SPECIAL REPORT

PLANNING AHEAD

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Delaware's New Beneficiary Well-Being Statute

Innovative trust law is the first of its kind in the country

There are considerable advantages to passing wealth through generations, such as tax savings, creditor protection, consolidated investment and management and protecting assets from imprudent waste. But more and more, planners and trust creators are recognizing that trust funds may grow in value so that too much money could become available to the beneficiaries before they've had an opportunity to learn about and know the value of money and the personal and social responsibilities that access to wealth entails. Trusts can hinder, or even become a disincentive, to the beneficiaries' growth, well-being and productivity. Trustors create trusts to improve their descendants' lives, not negatively impact their well-being. While traditional trust planning has attempted to mute the negative impact of inherited wealth by either restricting access to money or restricting access to information, a new approach has emerged so that the trust fund itself can be used as a financial resource to pay the costs of programs designed to prepare beneficiaries for the challenges of inherited wealth.

The Beneficiary Well-Being Trust

Consistent with Delaware's history of providing trustors with freedom of disposition and the ability to carry out their objectives, in 2024, Delaware enacted Section 3345 of Title 12 of the Delaware Code (the statute) to enable the creation of a beneficiary well-being trust. The statute allows a governing instrument to opt in to become a beneficiary well-being trust. Newly created trusts and existing trusts, by decanting, amendment or non-judicial settlement agreement, can use the statute. When the governing instrument does this, the trustee and other fiduciaries will have the powers and duties, and the beneficiaries will have the rights and interests, provided in Section 3345. Delaware's new statute is the first of its kind in the country. It facilitates the design and administration of trusts that support, rather than inhibit, beneficiary engagement, education, transparency and, ultimately, beneficiary well-being.

A beneficiary well-being trust turns the trust into a financial resource that enables the trustee to educate beneficiaries about financial matters, estate planning, family legacy, family dynamics and philanthropy to enhance beneficiary well-being. Rather than "protecting" a beneficiary by controlling distributions and silencing the flow of information, the trustee administers the trust more holistically, providing beneficiaries with access to the tools they need to navigate inheritance more skillfully with confidence, responsibility and knowledge.

The statute requires the trustees and advisors of a beneficiary well-being trust to provide the beneficiaries, individually or as a group, with "beneficiary well-being programs" as provided in the governing instrument or, in the absence of such provisions, as the trustee determines in its discretion. Thus, beneficiaries have the right to receive these well-being programs as part of their bundle of rights and interests as trust beneficiaries.

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The new statute provides what constitutes beneficiary well-being programs. Beneficiary well-being programs are "seminars, courses, programs, workshops, counselors, personal coaches, short-term university programs, group or one-on-one meetings, counseling, family meetings, family retreats, family reunions, and custom programs"[1] that have at least one of the following purposes:

1. Preparing each generation of beneficiaries for inheriting wealth by providing the beneficiaries individually or as a group with multi-generational estate and asset planning, assistance with navigating inter-generational asset transfers, developing wealth management and money skills, financial literacy and acumen, business fundamentals, entrepreneurship, knowledge of family businesses, and philanthropy and/or
2. Educating beneficiaries about the beneficiaries' family history, the family's values, family governance, family dynamics, family mental health and well-being, and connection among family members.[2]

The statute also provides that the governing instrument may provide additional powers, duties, rights and interests that expand the purpose or scope of beneficiary well-being programs. Trustors and drafters are expected to work together to craft tailored beneficiary well-being provisions into the governing instrument.

The trustee and other fiduciaries of a beneficiary well-being trust will personally engage with the beneficiaries and take time to get to know them and understand their challenges. The trustee, or other service providers arranged by the trustee, should communicate with the beneficiaries to discuss their progress and life goals, discuss wealth management and responsible wealth consumption, philanthropy, family dynamics, the family history and the origins of wealth creation within the family and assess their financial needs for future distributions. The trustee and other service providers should be appropriately compensated for the additional time and services necessary to fulfill the objectives and participate proactively in developing the beneficiaries' financial responsibility and well-being in relation to inherited wealth. The statute provides that the trustees and advisors of a beneficiary well-being trust shall pay the costs and expenses of beneficiary well-being programs from the trust. The trustee is entitled to its full fiduciary compensation without diminution by the fees and costs of the beneficiary well-being programs and without notice or disclosure to the beneficiaries. As a practical matter, these fee provisions will make it easier and more compelling for the trustee to proactively provide beneficiary well-being programs to beneficiaries and liberally fulfill the trustee's duties.

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Even if a trust isn't being created or modified, trusts administered in Delaware may enjoy some benefits of a beneficiary well-being trust through the addition of new paragraph (32) to Delaware's trustee powers statute, Section 3325 of Title 12. This new power provides trustees of all Delaware trusts with the power to:

> provide financial education services to the beneficiaries either individually or as a group, regarding multi-generational estate and asset planning, inter-generational asset transfers, developing wealth management and money skills, financial literacy and acumen, business fundamentals, entrepreneurship, personal financial growth, knowledge of family businesses, and philanthropy.

This should be a benefit to all beneficiaries of Delaware trusts.

Defining Well-Being

To determine what's likely to enhance the well-being of a beneficiary, it's helpful to define well-being and explore one of its empirical frameworks. While the field of positive psychology is relatively new (officially born in the late 1990s), the questions that have guided the research and application in the field of positive psychology have been asked for centuries. For thousands of years, since Confucius and Lao-Tsu in the East and the Greek philosophers in the West, thought leaders have been asking what constitutes the good life, what conditions support human thriving and what it means to be happy.[3] As stated in the preamble to the constitution of the World Health Organization, "Health is a state of complete physical, mental and social well-being and not merely the absence of disease or infirmity."[4] This definition implicitly recognizes that health isn't just defined by the absence of disease, but it's also about the presence of wellness. By extension, mental well-being isn't merely the absence of mental illness but the presence of psychological well-being.

> A beneficiary well-being trust not only allows for—but also encourages—the deeper, personal relationship between trustee and beneficiary.

Self-determination theory (SDT) is a well-established empirical framework that defines three fundamental components for psychological well-being. SDT is backed by over 40 years of research in human motivation and asserts that humans can be "active and engaged, or passive and alienated, largely as a function of the social conditions in which they develop and function."[5] At its core, SDT suggests people are wired to engage and contribute, and when they do, they experience a higher level of overall mental and physical well-being. Yet we know that the intrinsic drive of human motivation can be diminished, and when it is, individuals often thwart responsibility and growth. This is an all too familiar story told by trustees of trust beneficiaries.

SDT focuses on how human behavior is self-motivated and self-determined. It concludes that three psychological needs—autonomy, relatedness and competence—are critical to human motivation and well-being. When collectively tended to and fostered, they support growth, responsibility and engagement. When trusts are drafted and administered to support, rather than inhibit, the autonomy, relatedness and competence of the beneficiaries, the trust can go from being a legal structure focused exclusively on growing, preserving and protecting financial wealth to a source of wealth that can support not only the beneficiaries' financial needs but also the tools that are critical to sustaining well-being throughout phases of life, particularly as essential age- and stage-specific developmental milestones may be impacted by having access to inherited wealth.

Autonomy. SDT defines autonomy as the ability to exert personal agency over one's life and decisions.[6] By their very nature of limiting access to information, and establishing an external decision maker (the trustee) over the assets in trust for the beneficiary, traditional trust structures often reduce a beneficiary's autonomy. Imagine the different scenarios that could play out if a beneficiary had a beneficiary well-being trust inviting them on a path of education, engagement and growth. Where, in the context of their relationship with their trustee, they could demonstrate their increasing financial skills, life skills and grounded decision making and where they could engage in their own planning and asset management and pursue financial goals. The fostering of autonomy—even in a situation in which they don't have control over their inherited assets—is possible if they were to be invited by their trustee to consider how to use the resources in trust to enhance their well-being and their lives in meaningful ways.

Relatedness. This is defined as the ability to be in a relationship in a productive social ecosystem.[7] Often, especially with silent trusts, the opportunity for a

beneficiary to build a relationship and conversation with either the trustor or the trustee is greatly limited. This isolation often leads to misunderstandings about what the money is for, who "owns" it and its original intent. In their book, *Family Trusts: A Guide for Beneficiaries, Trustees, Trust Protectors, and Trust Creators*, Hartley Goldstone, James E. Hughes Jr. and Keith Whitaker assert that:

> [the] main criterion for a trustee is not necessarily any expertise but rather a moral one: it is someone that the trust creator deeply trusts to uphold his or her wishes with regards to the trust.[8]

A beneficiary well-being trust not only allows for—but also encourages—the deeper, personal relationship between trustee and beneficiary. Through a more holistic trustee-beneficiary relationship, the beneficiary can gain greater insight into the trustor's intent behind the resources in trust for them, while also building a trusting relationship with the trustee whose role it is to interpret the trust, making distributions in alignment with the trustor's intent. Additionally, through this enhanced experience, the beneficiary will have an opportunity to have a healthier relationship with money held in trust. The willingness of the trustee (and, if possible, the trustor) to be in a *relationship* with the beneficiary provides a significant opportunity for growth and learning.

Competence. This is defined as demonstratable skills that improve efficiency and performance in completing a job or task.[9] It isn't uncommon for the rising generation from financially significant families to have so many skilled professionals around them that they aren't forced to build the skills to become engaged and educated wealth-holders. What may start as well-intentioned professional support can quickly become a crutch. A beneficiary well-being trust can give the beneficiary access to age- and stage-appropriate education, beginning with basic personal financial skills and building to an understanding of portfolio design and investing options, annual family meetings exploring the family story and collectively held values and character strengths and individual meaningful support such as career coaching. These skills may not be important because the beneficiary needs the money but because they have the same human need that everyone has—to contribute and recognize that their contribution matters. Competence is an upward spiral—the more competent we feel, the more likely we are to take calculated risks and continue to grow and stretch, which builds resilience and ever-increasing levels of competence.

It's well studied that motivation—especially intrinsic motivation—is fundamentally important to human flourishing.[10] When beneficiaries are subjected to overly controlling conditions, they're left in a vacuum of meaningful guidance and relationships, undermining their ability to gain confidence and competence with complex trust and financial information. It's no wonder their motivation and engagement will likely stall under such conditions!

Benefits and Challenges

More often than not, the trustee only has a relationship with the trustor. When it's time to interact with the beneficiaries (because the trustor passes away), the trustee is replaced with a successor due to the minimal or total lack of relationship between the trustee and beneficiaries. By contrast, a beneficiary well-being trust necessarily promotes and cultivates communication between trustees and beneficiaries. The relationship extends beyond the trustor as the intent and purpose of the beneficiary well-being trust is to enhance and preserve the well-being of beneficiaries. This organically leads to the longevity of trusteeship.

Multigenerational trusts have their own set of administrative challenges as trustees have to manage multiple beneficiaries (often of different generations) who may not necessarily agree on the well-being programs and the associated costs to administer these programs. Although the language of Section 3345(b) is very broad in defining "beneficiary well-being programs" and gives the trustee wide-ranging discretion to determine what are appropriate well-being programs, a beneficiary may object and bring a claim against the trustee for improper use of the trust funds or for not appropriately following the terms of the trust. To address this, the trustee may provide one beneficiary

or a group of beneficiaries (excluding others) with beneficiary well-being programs (assuming the governing instrument provides this flexibility). But does this permit the trustee to disregard the interests of the other beneficiaries? Suppose a beneficiary is dissatisfied with the outcome of the well-being program. Does this expose the trustee to liability? These are challenges trustees have to navigate, but perhaps they aren't any more or less difficult than a trustee's responsibility of weighing the interests of all beneficiaries when making discretionary decisions.

Another challenge for trustees is determining whether the expenditures of these beneficiary well-being programs are considered distributions or expenses related to the trust administration. We discuss this in further detail below.

Distribution or Expense?

The trustee of a beneficiary well-being trust will certainly want guidance about the tax treatment of expenditures related to beneficiary well-being programs and whether expenditures should be treated as trust expenses chargeable to principal or income or as a distribution. An expenditure is treated as a distribution if it's made to or for the benefit of a beneficiary according to the provisions of the trust agreement.[11] Distributions typically include payments of income or principal made directly to a beneficiary or payments made on behalf of a beneficiary, such as payments for a beneficiary's college tuition, rent or medical bills.[12]

By contrast, an expenditure is treated as an administrative expense if it's an ordinary and necessary expense of the management of the trust.[13] Common administrative expenses include a trustee's or other fiduciary's commission and the trust's legal and accounting fees.[14] But administrative expenses also include expenditures necessary to effectively administer the trust.[15]

The language of the trust agreement plays a critical role in determining whether an expenditure should be treated as a distribution or an administrative expense. Paragraph (d) of Section 3345 states that subject to the governing instrument, trustees and advisors of a beneficiary well-being trust *shall* pay from the trust the costs and expenses of beneficiary well-being programs. The statute further states that payments under this subsection are administrative expenses of the trust to the extent permitted by law. With a beneficiary well-being trust, when a trustee provides beneficiary education programs, health and wellness coaching and similar initiatives, these services are central to the trust's purpose. Suppose a trust has several beneficiaries living in multiple states and countries, and the trustee is required to have all beneficiaries participate in a financial literacy program. This may require flying all the beneficiaries to one location. Would the costs of airfare be considered ancillary costs that are necessary and appropriate to the trustee's duties to carry out the terms of the trust? What if the well-being program was held in a faraway location like Tahiti? A statement of the trustor's intent and the incorporation of language from the statute may help provide the foundation on which the trustee may classify beneficiary well-being programs as administrative expenses rather than distributions. When making this determination, a trustee will consider whether the expenditure is necessary and appropriate to carry out the trust's purpose. However, the trustee will need to make this determination on a case-by-case basis. If the trustee determines these are administrative expenses, they aren't considered taxable distributions to the beneficiary (in the case of a non-grantor trust). This is impactful.

Scope of Deductibility

If the trustee has determined that an expenditure should be classified as an administrative expense, the next inquiry is whether such an expense is fully deductible or only deductible to the extent it exceeds 2% of the trust's adjusted gross income (AGI). In *William L. Rudkin Testamentary Trust v. Commissioner*,[16] the U.S. Supreme Court addressed this issue.

Section 67(e) of the Internal Revenue Code states that administrative expenses "which would not have been incurred if the property were not held in such trust or estate" are fully deductible.[17] In *Rudkin*, the trustee of a trust argued that investment advisory fees should be fully deductible administrative expenses.[18] The Court disagreed, determining that only administrative expenses that wouldn't otherwise

be incurred by a taxpayer but for the existence of the trust are fully deductible.[19] That is, the expenses aren't deductible if unrelated to the trust administration. The Court specifically identified fiduciary fees, accounting fees directly related to tax filing obligations and legal fees necessary for trust administration as examples of fully deductible expenses, reasoning that these expenses arise solely because of the trust's existence.[20]

While important details on the administration of beneficiary well-being trusts will continue to be refined, the goal of these trusts will remain a compelling factor in using them.

In the context of a beneficiary well-being trust, the administrative expense deduction associated with beneficiary education programs, health and wellness coaching and similar initiatives will likely only be deductible to the extent they exceed 2% of the trust's AGI. These types of services could be provided to family members in the absence of a trust. Consequently, their deductibility likely will be subject to the 2% floor.

Helping Beneficiaries Flourish

Like all innovative ideas, how this statute becomes adopted and operationalized by trustors, planners, administrators and beneficiaries alike will unfold in the coming years. While important details on the administration of beneficiary well-being trusts will continue to be refined, the goal of these trusts will remain a compelling factor in using them. By using beneficiary well-being programs to enhance autonomy, relatedness and competency, trustors, planners and trustees can help beneficiaries thrive as they pass through important life stages, particularly as their development may be impacted by the experience of being trust beneficiaries.

Endnotes

1. 12 Del. C. Section 3345(b).
2. *Ibid.*
3. Katherine Dahlsgaard, Christopher Peterson and Martin E. P. Seligman, "Shared Virtue: The Convergence of Valued Human Strengths Across Culture and History," *Review of General Psychology* (2005); Christopher Peterson, *A primer in Positive Psychology* (Oxford University Press 2006).
4. World Health Organization, "Health and Well-Being," *www.who.int/data/gho/data/major-themes/health-and-well-being#:~:text=The%20WHO%20constitution%20states%3A%20%22Health,of%20mental%20disorders%20or%20disabilities*. As listed in the Preamble to the Constitution of the World Health Organization as adopted by the International Health Conference, New York, June 19-22, signed on July 22, 1946 by the representatives of 61 States (Official Records of the World Health Organization, no. 2, at p. 100) and entered into force on April 7, 1948.
5. Richard M. Ryan and Edward L. Deci, "Self-determination theory and the facilitation of intrinsic motivation, social development, and well-being," *American Psychologist,* at pp. 68-78 (2000).
6. Richard M. Ryan and Edward L. Deci, *Self-Determination Theory: Basic Psychological Needs in Motivation, Development, and Wellness* (The Guilford Press 2017).
7. *Ibid.*
8. Hartley Goldstone, James E. Hughes, Jr., and Keith Whitaker, *Family Trusts: A Guide for Beneficiaries, Trustees, Trust Protectors, and Trust Creators* (Wiley & Sons 2016), at p. 54.
9. *Supra* note 5.
10. *Supra* note 4.
11. Internal Revenue Code Section 643(a).
12. *Ibid.*; Treasury Regulations Section 1.643(a)-3.
13. *Bingham's Trust v. Commissioner*, 325 U.S. 365, 368 (1945).
14. *Scott v. United States*, 328 F.3d 132, 140 (4th Cir. 2003).
15. *Supra* note 13, at p. 368.
16. *William L. Rudkin Testamentary Trust v. Comm'r*, 552 U.S. 181, 187 (2008).
17. IRC Section 67(e).
18. *Supra* note 16, at p. 186.
19. *Ibid.,* at p. 190.
20. *Ibid.,* at pp. 189-191.