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Office of Government Ethics
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MEMORANDUM

TO: Designated Agency Ethics Officials

FROM: Robert I. Cusick
Director

SUBJECT: Discretionary Trusts

The Office of Government Ethics (OGE) recently has received inquiries concerning the treatment of income beneficiaries of discretionary trusts, for purposes of the disqualification requirements of 18 U.S.C. § 208 as well as the financial disclosure requirements of section 102(f)(1) of the Ethics in Government Act, 5 U.S.C. app. This memorandum advises you of OGE's general approach to analyzing such issues, which focuses primarily on whether the trust creates any enforceable right to payment.

By "discretionary trust," OGE means a trust whose terms provide that the trustee pays to a beneficiary "only so much of the income and principal or either as the trustee in his uncontrolled discretion shall see fit." Restatement of the Law (Second) Trusts § 155. It is the essence of a "true 'discretionary trust' . . . that there is a discretion to give the named beneficiary some benefits under the trust or to give him nothing." G. Bogert, Trusts 160 (1987). In short, a discretionary trust does not give the beneficiary an enforceable right to payment. See, e.g., D.L. v. G.L., 61 Mass. App. Ct. 488, 497, rev. den. 492 Mass. 1108 (2004).

OGE does not view the income beneficiary of a discretionary trust as having a financial interest arising from the holdings of the trust for purposes of section 208. Similarly, OGE does not consider an income beneficiary of such a trust to have a reportable interest in trust holdings and income, under section 102(f)(1), merely because the individual potentially could receive payments. In various contexts involving trusts and other financial instruments, OGE has found it useful to distinguish between a "financial interest" and a "mere expectancy." See, e.g., "Revocable Living Trusts," DO-02-015, http://www.usoge.gov/pages/daeograms/dgr_files/2002/do02015.pdf. The former is covered by section 208 and also gives rise to a reportable "beneficial interest in principal or income . . . held by" the filer, under section 102(f)(1); the latter is covered by neither, as any gain or loss to the individual is only speculative. This distinction applies also in the case of discretionary trusts: "Where a trustee is given discretion to refuse all payments to the beneficiary, the beneficiary clearly has a mere expectancy rather than a property interest." U.S. v. Delano, 182 F. Supp.2d 1020, 1023 (D. Colo. 2001).

Nevertheless, if the filer (or spouse or dependent child) actually receives a distribution from a discretionary trust during the reporting period, the filer must report the trust and its holdings. In such circumstances, the trust has become one "from which income is received by" the filer. § 102(f)(1). This does not mean, of course, that the filer has a disqualifying financial interest under section 208, because any future payment remains a mere expectancy at the time the employee might participate in a particular matter affecting the holdings of the discretionary trust. See, e.g., In re Marriage of Jones, 812 P.2d 1152, 1156 (Colorado 1991) (fact that some income has been distributed at sole discretion of trustee does not change nature of underlying trust). However, where there is a history of discretionary payments actually received by the beneficiary, potential appearances of a lack of impartiality should be handled under 5 C.F.R. § 2635.502, including paragraph (a)(2) of that provision.

Finally, OGE wants to emphasize that the analysis outlined above applies only to truly discretionary trusts, i.e., those that really do not provide any standard for an enforceable right to payment. In OGE's experience, many trusts provide the trustee with discretion over only certain matters, for example, the timing, amount or source (principal or income) of payment. Such terms are not sufficient to preclude an enforceable right to payment. See Restatement § 155, comment c. Moreover, the approach described in this memorandum does not apply if the beneficiary also has a vested remainder interest, see 5 C.F.R. § 2634.310(a)(2), is a trustee or co-trustee, or is the settlor, see Restatement § 156.