children is single and not married; and that any one of them resides in the said property. It is my wish and I direct that the property be retained as a home and place of residence for any one or ones of my single and unmarried child or children. … I further direct that, when all of my children are married or when all of the children leave the above house and live elsewhere, whether they be married or single, the said property at 65-26 Myrtle Avenue, Glendale, New York, is to be sold …"

19 Id. at 633-34.

20 Gordon v. Gordon, 124 N.E.2d 228, 230 (Mass. 1955). "If any of my said children shall marry a person not born in the Hebrew faith, then I hereby revoke the gift or gifts and the provision or provisions herein made to of for such child, and I direct that the portion or portions of my estate, and the interest or interests therein which I have by this will given to such child so marrying a person not born in the Hebrew faith shall be paid and made over to that person or persons who would have been entitled thereto under this will if such beneficiary had died before becoming entitled by the provisions thereof to such portion or portions, interest or interests, without leaving lawful issue."

21 Id. at 230.

22 Id.

23 Id.

24 United States Nat'l Bank v. Snodgrass, 275 P.2d 860 (Or. 1954).

25 Snodgrass, supra, 275 P.2d 868.

26 Clayton's Estate, 13 Pa. D. & C. 413 (Pa. Common Pleas Ct. 1930).

27 Id.

28 Id.

29 Id. at 414.

30 Id. at 415.

31 Shapira v. Union Nat. Bank, 315 N.E.2d 825 (Ohio 1974).

32 Id. at 832.

33 In re Estate of Feinberg, 235 Ill.2d 256 (Illinois 2009).

34 Id. at 285.

35 Maddox v. Maddox, 11 Gratt. 804 (Va. 1854).

36 Id. at 809.

37 Id.

38 Jeffrey G. Sherman, Posthumous Meddling: An Instrumentalist Theory of Testamentary Restraints on Conjugal and Religious Choices, 99 U. Ill. L. Rev. 1273, 1308 (1999).

39 Winterland v. Winterland, 59 N.E.2d 661, 662 (Ill. 1945).

40 Id.

41 Id. at 663.

42 Id.

43 Id.

44 Estate of Gerbing, 337 N.E.2d 29, 31 (Ill. 1975).

45 Id.

46 Id. at 32.

47 Id.

48 97 C.J.S. Wills § 1395 (West 2009).

49 Appleby v. Appleby's Estate, 111 N.W. 305, 307 (Minn. 1907).

50 Id. at 306-07.

51 Id. at 307.

52 Id. at 310.

53 Id.

54 Lewis v. Johnson, 251 S.W. 136, 136 (Mo. Ct. App. 1923).

55 Id. at 136.

56 Id. at 137.

57 Id. at 138.

58 Id.

59 Jeffrey G. Sherman, Posthumous Meddling: An Instrumentalist Theory of Testamentary Restraints on Conjugal and Religious Choices, 99 U. Ill. L. Rev. 1273, 1312 (1999).

60 In re Kempf's, 252 A.D. 28 (N.Y. App. Div. 1937).

61 Id. at 32.

62 Id.

63 Id.

64 Id.

65 Restatement (Second) of Property: Donative Transfer § 8.1 (1983). An otherwise effective provision in a donative transfer which is designed to prevent the acquisition or retention of property on account of adherence to or rejection of certain religious beliefs or practices on the part of the transferee is valid.

66 Id. at cmt. a.

67 Barnum v. Baltimore, 62 Md. 275, 288 (1884).

68 Id. at 289.

69 Id. at 291.

70 Id.

71 In re Paulson's Will, 107 N.W. 484, 484 (Wis. 1906).

72 Id. at 486.

73 Id. at 487.

74 In Magee v. O'Neill, the bequest required that the beneficiary was educated in the Roman Catholic faith. Magee v. O'Neill, 19 S.C. 170 (1883).

75 Paulson, supra, 107 N.W. at 487.

76 Delaware Trust Co. v. Fitzmaurice, 31 A.2d 383, 386 (Del. 1943).

77 Id. at 389.

78 Id.

79 Id.

80 See also, John P. Luddington, Annotation, Wills: Condition That Devisee or Legatee Shall Renounce, Embrace, or Adhere to Specified Religious Faith, 89 A.L.R.3d 984, *2b (2008).

81 Restatement (3d) of Trusts § 29.

82 Tracy Francis and Fernanda Hoefel,'True Gen': Generation Z and its implications for companies, November 2018, available at: https://www.mckinsey.com/industries/consumer-packaged-goods/our-insights/true-gen-generation-z-and-its-implications-for-companies, last accessed May 4, 2019. Note that scholars differ somewhat regarding the names they assign to the generations and the years of birth used to define the generations. Generation X and Generation Y sometimes are referred to collectively as the "Me Generation". Generation Y is sometimes referred to as "Millennials."

83 Reynol Junco and Jeanna Mastrodicasa, authors of "Connecting To The Net.Generation: What Higher Education Professionals Need To Know About Today›s Students," found in their survey of U.S. college students that: 97 percent own a computer; 94 percent own a cell phone; 76 percent use Instant Messaging; 15 percent of IM users are logged on 24 hours a day/7 days a week; 34 percent use websites as their primary source of news; 28 percent author a blog and 44 percent read blogs; 49 percent download music using peer-to-peer file sharing; 75 percent of college students have a Facebook account; and 60 percent own some type of portable music and/or video device such as an iPod.

84 Charles J. Sykes, 50 Rules Kids Won't Learn In School: Real World Antidotes to Feel-Good Education 80-81 (Martin's Press 2007).

85 Tracy Francis and Fernanda Hoefel,'True Gen': Generation Z and its implications for companies

86 Kim Parker, Nikki Graf, and Ruth Igielnik, Generation Z Looks a Lot Like Millennials on Key Social and Political Issues, January 17, 2019, available at: https://www.pewsocialtrends.org/2019/01/17/generation-z-looks-a-lot-like-millennials-on-key-social-and-political-issues/, last accessed May 4, 2019.

87 Id. at 32. A 2003 survey by Public Agenda found that only 41 percent of the employers surveyed felt that younger generation job-seekers had the necessary skills to succeed at work.

88 Id. at 25.

89 Richard I. Kirkland Jr. and Carrie Gottlieb, Should You Leave It All To The Children?, Fortune Magazine, September 29, 1986

90 Merrill Lynch, 2006 World Wealth Report, http://www.pt.capgemini.com/m/pt/doc/2006_WorldWealthReport%28Merrill_Lynch%29.pdf.

91 Charles Collier, Wealth in Families 54-56 (Harvard University ed., Harvard University 2006).

92 Charles J. Sykes, 50 Rules Kids Won't Learn In School: Real World Antidotes to Feel-Good Education 68 (Martin's Press 2007).

93 Stephen J. Bahr, Social Science Research on Family Dissolution: What It Shows and How It Might Be of Interest to Family Law Reformers, 4 J.L Fam. Stud. 5, 5 (2002). See also Number, Timing and Duration of Marriages and Divorces: 1996, February 2002 available at http://www.census.gov/prod/2002pubs/p70-80.pdf last visited July 29, 2009. This increase can be attributed to cultural influences, including high marital expectations, economic independence of women, social acceptance of divorce, later marriages or second marriages and no-fault divorce laws. Id. at 5-7. See also Divorce Statistics Collection available at http://www.divorcereform.org/stats.html last visited July 29, 2009. This site contains more statistics as to the factors influencing the divorce rate.

94 Claflin v. Claflin, 20 N.E. 454, 455 (Mass. 1889).

95 Id. at 455.

96 Id.

97 Id.

98 Id. at 456.

99 Id.

100 For additional discussion on Claflin and the history of incentive trusts in American law, see Joshua C. Tate, Conditional Love: Incentive Trust and the Inflexibility

Problem, 41 Real Prop. Prob. & Tr. J. 445, 480 n150 (Fall 2006).

101 Restatement, Third, of Trusts, § 29 cmt. a.

102 See Restatement (Third) Property § 11.1 (2003).

103 See id. § 11.3.

104 See, e.g., In re Estate of Maxedon, 946 P.2d 104, 106 (Kan. Ct. App. 1997).

105 Tiffany, The Law of Real Prop. § 195 (3d. ed. 1939); Woodville, Okla. v. U.S., 152 F.2d 735 (10th Cir. 1946).

106 Id.; True v. Cook, 60 A.2d 138 (N.H. 1948).

107 Tiffany, supra, § 195.

108 Id.

109 Jones v. Jones, 123 S.W. 29, 29 (Mo. 1909).

110 Id. at 30.

111 Id.

112 Id. at 32.

113 Id.

114 Id. at 38.

115 Id. at 37.

116 Id. at 38.

117 See discussion of virtual representation at VII, below.

118 Nancy G. Henderson, Managing "Carrot and Stick" Provisions: Selected Fiduciary Issues in Drafting and Administering Trusts with "Incentive" Provisions, SP004 ALI-ABA 485, 493 (July 17-18, 2008).

119 Id. at 491-92.

120 Restatement, Third, of Trusts § 29.

121 See Estate of Wall, 101 T.C. 300 (Tax Ct. 1993). "To recapitulate the salient facts: Mrs. Wall, the grantor, retained the right in each trust indenture to remove the corporate sole trustee and replace it with another corporate trustee which had to be «independent» from the grantor. In each case the trustee was given the authority to distribute principal and income to a beneficiary essentially unrestrained by an ascertainable standard. Did the right to replace the corporate trustee in turn encompass the right to exercise the powers of the trustee? For the following reasons, we think not."