

# DRUG ADDICTION TRUST

PROVIDING FOR YOUR CHILD SUFFERING FROM DRUG OR ALCOHOL ADDICTION AFTER YOU DIE

By

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Mom and Dad work hard all their lives and amass a significant fortune. They have several children and intend to pass their estate to the children when they are gone. But all too often, one of the children suffers from drug or alcohol addiction. And the parents know, through hard experience, that money given to an addict is an enabler and inevitably makes the situation much worse.

So, how do the parents provide for their addict child<sup>1</sup> in a manner that will not exacerbate the bad aspects of the child's behavior?

One option is to simply disinherit the problem child. But for most parents, this draconian measure is not their preferred solution. They love all their children and want to provide for all of them - but only if it doesn't hurt them in the process.

A potential answer is a Discretionary Trust for the benefit of the troubled child.

## DISCRETIONARY TRUST

The primary feature of a Discretionary Trust is providing the trustee broad discretion on how and when to distribute trust funds. So the addict child

gets nothing unless the trustee, in his or her discretion, decides to distribute money from the trust. Many attorneys use fancy phrases to describe the trustee's discretion, such as:

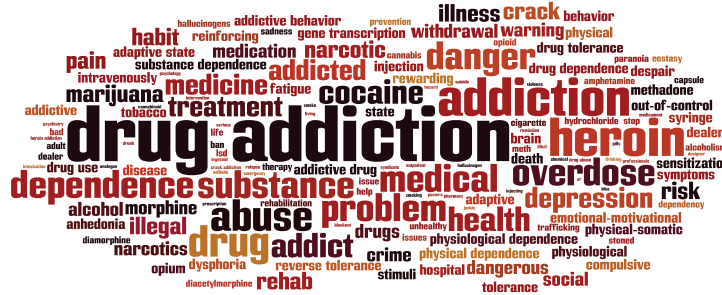
- absolute discretion
- sole and absolute discretion
- sole, absolute, and unreviewable discretion.

Regardless of the adjectives used, is a trustee's discretion

truly absolute and beyond review by a court? The answer, at least in California, is no.<sup>2</sup> A grant of absolute

discretion is viewed as an exculpatory clause, and is strictly construed. Even when a trustee is apparently granted absolute discretion, review of the entire trust instrument may show that the grantor intended to constrain such discretion.

But this apparent quandary is easy to fix. The grantors (i.e., parents) can give the trustee absolute discretion to act within the confines of specific guidelines which are reasonable in the context of



<sup>1</sup> The word "child" implies a young person. Maybe a teenager or young adult. However, aging parents often have to deal with children in their 40s, 50s, or even 60s. Drug and alcohol addiction affects people of all ages.

<sup>2</sup> Drafters sometimes attempt to confer "absolute discretion" on the holder of the distribution power. But doing so risks converting the discretionary power into a general power of appointment. To protect against that risk, California law provides that a trustee with an "absolute," "sole," or "uncontrolled" discretion must nevertheless act in accordance with fiduciary principles and shall not act in bad faith or in disregard of the purposes of the trust. Probate Code § 16081(a).

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the trust's objectives. If the trustee is acting within those guidelines, it is unlikely any court would interfere - regardless of what words were used to describe the discretion.

There are actually four legs to the discretionary trust stool:

- recital of facts;
- objectives of the trust;
- guidance given to the trustee; and
- trustee's discretionary actions.

### RECITAL OF FACTS

A recital of facts based on grantor's experiences would provide a helpful foundation and strengthen the trust. This recital can include past attempts to deal with the addiction, frustration with the addict's lies and deceit, evidence that money given to the addict led to additional drug use, etc. In short, the recital of facts provides the basis for why a discretionary trust is required and can be enormously helpful to understand the grantor's intent.



### OBJECTIVES

The objectives focus on "what" the trustee should achieve with the proper management of trust resources. Creators of a trust are typically given wide latitude and deference regarding its objectives. With a child suffering from some form of addiction, a reasonable objective would be to provide for the

child's basic needs while at the same time not enabling the drug or alcohol use. Other objectives could address recovery and rehabilitation, career change, education, rewarding behavioral change (i.e., sustained periods of sobriety), etc.

### GUIDANCE

The next step, guidance, focuses on "how" to achieve the objectives. The grantors should establish the framework for the trust by providing guidelines for the trustee to follow. For example, it's common to condition distributions to an addict upon demonstration of specific behavior, such as: a period of sobriety, good grades at school, having a job, etc. Evidence of conformance might include passing a lab test administered by a certified drug or alcohol screening facility. Or the guidance could limit how trust money will be spent and require receipts to document appropriate expenditures.

In more extreme cases, guidelines may require the addict (beneficiary) to give the trustee a HIPAA release authorizing the trustee to view medical records and consult with the addict's physician. Coordination with the physician or other medical providers may be essential to funding successful rehabilitation or recovery programs.

### TRUSTEE'S DISCRETIONARY ACTIONS

Trustee discretion is not absolute in a broad sense, but rather it is constrained by the objectives and guidelines in the trust instrument. However, when acting within that constraining box, the trustee should have unfettered authority to make factual determinations and appropriate decisions. Most people, when they say they'll do something, can be believed and relied upon. Not so with addicts. A key element of the disease of addiction is just the opposite - they are often compulsive liars and un-

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trustworthy. Accordingly, a key element of the trustee's job is to determine when the addict is telling the truth and following rules. And that factual determination, made by the trustee, is prerequisite for making monetary distributions to, or for the benefit of, the addict beneficiary. When acting within the guidelines, the trustee's discretion and judgement should be sole, absolute, and unreviewable.

### **FIDUCIARY DUTIES**

A trustee owes fiduciary duties to the beneficiaries of the trust. General duties are prescribed by statute, such as administer the trust (Probate Code §16000), be impartial (Probate Code §16003) and act as would a prudent person (Probate Code §16040). Specific duties related to the grantor's intent are expressed in the objectives and guidance. That's the sword of Damocles that hangs over every trustee.

However, the discretionary trust addressed herein is especially difficult due to the inevitable friction between the beneficiary and trustee. Beneficiaries, who happen to be alcohol or drug addicts, are desperate for money. They often lie, cheat and steal to get it. Addicts become expert at altering or concealing facts, spinning stories, and doing anything necessary to feed their dependency. The trustee is given the unenviable task of uncovering the truth and following the grantor's guidance accordingly. And beneficiaries will most likely resent interrogation techniques used to elicit basic information.

Another complicating factor is the presence of residual beneficiaries. Understandably the focus of a discretionary trust is on the child suffering from the addiction - who is the primary beneficiary. Ultimately however, money not distributed to the primary beneficiary goes to the residual beneficiaries - often siblings or other family members, or maybe a charity. Clearly there is a potential conflict of interest which can induce significant tension between the primary and residual beneficiaries, all

of whom may scrutinize the actions of the trustee. The trustee could be caught between antagonistic beneficiaries each pressuring the trustee to do their bidding.

### **TRUST PROTECTOR**

Besides the intrinsic friction between the trustee and primary (addict) beneficiary, and the potential conflict with residual beneficiaries, there can also be changed circumstances. This could be either factual situations or changes in the law that render the original trust objectives impossible or impractical to achieve. What happens then?

A common technique to dealing with changed circumstances, and a a myriad of other issues, is to appoint a Trust Protector with explicit power to:

- change the trustee;
- modify or interpret the trust;
- resolve disputes (without court intervention);
- move the trust to a different venue (state); or
- dissolve the trust.

A trust protector mechanism is a form of a "directed trust" wherein the grantor seeks to divide and allocate the duties and powers of the office of trustee between two or more persons. The grantor provides to a third party the power to direct or supervise some aspect of the trust or its administration. Ideally, the trust protector should be independent of both the trustee and beneficiaries - i.e., without any skin in the game.

A question often arises whether the trust protector is also a fiduciary with corresponding duties to the beneficiaries. While California doesn't have a statute explicitly covering directed trusts or trust protectors, the answer is almost certainly yes. The trust protector, holding powers which benefit others, will almost certainly be held as fiduciary to those beneficiaries and will be bound by assigned duties in the trust document.

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### REMEDIES

When creating the discretionary trust, the grantor can include terms which prove to be powerful disincentives to using the courts to solve problems. These may include:

- no contest clause;
- limits to trustee liability;
- use of trust protector to address issues and disputes with the trustee;
- mandatory mediation or arbitration;
- pay additional fees to a trustee when engaged in extraordinary service (e.g., litigation); and
- award costs and attorney fees to prevailing party.

Notwithstanding, there is always a chance a disgruntled beneficiary will circumvent recommended procedure and file a law suit. Absolute discretion may not be exercised fraudulently, in bad faith, or in a manner that constitutes abuse of discretion, so there may be a cause of action. Nonetheless, the unhappy beneficiary will have a difficult up-hill battle. The trustee is entitled to a presumption that he or she acted in good faith. If there is an alternative dispute resolution procedure specified in the trust, the court will probably insist it be utilized first. Lastly, if the grantor's intent is adequately stated in the objectives and guidance, the courts are unlikely to question discretion when the trustee is acting within the guidelines. And if there is a provision allowing a trust protector to resolve issues, the court is likely to accept any decision of the trust protector absent a showing of blatant disregard of the trust's objectives.

Given the potential antagonism regarding "the settlor's intent," and where the trustee's action is not clearly within the realm of discretion granted by the trust instrument, it may be worthwhile for the trustee to take preemptive strike and utilize the notice of proposed action procedure (Probate Code §16500-16504) to obtain court guidance on

the proper course of action. Additionally, a trustee can use this procedure to ratify a decision by the trust protector.

### WHO WILL BE THE TRUSTEE?

Given the difficulties described above, who in the world would every want to be a trustee for a Drug Addiction Trust? Who indeed. Certainly no corporate trustee would assume this role, regardless of the fee. Its unlikely any amount of money would motivate a person to take on this sort of duty with the inevitable acrimony, frustration, and stress. Probably the only candidate would be a family member or a close friend of the grantor - someone with thick skin.

Another alternative may be a professional fiduciary who is licensed by the California Professional Fiduciaries Bureau. They generally provide a wide range of services typically delegated to a trustee, agent, or conservator. In general, they are independent, far less expensive than corporate trustees, but offer many of the same benefits. And they are bonded.

The grantor can also have several individuals acting as co-trustees. Unless stated otherwise in the trust document, co-trustees must have unanimous agreement to act.

Or you can mix and match individuals with corporate trustees or professional fiduciaries. Actually, this makes a lot of sense in many situations. Family members may not object to one sibling acting as the trustee as long as there is an independent trustee who must agree to all decisions. Also, there are situations where significant transfer tax issues can arise if a member of the family is the sole trustee, where adding the independent co-trustee can defer imposition of gift, estate, or income taxes.

Other options include delineating different powers to different co-trustees and appointment of special trustees for certain property or duties.

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All things considered, it is usually a bad idea to have two or more siblings or family members acting as co-trustees. Suffice it to say, if there is any dysfunction whatsoever in the family, this is a good way to expose it - with potential escalation to costly litigation. Its better to select one trustee and provide detailed guidance in the trust instrument.

### **CONCLUSION**

A Drug Addiction Trust represents the intent of parents to deal with a very difficult situation once they are gone. Most parents who have cared for children stricken by the disease of drug or alcohol addiction are fully aware of the unpleasant realities. The habit is sustained by money - to buy drugs and support a basic living expenses for the addict who cannot hold a job and is facing a dire existence, maybe even homelessness. Under the circumstances, outright distribution of cash to an addict is out of the

question.

But addict or not, the parents still love their child and want to do something to help after they are gone. Disinheritance is too drastic with no ability to help the addict child. The only sensible answer is a discretionary trust with clear objectives, sensible guidelines and a reliable, tough-minded and resourceful trustee to administer the trust accordingly.

The trustee will have fiduciary duties to the beneficiaries and, as a consequence, exposure to litigation and potential harassment from disgruntled beneficiaries (especially the addict). Accordingly, it is important to draft the trust with adequate protections for the trustee, such as limited liability, alternative dispute resolution procedures, additional fees for extraordinary services, etc. Additionally, a Trust Protector may be useful means to monitor the trust's administration and resolve issues without court intervention.