

IN THE COURT OF APPEALS OF IOWA

No. 9-898 / 08-1625
Filed February 10, 2010

**IN THE MATTER OF THE TRUST
ESTABLISHED UNDER THE LAST WILL
AND TESTAMENT OF
ORVILLE J. KINSEL, Deceased,**

DARRIN R. SCHAPPERT,
Appellant.

Appeal from the Iowa District Court for Black Hawk County, Walter W. Rothschild, Judge.

A remainder beneficiary under a residuary trust appeals from the district court's ruling ordering the trustee to pay the corpus of the residuary trust to the Iowa Department of Human Services Estate Recovery Program to satisfy the Medicaid debt of the trust beneficiary. **AFFIRMED.**

Wallace D. Parrish of Parrish Law Firm, Waterloo, for appellant.

Thomas J. Miller, Attorney General, Barbara E.B. Galloway, Assistant Attorney General, and Benjamin C. Chatman, Des Moines, for appellee Iowa Department of Human Services.

Eric W. Johnson of Beecher, Field, Walker, Morris, Hoffman & Johnson, P.C., Waterloo, for intervenor trustee.

Heard by Vaitheswaran, P.J., and Potterfield and Mansfield, JJ.

MANSFIELD, J.

This case requires us to determine whether a particular trust is a “discretionary trust with standards,” and if so what effect Iowa Code section 633A.4702 (2007) has on the Iowa Department of Human Services’ (DHS’s) right to recover Medicaid benefits from the corpus of that trust following the death of the beneficiary. For the reasons set forth herein, we affirm the ruling of the district court.

I. Background Facts and Proceedings.

In 1992, Orville Kinsel executed his last will and testament. At the time, Orville was living with and providing for the care of his sister, Faye Kinsel, who was born with a mental disability. In his will, Orville made several specific bequests before placing the remainder of his estate into a trust (Kinsel Trust), which stated:

The rest, residue and remainder of my estate shall be held in trust by The National Bank of Waterloo^[1] for my sister, Faye Kinsel, as beneficiary, to be used for her care and support, but only after the trust assets under the trust which was established for her under the Last Will and Testament of my mother, Rosena L. Kinsel, . . . have been depleted.^[2] Thereafter such assets from the residue of my estate . . . shall be held in trust by said Trustee, to be used for the care and support of said Faye Kinsel, according to the best discretion of my Trustee. Upon the death of the said Faye Kinsel, any assets remaining in said Trust shall go to my nephew, Darrin R. Schappert, to be his absolutely.

On December 28, 1996, Orville passed away. In February 1997, Faye was admitted to a nursing home and began receiving Medicaid benefits. Faye remained in the nursing home and continued to receive Medicaid benefits until

¹ The National Bank of Waterloo has been succeeded by Regions Bank.

² At all times relevant to this matter, the trust of Rosena L. Kinsel had been depleted.

her death on January 16, 2008. At the time of Faye's death, the State had provided her with Medicaid benefits totaling \$376,628.89. Although the trustee was paying the interest received from the Kinsel Trust's assets toward Faye's care while she lived in the nursing home, this amounted to only approximately \$300 per month. The trustee did not invade the corpus of the trust for Faye's support during Faye's lifetime. Medicaid paid for the vast bulk of her care.

Following Faye's death, DHS and Darrin asserted competing claims to the remaining corpus of the Kinsel Trust, which amounted to approximately \$100,000. Under Iowa's Medicaid recovery system, when a person who received certain Medicaid services dies, DHS is authorized to recover from his or her estate the costs of medical assistance previously provided on his or her behalf. Iowa Code § 249A.5(2)(a). Further, the estate is deemed to include certain non-probate assets, including any "interest" in a trust that the beneficiary had the time of his or her death. *Id.* § 249A.5(2)(c). Seeking guidance on how to resolve the parties' conflicting claims, the trustee petitioned the district court for a ruling as to how the trust corpus should be distributed.

On August 8, 2008, the district court determined that the specific language of Orville's trust created a discretionary support trust.³ Under supreme court precedent, see *In re Barkema Trust*, 690 N.W.2d 50 (Iowa 2004), this meant Faye had an "interest" in the trust and would allow DHS to recover Faye's Medicaid debt from its corpus. The district court further found that a statute enacted after the filing of the *Barkema* case, Iowa Code section 633A.4702, did

³ The Restatement (Third) of Trusts now refers to a discretionary support trust as a discretionary trust with standards. Regardless, "they are the same animal." *In re Estate of Gist*, 763 N.W.2d 561, 565 (Iowa 2009).

not alter that result.⁴ Although that statute appears to give preference to language in a trust granting the trustee discretion to make or withhold distributions, the district court concluded the language of the Kinsel Trust contained an “express mandate” that “requir[ed] the trustee to use the total assets for the care and maintenance of Faye Kinsel.” Accordingly, Faye had an “interest” in the trust as described in section 249A.5(2)(c). Thus, the district court directed the trustee to pay the remaining corpus of the trust to the DHS Estate Recovery Program.

Darrin appeals. He argues that the trust was not a discretionary trust with standards. Further he maintains that even if it were such a trust, in light of section 633A.4702, the trustee’s discretion trumped any enforceable right to payments, and accordingly Faye had no “interest” to which DHS may now lay claim.

II. Scope of Review.

Our review of this equitable proceeding is de novo. *Gist*, 763 N.W.2d at 563; *Barkema*, 690 N.W.2d at 53.

III. Analysis.

A. *Barkema* and *Gist*.

We begin our analysis by discussing the two supreme court decisions that provide the backdrop to this case: *Barkema* and *Gist*. In *Barkema*, the testator

⁴ Iowa Code section 633A.4702 provides:

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

left one-fourth of his estate to three of his children to hold in trust for his fourth child, Lois. 690 N.W.2d at 52. The trust provided, “If possible, only the income from said share shall be used for Lois, however, if necessary for her proper support and maintenance, then the corpus of said trust may be invaded to the extent said trustees deem necessary.” *Id.* Upon Lois’s death, DHS asserted a claim to the corpus of the trust as against the residuary beneficiaries. *Id.* at 53. The supreme court held in favor of DHS. The court first concluded that the trust was a “discretionary support trust.” *Id.* at 54. In other words, although it conferred discretion in the trustee, the trust provided the beneficiary with an enforceable right to *some* level of support. As the court explained, “The trust agreement contained a support provision and provided directions for the trustee to use the trust corpus if necessary for Lois’s support and maintenance.” *Id.* Having concluded the trust was a discretionary support trust that “gave Lois the legal ability to compel the trustee to invade the corpus of the trust and make distributions to her for her support,” the court then reasoned that Lois had an “interest” within the meaning of Iowa Code section 249A.5(2)(c) that could be reached by DHS upon Lois’s death. *Id.* at 56.

Five years after *Barkema*, in 2009, the supreme court decided *Gist*. There the trust stated that the trustee would use so much of the trust income

as may be necessary to provide [Elenore] with a reasonable standard of living, considering any other means of support or resources which she may have. If the income shall be insufficient to provide her with a reasonable standard of living the trustee may invade the principal or corpus of the trust assets.

Gist, 763 N.W.2d at 564. The supreme court concluded the *Gist* trust fell into the same category as the trust in *Barkema*; however, the terminology had evolved,

and it was now referred to as a “discretionary trust with standards” rather than a “discretionary support trust.” *Id.* at 565. In any event, they were “the same animal.” *Id.* Accordingly, the beneficiary had an “interest” in the trust, and the trust was subject to DHS’s claim upon her death. *Id.* at 566. A major issue in *Gist*, which does not arise here, was whether a separate “spendthrift” provision in the trust barred recovery by DHS. The supreme court found it did not. *Id.* at 567.

Neither *Barkema* nor *Gist* addressed (or even mentioned) Iowa Code section 633A.4702. *Barkema* arose before the statute had been enacted, and although DHS mentioned that statute in its briefing in *Gist*, the supreme court did not discuss it in its opinion.

B. Discretionary Trust with Standards.

We now turn to the trust involved in this case. Taking our cues from *Barkema* and *Gist*, our first task is to classify the trust at issue. *Gist*, 763 N.W.2d at 565. We believe the language of the Kinsel Trust created a discretionary trust with standards:

[A] settlor creates a discretionary trust with standards if the stated purpose of the trust is to furnish the beneficiary with support, and the trustee is directed to pay to the beneficiary whatever amount of trust income or principal the trustee deems necessary for his support. Generally, if the trust is a discretionary trust with standards, the beneficiary has a right that the trustee pay him the amount which in the exercise of reasonable discretion is needed for his support; and the beneficiary can transfer this interest or his creditors may reach it, unless it is protected by a spendthrift clause.

Id. (quoting *Barkema*, 690 N.W.2d at 54) (internal quotations omitted).

The stated purpose of the Kinsel Trust was to provide for the “support and care” of Faye Kinsel and to do so “according to the best discretion of [the] Trustee.” Thus, the inclusion of the “support and care” language in the Kinsel

Trust provides an enforceable standard requiring the trustee to make the minimal distributions needed to comport with the settlor's intent of providing basic support. *Barkema*, 690 N.W.2d at 54. Furthermore, the Kinsel Trust provides the trustee with the discretion to invade the principal or the corpus of the trust in order to meet this minimum level of support. *Id.*

Darrin points out that the operative language of the trusts involved in *Barkema and Gist* differed somewhat from the language here. In *Barkema*, the trust stated that “*if necessary* for her proper support and maintenance, then the corpus of said trust may be invaded to the extent said trustees deem necessary.” 690 N.W.2d at 52 (emphasis added). In *Gist*, the trust provided that the income shall be paid to the beneficiary “*as may be necessary* to provide her with a reasonable standard of living,” and if the income is insufficient “the trustee may invade the principal or corpus.” 763 N.W.2d at 564 (emphasis added). As Darrin notes, the word “necessary” present in those cases is absent here. However, reading the trust instrument as a whole, we find this is a distinction without a difference. The Kinsel Trust still establishes a safety net for the protection of the beneficiary, accompanied by a quantum of discretion.

Notably, the Kinsel Trust begins, “The rest, residue and remainder of my estate shall be held in trust . . . for my sister, Faye Kinsel, as beneficiary, *to be used for her care and support . . .*” (Emphasis added.) This directive—“to be used for her care and support”—is straightforward and mandatory. The concept of discretion is not even introduced until the next sentence, which says the funds “shall be held in trust by said Trustee, to be used for the care and support of said Faye Kinsel, *according to the best discretion of my Trustee.*” (Emphasis added.)

Combining these two sentences, we agree that the trust contains a bedrock requirement of support, but with some topsoil of discretion. In this respect, it does not differ from the trusts involved in *Barkema* and *Gist*.

We also find this conclusion bolstered by our earlier decision in *Strojek ex rel. Mills v. Hardin County Board of Supervisors*, 602 N.W.2d 566 (Iowa Ct. App. 1999). *Strojek* predates *Barkema* and *Gist* but is not inconsistent with them, and is actually cited in *Barkema*. See 690 N.W.2d at 53-54. In *Strojek*, we interpreted a trust provision that the trustee

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

See 602 N.W.2d at 568. Despite the seemingly broad discretionary language (i.e., “sole discretion”), we held the instrument was a “discretionary support trust” (now referred to as a discretionary trust with standards). *Id.* at 570. In other words, we decided the trust language required the trustee to provide “basic support,” while nonetheless giving him “broad discretionary powers.” *Id.* Significantly, the discretionary language in *Strojek* (“sole discretion”) was broader than the discretionary language of the Kinsel Trust (“best discretion”). None of that kept us from characterizing the trust as containing a basic support obligation.⁵

⁵ Darrin argues that the presence of the word “necessary” in *Strojek* made the support obligation more mandatory there than it is here. We find Darrin’s approach too simplistic. Word placement can matter as much as (or more than) word selection. As the trust was worded in *Strojek*, what was “necessary” was only what the trustee *in her sole discretion deemed necessary*.

C. Impact of Iowa Code Section 633A.4702.

Having found the Kinsel Trust to be a discretionary trust with standards, we must now consider the potential impact of Iowa Code section 633A.4702 on this determination. Section 633A.4702 provides:

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

As the district court observed, there have been no Iowa appellate cases interpreting this provision. We are also unaware of such a statute having been enacted in any other jurisdiction. To us, the statute raises a number of potential questions. What constitutes language “granting a trustee discretion to make or withhold a distribution”? Does such language “prevail” over language providing for a right to distributions even if the two are not in conflict, i.e., both can be given effect and reconciled? What is “clear and convincing evidence to the contrary”? Does such “evidence” reside in the trust instrument itself or can it come from extrinsic evidence? Is section 633A.4702 intended to apply only to specific instances where a beneficiary is trying to compel a distribution, or can it transform the overall characterization of a trust (e.g., from a discretionary trust with standards to something else)? We do not see easy answers to many, if not all, of these questions. We agree with Darrin that section 633A.4702 has to mean *something*.

For present purposes, however, we agree with DHS and the district court that section 633A.4702 should not alter the outcome in *this* case. We reach this

conclusion for at least two reasons: First, we do not believe the legislature intended in 2004 to make a substantive change in existing beneficiaries' rights. If it had, serious constitutional questions would be raised. See *In re Will of Uchtorff*, 693 N.W.2d 790, 797 (Iowa 2005) (interpreting the Iowa Trust Code, adopted in 1999, as not divesting previously vested rights). In this case, Orville Kinsel executed his will in 1992, and died in 1996, at which point the trust came into existence and his mentally disabled sister Faye began receiving distributions. We do not believe the legislature intended to alter Faye's rights retroactively when it enacted section 633A.4702.⁶

Second, like the district court, we find clear and convincing evidence establishes the existence of a mandatory support obligation. The first sentence of the trust describes a clear support obligation, with no reference at all to discretion—i.e., “shall be held in trust . . . to be used for the care and support” The second sentence reiterates the support obligation, but adds language allowing for “the best discretion” in implementing this support obligation. The third sentence states that on Faye's death, “any assets remaining” shall go to Darrin, suggesting the possibility that nothing may be left.

In interpreting testamentary trusts, “the intent of the testator is the polestar and must prevail.” *Strojek*, 602 N.W.2d at 570-71. The testator's intent is derived from: (1) the four corners of the will, (2) the scheme for distribution, and (3) the surrounding circumstances at the time of the will's execution. *Id.* at 571. The circumstances surrounding Orville's will provide strong evidence of an intent

⁶ By 2004, Faye had been in the nursing home for approximately seven years, and her rights to support under the trust already had vested, at least as to those seven years.

to establish a binding obligation to support and care for Faye. Faye had a mental disability. At the time of the execution of Orville's will, she lived with Orville and was dependent upon him. Faye's long-term needs would have been readily apparent to Orville. At the time of the execution of the will, i.e., in 1992, Medicaid estate recovery had not yet been enacted by the legislature. Thus, it would not have occurred to Orville to try to shield assets from DHS's eventual reach by making their availability to Faye purely discretionary.⁷

IV. Conclusion.

For the foregoing reasons, we affirm the district court's ruling ordering the corpus of the Kinsel Trust to be paid to the DHS Estate Recovery Program.

AFFIRMED.

⁷ As we have noted, when the supreme court decided *Gist*, it did not mention section 633A.4702 in its opinion, although DHS had mentioned the statute in its briefing. It is reasonable to conclude that the supreme court did not believe section 633A.4702 affected the outcome in that case, just as we conclude it does not affect our determination of DHS's rights regarding the discretionary trust with standards involved here.