

Title

The spendthrift trust: Its doctrinal underpinnings

Text

The typical enforceable trust spendthrift provision forecloses assignment and attachment of the equitable property interests that are incident to the particular trust relationship. Assume an income-only non-self-settled irrevocable trust for X's life that ultimately terminates in favor of Y. Y would be foreclosed from assigning his equitable quasi-remainder during X's lifetime. Once the trust has terminated and legal title to its corpus has passed from the trustee to Y free of trust, then the fee becomes fully assignable by Y and reachable by Y's creditors, absent special facts. (A "currently distributable" item of income or principal in the hands of the trustee may be creditor-vulnerable as well.) One Illinois court has garbled its explanation of all this core doctrine. "Spendthrift trust provisions," asserts the court, "restrict the beneficiary's ability to alienate and the beneficiary's creditors' ability to attach the trust corpus." See *In re Marriage of Sharp*, 860 N.E.2d 539 (Ill. App. 2006). But the right of alienation of the corpus itself is in the title-holding trustee while the trust is ongoing, not in the beneficiary. It is a right that is generally untrammelled until title ultimately passes. Thus, a trust spendthrift clause is not the type of restraint on the alienability of property that has traditionally been unenforceable on public policy grounds. All this spendthrift doctrine is fleshed out in §5.3.3.3(c) of *Loring and Rounds: A Trustee's Handbook* [pages 364-377 of the 2018 Edition], which sub-section is reproduced in the Annex below.

Annex

§5.3.3.3(c) The non-self-settled spendthrift trust. [from *Loring and Rounds: A Trustee's Handbook* [pages 364-377 of the 2018 Edition].

History of the spendthrift trust. In England, trust spendthrift provisions have generally been unenforceable, at least since 1811.³⁴¹ In the United States this was generally also the case until 1875, when the U.S. Supreme Court handed down its spendthrift-friendly decision in *Nichols v. Eaton*.³⁴² Once the Massachusetts Supreme Judicial Court had held—in *Broadway National Bank v. Adams* (1882)³⁴³—that a trust spendthrift provision was a permissible form of alienation restraint, there was little doubt that the spendthrift trust had gained an important strategic foothold on this side of the Atlantic, and that it was

³⁴¹Lewin ¶15-109 (England); 3 Scott & Ascher §15.2.1 (the leading English case standing for the proposition that direct restraints on the alienability of equitable interests are unenforceable being *Brandon v. Robinson*, a case decided by Lord Eldon in 1811 [18 Ves. 429 (1811)]). Note, however, that while the English courts have generally never permitted restraints on the alienation of equitable interests, they have uniformly upheld restraints against the alienation of a married woman's equitable interest under a marriage settlement. Scott on Trusts §146.1 (1939 ed.). See generally §9.30 of this handbook (marriage settlements (England)).

³⁴²See *Nichols v. Eaton*, 91 U.S. 716, 727 (1875) ("Why a parent, or one who loves another, and wishes to use his own property in securing the object of his affection, as far as property can do it, from the ills of life, the vicissitudes of fortune, and even his own improvidence, or incapacity for self-protection, should not be permitted to do so, is not readily perceived."). Followed by *Broadway Nat'l Bank v. Adams*, 133 Mass. 170 (1882). See also 3 Scott & Ascher §15.2.1, n. 12 for a catalog of U.S. jurisdictions in which direct restraints on the alienability of equitable interests in non-self-settled trusts have been enforced by the courts in the absence of legislation addressing one way or another the enforceability issue. But see Restatement (Third) of Trusts §58 cmt. e (providing that a spendthrift restraint is not valid with respect to any interest retained by the settlor).

³⁴³133 Mass. 170 (1882).

probably here to stay. Prof. John Chipman Gray was not amused: “My modest task has been to show, that spendthrift trusts have no place in the system of the Common Law. But I am no prophet, and certainly do not mean to deny that they may be in entire harmony with the Social Code of the next century. Dirt is only matter out of place; and what is a blot on the escutcheon of the Common Law may be a jewel in the crown of the Social Republic.”³⁴⁴

The spendthrift clause explained. A “spendthrift provision” is “a term of a trust which restrains both³⁴⁵ voluntary³⁴⁶ and involuntary ... [irrevocable]³⁴⁷... transfer[s] of a beneficiary's ... [equitable or beneficial]³⁴⁸... interest.”³⁴⁹ Again, it restrains alienation of the equitable or beneficial interest. Its purpose is not to tie up distributions of income and/or principal once in the hands of a beneficiary, nor could it do so.³⁵⁰ Similarly a spendthrift clause in a trust purporting to restrain alienation of the outstanding nonpossessory vested equitable *reversionary interest* under that trust or to insulate that interest from the reach of the settlor's creditors would be unenforceable.³⁵¹ This durable right of alienation would accrue to the settlor's successors in interest as well. Nor would a spendthrift provision in and of itself prevent a beneficiary's court-appointed guardian or agent acting under a durable power of attorney from compelling or taking distributions *on behalf of the beneficiary*.³⁵² Even in the face of a restriction on the right to alienate the *equitable interest*, the beneficiary of a spendthrift trust who has been granted a nonfiduciary power of appointment may effectively transfer the *underlying trust property* by an exercise of the power.

Rights of assignees of spendthrifted equitable interests. If the trustee of a spendthrift trust makes a distribution of a portion of the trust property to an assignee in the face of a valid spendthrift provision, the transfer is nonetheless effective³⁵³ and the trustee is protected.³⁵⁴ The beneficiary's assignment is treated as an agency, the trustee being the agent and the beneficiary the principal.³⁵⁵ The terms of the constructive agency are that the trustee shall transfer to the purported assignee “whatever distributions the beneficiary is entitled to receive and has purported to assign.”³⁵⁶ The authorization, as with any agency, however, is revocable.³⁵⁷ “Thus, a spendthrift restraint merely prevents the beneficiary from making an *irrevocable*

³⁴⁴John Chipman Gray, *Restraints on the Alienation of Property* x (2d ed. 1895) (preface to the second edition).

³⁴⁵“For reasons of policy, a spendthrift restraint that seeks only to prevent creditors from reaching the beneficiary's interest, while allowing the beneficiary to transfer the interest, is invalid” Restatement (Third) of Trusts §58 cmt. b(2).

³⁴⁶“A spendthrift restraint prevents the transfer of a trust beneficiary's interest to another, whether the attempted assignment is by gift, sale, or exchange, or as security for a new or existing debt.” Restatement (Third) of Trusts §58 cmt. c.

³⁴⁷Restatement (Third) of Trusts §58 cmt. d(1).

³⁴⁸Restatement (Third) of Trusts §58 cmt. d(1).

³⁴⁹UTC §103(15). *See also* UTC §502(a).

³⁵⁰Restatement (Third) of Trusts §58 cmts. d. & d(2); 3 Scott & Ascher §15.2.5.

³⁵¹6 Scott & Ascher §40.4 (Transfer by Beneficiary). The settlor, however, could assign the equitable reversionary interest to the trustee of another spendthrift trust for the benefit of a third person. In that case, the spendthrift clause of the other trust might well be enforceable. An outstanding equitable reversionary interest would become possessory upon the imposition of a resulting trust, a topic we take up in §4.1.1.1 of this handbook.

³⁵²*See generally* 3 Scott & Ascher §15.6 (Disability of Beneficiary of Spendthrift Trust).

³⁵³Restatement (Third) of Trusts §58 cmt. d(1).

³⁵⁴Restatement (Third) of Trusts §58 cmt. d(1).

³⁵⁵Restatement (Third) of Trusts §58 cmt. d(1).

³⁵⁶Restatement (Third) of Trusts §58 cmt. d(1).

³⁵⁷“If the beneficiary of a spendthrift interest purports to transfer it to another for value but later revokes the assignment and the trustee's authority pursuant to it, the beneficiary is liable to that other person.” Restatement (Third) of Trusts §58 cmt. d(1). “Although that person cannot reach the

transfer of his or her beneficial interest,”³⁵⁸ that is of the equitable income stream itself. On the other hand, “[a] number of cases have held that an assignment is valid and presumably irrevocable as to income that is *already in the hands of the trustee at the time of the assignment*.”³⁵⁹

Liability of third parties. Third parties, as well as the trustee, can incur liability for violating the terms of a valid spendthrift provision. Take, for example, the trustee who holds legal title to contractual rights against a third party, such as rights against the corporate issuer of a bond or rights against an insurance company incident to an insurance policy. The third party, instead of making a payment to the trustee, who is the other party to the contract, takes it upon itself to make a payment directly to the beneficiary. The trustee may have a fiduciary duty to seek to compel the third party to make the payment a second time, this time to the trustee.³⁶⁰

Constructive receipt by the beneficiary of a spendthrift trust. When does a mandatory nondiscretionary distribution³⁶¹ “reach the hands” of the beneficiary? One court has held as early as when the trustee writes out the distribution check: Although the check for \$862.95 representing “accrued income, ready for distribution” had not left the hands of the trustee, let alone been delivered to the beneficiary, the beneficiary's creditor was allowed to seize it. “[W]e think ... [the beneficiary's right]... vested in his share of the income when the amount was ascertained, ready for distribution and the accounting made.”³⁶² The Restatement (Third) of Trusts is generally in accord. It would deem distributable spendthrifted funds held by a trustee for an unreasonably long period of time to be constructively received by the beneficiary and therefore subject to attachment by his or her creditors.³⁶³ The UTC similarly provides that the creditor of the beneficiary of a spendthrift trust can reach a mandatory distribution of income or principal that has not been made to the beneficiary “within a reasonable time after the designated distribution date.”³⁶⁴ In

beneficiary's interest under the trust, satisfaction of the claim can be obtained from other property of the beneficiary or from trust funds after they have been distributed to the beneficiary.” Restatement (Third) of Trusts §58 cmt. d(1). For a discussion of the “charging order” option, see §5.3.3 of this handbook.

³⁵⁸Restatement (Third) of Trusts §58 cmt. d(1).

³⁵⁹3 Scott & Ascher §15.2.5, n.10 and accompanying text.

³⁶⁰The third-party obligor who makes a payment directly to the trust beneficiary instead of to the title-holding trustee, the other party to the contract, does so at his, her, or its peril, unless directed to do so by the trustee. 5 Scott & Ascher §32.1 (Discharge by Beneficiary of Claim Against Third Person). If the beneficiary is not of full age and legal capacity, the third party obligor runs the risk of having to pay twice. 5 Scott & Ascher §32.1 (Discharge by Beneficiary of Claim Against Third Person). There is a similar risk if following the direction were to constitute a knowing participation with the trustee in a breach of trust, or if the trust were a spendthrift trust. 5 Scott & Ascher §32.1 (Discharge by Beneficiary of Claim Against Third Person). In the case of a direct payment to the beneficiary in the face of a valid spendthrift provision, “[i]t would seem, ... that the third person is entitled to maintain an action against the beneficiary personally to recover the amount paid to the beneficiary if the beneficiary was not under a legal incapacity at the time of the payment.” 5 Scott & Ascher §32.1 (Discharge by Beneficiary of Claim Against Third Person). This claim for restitution would have to be satisfied from any property belonging to the beneficiary that is lawfully not in the trust.

³⁶¹A mandatory distribution is “a distribution of income or principal which the trustee is required to make to a beneficiary under the terms of the trust, including a distribution upon termination of the trust.” UTC §506(a). “The term does not include a distribution subject to the exercise of the trustee's discretion even if (1) the discretion is expressed in the form of a standard of distribution, or (2) the terms of the trust authorizing a distribution couple language of discretion with language of direction.” UTC §506(a).

³⁶²Knettle v. Knettle, 197 Wash. 225, 229, 84 P.2d 996, 998 (1938).

³⁶³Restatement (Third) of Trusts §58 cmt. d(2); UTC §506(b). See generally 3 Scott & Ascher §15.2.5.

³⁶⁴UTC §506(b).

California it is after the distribution has become due and payable.³⁶⁵

Discretionary payments to the creditors of the beneficiary. The trustee's fiduciary duties, of course, run to the beneficiary and not his or her creditors. Thus, when neither trustee retention nor distribution out is an attractive option from the beneficiary's perspective, the trustee of a spendthrift trust may want to consider a third option, namely, making distributions in the form of cash payments to certain creditors of the beneficiary, *e.g.*, credit card companies, automobile leasing companies, and the like, provided doing so is for the benefit of the beneficiary and provided the terms of the trust permit such indirect applications of trust funds. An indirect distribution out toward the outright purchase of an item of property, *e.g.*, an automobile, on the other hand, might well subject the item itself to creditor attachment. Carefully considered indirect applications of trust funds to certain creditors of and service providers to a beneficiary are likely to conform to the equitable spirit if not the letter of most trust spendthrift provisions.³⁶⁶

Drafting the spendthrift provision. “No specific form of words is necessary to impose a ... [direct]... restraint on alienation.”³⁶⁷ The key is that the settlor intended to impose such a restraint. Some courts have even construed express voluntary restraints to include involuntary restraints, and vice versa.³⁶⁸ Some have even enforced one-sided restraints that operate only against creditors.³⁶⁹ “In their enactment of the UTC, Arizona, Kansas, Missouri, and North Dakota allow spendthrift provisions that restrain either the voluntary or involuntary transfer of the beneficiary's interest. The Ohio version of the UTC allows a trust to restrain involuntary transfers but to allow voluntary transfers with the consent of a trustee who is not the beneficiary.”³⁷⁰ Assuming, however, that a prospective settlor intends to create a spendthrift trust that is squarely in the mainstream, then he or she would be well advised to put in the governing instrument clear and unambiguous language to the effect “that the beneficiary may not assign, sell, mortgage, or otherwise dispose of the interest and that the interest is not liable for the beneficiary's debts.”³⁷¹ To be valid under the model UTC, a spendthrift provision must restrain both voluntary and involuntary alienations of a beneficiary's equitable interest, except for the equitable reversion.³⁷²

Current and future equitable interests are generally protectable. By “interest” we mean not only the equitable right to benefit from a trust's income stream but also the equitable right to receive its principal in the future. At one time, however, a direct restraint on, say, a trust remainderman's right *during the lifetime of the income beneficiary* to alienate the equitable remainder interest was invalid.³⁷³ This is generally no longer the case, with one possible exception; an exception, by the way, that should not be confused with the possession of a general testamentary power of appointment:³⁷⁴

The rule is different, however, in the case of a restraint on the alienability of an

³⁶⁵See *Carmack v. Reynolds*, 2 Cal. 5th 844 (2017).

³⁶⁶See generally Alan Newman, *Spendthrift and Discretionary Trusts: Alive and Well under the Uniform Trust Code*, 40 Real Prop. Prob. & Tr. J. 567, 570–571 (Fall 2005).

³⁶⁷3 Scott & Ascher §15.2.4.

³⁶⁸See generally 3 Scott & Ascher §15.2.4.

³⁶⁹See generally 3 Scott & Ascher §15.2.3.

³⁷⁰Kevin D. Millard, *Rights of a Trust Beneficiary's Creditors under the Uniform Trust Code*, 34 ACTEC L.J. 58, 60 (2008) (citations omitted).

³⁷¹3 Scott & Ascher §15.2.4.

³⁷²UTC §502(a). See generally §4.1.1 of this handbook (the equitable reversion) and §4.1.1.1 of this handbook (the resulting trust).

³⁷³3 Scott & Ascher §15.2.7. Apparently, the restraint seemed too much like a direct restraint on the alienability of a legal interest in land in fee simple or of an absolute legal interest in personality, both of which were, and today generally are, forbidden on public policy grounds.

³⁷⁴See generally §8.1 of this handbook (powers of appointment)

interest of principal that is payable to the beneficiary's *estate*. Such a restraint *cannot* advantage the beneficiary. It would serve only to ensure that, at death, the beneficiary could dispose of the property free of the claims of creditors. Accordingly, such a restraint is not effective, and upon the beneficiary's death, creditors can reach the principal. In addition, it would seem that if the income is payable to a beneficiary for life and the principal is payable to the same beneficiary's estate, the beneficiary's creditors ought to be able, during the beneficiary's lifetime, to reach the interest in principal, even if a spendthrift provision denies them access to the income interest.³⁷⁵

Trustee of a spendthrift trust is still entitled to be indemnified from the trust estate. Notwithstanding the existence of a spendthrift clause, a trustee is entitled to indemnity out of the trust estate for expenses properly incurred by him in the administration of the trust.³⁷⁶ Moreover, it would seem equally appropriate that the equitable interest of the beneficiary of a spendthrift trust should nonetheless be subject to a charge for losses caused by the beneficiary's wrongdoing.³⁷⁷ “The relevant cases are, however, a mixed lot, including those dealing with pension plans subject to ERISA.”³⁷⁸ There is also a difference of opinion as to whether a trustee of a spendthrift trust who makes an advancement of trust property to a beneficiary is entitled to withhold future income to reimburse the trust.³⁷⁹

The public policy rationale for enforcing spendthrift provisions. The rationale for the court's enforcement of a spendthrift trust is that it is the prerogative of the settlor—the owner of the property—to determine what restrictions (if any) will be placed on the use of his property.³⁸⁰ It is a privilege that comes with ownership.³⁸¹ After all, the settlor need not have created the trust in the first place but could have instead consumed the property or given it away outright and free of trust.³⁸² Other policy justifications for enforcing spendthrift clauses include the following: “[t]he public interest in protecting spendthrift individuals from personal pauperism, so that they do not become public burdens”³⁸³ and “the responsibility of creditors to make themselves aware of their debtors' spendthrift trust protections.”³⁸⁴ The Restatement (Third) of Trusts accepts the spendthrift doctrine, except as it may apply to the settlor-beneficiary³⁸⁵ and

³⁷⁵3 Scott & Ascher §15.2.7. Some of this brings to mind the old Rule in Shelley's case, or at least its ghost, particularly when the terms of a trust are that principal is ultimately to be paid to the probate estate of the income beneficiary. *See generally* §8.15.3 of this handbook (Rule in Shelley's Case).

³⁷⁶Restatement (Second) of Trusts §244 cmt. d.

³⁷⁷4 Scott & Ascher §25.2.3 (Beneficiary Who Deals Wrongfully with Trust Property). *See generally* §5.6 of this handbook (duties and liabilities of the beneficiary).

³⁷⁸4 Scott & Ascher §25.2.3 n.7.

³⁷⁹*See generally* 4 Scott & Ascher §25.2.5.1 (Advances to Beneficiary of Spendthrift Trust).

³⁸⁰*Nichols v. Eaton*, 91 U.S. 716 (1875) (pro-spendthrift policy dicta); *Broadway Nat'l Bank v. Adams*, 133 Mass. 170 (1882) (actually upholding a direct restraint on the alienability of an equitable interest). For the public policy argument against enforcement of spendthrift trusts, *see John Chipman Gray, Restraints on the Alienation of Property* 262 (1883). *See also* Restatement (Third) of Trusts, Reporter's Notes on §58.

³⁸¹*Nichols v. Eaton*, 91 U.S. 716 (1875) (pro-spendthrift policy dicta); *Broadway Nat'l Bank v. Adams*, 133 Mass. 170 (1882) (actually upholding a direct restraint on the alienability of an equitable interest).

³⁸²*See generally* 3 Scott & Ascher §15.2.1 (observing that “both those who have advocated and those who have opposed the validity of restraints on alienation have relied on the notion of individualism”).

³⁸³*Sligh v. First Nat'l Bank of Holmes Cnty.*, 704 So. 2d 1020, 1027 (Miss. 1997), *superseded by statute as noted in Duvall v. McGee*, 375 Md. 476 (2003).

³⁸⁴*Sligh v. First Nat'l Bank of Holmes Cnty.*, 704 So. 2d 1020, 1027 (Miss. 1997), *superseded by statute as noted in Duvall v. McGee*, 375 Md. 476 (2003).

³⁸⁵Restatement (Third) of Trusts §58.

except as it may apply to a nonsettlor who has the equivalent of ownership in the trust property.³⁸⁶ Ownership equivalence might take the form of possession of a general inter vivos power of appointment.³⁸⁷

Spendthrift protection as . In some states, by statute, a non-self-settled trust is a quasi-spendthrift trust, absent language in the governing instrument to the contrary.³⁸⁸ *Special creditors of the beneficiary of a spendthrift trust may have access to the equitable interest, either by statute or case law.* The express reference in many spendthrift clauses to creditors over the years has invited assaults on the very institution of the spendthrift trust.³⁹¹ In one dramatic case, the mother of a minor victim of sexual molestation unsuccessfully sought to reach in satisfaction of a default judgment the perpetrator's equitable interest in a non-self-settled spendthrift trust.³⁹² In another, the personal representative of a murder victim unsuccessfully attempted to reach the property of a spendthrift trust established for the benefit of the murderer by his mother in order to satisfy a tort judgment against the murderer.³⁹³ While ordinary contract creditors may have only themselves to blame for failing to exercise due diligence when entering into transactions with beneficiaries of spendthrift trusts, this generally cannot be said for tort creditors³⁹⁴ and other such “involuntary” creditors:

This line of reasoning, however, is plainly insufficient to justify the exemption of a beneficiary's interest from the claims of those who have not voluntarily extended credit. It does not apply, for example, to tort creditors. Nor does it apply to governmental claims for taxes. It does not apply to the beneficiary's children when they claim support, and it may not apply to the claim of a beneficiary's spouse for support or alimony. Moreover, even a contract creditor who has furnished the beneficiary with necessities stands in quite a different position from ordinary contract creditors.³⁹⁵

Some assaults on the clause have been partially or wholly successful, leading to noteworthy divergences across the jurisdictions.³⁹⁶ A few states, such as North Carolina, will not enforce a spendthrift provision.³⁹⁷ On the other hand, Minnesota has a long history of enforcing spendthrift trusts against all comers, including those seeking alimony and child support.³⁹⁸ So does Massachusetts, with one possible divorce-related exception.³⁹⁹ Arkansas, Kansas, and Maine have included no exceptions for certain creditors in their

³⁸⁶Restatement (Third) of Trusts §58 cmt. b(1).

³⁸⁷A “presently exercisable general power of appointment” is a synonym for a “general inter vivos power of appointment.” Restatement (Third) of Trusts §58 cmt. b(1).

³⁸⁸ See generally 3 Scott & Ascher §15.2.1.

³⁹¹See Bogert §222 (Arguments for and Against Spendthrift Trusts).

³⁹²*Scheffel v. Krueger*, 146 N.H. 669, 782 A.2d 410 (2001) (addressing the scope of New Hampshire's spendthrift statute (N.H. Rev. Stat. Ann. §564:23)). See generally Douglas E. Zemel, *Underused Spendthrift Trusts Can be Bulletproof*, 2001 LWUSA 873 (in part discussing *Scheffel v. Krueger*).

³⁹³See *Duvall v. McGee*, 375 Md. 476, 826 A.2d 416 (2003).

³⁹⁴See generally 3 Scott & Ascher §15.5.5 (Tort Claims).

³⁹⁵3 Scott & Ascher §15.5.

³⁹⁶Bogert §222 n.59.

³⁹⁷Bogert §222 n.59. See also Annot., *Invalidity of Spendthrift Provision as Affecting Other Provisions of Trust*, 9 A.L.R.2d 1361 (1950).

³⁹⁸See *In re Moulton's Estate*, 233 Minn. 286, 46 N.W.2d 667 (1951).

³⁹⁹See *Lauricella v. Lauricella*, 409 Mass. 211, 565 N.E.2d 436 (1991) (nonsettlor beneficiary's interest in realty trust subject to equitable division in divorce proceeding notwithstanding spendthrift

versions of the UTC.⁴⁰⁰

Mississippi's highest court has allowed attachment of a beneficiary's interest in a spendthrift trust by his intentional and gross negligence tort creditors, the court noting that "[a] man who is about to be knocked down by an automobile has no opportunity to investigate the credit of the driver of the automobile."⁴⁰¹ The Restatements would seem more or less in accord.⁴⁰² The UTC, however, does not appear to be.

Some states allow spendthrift provisions to protect the income stream only,⁴⁰³ while others allow principal to be protected as well.⁴⁰⁴ Some spendthrift jurisdictions draw a line when it comes to the beneficiary's spouse and children⁴⁰⁵ or to a creditor who has supplied "necessaries,"⁴⁰⁶ which has been held in some cases to include a government agency that has provided institutional care to the beneficiary.⁴⁰⁷ As a general rule, governmental claims for unpaid taxes may be satisfied from the taxpayer's equitable interest in a spendthrift trust.⁴⁰⁸ By statute, the equitable interests of enemy aliens in spendthrift trusts are generally subject to governmental seizure.⁴⁰⁹ "As we have seen, ERISA, which preempts state law as to a great many retirement plans, requires that each plan prohibit the assignment or alienation of benefits but provides that benefits may be reached by a qualified domestic relations order for child support, alimony, and marital property rights."⁴¹⁰

clause). *See generally* §5.3.4 of this handbook (rights of beneficiary's spouse and children to trust property or equitable interest).

⁴⁰⁰Kevin D. Millard, *Rights of a Trust Beneficiary's Creditors under the Uniform Trust Code*, 34 ACTEC L.J. 58, 61 (2008).

⁴⁰¹*See* *Sligh v. First Nat'l Bank of Holmes Cnty.*, 704 So. 2d 1020 (Miss. 1997) (also providing a scholarly discussion of the pros and cons of creating a tort exception to the enforceability of spendthrift clauses). *Sligh* by legislation is no longer the law in Mississippi. *See* Miss. Code Ann. §91-9-503 (2003) (eliminating Mississippi's judicially created tort exception). *See also* Alaska Stat. §34.40.110(b) (amounting to a legislative rejection of the tort exception).

⁴⁰²*See* Restatement (Third) of Trusts §59 cmt. a; Restatement (Second) of Trusts §157 cmt. a.

⁴⁰³2A Scott on Trusts §152.

⁴⁰⁴2A Scott on Trusts §153.

⁴⁰⁵*E.g.*, California, Kentucky, Louisiana, Missouri, New York, Oklahoma, Texas, Washington, and Wisconsin by legislation afford the spouse and dependents, under certain circumstances, access to a beneficiary's equitable interest in a spendthrift trust. *See* 3 Scott & Ascher §15.5.1 (Dependents of the Beneficiary); 2A Scott on Trusts §157.1 n.2. *See generally* Dessin, *Feed a Trust and Starve a Child: The Effectiveness of Trust Protective Techniques Against Claims for Support and Alimony*, 10 Ga. St. U. L. Rev. 691 (1994). *See also* UTC §503(b) (providing that "[e]ven if a trust contains a spendthrift provision, a beneficiary's child, spouse, or former spouse who has a judgment or court order against the beneficiary for support or maintenance, or a judgment creditor who has provided services for the protection of a beneficiary's interest in the trust, may obtain from a court an order attaching present or future distributions to or for the benefit of the beneficiary."). The Restatement (Third) of Trusts is in accord. *See* Restatement (Third) of Trusts §59. *See* *Marriage of Chapman*, 297 Ill. App. 3d 611, 697 N.E.2d 365 (1998) (holding that the principal of a spendthrift trust was available to satisfy a child support judgment against the beneficiary because the beneficiary possessed a limited power to appoint the principal to a class of which his children were members).

⁴⁰⁶*See* 3 Scott & Ascher §15.5.2; 2A Scott on Trusts §§157.1, 157.2. Unlike Restatement (Third) of Trusts §59, and Restatement (Second) of Trusts §157(b) the UTC does not create an exception to the spendthrift restriction for nongovernmental creditors who have furnished necessary services or supplies to the beneficiary. UTC §503 cmt.

⁴⁰⁷*See* 3 Scott & Ascher §15.5.4; 2A Scott on Trusts §§157.1, 157.2.

⁴⁰⁸*See generally* 3 Scott & Ascher §15.5.4.

⁴⁰⁹*See generally* 3 Scott & Ascher §15.5.4.

⁴¹⁰*See* 3 Scott & Ascher §15.5.1 (referring to 29 U.S.C. §1056(d)(3)).

The Restatement (Third) of Trusts provides that the interest of a beneficiary in a valid spendthrift trust can be reached in satisfaction of an enforceable claim against the beneficiary for services or supplies provided for the protection of the beneficiary's interest in the trust,⁴¹¹ e.g., services rendered by an attorney-at-law.⁴¹² So does the UTC.⁴¹³

A spendthrift provision will not prohibit the United States or a state from attaching the beneficial interest for taxes owed by the beneficiary.⁴¹⁵

Assume the trustee of a spendthrift trust is among the beneficiaries of that trust. The trustee-beneficiary commits a breach of trust. Presumably the trust estate may be made whole out of the trustee-beneficiary's equitable interest, notwithstanding the presence of a spendthrift clause, assuming that interest is severable from the other equitable interests. At least one California court has so held.⁴¹⁶

Bankruptcy of beneficiary. Unlike the settlor of a discretionary trust, the settlor of a spendthrift trust directly confronts the creditor by withholding from the trustee the authority to honor assignments and attachments of the equitable interests.⁴¹⁷ What the beneficiary cannot alienate, the creditor cannot attach.⁴¹⁸ If such restraints are valid under state law, they generally will be honored in the bankruptcy context.⁴¹⁹

As a general rule, a beneficiary's equitable property interest in a trust with a spendthrift provision that is enforceable under state law is not reachable by the beneficiary's trustee in bankruptcy,⁴²⁰ unless the trust is self-settled.⁴²¹ In one case, however, a bankruptcy trustee was afforded access to the assets of a spendthrift trust of which the bankrupt was a beneficiary. If the creditors of the beneficiary, notwithstanding the spendthrift clause and over the objections of the trustee, could have been reimbursed from the trust estate

⁴¹¹Restatement (Third) of Trusts §59.

⁴¹²*See generally* 3 Scott & Ascher §15.5.3.

⁴¹³*See* UTC §503 cmt.

⁴¹⁵*See* Restatement (Third) of Trusts §59 cmt. a(1); 2A Scott on Trusts §157.4; Bogert §224 (collecting the case law and relevant Internal Revenue Code provisions authorizing the satisfaction of federal tax claims from interests in spendthrift trusts). *See also* UTC §503(c) (providing that a spendthrift provision is unenforceable against state and federal claims to the extent state or federal law so provides). *See, e.g.,* United States v. Riggs Nat'l Bank, 636 F. Supp. 172 (D.D.C. 1986); LaSalle Nat'l Bank v. United States, 636 F. Supp. 874 (N.D. Ill. 1986).

⁴¹⁶*See* Chatard v. Oveross, 179 Cal. App. 4th 1098 (2009).

⁴¹⁷*See* 2A Scott on Trusts §§151, 152 (Restraint on Alienation of Income), 153 (Restraint on Alienation of Principal, *i.e.*, Remainders); Bogert §222 n.59 (For the Current Status of Spendthrift Trusts in All States).

⁴¹⁸Ritchie et al., Decedent's Estates and Trusts 630 (8th ed. 1993); 3 Scott & Ascher §15.2.3; 2A Scott on Trusts §152.3; UTC §502(a) (providing that a spendthrift provision is valid only if it restrains *both* voluntary and involuntary transfers of the beneficial interest). *But see* Bank of New England v. Strandlund, 402 Mass. 707, 529 N.E.2d 394 (1988) (enforcing a one-sided restraint on involuntary alienation). On the subject of "one-sided restraints," *see generally* Restatement (Third) of Trusts, Reporter's Notes on §58; 3 Scott & Ascher §15.2.3 (Whether It Is Necessary to Restrain Both Voluntary and Involuntary Alienation) (containing at note 5 a catalog of jurisdictions in which one-sided restraints on the alienability of equitable interests, in this case restraints that operate against the creditor but not the beneficiary, are still enforced; and suggesting that while such one-sided restraints would seem contrary to public policy, one-sided restraints that operate only against the beneficiary would seem not to).

⁴¹⁹Bankruptcy Code §541(c)(2). *See generally* 3 Scott & Ascher §15.2.2.

⁴²⁰*See, e.g.,* Kerr v. T.D. Bankworth, No. 05-31801, 2008 WL 1827606 (Bankr. S.D. Tex. Apr. 22, 2008). *See generally* Kevin D. Millard, *Rights of a Trust Beneficiary's Creditors under the Uniform Trust Code*, 34 ACTEC L.J. 58, 75 (2008) ("The UTC should have no effect on the treatment of trusts in bankruptcy").

⁴²¹11 U.S.C. §541(c)(2). *See generally* 3 Scott & Ascher §15.2.2 (Bankruptcy of Beneficiary).

for “necessaries” furnished the beneficiary, then the bankruptcy trustee can divert the reimbursements to the bankruptcy estate:

[the bankrupt beneficiary]... incurred debts for numerous necessities such as doctors, ambulance services, telephone services, utilities and hospitalsWe modify the Court of Appeals decision by holding that the ability of the trustee in bankruptcy to reach a beneficiary's interest in a spendthrift trust is not dependent upon the exercising of the trustee's discretionary power. Section 70(c) of the Bankruptcy Act allows the trustee in bankruptcy, as a hypothetical lien creditor holding a judgment against the debtor on the date of the bankruptcy, to reach the spendthrift trust for debts incurred by ... [the bankrupt beneficiary]... for necessities of life.⁴²²

English law has not been receptive to the spendthrift trust. As noted, English law, in contrast to U.S. law, has never recognized the spendthrift trust.⁴²³ The English scrivener, however, is not without options when it comes to cordoning off the equitable interest. There is always the quasi-forfeiture provision; namely, in the event the beneficiary attempts to assign the equitable interest or becomes insolvent, the beneficiary loses the automatic right to receive income and instead becomes the permissible beneficiary of a discretionary trust.⁴²⁴ Such a provision would be the functional equivalent of a direct restraint on the alienability of the equitable interest, but for the forfeiture of the beneficiary's autonomy. On this side of the Atlantic, a quasi-forfeiture provision in a U.S. trust was honored by none other than the Supreme Court in an 1875 federal bankruptcy case.⁴²⁵

Disclaimers, releases, and powers of appointment. Spendthrift restrictions on voluntary alienation generally do not cover proper disclaimers,⁴²⁶ releases of powers of appointment, and exercises of powers of appointment.⁴²⁷ One court has confirmed the validity of a permissible beneficiary's release of her equitable interest under a discretionary spendthrift trust.⁴²⁸ The UTC negates any presumption that the presence of a spendthrift clause evidences a material purpose, which, under the *Clafin* (material purpose) doctrine, would bar the judicial termination or modification of a one-beneficiary trust.⁴²⁹ The Restatement (Third) of Trusts is in accord.⁴³⁰ There is much case law, however, that is not.⁴³¹ Merger may well extinguish

⁴²²Erickson v. Bank of Cal., 97 Wash. 2d 246, 253–254, 643 P.2d 670, 674 (1982).

⁴²³Brandon v. Robinson, 34 Eng. Rep. 379 (ch. 1811). *See generally* Lewin ¶5-109 (England).

⁴²⁴3 Scott & Ascher §15.1.

⁴²⁵Nichols v. Eaton, 91 U.S. 716 (1875).

⁴²⁶Restatement (Third) of Trusts §58 cmt. c; 3 Scott & Ascher §15.2.9.

⁴²⁷3 Scott & Ascher §15.2.9, UTC §502 cmt. (citing Restatement (Third) of Trusts §58 cmt. c (Tentative Draft No. 2, approved 1999)).

⁴²⁸*See* Guerriero v. Comm’r, 433 Mass. 628, 745 N.E.2d 324 (2001) (upholding the right of a beneficiary to release her equitable interest under a discretionary trust which also contained a spendthrift provision).

⁴²⁹UTC §411(c). *See generally* 5 Scott & Ascher §34.1.2 (Spendthrift Trusts); §8.15.7 of this handbook (the *Clafin* doctrine, also known as the material purpose doctrine).

⁴³⁰Restatement (Third) of Trusts §65 cmt. e. *See generally* 5 Scott & Ascher §34.1.2 (Spendthrift Trusts). Likewise, a discretionary provision may or may not evidence a material purpose that would bar termination or modification. Restatement (Third) of Trusts §65 cmt. e.

⁴³¹5 Scott & Ascher §34.1.2 n.1.

any outstanding spendthrift restraints, a topic we cover in §8.7 of this handbook.⁴³²

The presently exercisable general inter vivos power of appointment. Involuntary alienation restraints are generally in abeyance as well in the face of an outstanding presently exercisable general inter vivos power of appointment. By that we mean that a trust spendthrift clause is not only ineffective as against the creditors of the powerholder insofar as the subject property is concerned⁴³³ but also for all intents and purposes, redundant as against the creditors of the other beneficiaries, as long as the power is exercisable but unexercised. The very existence of such a power renders the equitable interests of the other beneficiaries so ephemeral, so expectancy-like, that *their* creditors have few practical options. Certainly they can do nothing that would interfere with the powerholder's functional equivalent of ownership.⁴³⁴

The Uniform Trust Code. The UTC provides that even if a trust contains a spendthrift provision, a beneficiary's child, spouse, or former spouse who has a judgment or court order against the beneficiary for support or maintenance, or a judgment creditor who has provided services for the protection of a beneficiary's interest in the trust, may obtain from a court an order attaching present or future distributions to or for the benefit of the beneficiary.⁴³⁵ The UTC, however, unlike the Restatements,⁴³⁶ does not create an exception for tort claimants.⁴³⁷ The court also may have discretionary authority incident to its general equitable powers to order that the legal fees of the child, spouse, or former spouse be paid from the trust estate.⁴³⁸ “The third category of ... [UTC]... exception creditor is the state or federal government, but only ‘to the extent a statute of this State or federal law so provides.’”⁴³⁹ Under the UTC, a provider of necessities to a beneficiary is not an exception creditor.⁴⁴⁰ The Restatement of Trusts is not in accord in this regard.⁴⁴¹

Section 503 is where the UTC's categories of exception creditor are specified. It is a section that almost every enacting state has modified in some way. For more on these modifications the reader is referred to Kevin D. Millard.⁴⁴²

Alaska is an unusually strong spendthrift jurisdiction. The protection which an Alaska spendthrift clause provides against creditors is “extremely powerful because all creditors, of whatsoever nature and kind, are barred from attaching the trust assets before payment or delivery of the assets to the

⁴³²See Restatement (Third) of Trusts §69 cmt. d; *but see* 5 Scott & Ascher §34.7 (Conveyance by Beneficiary to Trustee). *See also* 5 Scott & Ascher §34.5.1 (Acquisition of Legal Title by Beneficiary of Spendthrift Trust).

⁴³³See generally 3 Scott & Ascher §15.2.8.

⁴³⁴See generally §8.11 of this handbook (duties of the trustee of a revocable inter vivos trust).

⁴³⁵UTC §§503(b), 503(c).

⁴³⁶Restatement (Third) of Trusts §59 cmt. a; Restatement (Second) of Trusts §157 cmt. a.

⁴³⁷UTC §503 cmt. *See, however,* Alan Newman, *The Rights of Creditors of Beneficiaries under the Uniform Trust Code: An Examination of the Compromise*, 69 Tenn. L. Rev. 771, 825–830 (2002) (suggesting that at least when the beneficiary's tortious conduct is intentional, reckless, or grossly negligent, those injured by such conduct ought to be able to reach at least a part of trust assets available for distribution to or for the benefit of the beneficiary without regard to whether the trust instrument includes a spendthrift provision).

⁴³⁸UTC §1004.

⁴³⁹Kevin D. Millard, *Rights of a Trust Beneficiary's Creditors under the Uniform Trust Code*, 34 ACTEC L.J. 58, 60 (2008) (referring to UTC §503(b)(3)).

⁴⁴⁰Kevin D. Millard, *Rights of a Trust Beneficiary's Creditors under the Uniform Trust Code*, 34 ACTEC L.J. 58, 61 (2008).

⁴⁴¹Restatement (Second) of Trusts §157(b); Restatement (Third) of Trusts §59(b).

⁴⁴²*Rights of a Trust Beneficiary's Creditors under the Uniform Trust Code*, 34 ACTEC L.J. 58, 61–62 (2008).

beneficiary.”⁴⁴³ In Alaska, there are no exceptions for spouses seeking support, ex-spouses seeking alimony, providers of necessities, tort creditors, or children seeking support.⁴⁴⁴

Terminating the small spendthrift trust. In California, a spendthrift trust whose principal does not exceed \$20,000 in value may be terminated by the trustee without court involvement.⁴⁴⁵

The spendthrift QTIP trust. A spendthrift clause will not jeopardize a trust's eligibility for QTIP status.⁴⁴⁶ A spendthrift clause coupled with a forfeiture provision will.⁴⁴⁷

Nonenforceability of a contract to assign a spendthrifted equitable interest. If a beneficiary of a non-self-settled spendthrift trust enters into a contract to assign for consideration the equitable interest, or purports to make a present assignment of it for value, the contract is generally not *specifically enforceable*.⁴⁴⁸ That does not mean, however, that the beneficiary could not be held personally liable to the other party, at least for restitution of amounts paid, and possibly also any damages occasioned by the contract breach. “Thus, the other party ... [might be able to]... obtain a personal judgment against the beneficiary and obtain satisfaction out of any property available to creditors but ... [could]... reach the beneficiary's interest in the trust only if and to the extent other creditors ... [could]...”⁴⁴⁹ We leave to the contracts treatises, however, the question of whether impossibility of performance should be a defense that is available to the beneficiary in these situations.

Why a spendthrift provision in a trust is not an impermissible alienation restraint. At this point, a comment on *alienation restraints* is in order. It is a cardinal principle of law that a restraint upon alienation of a legal fee simple, or of an absolute interest in personal property, is invalid.⁴⁵⁰ Courts that enforce spendthrift provisions circumvent this rule by drawing a distinction between legal interests and equitable interests.⁴⁵¹ Because the spendthrift restraint goes to the equitable interest and not to the trustee's legal interest, the power of alienation under a spendthrift provision continues unimpaired.⁴⁵² And even when alienation of the legal interest is ostensibly restrained in perpetuity in the charitable context, such as when a specific parcel of real estate has been entrusted in perpetuity for a charitable purpose, the trustee may still

⁴⁴³Stephen E. Greer, Esq., *Creditor Protection Vastly Improved with Enactment of 2003 Alaska Trust Bill*, available at <https://www.alaskabar.org/library/estate7-03_aktrustbill.pdf> (last visited Aug. 18, 2017).

⁴⁴⁴Alaska Stat. §34.40.110(h).

⁴⁴⁵Cal. Prob. Code §15408(c). *See generally* §3.5.3.2(k) of this handbook (the power to terminate the trust).

⁴⁴⁶Treas. Reg. §§20.2056(b)-5(f)(7) and 25.2523(e)-1(f)(7). *See generally* §8.9.1.3 of this handbook (the marital deduction) (discussing in part the QTIP trust).

⁴⁴⁷*See, e.g., Miller v. United States*, 267 F. Supp. 326 (Fla. 1967).

⁴⁴⁸*See generally* 3 Scott & Ascher §15.2.6. (Contract to Assign Beneficiary's Interest).

⁴⁴⁹3 Scott & Ascher §15.2.6.

⁴⁵⁰*See generally* §8.15.40 of this handbook (the trust exception to the rule against direct restraints on one's ability to alienate one's property); 2A Scott on Trusts §152. *See also* 92 C.J.S. Vendor & Purchaser §311a.(2)(a) (noting that a covenant that absolutely prohibits a purchaser from selling or assigning his interest has been held to be an unlawful restriction on the power of alienation).

⁴⁵¹*See Broadway Nat'l Bank v. Adams*, 133 Mass. 170 (1882).

⁴⁵²*See Broadway Nat'l Bank v. Adams*, 133 Mass. 170 (1882). *See also* 2A Scott on Trusts §152 n.8 (speculating on the politics behind the *Adams* case). New York, however, does not draw a distinction in the trust context between the legal interest and the equitable interest when it comes to the suspension of the power of alienation. There is a suspension of the alienability of the underlying trust property if the alienability of either interest is suspended. N.Y. Est. Powers & Trusts Law §9-1.1(a). Presumably, the New York statute that deems a trust to be a spendthrift trust, absent language in the governing instrument to the contrary, takes care of the common law alienability problem for trusts that do not violate the applicable Rule Against Perpetuities. N.Y. Est. Powers & Trusts Law §7-1.5 (1998).

irrevocably alienate the legal title to a BFP in contravention of the terms of the trust.⁴⁵³ Thus, a provision in a “nonqualified” personal residence trust that limits the trustee's right to alienate the underlying property, *i.e.*, the residence, may be unenforceable under local law.⁴⁵⁴ Note also that if one is designated the sole beneficiary and the sole trustee of a spendthrift trust, there is a merger⁴⁵⁵ such that one holds legal title to the underlying property not only free of trust but also free of any enforceable spendthrift restrictions.⁴⁵⁶ Recall that a proper trust spendthrift provision restrains alienation of the equitable interest only. In the case of merger, there is no equitable interest because there is no trust; there is only a legal interest that is pretending to be a trust. And a direct restraint on the alienation of a legal interest, say, a legal life estate, is generally invalid.⁴⁵⁷

⁴⁵³See generally §8.15.63 of this handbook (doctrine of bona fide purchase).

⁴⁵⁴See Treas. Reg. §25.2702-5(b)(1) (providing that a trust shall not meet the requirements of a “nonqualified” personal residence trust if, during the original duration of the term interest, the residence may be sold or otherwise transferred by the trustee or may be used for a purpose other than as a personal residence of the term holder). *But see* Blattmachr & Slade, 836 T.M., Partial Interests—GRATs, GRUTs, QPRTs A-24 n.153 (1996) (suggesting that local law may make it impossible to comply with the anti-alienation requirements of Treas. Reg. §25.2702-5(b)(1)). See generally §9.15 of this handbook (the qualified personal residence or QPRT).

⁴⁵⁵See generally §8.15.36 of this handbook (merger).

⁴⁵⁶3 Scott & Ascher §15.2.

⁴⁵⁷3 Scott & Ascher §15.2.1. See generally §8.27 of this handbook (the difference between a legal life estate and an equitable life estate incident to a trust).