

## Memorandum 85-33

Subject: Study L-640 - Trusts (Spendthrift Trusts)

This memorandum considers policy questions involved in preparation of the part of the comprehensive trust statute dealing with spendthrift trusts. A background study on this subject has been prepared by Professor Russell Niles, a Commission consultant. A copy is attached to this memorandum; you should read this study prefatory to considering the questions in this memorandum, since the memorandum does not repeat most of the information in the background study.

Existing Statutory Scheme

There are three important statutes relating to spendthrift trusts in California. Civil Code Section 867 permits the trustor to impose a disabling restraint on the voluntary alienation of the interest of the income beneficiary:

867. The beneficiary of a trust for the receipt of the rents and profits of real property, or for the payment of an annuity out of such rents and profits, may be restrained from disposing of his interest in such trust, during his life or for a term of years, by the instrument creating the trust.

Civil Code Section 859, however, permits creditors to reach the "surplus" income:

859. Where a trust is created to receive the rents and profits of real or personal property, and no valid direction for accumulation is given, the surplus of such rents and profits, beyond the sum that may be necessary for the education and support of the person for whose benefit the trust is created, may be applied to the satisfaction of a money judgment against the person as provided in Section 709.010 of the Code of Civil Procedure [the successor of supplementary proceedings as applied to trusts].

The third statute is Code of Civil Procedure Section 709.010 in the Enforcement of Judgments Law. This section permits the judgment creditor to reach periodic payments from a trust in generally the same amount that would be available on a wage garnishment by supplementary proceedings. (The text of Section 709.010 is set out in the Background Study, at 35-37 n.4.)

The staff believes that the substance of these provisions should be retained in the comprehensive trust statute. Hence, the trustor would be able to restrain the alienation of the beneficiary's right to income subject to the "surplus" rule of Civil Code Section 859, and the periodic payment rules of Code of Civil Procedure Section 709.010. However, continuing the substance of existing law does not deal adequately with all questions. Accordingly, some further issues need to be considered.

#### Distinctions Between Spendthrift, Support, and Discretionary Trusts

Professor Niles suggests, and the staff concurs, that it would be useful to define spendthrift, support, and discretionary trusts. (See Background Study, at 23.) The staff proposes to define "discretionary trust" substantially as follows:

A "discretionary trust" is a trust that gives the trustee [uncontrolled] discretion whether to make payments or distribution of income or principal to the beneficiary or to determine the amount of any such payments. If the trustee has discretion only as to the time of payment, but not whether the beneficiary will ultimately receive the payment or distribution, the trust is not a discretionary trust.

The word "uncontrolled" is drawn from Section 155 of the Restatement (Second) of Trusts. If it is included in this definition, it will be subject to Section 741 (in the draft statute attached to Memorandum 85-32) which makes clear that a trustee with "uncontrolled" discretion may not act in bad faith or in disregard of the purposes of the trust. Inclusion of the word "uncontrolled" is useful to distinguish the discretion of a trustee to act pursuant to a standard, such as that involved in a support trust.

"Support trust" could be defined as follows:

A "support trust" is a trust which provides that the trustee shall make payments or distributions of income or principal to the beneficiary in an amount that is necessary for the education or support of the beneficiary. If the trust gives the trustee discretion to determine the amount or timing of payments or distributions for support or education, the trust is a support trust and is not a discretionary trust.

This definition attempts to distinguish between a "pure" discretionary trust and a trust that may provide discretion, but is in fact intended to provide for the support and education of the beneficiary. The significance of this distinction is that a creditor may reach part of payments out of a support trust based on the wage garnishment standard provided

in Code of Civil Procedure Section 709.010. Where the trustee does not have "uncontrolled" discretion, but discretion subject to a standard provided in the trust, then the court would be able to compel payment out of periodic payments pursuant to Section 709.010. Section 709.010 makes clear that its provisions do not affect or limit the trustee's discretion or require its exercise in any particular manner. See Section 709.010(e). This provision does not, however, affect the power of the court to order a trustee to exercise discretion when required to do so under some other law.

Finally, "spendthrift trust" might be defined as follows:

A "spendthrift trust" is a trust in which the trustor imposes a disabling restraint on voluntary or involuntary alienation of the beneficiary's interest in income or principal.

The definition of a spendthrift trust in relation to income is somewhat misleading. As already mentioned, Civil Code Section 859 permits creditors to reach the surplus income over the amount needed for the support and education of the beneficiary. Under existing law there are no absolute spendthrift trusts such as are known in some other jurisdictions. Section 859 converts them into statutory support trusts, and the court in supplementary proceedings (see now Code Civ. Proc. § 709.010(b), (f)) will determine the amount necessary for support based on a "station in life" test. The consequence of this definition of spendthrift trust would be to recognize the validity of such trusts, subject to the rule making the surplus available to involuntary alienation.

#### Restraint on Alienation of Principal and Remainder

California law is unclear as to whether the trustor may validly restrain alienation of principal. (See Background Study, at 19.) The wording of Civil Code Sections 859 and 867 applies to rents and profits from the trust corpus. Except to the extent that an annuity as mentioned in Section 867 might involve the distribution of principal, the old statutes ignore distributions of principal. The new provision in Code of Civil Procedure Section 709.010, however, applies to periodic trust payments without regard to source. But again, there is a gap, since non-periodic payments out of principal and the distribution to a remainderman are not covered.

Professor Niles discusses the tension between the interest of the trustor, frequently the "dead hand", and the countervailing policy

against restraints on alienation. (See Background Study, at 19-22.) Professor Niles recommends that the entire area of restraints on alienation be studied. This is a project that must await the conclusion of the Probate Code study. Pending any comprehensive review of restraints on alienation, the staff suggests that the statute should provide that the trustor can impose a disabling restraint on voluntary alienation of an interest in principal.

The Restatement (Second) of Trusts in Section 153 permits the restraint of alienation of principal, except in the case of self-settled trusts and certain favored claimants. The Restatement also provides two other exceptions which the staff recommends for adoption in California: the restraint is not valid if the beneficiary is entitled to have the principal conveyed immediately or if the principal is not to be conveyed to the beneficiary during the beneficiary's lifetime.

There is another possibility that the Commission should consider. One problem with allowing creditors to reach future interests, such as the right to principal in the future, is that enforcement may cause a great sacrifice of the debtor's interest. Because of this, rules have been developed that prevent creditors from reaching such interests at all. However, a less drastic step is recognized in the Enforcement of Judgments Law. Code of Civil Procedure Section 709.020 permits the court to impose a lien on a conditional or contingent interest in order to protect the creditor's priority and give some remedy which may prove useful if the right vests in enjoyment. The staff suggests that this power to impose a lien should be extended to cover the interest of a beneficiary in principal under a spendthrift trust. Creditors would be protected in an orderly and nonintrusive manner while at the same time remaindermen and other principal beneficiaries would not be subjected to a sacrifice sale of an interest.

#### Restraint on Voluntary Alienation of Trust Income

As already noted, Civil Code Section 867 permits an absolute restraint on alienation of the beneficiary's interest in income. Should this principle be modified? Professor Niles suggests several alternative schemes. (See Background Study, at 15-18.) It appears that there may be tax advantages in permitting the beneficiary to assign some of the income to family members. Logically it might be thought that the ability to voluntarily assign should be coextensive with the right of a

creditor to reach the interest, but this would involve a high degree of speculation if the law relating to involuntary alienation remains unchanged. Another scheme is to set a certain dollar level of income over which the beneficiary is free to make assignments. It appears that Professor Niles prefers this last alternative. (See Background Study, at 18.)  
Does the Commission wish to limit the power of the trustor to impose a total restraint on involuntary alienation of trust income?

#### Invalidity of Spendthrift Protection in Favor of Trustor

A spendthrift trust statute should codify the case-law rule that a trustor may not create a spendthrift trust for himself or herself. Such a provision might read as follows:

\_\_\_\_\_. Except as otherwise provided in Section 704.115 of the Code of Civil Procedure, if a trustor attempts to create a trust for his or her own benefit with a provision restraining the voluntary or involuntary transfer of his or her interest, whether the trust is a spendthrift, support, or discretionary trust, the restraint is invalid against transferees or creditors. The invalidity of the restraint does not affect the validity of the trust.

This provision would codify the rule applicable under Nelson v. California Trust Co., 33 Cal.2d 501, 202 P.2d 1021 (1949). The introductory clause recognizes the exemption for certain self-settled retirement plans in the Enforcement of Judgments Law.

The Restatement (Second) of Trusts has a more refined approach. Section 156 makes spendthrift clauses invalid, but permits support and discretionary trusts to have a limiting effect by permitting the transferee or creditor to reach the maximum amount the trustee could pay to the trustor-beneficiary. In the case of a support trust, this rule would limit the amount available to creditors or transferees to the amount payable pursuant to a standard, if one is provided. In many, if not most cases, the Restatement rule and the staff draft above would probably yield the same amount.

#### Pension Trusts

Professor Niles discusses the broad outlines of the law relating to pension trusts with spendthrift features. (See Background Study, at 30-32.) He recommends that this area be the subject of a separate study, and the staff concurs. For now, as noted above, the staff would continue the existing exemption for pensions in the Enforcement of Judgments Law

and recognize it as an exception to the general rule against self-settled spendthrift trusts.

#### Claims of Public Institutions

Professor Niles also suggests that a separate study be made of the right of a public entity or institution to reimbursement for assistance paid or care furnished. The staff agrees that such a study would be useful, but we also think that some sort of provision will need to be included in the law before the study is completed. The recently enacted provision for reaching a percentage of periodic payments from a trust recognizes that the wage garnishment standard does not limit the right of the state or other public entity to recover for support provided to a trust beneficiary or to recover for payments made for the support of a trust beneficiary. Code Civ. Proc. § 709.010(c). The comment cites Estate of Lackmann, 156 Cal. App.2d 674, 320 P.2d 186 (1958), which is briefly discussed by Professor Niles in the Background Study on pages 25-26. Perhaps the best that can be done in the absence of a study on this subject is to preserve Estate of Lackmann for these types of trusts as was done in Code of Civil Procedure Section 709.010.

Another possibility would be to adopt the approach of Wisconsin law. See Wis. Stat. Ann. § 701.06(5)(a)-(c), (5m), set out in the Background Study, at 51. This statute does not allow the public entity to get reimbursement from a discretionary trust if the trustee has not exercised its discretion to make payments, unless the beneficiary is a settlor or a spouse or child of the settlor, in which case the trustee's discretion is ignored. The staff is not sure whether subdivision (5m) of the Wisconsin statute is desirable, however. This provision could not be adopted without some further study since it exempts from the claims of the public entity certain trusts for disabled persons if the trust does not result in ineligibility for public assistance under other Wisconsin law. What does the Commission wish to do?

Respectfully submitted,

Stan G. Ulrich  
Staff Counsel

MEMORANDUM

To: California Law Revision Commission  
From: Russell D. Niles  
Re: Spendthrift and Related Trusts  
Date: November 6, 1984

I. Introduction

In this paper it is assumed that protective trusts are needed in contemporary America<sup>1</sup> and that the bar will insist on retaining the spendthrift trust in some form.<sup>2</sup> No direct attack on the spendthrift trust is justified if certain excesses can be removed.<sup>3</sup>

This paper will comment first on the recent amendments to the Code of Civil Procedure to extend the remedy of garnishment to judgment creditors of beneficiaries of spendthrift and support trusts,<sup>4</sup> with the limitations and protections provided in the Wage Garnishment Law.<sup>5</sup> As pointed out in the Comment to the Commissions's Recommendation Relating to Garnishment of Amounts Payable to Trust Beneficiaries,<sup>6</sup> the amendments to C.C.P. § 709.010 constitute only a limited change in existing law because the added remedy will apply only "to all or a portion of the amount that otherwise would be paid periodically to the judgment debtor from the trust." The principal consequence of the bill as enacted is to permit a judgment creditor to apply for a court order to reach funds in the hands of a trustee of a spendthrift trust without meeting the

requirement of Civil Code § 859 that trust income can be reached only if it is in excess of the amount needed by the beneficiary for his or her education and support. A further consequence will be that for the first time there will be an explicit recognition that some classes of claims are favored over others.<sup>7</sup> There are also new protections afforded to judgment debtors, not only by the wage minimum exemptions in state and federal law but by the availability of hardship defenses which may be asserted by the debtor.<sup>8</sup>

The new trust garnishment statute has an obvious appeal. By incorporating by reference the carefully worked out Wage Garnishment Law it reaches indirectly some of the objectives which the Restatement attempted to reach directly by recognizing that public policy demands that certain classes of claims should prevail against the beneficiary of a spendthrift trust even if this result is contrary to the intent of the donor.<sup>9</sup> The new statute by permitting a commercial judgment creditor to reach about 25% of the amount payable and by allowing claimants for spousal and child support to reach 50% or more, may come close to a generally accepted norm.<sup>10</sup> The statute, indeed, may be more precise than the Restatement approach with respect to periodic trust payments.<sup>11</sup>

This paper will address these questions: How will the trust garnishment statute change the pre-existing California law relating to spendthrift trusts? Are there other areas

in the law of protective trusts that should be studied? Are there statutes in other states that suggest other changes that should be considered in California?

## II. Spendthrift Restraints: Creditor's Rights in Trust Income

Since 1872 the California courts have been bound by Civil Code § 859 as to restraints on the involuntary alienation of income in a spendthrift trust and by § 867 as to restraints on voluntary alienation.<sup>12</sup>

The recommendation of the Commission to retain C.C. § 859 (except as modified by the trust garnishment statute) is ameliorated by the improvements made in the traditional creditor's bill by C.C.P. § 709.010(b).<sup>13</sup> The current procedure to enforce judgments supplementary to execution reduces the burden of proving what income is surplus by a more sensible approach to the "station-in-life" test.<sup>14</sup>

Other states have recognized a need for an economical, simplified method by which a creditor could reach a percentage of the periodic income of a spendthrift trust beneficiary without a consideration of the special equities involved in a creditor's bill. The pioneer garnishment statute was adopted in New York and allowed any judgment creditor to levy on shielded trust income before payment to the beneficiary in the amount of 10% over \$12 a week.<sup>15</sup> Although New York had a statute requiring a creditor ordinarily to prove that spendthrift trust income was surplus, such proof was not needed for the small percentage

available by garnishment.<sup>16</sup> In some other states by statute, garnishment of 10% over a stated minimum is allowed, without the need to prove that the claim is a favored claim, or that the income is more than the amount needed for the beneficiary's basic needs.<sup>17</sup> In one state, New Jersey, the amount that may be levied on before payment is up to 30% in larger trusts.<sup>18</sup>

It should be observed that the Restatement of Trusts attempted to ameliorate and modernize the common law of protective trusts, first by recognizing and defining spendthrift,<sup>19</sup> support,<sup>20</sup> and discretionary trusts;<sup>21</sup> and second by recognizing that certain classes of claimants--especially spouses and children with claims for support, and suppliers of necessaries--could reach support and spendthrift trust income when commercial creditors could not.<sup>22</sup> The Restatement thus recognized the right of a donor to dispose of his property as he wished, within certain time limits, but subject to the strong public policy in imposing certain obligations on the beneficiary notwithstanding the intention of the donor.

The Restatement approach has worked out reasonably well but not perfectly.<sup>23</sup> The modern credit system seems able to warn merchants and other suppliers about the risk in dealing with protected beneficiaries, but spouses and children, public institutions, and some suppliers of necessaries have claims not based on voluntary contracts.<sup>24</sup>

There have been only a few landmark cases in California in this century. It is interesting to determine how typical cases would have been decided under the trust garnishment statute and the recent revision of the subsection relating to proceedings supplemental to execution. It may then become apparent whether or not further legislative reforms are desirable.

In *San Diego Trust & Savings Bank v. Heustis*<sup>25</sup> the testatrix created a testamentary trust to pay her son \$150 a month for ten years, and to pay over the principal to the son if alive at the end of that period, and if not, then over to others. The son's interest was expressly made inalienable and free from the claims of creditors. The son moved to Texas and thereafter the son's estranged wife obtained a judgment against him for support and maintenance in the amount of \$100 a month. When \$2400 had accumulated in the income account of the trust the wife sought to levy execution on the trustee. Cases from other jurisdictions were cited (especially Pennsylvania) to establish that it was against public policy to deny a wife's claim for support because of a spendthrift clause. This was the view later taken by the Restatement of Trusts.<sup>26</sup> In 1932, however, the Court of Appeal held that the testatrix was under no obligation, legal or moral, to support the wife of her son, but had the right to dispose of her property as she saw fit. Once the wife had reduced her claim to judgment, the court stated, she was like any other judgment creditor. Nor could the wife levy execution against her husband's remainder because the remainder was subject to a condition of survival.<sup>27</sup>

Under the trust garnishment law the wife could have reached 50% of the funds "otherwise payable periodically to the judgment debtor from the trust"<sup>28</sup> regardless of the

intent of the testatrix. Although she could not even under the new Enforcement of Judgments Law have the remainder interest of her husband sold immediately, she could now obtain a lien on his interest.<sup>29</sup>

In 1939 the Supreme Court decided *Caufield v. Security First National Bank*.<sup>30</sup> The case involved a spendthrift discretionary trust for the support of one of the testator's children with a principal of \$900,000. The child, Charles, was to receive income in the modest amount of \$1200 a year, not subject to assignment or legal process. The balance of the income was to be paid or applied for his support, maintenance and education as the trustee in its absolute discretion should determine.

Charles' wife, Pearl, recovered a decree for divorce by which she was awarded \$800 a month for support. The court held that the discretion of the trustee did not include a power to determine how much income was needed to maintain the debtor in his style of life. After the trial court had decided that the amount needed was \$30,000 a year, any excess over that amount paid to the beneficiary became the personal liability of the trustee.<sup>31</sup>

Under the trust garnishment statute, Pearl could have reached 50% of the income of \$1200 a year which was protected by the spendthrift clause but no more unless the trustee, in the exercise of its discretion had determined to

pay the income and not withhold it. The trust garnishment statute would not help the claimant if no discretion had been exercised or payments made. Apparently the only present remedy, if any, in the case of a discretionary trust would be in supplementary proceedings under C.C.P. § 709.010(b) and (f) subject to the limitations of C.C. § 859.

In 1967 the Court of Appeal again had to consider a spendthrift trust where the beneficiary was beyond the jurisdiction. In re Estate of Johnston,<sup>32</sup> the testatrix had devised most of the residue of her estate to a trustee of a spendthrift trust to pay the income to her son for life, with remainder to his issue living at his death. Two years after the death of the testatrix, the son's wife obtained a divorce decree, including an order to the beneficiary to make payments for the support of the two children of the marriage. The divorced wife then attempted to levy execution on the accumulated trust income without proving what part of the income was not needed by the beneficiary for his support. The court pointed out that California had not recognized the favored claims approved by the Restatement of Trusts and therefore held that C.C. § 859 had to be followed.

Under the trust garnishment statute, at least 50% of accrued income could be reached by execution prior to payment, regardless of § 859 or of the intention of the testatrix.<sup>32</sup> Under the Restatement view the amount that may

be reached is a matter for the exercise of discretion by the court.<sup>33</sup>

The most recent case in the series is *In re Marriage of Parscal*.<sup>34</sup> It illustrates a trend away from the early view that the intent of the donor is dominant and that the public policy in favor of the claimant of spousal or child support is subservient. The claimed spendthrift trust was not of the usual type: an attempt was made to convert what was essentially a self-settled trust into a spendthrift trust created by a third party. Painting contractors under a collective bargaining agreement contributed \$4.50 for each hour worked by an employee to a trust fund for vacation, health, welfare and pension benefits. Each employee was to have benefit credits according to the amount contributed by the employer to the employee's account. These benefits were specifically subject to spendthrift restraints on voluntary and involuntary alienation. One beneficiary's wife obtained a divorce and a decree ordering the beneficiary to pay for support of the three children of the marriage. The Court, after discussing the *Heustis*, *Caufield* and *Johnston* cases and the Restatement, concluded that the correct rule is that "a spendthrift trust, at least as here, does not bar execution upon a judgment against its beneficiary for child support."

The court reasoned:

"We find but one judicial authority in California dealing with an issue similar to that before us. It is Estate of Johnston, \* \* \* where we reluctantly (in 1967) concluded that a child's claim for support would not prevail over an otherwise valid spendthrift trust. We there stated that we found 'persuasive support for the contrary position in other jurisdictions, which have held that spendthrift trust provisions barring support claims of the beneficiary's child against the beneficiary's interest in the trust are against public policy. \* \* \* This position has also been adopted by the Restatement \* \* \* and various texts and law reviews. \* \* \* In taking this position, these authorities note that the privilege of disposing of property is not absolute but is hedged with various restrictions where there are policy considerations warranting the limitations. \* \* \* These authorities then proceed to point to the public policy consideration that whereas a general creditor has achieved his status merely by voluntarily extending credit to the beneficiary, a child is owed a duty of support by his parent which is established by statute and is based upon solid grounds of public policy."

"But in Estate of Johnston we felt compelled--by the force of Civil Code section 859, seemingly stating that a child support claim against the beneficiary of an otherwise valid spendthrift trust was limited to the surplus of its income not needed by its beneficiary--to hold contrary to the general rule."

It is uncertain how the trust garnishment statute would have applied to the Parscal case. It is not clear what amounts were payable or when. It is not clear whether or not the trust was considered to be self-settled. The case will be reconsidered later when pension trusts with spendthrift provisions, including Keough trusts and trusts covered by ERISA, are discussed.

The four cases reviewed suggest that the trust garnishment statute will afford an important but limited reform. In an ordinary case where a support order has been obtained, a spouse or child may have a simple, inexpensive remedy without the burden of proving whether or not the sums payable are surplus. Garnishment will be especially useful to reach a percentage of periodic payments. These payments need not be income (as in New York); the payments could be principal (as in a sprinkling trust) or they could be part income and part principal (as in an annuity trust). In many situations, however, the garnishment statute will not be of value. In discretionary trusts the remedy will not be available until and unless the trustee's discretion has been exercised in favor of the beneficiary. Nor will garnishment be the proper remedy in many trust problems involving trust assets other than funds available for periodic payments.

The Parscal case was considered by the court to be in substance a proceeding supplementary to execution.<sup>35</sup> Such a proceeding in its current form is a flexible remedy with

very broad discretion in the court. Applied with common sense, it fairly balances the interests of the creditor and the debtor and minimizes the station-in-life test.<sup>36</sup> In cases involving trust assets other than funds available for periodic payments or trusts with discretionary powers to invade principal, or trusts (such as pension trusts) where payments have not started,<sup>37</sup> this modernized creditor's bill will still be needed. As Erwin Griswold has suggested, supplementary procedure is the most satisfactory type of statutory provision which has yet been developed. After citing a number of New York cases Dean Griswold stated: "It seems not too much to state that the ultimate solution of the spendthrift trust problem may be found in the development of such statutes."<sup>38</sup>

The garnishment statute is of value in uncomplicated trusts with ascertained, periodic payments, and is especially important in cases where the debtor has fled the jurisdiction. The statute shifts the burden of proof of hardship to the debtor.<sup>39</sup> And the statute makes a start toward the explicit recognition that some claims deserve to be favored.<sup>40</sup>

In summary it may be stated that so far as creditor's rights in support and spendthrift trusts are concerned, the various subsections of C.C.P. § 709.010 give modern and flexible relief notwithstanding C.C. § 859. There remain problems about creditor's rights in discretionary trusts,

and pension trusts, and the rights of public institutions to recover for support of trust beneficiaries. It is first necessary, however, to consider the California law relating to the disability of the beneficiary of a spendthrift trust to make a voluntary alienation of trust benefits.

### III. Restraints on Voluntary Alienation

The foregoing discussion has related primarily to the liability of an income beneficiary to the claims of various types of judgment creditors--in other words to liability to involuntary alienation. Generally in America (but not always)<sup>41</sup> the disabling restraint of a spendthrift trust applies equally to voluntary and involuntary alienation.<sup>42</sup> A spendthrift beneficiary is protected against the debts that he improvidently incurred but also is protected from anticipating future income by assigning it or by encumbering it.

In California, as mentioned before, the restraint that may be imposed on involuntary alienation is limited<sup>43</sup> but the restraint that may be imposed on voluntary alienation is absolute.<sup>44</sup> The two types of restraint could be made uniform by permitting the beneficiary to alienate income in excess of his or her needs for education or support but such an interest would probably be too uncertain in amount to be marketable. Should the Commission consider some other limitation on the right of a donor to impose a disabling restraint on the voluntary alienation of trust income?

There are reasons why a beneficiary should be permitted to assign part of his income interest, especially in a large trust. In New York, a beneficiary of a spendthrift trust may assign income in excess of \$10,000 a year, but only to

relatives and only by gift.<sup>45</sup> The basic reason for the statute is to minimize taxation, usually by permitting a beneficiary to share with a descendant or a sibling. One state that has adopted the Griswold model statute<sup>46</sup> permits voluntary alienation of trust income to anybody in excess of \$10,000 year.<sup>47</sup>

The general policy of the law is not to favor restraints on alienation--especially disabling restraints--which do not serve a reasonable purpose.<sup>48</sup> Obviously a protective trust should not interfere with a beneficiary's freedom if it is not necessary.

If a beneficiary could assign all rights in the income of a trust over, say, \$10,000 a year, the beneficiary could often effect tax savings within a family. The beneficiary could in addition consent to the modification or partial termination of large trusts that no longer serve family needs.<sup>49</sup>

There are some situations where the absolute restraint on alienation affects creditors unfairly. The federal bankruptcy law, by a local conformity provision, passes to the bankrupt estate the interest of a beneficiary of a trust to the extent that the beneficiary could have alienated the interest under state law.<sup>50</sup> If there is no limit on the amount of trust income that can be made inalienable, then a beneficiary of a large spendthrift trust

could retain his or her interest in the trust at the expense of the creditors whom the trustee in bankruptcy represents. While individual judgment creditors may have a remedy, there are advantages in permitting a trustee in bankruptcy to acquire the assignable income interest of a bankrupt beneficiary of a spendthrift trust for the protection of all creditors equitably. California law should be fair to the California trust beneficiary but also to his or her creditors who, presumably, are also Californians.<sup>51</sup>

While there are reasons, as suggested, why a statute might be adopted placing a limit on the permitted restraint on alienation of trust income, there are also reasons why the need may not be thought to be compelling.

First, it is now settled that a beneficiary of a spendthrift trust can disclaim within a stated time.<sup>52</sup>

Secondly, a beneficiary presumably may assign an income interest to a spouse or child in recognition of the beneficiary's duty of support.<sup>53</sup>

Thirdly, a beneficiary may appoint a creditor as his attorney-in-fact to collect future income payments,<sup>54</sup> and may contract not to revoke the authority.<sup>55</sup> The beneficiary can be liable in damages for a breach of such a contract<sup>56</sup> and a creditor who has obtained a judgment could, under the garnishment statute, levy execution on trust income before payment.<sup>57</sup>

On net balance, the Commission might decide to modify C.C. § 867 by permitting a restraint on alienation only up to a fixed amount a year.<sup>58</sup> This would limit the protection against alienation and anticipation in the general range of other exemption statutes.<sup>59</sup> The Commission might well decide that there is no compelling reason to change existing law.

IV. Involuntary and Voluntary Restraints  
on Alienation of Trust Principal

In California may a disabling restraint be imposed on the principal of a spendthrift trust? C.C. § 711 provides: "Conditions restraining alienation, when repugnant to the interest created, are void."<sup>60</sup> Under the model statute proposed by Erwin Griswold, the spendthrift restraint could not be extended to trust principal<sup>61</sup> and a fortiori not to a remainder after a spendthrift trust. In the second Restatement of Trusts, however, the principal of a spendthrift trust could be shielded in some cases but not in others.<sup>62</sup>

California has no settled law about disabling restraints on trust principal.<sup>63</sup> The case of Kelly v. Kelly,<sup>64</sup> sometimes cited,<sup>65</sup> is not controlling.<sup>66</sup>

The trust garnishment statute does not apply to trust principal except when payable periodically.<sup>67</sup> It does not apply to voluntary alienation of principal interests at all. Contingent or conditional remainders are protected from sale on execution,<sup>68</sup> but this protection against needless sacrifice applies to all future interests and not only to remainders after spendthrift trusts. Where the income interest of a spendthrift trust beneficiary is created for the life of the beneficiary, then, of course, the trust principal cannot be impaired or destroyed by any action of

the remainderman or of his or her creditors. An income beneficiary who is entitled to payments from principal at successive ages, or as needed to meet a standard of support, cannot be deprived of such interest in income or principal while he or she lives.<sup>69</sup> But assume that A creates a spendthrift trust to pay the income to B, and at B's death to pay over the trust fund to C. May a disabling restraint on alienation be imposed not only on B, but on C while the trust endures?

It has long been the settled law that disabling restraints on alienation of present legal estates are void,<sup>70</sup> and C.C. § 711 reflects that view. All future interests are said to be alienable in California.<sup>71</sup> The disabling restraint on trust income permitted by C.C. § 867 is expressly limited to the life of the beneficiary. Should the creator of a spendthrift trust in California be able to impose a restraint against alienation on a remainderman after a spendthrift trust at least for the duration of the trust?

The answer of the first Restatement of Property was that such a restraint was void.<sup>72</sup> Such a restraint was clearly void with respect to a remainder after a legal life estate and the nature of the precedent estate made no difference. The leading scholars in property law (Griswold,<sup>73</sup> Powell,<sup>74</sup> Schnebly,<sup>75</sup> Simes and Smith<sup>76</sup>) agreed that the disabling restraint of a spendthrift trust could not be extended to a

remainderman entitled to trust principal at the termination of the trust.

A few states have taken another view (including Pennsylvania as indicated in Kelly v. Kelly).<sup>77</sup> The reason why this question must now be considered in California is that the second Restatement of Trusts<sup>78</sup> (contrary to the first Restatement of Trusts<sup>79</sup>) has indicated that a spendthrift clause could restrain some interests in trust principal but not others. Illustration 2 under § 153(1) involved a remainder after a spendthrift trust for the life of an income beneficiary. The remainder, expressly covered by a spendthrift clause, was stated not to be alienable or reachable by creditors.

In Matter of Vought,<sup>81</sup> a recent New York case, the testator created a spendthrift trust to pay the income from the fund to his widow, with a vested remainder in shares to his two sons. One son was improvident and assigned his remainder interest to money lenders for about 15% of its value. He could not get what its value would be according to the mortality tables because of the doubt about his right to assign. The testator had purported to protect not only his widow but also his sons from voluntary (or involuntary) alienation while the income trust endured. The Court of Appeals (with Chief Judge Fuld dissenting) held that the assignment by the remainderman during the continuation of the widow's life was invalid because of the disabling restraint on alienation.

The New York decision has been criticized<sup>82</sup> and, in my judgment, should not be adopted in California. The problems involved in restraints on alienation, however, should be considered broadly, not just in the context of spendthrift trusts. The Restatement of Property, Second, Donative Transfers,<sup>83</sup> offers an opportunity to study all aspects of a subject of increasing current importance.

C.C. § 711 should be re-examined. The way to a more enlightened view of restraints on alienation was shown by Chief Justice Traynor in *Coast Bank v. Minderhout*.<sup>84</sup> His opinion cited contemporary judicial and scholarly opinion in England<sup>85</sup> and America.<sup>86</sup> Unfortunately, this opinion has been overruled by the Supreme Court of California in the "due on sale" cases.<sup>87</sup> I suggest that the whole subject of restraints on alienation be studied by the Commission. As a minimum C.C. § 711 should be repealed or amended in harmony with the recent Restatement of Property.

## V. Support and Discretionary Trusts

Both support and discretionary trusts are recognized in California,<sup>88</sup> but they are often confused with spendthrift trusts and sometimes confused between themselves when discretionary powers have been given to the trustee. The garnishment statute applies expressly to spendthrift and support trusts.<sup>89</sup> The statute does not apply to discretionary trusts. The statute reads: "Where the trust gives the trustee discretion over the payment of either principal or income of a trust, or both, nothing in this section affects or limits that discretion or requires the exercise of that discretion in any particular manner."<sup>90</sup>

The distinctions between the various types of protective trusts must be perceived. It would be worthwhile to include in a California statute a definition of each type, tracking the definitions in the Restatement of Trusts.

The cause of most of the confusion seems to come from the particular grant of discretionary powers to a trustee. A true discretionary trust, as it developed in England<sup>91</sup> and as it is recognized in California,<sup>92</sup> involves a discretion to pay over income (or principal) or to withhold it. It is not an abuse of discretion (if there is no improper motivation) for the trustee to pay nothing.<sup>93</sup> The theory is that a complete cut-off may be necessary to protect, and perhaps to discipline, the beneficiary. A complete cut-off,

presumably, will end in an agreement between the trustee and the creditor to pay the debt over a period of time.<sup>94</sup> In the alternative, the trustee may have the power to shift benefits over to others, usually to dependents of the beneficiary.<sup>95</sup>

In a support trust, there is no disabling restraint<sup>96</sup> (as in a spendthrift trust) or a forfeiture restraint<sup>97</sup> (as in a discretionary trust). The beneficiary is entitled to support, nothing more, nothing less, and creditors have no claim except through the beneficiary's right to support.

Creditors have no right to the income of a discretionary trust if the trustee has exercised the power to withhold income payments. The protection of creditors is that a trustee, with knowledge of a judgment creditor's claim, will be personally liable if the trustee pays over income to the beneficiary without protecting the creditor.<sup>98</sup> This view of the discretionary trust was clearly enunciated in the Canfield case.<sup>99</sup>

The fact that the trustee has been give "sole," "absolute," or "uncontrolled" power is not decisive--as shown in two leading California cases.

In Estate of Miller,<sup>100</sup> the testatrix created a testamentary trust of one-third of her estate for her daughter, Miriam, who suffered from alcoholism. The sole trustee, a lawyer, was directed to pay from the income of

the trust to or on behalf of Miriam "such sums as my trustee, in his sole discretion, shall determine to supplement any other income \* \* \* to provide for her support and maintenance." Income not so paid was to become part of the corpus of the trust, and the remainder at Miriam's death was limited to the grandchildren of the testatrix. If the income was not sufficient to provide for the support and maintenance of Miriam, the trustee had the power to augment income out of principal. Later, when Miriam was rehabilitated and was able to reestablish herself as a practicing physician, the trustee declined to pay anything to Miriam for her support or to re-equip her office to enable her to earn her living as an ophthalmologist. The court held that the primary purpose of the trust was to assure to Miriam the standard of living to which she was accustomed and that the trustee abused his discretion in giving no more than nominal assistance. The court outlined the standards that should be met by the trustee.

In Estate of Lackmann,<sup>101</sup> the testatrix was survived by three children, including George, who had been committed to a state hospital. The testatrix's will (executed before George's commitment) gave her trustee "complete and absolute discretion" in the amount he should expend for George's care and maintenance. The trustee claimed that the Department of Mental Hygiene was a creditor barred by the spendthrift clause and further that the trustee had the discretion to

determine that the funds should not be used for George's care because he was being provided for otherwise. The court held that the trustee had a duty to exercise his discretion in favor of George, and not limited to one-third of the income. The court did not expressly say whether the state had a claim superior to a commercial creditor because it was the state, or because the state hospital was furnishing necessaries.

What is the difference between the trusts in Miller and Lackmann, on the one hand, and, on the other hand, a true discretionary trust such as the one in Caufield? The distinction is believed to be this: a support trust (with or without discretion) is intended to furnish support on an ascertainable standard.<sup>102</sup> A support trust cannot be turned into a discretionary trust by giving the trustee sole, absolute or uncontrolled discretion. The trustee may have discretion as to when and how the support is to be available but only so long as the standard of support is somehow met. Under the Restatement those who supply the necessaries of life may recover through the beneficiary's right to support.<sup>103</sup> Under the garnishment statute, suppliers of necessaries may be able to receive payment through the wage garnishment provisions.<sup>104</sup>

In draft §§ 740 and 741 attached to staff Memorandum 84-21,<sup>105</sup> the duties of trustees with respect to discretionary powers are considered.<sup>106</sup> If the purpose of

the trust is support of the beneficiary, and there is an external standard by which the trustee's conduct can be judged, then even a grant of absolute or uncontrolled discretion should not excuse a failure to meet the standard.<sup>107</sup> Broad discretion is often useful, for example, to indicate that no absolute gift of support was intended when other alternative sources of income are or become available.

If the spendthrift trust, the support trust, and the discretionary trusts were defined in a California Code, and the discretionary powers of the trustees of the various trusts were clarified and tied in with § 2269 of the Civil Code, much litigation could be avoided.<sup>108</sup>

## VI. Claims of Public Institutions

The trust garnishment statute<sup>109</sup> provides: "Nothing in this subdivision limits the right of the state or other public entity to recover for support provided to a trust beneficiary or to recover for payments made for the support of a trust beneficiary." This sentence indicates that the remedies now available to a public entity are not subject to the provisions in subdivision (c) which for other creditors, limit the amount of trust funds payable to a creditor in accordance with the wage garnishment law. In other words the statute does not purport to affect the holding in Matter of Lackmann.<sup>110</sup>

A public entity that proceeds under subdivision (c) presumably may reach 25% of the amount payable periodically to a beneficiary of a spendthrift or a support trust like any other judgment creditor, but if the claim is for a debt "incurred for the common necessities of life furnished to the judgment debtor"<sup>111</sup> the debtor may not have the exemptions provided in C.C.P. §§ 706.050-706.051, and therefore, more income may be recovered, subject only to § 706.052, which incorporates Section 1673 of Title 15 of the United States Code.<sup>112</sup> Where the trustee has been given discretion over the payment of either principal or income, however, garnishment is available only after the trustee has made a determination that the amount is payable.<sup>113</sup>

There is an increasing amount of litigation in the United States about the right of a public institution to recover from private sources at least some share of the cost of maintaining indigent persons in hospitals, asylums homes for the aged and the like.<sup>114</sup> Does the state have a priority over other claimants, as it usually has in taxation?<sup>115</sup> Are trust funds liable to exhaustion for necessities supplied to a shielded beneficiary?<sup>116</sup> If a trustee has the discretion to make payments for the support of a beneficiary but has not made any, is the beneficiary ineligible for public assistance?<sup>117</sup> It is suggested that the Commission should have these problems studied, not to try to reconcile the many cases, but to consider what is the best balance between the welfare of trust beneficiaries, the claims of state and local agencies, and the reasonable expectations of donors. It is in the interest of the state to encourage the creation of private trusts--trusts that pay full support if possible, or at least for the comforts and amenities not otherwise available.

My suggestion is to have this problem studied by someone who knows trust law but is sympathetic with the needs of public institutions and is understanding about the needs of the wards of these institutions. A few new statutes in other states are worth reviewing.<sup>118</sup>

## VII. Pension Trusts

The newest type of protective trust may prove to be the most important: the pension trust with spendthrift features. The federal statute, Employment Retirement Income Security Act (ERISA),<sup>119</sup> requires that every plan covered by the Act contain a spendthrift clause.<sup>120</sup> Such a clause is not the usual one: it provides "benefits provided under the plan may not be assigned or alienated."<sup>121</sup> The Act itself does not make beneficial interests inalienable or exempt. The Act requires a disabling clause to be written into the plan.<sup>122</sup>

The first question to be considered is how far pension trusts are to be controlled by federal law and how far by state law. Obviously, federal law controls in so far as it preempts state law. Since ERISA is not per se an exemption law, the rights of creditors will be determined by the state law of spendthrift trusts.<sup>123</sup>

In California, if a pension trust is funded not by the beneficiary, but is funded by an employer or some other person, then a spendthrift clause protecting the beneficiary from voluntary or involuntary alienation would presumably be the same as in an ordinary spendthrift trust.<sup>124</sup>

A self-settled pension trust, such as a Keough plan trust, normally could not be protected by a spendthrift clause,<sup>125</sup> but the recently enacted California statute

makes private pension plans "exempt" until the time for payment of benefits arrives.<sup>126</sup> There is, however, no provision in the law that enables the creator of a self-settled trust, even a pension trust, to make the trust irrevocable or to make trust benefits inalienable.<sup>127</sup> The beneficiary is shielded from creditors but not from himself or herself.

The problems involved in pension plans, ERISA-covered and others, are especially interesting when they arise in connection with the new National Bankruptcy Act.<sup>128</sup> The Act has two relevant sections: the bankrupt estate is subject to certain exemptions (state or federal)<sup>129</sup> and, in addition, the beneficiary's interest in a spendthrift trust does not pass to the bankruptcy estate if such an interest is not alienable under state law.<sup>130</sup> In California, as suggested earlier, the restraint on alienation of income interests in spendthrift trusts may be absolute--but<sup>131</sup> not in self-settled trusts.<sup>132</sup> Therefore in California, the trust fund of an ordinary self-settled trust would be included in the bankrupt estate subject to the state exemption.<sup>133</sup> If a different result is desired, then, according to a recent decision,<sup>134</sup> the interest of the settlor-beneficiary of a pension trust should be made irrevocable and inalienable by state law as well as exempt. Such an amendment would go beyond the Bankruptcy problem by disabling the settler-beneficiary from making any

assignments before the pension payments begin. This would require new statutory provisions in California.

There are other questions that should be determined by legislation. Should pension payments be available for support claims?<sup>135</sup> Should support claims be permitted out of the fund before pension payments are due?<sup>136</sup> These questions are raised in the Parscal case if it is considered to be a self-settled trust. Much has been done in the recent amendments to the Code of Civil Procedure with respect to pensions and insurance, but current litigation suggests that clarification of state law is yet needed where pension law has not been preempted by federal statutes.<sup>137</sup>

This area, involving federal pension and bankruptcy law as well as state trust law, requires a careful study by an expert consultant, and perhaps more time for guidance from federal courts. I recommend that the Commission, in the interim, make private pension plans, if so intended by the settlor, irrevocable and inalienable until payments begin, and that the Commission reconsider the existing exemption provision to allow spousal and child support claims to be asserted before payments begin in proceedings supplemental to judgment (as in Parscal).

## Conclusion

The recent changes in the California statutes, especially in C.C.P. § 709.010, substantially improve the law of protective trusts. Nevertheless a chapter in the new Probate Code would be useful, would be a guide to the profession and would minimize future litigation.

There are three models of comprehensive statutes that could be used as starting points. The Oklahoma statute is an enactment of the model statute suggested by Erwin Griswold at the conclusion of his treatise on spendthrift trusts. The Oklahoma statute is reprinted in Appendix I. The best modern statute, largely following the Restatement of Trusts, is the 1969 Act in Wisconsin which is reprinted in Appendix II. A third model would track most of the blackletter text in the Restatement of Trusts, but would retain C.C. §§ 859 and 867. The Restatement version (with brief commentary and a few suggested changes), is set forth in Appendix III.

The recommended studies on claims of public institutions, and on pension problems, might result in revisions or supplements.

The specific issues raised in the background study which would have to be decided by the Commission before a model code could be adopted or drafted include:

1. Are the rights of creditors of trust beneficiaries of all types of trusts fully covered by the recent statutes?

2. What disabling restraints on the voluntary alienation of income and principal should be permitted?

3. How are discretionary trusts and discretionary powers in spendthrift and support trusts to be differentiated and controlled?

4. What is the right balance between the rights of public institutions, donors, and beneficiaries in the public interest?

5. What is the proper balance between claimants and beneficiaries in pension funds, including self-settled trusts, before payments begin?

6. Are there favored claims that are not completely covered by existing legislation?

## FOOTNOTES

### I. AND II.

1. See: Rationale for the Spendthrift Trust, 64 Colum.L.Rev. 1323 (1964); Costigan, Those Protective Trusts Which are Miscalled "Spendthrift Trusts" Reexamined, 22 Calif.L.Rev. 471 (1934).
2. If spendthrift trusts were not permitted in California, it would be easy for settlors to create spendthrift trusts in other states--as the Dowager Duchess of Manchester established a trust in New York. *Hamilton v. Drogo*, 241 N.Y. 401, 150 N.E. 821 (1936).
3. Irwin Griswold at the end of his treatise on spendthrift Trusts, gave this summary: "There are situations in which spendthrift trusts admittedly serve a useful function. Where they are created of moderate amount for the benefit of widows or for people who are really unable to manage their own affairs there can be little reason to argue against them in a regime of private property. The difficulty comes not so much from the existence of spendthrift trusts as from their generally unrestrained extent. The arguments for and against such trusts may in a large measure be reconciled by legislation expressly authorizing them of a fixed and moderate amount, while allowing creditors to reach all income in excess of the specified amount. Special classes of creditors should also be expressly allowed to reach part of the income exempt from the claims of ordinary creditors." Griswold, *Spendthrift Trusts* (2d ed. 1947), § 556.
4. Assembly Bill No. 2290, Ch. 2290, Sec. 2.5, amending Code of Civil Procedure § 709.010, approved by the Governor September 5, 1984. C.C.P. § 709.010 in its final form is as follows:

709.010. (a) As used in this section, "trust" has the meaning provided in Section 1138 of the Probate Code but includes a trust subject to court supervision under Article 1 (commencing with Section 1120) of Chapter 19 of Division 3 of the Probate Code.

(b) The judgment debtor's interest as a beneficiary of a trust is subject to enforcement of a money judgment only upon petition under this section by a judgment creditor to a court prescribed in Chapter 19 (commencing with Section 1120) of Division 3 of the Probate Code (administration of trusts). The judgment debtor's interest in the

trust may be applied to the satisfaction of the money judgment by such means as the court, in its discretion, determines are proper, including but not limited to imposition of a lien on or sale of the judgment debtor's interest, collection of trust income, and liquidation and transfer of trust assets by the trustee.

(c) Upon petition of the judgment creditor under this section, the court may make an order that the trustee withhold and pay to the judgment creditor all or a portion of the amount that otherwise would be paid periodically to the judgment debtor from the trust. Unless the order otherwise provides, the order shall continue in effect until the judgment of the judgment creditor is satisfied or the order is modified or terminated. In the case of periodic payments from a spendthrift or support trust, the order may not require that the trustee pay to the judgment creditor any exempt portion of the amount that otherwise would be paid periodically to the judgment debtor from the trust; and for this purpose, the exempt portion is the amount that the court determines is substantially equivalent to the amount that would be exempt on a like amount of earnings under Chapter 5 (commencing with Section 706.010) (Wage Garnishment Law) including but not limited to, amounts determined under Sections 706.050, 706.051, and 706.052. Nothing in this subdivision limits the right of the state or other public entity to recover for support provided to a trust beneficiary or to recover for payments made for the support of a trust beneficiary.

(d) Except to the extent that the court order otherwise specifically provides, the provisions of any order entered under subdivision (c) shall not become effective until 30 days after the order has been served upon the trustee, except that the trustee may waive all or any portion of the 30-day period. The trustee may file with the court that made the order a petition requesting modification or clarification of any of the provisions of the order. Notwithstanding any contrary provision of law, the trustee is not required to pay any fee to the clerk of the court as a condition to filing a petition under this subdivision or any subsequent document in connection with a petition. If any provision of the order is modified or set aside, the court, on motion of the judgment creditor or judgment debtor, may set aside or modify other provisions of the order. The trustee, the judgment creditor, and the judgment debtor may present evidence or further evidence that is relevant to the issues to be decided by the court at any hearing on the trustee's petition. The court

shall take this evidence into account in determining those issues. Nothing in this subdivision limits any right of a trustee to petition a court under Chapter 19 (commencing with Section 1120) of Division 3 of the Probate Code.

(e) Where the trust gives the trustee discretion over the payment of either principal or income of a trust, or both, nothing in this section affects or limits that discretion or requires the exercise of that discretion in any particular manner. The trustee has no duty to oppose a petition under this section or to make any claim for exemption on behalf of the trust beneficiary. The trustee is not liable for any action taken, or omitted to be taken, in compliance with any court order made under this section.

(f) Except as provided in subdivisions (c), (d), and (e), nothing in this section affects the law relating to enforcement of a money judgment against the judgment debtor's interest in a spendthrift trust, but surplus amounts from a spendthrift trust liable pursuant to Section 859 of the Civil Code are subject to enforcement of a money judgment under this section.

5. C.C.P. Title 9, Enforcement of Judgment, Ch. 5, Wage Garnishment, §§ 706.010-706.152, Assembly Bill no. 707, March 2, 1981, as amended.
6. Dated September 23, 1983. The comment in the Recommendation in relevant part reads as follows:

"The Wage Garnishment Law provides a statutory formula for determining amounts that are to be withheld from earnings to satisfy a money judgment. Under existing law, \$435.50 per month is protected from a general creditor. A general creditor can reach the amount over \$435.50 up to \$580.66 and can reach one-fourth of the amount payable where monthly payments exceed \$580.66. Where the debtor can show that a greater amount is necessary for his or her support or the support of his<sup>(1)</sup> or her dependents, a hardship claim may be made. Where the garnishment is made to collect delinquent amounts payable under a judgment for the support of a child or spouse or former spouse of the debtor, the<sup>(2)</sup> creditor can reach one-half of the amount payable, but any party may apply to the court for an equitable<sup>(3)</sup> division that varies this 50-50 division rule.

- (1) Code Civ. Proc. § 706.051.
- (2) Code Civ. Proc. § 706.052.
- (3) Code Civ. Proc. § 706.052(b).

The court may reduce the amount to be withheld, but federal law limits the extent to which the court can increase the amount to be withheld. Under certain circumstances, as much as 65% may be withheld. See Code Civ. Proc. § 706.052(c) and the Comment thereto.

7. Especially claims for spousal or child support or for the common necessities of life. C.C.P. § 706.051.
8. See Comment to Commission Recommendation, *supra*, n. 6, text related to nn. 6-9.
9. Restatement of the Law, Second, Trusts (hereafter Rest. Trusts 2d) § 157.
10. Cf. Molinari, J. in Estate of Johnston, 252 Cal.App. 923, 60 Cal.Rptr. 852 (1967). See also Shelley v. Shelley, 223 Or. 328, 354 P.2d 282 (1960).
11. Not all courts have accepted all of the favored Restatement favored claims; some classes are too broad, for example, "alimony" is broader than "support." See, Lippincott v. Lippincott, 28 Pa.D&C 28 (1936). For a general account, see Griswold, *supra* n. 3, §§ 339-403.
12. Both sections were adopted in 1872 as parts of the Field Code.
13. *Supra* n. 4.
14. Illustrative cases are: Smith v. Smith 51 Cal.App. 2d 29, 124 P.2d 117 (1942); Magner v. Crooks, 139 Cal. 640, 73 P. 585 (1903) Cf. Alvis v. Bank of America, 95 Cal.App.2d 118, 212 P.2d 608 (1949).
15. N.Y.Laws, 1903, c. 561, N.Y. Civ. Proc. Act § 684.
16. Griswold, *supra* n. 3, §389.
17. *Id.*, §§ 390, 390.1; draft statute, § 565, sec. 2(b).
18. N.J.C. 2A:17-56; 2A:17-57 (amended 1970 to permit more than 10% if the trust income is over \$7,500 per annum).
19. Rest. Trusts 2d, § 152.
20. *Id.*, § 154.
21. *Id.*, § 155.

22. Id., § 157.
23. Schwager v. Schwager, 109 F.2d 754 (Ca.7th 1940); Rooda v. Rooda, 230 10 Wa. 1103, 300 N.W. 294 (1941); Bucknam v. Bucknam, 294 Mass. 214, 200 N.E. 918, 104 ALR 774 (1936); City of Bridgeport v. Reilly 133 Conn. 31, 47 A.2d 865 (1946).
24. Scott, Trusts. 3d ed (1967) § 157.
25. 121 Cal.App. 2d 675, 10 P.2d 158 (1932).
26. Restatement, Trusts 2d, § 157.
27. Anglo-California Nat. Bank v. Kidd, 58 Cal.App. 2d 651, 137 P.2d 460 (1943), (but voluntary alienation upheld.)
28. C.C.P. § 709.010(c).
29. C.C.P. § 709.020.
30. 13 Cal.2d 1, 87 P.2d 830 (1939).
31. Accord, Restatement, Trusts, 2d § 155(2).
32. C.C.P. §§ 706.050-706.050. See Comment to Commission Proposal, supra n. 6, text related to nn. (1)-(3).
33. Rest. Trusts, 2d, § 157(a), Comment b.
34. \_\_\_\_\_ Cal.App. \_\_\_\_\_, 196 Cal.Rptr. 462 (1983).
35. C.C.P. § 709.010(b).
36. Cases cited supra n. 14.
37. See Cartledge v. Miller (S.D.N.Y.), 457 F.Supp. 1146 (1978); American Tel. & Tel. v. Merry (2d Cir. 1979), 592 F.2d 118; Senco v. Florida, Inc. v. Clark (M.D.Fla.), 473 F.Supp. 902 (19).
38. Griswold, supra n. 3, § 390.2.
39. C.C.P. § 706.051(1).
40. Rest. Trusts 2d. § 157.
41. Young v. Handwork, 149 F.2d 70 (7th Cir. 1949), cert. den. 39 U.S. 949 (1950). Griswold, supra n. I.3., §§ 176-185.
42. Restatement, Trusts 2d, § 152.

43. C.C. § 859.
44. C.C. § 867.
45. N.Y. Estates, Powers, and Trust Law (EPTL) § 7-1.5.
46. Griswold, *supra* n. 3., § 565.
47. Louisiana, R.S. 9: § 2004. Several other states allow voluntary or involuntary alienation of income in excess of a fixed amount: Oklahoma (\$5,000), Okla. § 175.25, A(2). In Virginia, the limit is on the principal amount which may be placed in a spendthrift trust: \$500,000; Va. Code § 55-19 as amended 1980 c. 267. Other states have limitations on income or principal which may be shielded: Alabama, \$1,800 a year. Code § 19-3-1 (as amended 1982, Acts No. 82-625 § 1); North Carolina, \$500 a year, Code § 41-9.
48. Cf. A.L.I. Restatement of the Law, Second Property, Donative Transfers, (hereafter Rest. Prop. 2d) § 4.1 and Comments. (1981).
49. Some "Claflin"-type trusts, although alienable, may be nonterminable because of the "material purpose rule." In such cases, however, there is no disabling restraint; there is only equitable discretion to give effect to the donor's intent. *Claflin v. Claflin*, 149 Mass. 19, 20 N.E. 454, 3 L.R.A. 370.
50. 11 U.S.C. §§ 101-2107, especially § 541(c)(2).
51. Ironically the trustee in bankruptcy may have less of a right than an ordinary creditor because spendthrift restraints on alienation are absolute C.C. § 867 but a creditor can at least reach surplus under C.C. § 859.
52. P.C. § 190.8.
53. See discussion in Griswold, *supra* n. 3., § 338 citing cases from several states (not including California). Cf. *Gaskins v. Security First Nat. Bank*, 30 Cal.App.2d 409, 86 P.2d 681 (1939); *In re Knauth*, 12 N.Y.2d 259, 189 N.E.2d 482, 238 N.Y.S.2d 942 (1963). See annotation, *Transfer of Interest in Spendthrift Trust by Beneficiary*, 24 A.L.R.2d 1105 (1952).
54. *Spendthrift Trusts, Validity and Construction of Beneficiary's Arrangement for Payments to Another As They Become Due*, 83 ALR 3d 1142 (1974); *First Nat. Bank v. M & P Bank*, 510 S.W.2d 874 (1974).

55. Griswold, supra n. 3., §§ 372-375.
56. Kelly v. Kelly, 11 Cal.2d 356, 79 P.2d 1059 (1938).
57. Within the limits of the Wage Garnishment Law, supra nn. 5 and 6.
58. Cf. Griswold model statute, Griswold, supra n. 3., § 565. The amount would have to be adjusted from time to time (perhaps on the recommendation of the California Law Revision Commission) as for example in Louisiana (supra n. 47 or in Virginia (supra n. 47)).
59. See C.C.P. §§ 703.010-704.980, especially § 704.100 (a), unmatured life insurance policies.
60. This section has remained unchanged since it was adopted from the Field Code in 1872.
61. Griswold, supra n. 3., § 565, Sec. 4.
62. § 153. Under subsection (1), if the beneficiary is entitled to have the principal conveyed to him at a future time, the restraint is valid. The restraint is not valid if the beneficiary is entitled to have the principal conveyed to him immediately, or if it is not to be conveyed to him during his lifetime.
63. There are some statements not related to the decisions: e.g., Coughran v. First Nat. Bank, 19 Cal.App.2d 152, 64 P.2d 1013 (1937).
64. 11 Cal.2d 356, 79 P.2d 1059 (1928).
65. Witkin, Summary of California Law, Trusts, § 94, p. 5454.
66. The California court recognized the validity of Pennsylvania law as applied to a Pennsylvania trust but held that trust principal which had been delivered to a remainderman was subject to his contractual obligations like any other property.
67. C.C.P. § 709.010(c).
68. C.C.P. § 709.020.
69. Rest. Trust, 2d, § 153.
70. Rest. Prop. 2d. § 4.1.
71. C.C § 699.
72. § 162 (1936).

73. Griswold, *supra* n. 1.3., §§ 105-106.
74. Powell, *The Rule Against Perpetuities and Spendthrift Trusts in New York*, 17 *Colum.L.Rev.* 688, 701 (1971).
75. Schnebly, *Restraints upon the Alienation of Property*, 6 *Am. Law of Property* (A.J. Casner ed. 1952).
76. Simes and Smith, *The Law of Future Interests*, § 1146 (1956).
77. *Supra* n. 56.
78. Scott, *Trusts*, 3d ed. § 153; *Milner v. Outcalt*, 136 *Wash.Dec.* 668, 219 *P.2d* 982 (1950).
79. § 153 (1936).
81. 25 *N.Y.2d* 163, 250 *N.E.2d* 343, 303 *N.Y.S.2d* 61 (1969). The majority opinion has been followed by the intermediate appellate court in Michigan, *Preminger v. Union Bank and T Co.*, 54 *Mich. App.* 361, 220 *N.W. 2d* 795 (1974).
82. See criticism of the majority opinion: Powell, *The Rule against Perpetuities and Spendthrift Trusts in New York*, 71 *Colum.L.Rev.* 688, 701 (1971); Niles, *Matter of Vought's Will: a Tighter Grip by the Dead Hand*, 45 *N.Y.U.L.Rev.* 421 (1970); 21 *Syracuse L.Rev.* 213 (1969); 45 *N.Y.U.L.Rev.* 400 (1970).
83. Approved by the American Law Institute in 1981. See especially §§ 3.1-4.5.
84. *Coast Bank v. Minderhout*, 61 *Cal.2d* 311, 38 *Cal.Rptr.* 505, 392 *P.2d* 265 (1964).
85. Sweet, *Restraints on Alienation*, 33 *L.Q. Rev.* 236, 342 (1917).
86. Manning, *The Development of Restraints on Alienation Since Gray*, 48 *Harv.L.Rev.* 373; Bernhard, *The Minority Doctrine Concerning Direct Restraints on Alienation*, 57 *Mich. L.Rev.* 1173 (1959).
87. *Wellenkamp v. Bank of America*, 21 *Cal.2d* 943, 148 *Cal.Rptr.* 379, 585 *P.2d* 970 (1978); *Dawn Investment Co. v. Superior Court*, 30 *Cal.3d* 695, 180 *Cal.Rptr.* 332 (1982).
88. *Seymour v. McAvoy*, 121 *Cal.* 438, 53 *P.* 946, 41 *LRA* 544 (1898).

89. C.C.P. § 709.010(c), supra n.4.
90. Id. (e).
91. Scott supra n.24, § 155; Trustee Act, 1925, § 33; In re Richardson's Will Trusts, [1958] 2 WLR 414, note, 74 L.Q.Rev. 182 (1958).
92. Canfield v. Security First Nat. Bank, 13 Cal.2d 1, 148 P.2d 133 (1939).
93. Rest. Trusts, 2d, supra n.9. § 155.
94. In Hamilton v. Drogo, supra n.2, a settlement was ultimately reached. Griswold, supra n.3, p. 448 n.2.
95. Rest. Trusts, 2d, supra n.9, §§ 150, 155.
96. Id. § 154; Rest. Prop. 2d, Donative Transfers, § 3.1.
97. Id. § 32. See Note, Creditors Rights in Support Trusts, 156 Wash.Univ.L.Q. 106 (1956).
98. Rest. Trusts, 2d, supra n.9, § 155(2).
99. Supra n.92.
100. 230 C.A. 2d 888, 41 CR 410 (1964).
101. 156 C.A. 2d 674, 320 P.2d 186 (1958).
102. Rest. Trusts, 2d supra n.9, § 155, Comment e. In a recent article, Abravanel, Discretionary Support Trusts, 68 Iowa L.Rev. 272 (1983), the author, disturbed by cases such as Miller and Lackmann, suggests that three types of trusts should be recognized by the courts: support trusts, discretionary trusts, and discretionary support trusts. It is submitted that there are only two types, each ordinarily with discretionary powers in the trustee. A trustee of a support trust with broad discretionary powers, as in Miller, cannot cut off the beneficiary who needs support; a trustee of a true discretionary trust can.
103. Rest.T.2d. supra n.9, § 157(b).
104. Supra n.4., C.C.P. § 706.051(c)(1).
105. Feb. 21, 1984.
106. C.C § 2269.

107. This would be true in spendthrift trusts or trusts for support, but not true discretionary trusts if nothing is in fact paid. See *Canfield v. Security First Nat. Bank*, supra n.92. In general, see *Rest. Trusts 2d*. § 187.
108. Cf. Halbach *Problems of Discretion in Discretionary Trusts*, 60 *Colum.L.Rev.* 1425 (1960).
109. C.C.P. § 709.010(c).
110. Supra n.101.
111. C.C.P. § 706.051(c)(1).
112. The amount exempt under the Federal statute, of course, supersedes state law. C.C.P. 706.050.
113. C.C.P. § 709.010(e).

If a judgement creditor sought to reach trust funds under C.C.P. § 709.010(b), no relief would be available under the *Canfield* case if no discretion had been exercised to make funds payable to the beneficiary.

114. Representative cases, in addition to matter of *backmann* supra n.101 are: *Re Hinkley's Estate*, 195 *Cal.App.2d* 164, 15 *Cal.Rptr.* 570 (1961); *In re Johnson's Estate*, 198 *Cal.App. 2d* 503, 17 *Cal.Rptr.* 909 (1961); *Will of Wright*, 12 *Wisc. 2d* 375, 107 *N.W. 2d* 146, 92 *A.L.R. 2d* 832, 1961, *Annotation*, 92 *A.L.R. 2d* 846, *City of Bridgeport v. Reilly* 133 *Conn.* 31, 47 *A.2d* 865 (1946); *Dept. of Public Welfare v. Meek*, 264 *Ky.* 771, 955 *S.W. 2d* 599 (1936); *Town of Shrewbary v. Bucklin*, 105 *vt.* 188, 163 *A.* 626, 86 *A.L.R.* 133 (1933), 18 *Iowa L.Rev.* 550, 81 *U. of La.L.Rev.* 1009; *Constanza v. Vedona*, 137 *A.2d* 614 (N.J. 1958); *Bureau of Support v. Kreitzer*, 16 *Ohio St.2d* 147, 243 *N.E. 2d* 83 (1968) *State v. Caldwell*, 181 *Tenn.* 74, 178 *S.W. 2d* 624 (1944). See also *Beoli v. Comm. of Social Services*, 425 *A.2d* 553 (1979) and *Annotation: Welfare Benefits: Eligibility for Welfare benefits as affected by claimant's status or trust beneficiary*, 21 *A.L.R. 4th* 729 (1979) See also *Oddo v. Blum*, 83 *App.Div.* 868, 442 *N.Y.S. 2d* 23 (1981).
115. *Matter of Rosenberg*, 269 *N.Y.* 247, 199 *N.E.* 206, 105 *A.L.R.* 1238 (1935). See, *U.S. v. Canfield*, 29 *F.Supp.* 734 (S.D.Cal. 1935).
116. *Maul v. Fitzgerald*, 78 *App.Div.* 707 (1980); *Matter of Rath*, 58 *Misc. 2d* 184, 294 *N.Y.S.2d* 920 (1968).

117. See *Jensen v. Dept. of Public Welfare*, 201 Neb. 185, 266 N.W.2d 742 (1978). Cf. *McNiff v. Olmstead Co. Welfare Dept.* 187 Minn. 40, 176 N.W.2d 888 (1970).
118. Perhaps the most thoughtful one is the Wisc. 1969 Act, § 701.06, 5(a),(b) & (c) and 5m.
119. 29 U.S.C. § 1056d (1976) *Sherman, Spendthrift Trusts and Employee Pensions: The Problem of Creditor's Rights*, 55 Ind.L.Rev. 247 (1980).
120. ERISA § 206(d), I.R.C. § 401(a)(13).
121. *Id.*
122. *Sherman*, supra n.119 at 253 n.28.
123. Cf. *Nat.Bk. of N. America v. IBEW Local 3*, 93 Misc.2d 590, 400, N.Y.S.2d 482 (Sup. Ct. 1977), aff'd 69 App.Div.2d 679, 419 N.Y.S.2d 127 (1979); *Sherman* supra n.119 at 253.
124. Cf. *Pascal*, supra n.34 See *Electrical Workers Local no.1. Credit Union v. IBEW - NECA Holiday Trust Co.* \_\_\_\_\_ 583 SW 2d 154 (1979).
125. *Nelson v. Calif. T Co.*, 33 Cal.2d 501, 202 P.2d 1021 (1949). *Sherman*, supra n.119 at p.261.
126. C.C.P. § 704.115(b).
127. Cf. *Goff v. Goff*, 706 F.2d 574 (1983) applying Federal statutes to Texas law.
128. 11 U.S.C. § 101-2107.
129. 11 U.S.C. § 522; *Yukowich, Debtor's Exemption Rights Under the Bankruptcy Reform Act*, 58 N.C.L.Rev. 769 (1980).
130. 11 U.S.C. § 541(c)(2). The House Report, cited in *Yukowich*, supra n.129, at 669 n.8, stated: "The Bankruptcy of the beneficiary [of a spendthrift trust] should not be permitted to defeat the legitimate expectations of the settlor of a trust."
131. C.C. § 867.
132. *Witkin, Summary of California Law*, 8th ed. Trusts § 96.
133. C.C.P. § 704.115(b).
134. *Goff v. Goff*, supra n.127.

135. See cases cited by Sherman, *supra* n.119, at 273 n. 103, e.g. *Cody v. Riecker*, 594 F.2d 314 (2d C 1979).
136. See Pascal, *supra* n.34.
137. Reppy, *Community and Separate Interests in Pensions and Social Security Benefits After Marriage of Brown and ERISA*, 25 U.C. L.A.L.Rev 417, 519 (1978). See cases involving state pensions: *Ogle v. Heim* 69 Cal.2d 7, 69 Cal.Rptr. 5 \_\_ 9, 442 P.2d 659 (1968); *Miller v. Superior Ct.*, 69 Cal.2d 14, 69 Cal.Rptr. 583, 442 P.2d 663 (1968).

## Appendix I

### OKLAHOMA

Alienation of interest of beneficiary--Rights and remedies of creditors--Spendthrift trusts--Trustor's interest alienable and subject to claims of creditors

Any instrument creating a trust may provide by specific words that the interest of any beneficiary in the income of the trust shall not be subject to voluntary or involuntary alienation by such beneficiary. Subject to the following provisions of this Section, a direction to this effect shall be valid and enforceable.

A. Notwithstanding a provision in the terms of a trust restraining the alienation of the interest of a beneficiary, such interest shall be entitled to be reached in the satisfaction of claims to the following extent:

1. All income due or to accrue in the future to the beneficiary shall be subject to enforceable claims under the laws of this State for,

(a) support of a husband, wife, or child of the beneficiary,

(b) necessary services rendered or necessary supplies furnished to the beneficiary, or

(c) a judgment based on any such claim under (a) or (b).

2. In all cases not mentioned in preceding sub-section 1 herein all income due or to accrue in the future to the beneficiary in excess of five thousand dollars (\$5,000.00) per annum based upon calendar year of the trust, shall be subject to garnishment by creditors of the beneficiary and shall be fully alienable by the beneficiary.

B. Where two or more creditors undertake to reach the interest of any beneficiary of a trust, pursuant to the provisions of this Section, they shall be subject to priority of payment in the order of the service of a notice of garnishment on the trustee. The pendency of any attachment or garnishment shall not prevent the filing of a further attachment or garnishment by the same or any other creditor.

C. Where the beneficiary of any spendthrift trust is also the beneficiary under any other spendthrift trust created or administered either within or without this State, the aggregate income payable under all such trusts to the beneficiary shall be considered together for the purposes of determining the rights of creditors and assignees under this Section.

D. The right of any beneficiary of a trust to receive the principal of the trust or any part of it, presently or in the future, shall not be alienable and shall not be subject to the claims of his creditors.

E. Where the interest of the beneficiary of a trust is subject to the exercise of discretion by the trustee or by another, the provisions of this Act as to the rights of creditors and assignees shall apply with respect to any sums which the trustee or such other person determines shall be paid to or for the beneficiary.

F. A trust in which the interest of the beneficiary is subject to restraints on alienation as provided in this Act may be called a "spendthrift trust" and a direction in any instrument creating a trust that the interest of any beneficiary shall be held on or subject to a spendthrift trust shall be sufficient to restrain the alienation of such interest to the extent provided in this Act.

G. Nothing in this Act shall authorize a person to create a spendthrift trust or other inalienable interest for his own benefit. The interest of the trustor as a beneficiary of any trust shall be freely alienable and subject to the claims of his creditors.

H. The provisions of this Section may be enforced only by an action in a court of competent jurisdiction and the obligor beneficiary shall be a party defendant in such action. The trustee shall not be required to recognize any of the obligations provided for in this Section or to withhold any income from the beneficiary until said trustee has been served with summons or garnishment summons. Such action shall be governed by the rules of civil procedure under the laws of Oklahoma.

Laws 1941, p. 257, § 25.

#### Historical Note

Source. Laws of Louisiana, 1938, Act 81, amended (LSA-R.S. 9:1923).

#### Law Review Commentaries

Equitable future interests subject to claims of creditors. 14 Okl.Law.Rev. 216 (May 1961).

Satisfaction of decree for alimony from income of spendthrift trust in Oklahoma. 19 Okl.Law Rev. 122 (Feb.1966).

Spendthrift trusts in Oklahoma. 14 Okl.Law Rev. 233  
(May 1961).

D. The right of any beneficiary of a trust to receive the principal of the trust or any part of it, presently or in the future, shall not be alienable and shall not be subject to the claims of his creditors.

E. Where the interest of the beneficiary of a trust is subject to the exercise of discretion by the trustee or by another, the provisions of this Act as to the rights of creditors and assignees shall apply with respect to any sums which the trustee or such other person determines shall be paid to or for the beneficiary.

F. A trust in which the interest of the beneficiary is subject to restraints on alienation as provided in this Act may be called a "spendthrift trust" and a direction in any instrument creating a trust that the interest of any beneficiary shall be held on or subject to a spendthrift trust shall be sufficient to restrain the alienation of such interest to the extent provided in this Act.

G. Nothing in this Act shall authorize a person to create a spendthrift trust or other inalienable interest for his own benefit. The interest of the trustor as a beneficiary of any trust shall be freely alienable and subject to the claims of his creditors.

H. The provisions of this Section may be enforced only by an action in a court of competent jurisdiction and the obligor beneficiary shall be a party defendant in such action. The trustee shall not be required to recognize any of the obligations provided for in this Section or to withhold any income from the beneficiary until said trustee has been served with summons or garnishment summons. Such action shall be governed by the rules of civil procedure under the laws of Oklahoma.

Laws 1941, p. 257, § 25.

#### Historical Note

Source. Laws of Louisiana, 1938, Act 81, amended (LSA-R.S. 9:1923).

#### Law Review Commentaries

Equitable future interests subject to claims of creditors. 14 Okl.Law.Rev. 216 (May 1961).

Satisfaction of decree for alimony from income of spendthrift trust in Oklahoma. 19 Okl.Law Rev. 122 (Feb.1966).

Spendthrift trusts in Oklahoma. 14 Okl.Law Rev. 233 (May 1961).

Appendix II

WISCONSIN

1969 Act

Spendthrift provisions and rights of creditors of beneficiaries

(1) Income beneficiaries. A settlor may expressly provide in the creating instrument that the interest in income of a beneficiary other than the settlor is not subject to voluntary or involuntary alienation. The income interest of such a beneficiary cannot be assigned and is exempt from claims against the beneficiary until paid over to him pursuant to the terms of the trust.

(2) Principal beneficiaries. A settlor may expressly provide in the creating instrument that the interest in principal of a beneficiary other than the settlor is not subject to voluntary or involuntary alienation. The interest in principal of such a beneficiary cannot be assigned and is exempt from claims against the beneficiary, but a judgment creditor, after any payments of principal have become due or payable to the beneficiary pursuant to the terms of the trust, may apply to the court for an order directing the trustee to satisfy the judgment out of any such payments and the court in its discretion may issue an order for payment or part or all of the judgment.

(3) Disclaimer or reunication not an assignment. A disclaimer or reunication by a beneficiary of part or all of his or her interest under a trust shall not be considered an assignment under sub. (1) or (2).

(4) Claims for child support. Notwithstanding any provision in the creating instrument or subs. (1) and (2), upon application of a person having a valid order directing a beneficiary to make payment for support of the beneficiary's child, the court may:

(a) If the beneficiary is entitled to receive income or principal under the trusts, order the trustee to satisfy part or all of the claim out of part or all of payments of income or principal as they are due, presently or in the future;

(b) In the case of a beneficiary under a discretionary trust, order the trustee to satisfy part or all of the claim out of part or all of future payments of income or principal which are to be made pursuant to the exercise of the trustee's discretion in favor of such beneficiary.

(5) Claims for public support. Notwithstanding any provision in the creating instrument or subs. (1) and (2), if the settlor is legally obligated to pay for the public support of a beneficiary under s. 46.10 or the beneficiary is legally obligated to pay for his public support or that furnished his spouse or minor child under s. 46.10, upon application by the appropriate state department or county official, the court may:

(a) If such beneficiary is entitled to receive income or principal under the trust, order the trustee to satisfy part or all of the liability out of part or all of payments of income or principal as they are due, presently or in the future;

(b) Except as otherwise provided in par. (c), in the case of a beneficiary under a discretionary trust, order the trustee to satisfy part or all of the liability out of part or all of future payments of income or principal which are to be made pursuant to the exercise of the trustee's discretion in favor of such beneficiary;

(c) In the case of a beneficiary under a discretionary trust who is a settlor or a spouse or minor child of the settlor, order the trustee to satisfy part or all of the liability without regard to whether the trustee has then exercised or may thereafter exercise his discretion in favor of the beneficiary.

(5m) Trust for disabled individual. Subsection (5) does not apply to any trust that is established for the benefit of an individual who has a disability which has continued or can be expected to continue indefinitely, substantially impairs the individual from adequately providing for his or her own care or custody, and constitutes a substantial handicap to the afflicted individual if the trust does not result in ineligibility for public assistance under ch. 49. A trustee of a trust which is exempt from claims for public support under this subsection shall notify the county department of social services or public welfare in the county where the disabled beneficiary resides of the existence of the trust.

(6) Settlor as beneficiary. Notwithstanding any provision in the creating instrument and in addition to the remedies available under subs. (4) and (5) where the settlor is a beneficiary, upon application of a judgment creditor of the settlor, the court may, if the terms of the instrument require or authorize the trustee to make payments of income or principal as they are due, presently or in the future, or which are payable in the trustee's discretion, to the extent in either case of the settlor's proportionate contribution to the trust.

(7) Subsequent modification of court's order. Any order entered by a court under sub. (4), (5) or (6) is

subject to modification upon application of an interested person.

(8) Exempt assets. Assets of a trust, to the extent they are exempt from claims of creditors under other statutes, shall not be subject to sub. (4), (5) or (6).

Perpetuities under Wisconsin statutes. Nelson Trotman. 1922, 2 Wis.L.Rev. 14.

Restraints on alienation of property held in trust. Leo M. McDonnell. 36 Marquette L.Rev. 97 (1952).

Restricted scholarships. 1963 Wis.L.Rev. 254.

"Specific Portion" trusts and the marital deduction. 51 Marquette L.Rev. 171 (1967).

Spendthrift trusts in Wisconsin. Lawrence J. Binder. 36 Marquette L.Rev. 167 (1952).

Spendthrift trusts of personalty. E. H. Snyder, 15 Gavel 6 (Spring 1954).

Termination of trust of personalty by beneficiary. 1926, 3 Wis.L.Rev. 354.

## Appendix III

Draft statute based on Restatement of Trusts, Second.

### § 1. Exemptions

If a legal interest is exempt from the claims of creditors, the corresponding interest of the beneficiary of a trust cannot be reached by his creditors.

Comment: This section is the same as § 149 of Rest. Trusts 2d. A similar provision is found in The 1969 Wisconsin statute § 701.06(8). Since the term "exemption" is used in statutes that apply to trust assets, this section is desirable but not essential. See Comment c to Rest. Trusts 2d § 149.

### § 2. Forfeiture for alienation.

A provision in the terms of the trust that the interest of a beneficiary shall terminate upon an attempt by him to transfer it or by his creditors to reach it or upon his bankruptcy is valid as to his interest in income and is valid as to his interest in principal to the extent to which a restraint on alienation of an interest in principal is valid under the rules stated in § 5.

Comment: This section provides for a forfeiture restraint on alienation as distinguished from the disabling restraint of a spendthrift trust and is to be considered with the first Restatement of Property, §§ 404-417, and the second Restatement of Property, Donative Transfers, §§ 3.2 & 4.2.

### § 3. Restraint on Involuntary Alienation of Income.

Where a trust is created to receive the rents and profits of real or personal property, and no valid direction for accumulation is given, the surplus of such rents and profits, beyond the sum that may be necessary for the education and support of the person for whose benefit the trust is created, may be applied to the satisfaction of a money judgment against the person as provided in Section 709.010 of the Code of Civil Procedure.

Comment: This is the new version of C.C. 659. This section provides for a disabling restraint on involuntary alienation. See Rest.Prop. 2d §§ 3.1 and 4.1. Unlike Rest.Trusts 2d § 152 it is only a partial restraint.

Commentary to this section should be adapted from the commentary in Rest.Trusts, 2d, § 152.

### §4. Restraint on Voluntary Alienation of Income.

The beneficiary of a trust for the rents and profits of real property, or for the payment of an annuity out of such rents and profits, may be restrained from disposing of his interest in such trust, during his life or for a term of years, by the instrument creating the trust.

Comment: The section is the present C.C. § 867. The section should be modernized to include income from personal property.

If the Commission should decide that trust income should be alienable above a certain amount, such as \$10,000 a year, then the sections would be modified by adapting the text of the New York statute or the text of Griswold's model statute.

The commentary would include matters mentioned in the commentary to Rest.T. 2d. § 152. Reference should be made to the application of the National Bankruptcy Act.

#### § 5. Restraint on the Voluntary or Involuntary Alienation of Principal.

(1) Except as stated in §§ [8 and 9] if by the terms of a trust the [income] beneficiary is entitled to have the principal conveyed to him at a future time, a restraint on the voluntary or involuntary transfer of his interest in the principal is valid.

(2) If [a] beneficiary is entitled to have the principal conveyed to him immediately, a restraint on the voluntary or involuntary transfer of his interest in the principal is invalid.

(3) If the principal is not to be conveyed to [a] beneficiary during his lifetime, a restraint on the voluntary or involuntary transfer of his interest in the principal is invalid.

Comment: The suggested changes [adding "income" in (1) and substituting "a" for "the" in (2) and (3)] would cause the Restatement comment on Subsection 1 (b) Illustration 2 to be reversed, and would in effect disapprove of Matter of Vought.

If the Commission adopted the Pennsylvania rule that restraints on the alienation of principal are valid, then the Wisconsin subsection (2) is recommended.

#### § 6. Spendthrift Trust.

A spendthrift trust as the term is used in this part, as opposed to a trust for support (§ 7), or a discretionary trust (§ 8), is a trust in which a disabling restraint on voluntary or involuntary alienation has been imposed on a beneficiary by the settlor.

No specific language is necessary to create a spendthrift trust but extrinsic evidence is not admissible to show the intention of the settlor to prevent the voluntary or involuntary alienation of the beneficiary's interest.

Comment: The second paragraph could be placed in a comment to the section.

This section has no exact counterpart in the Rest. Trusts 2d. but is similar to § 152 Comment: (b), (c) and (f).

#### § 7. Trusts for Support.

Except as stated in §§ 8 and 9, if by the terms of a trust it is provided that the trustee shall pay or apply only so much of the income and principal or either as is necessary for the education or support of the beneficiary, the beneficiary cannot transfer his interest and his creditors cannot reach it, except as provided in § 709.010 of the Code of Civil Procedure.

If discretionary powers are given to the trustee relating to payments for support, the trustee may exercise such discretion but if the settlor has manifested that support be available to the beneficiary on an ascertainable standard, then the trustee must not exercise discretion to reduce payments so that income from all sources available to the beneficiary are below the standard.

Comment: It might be better to omit the second sentence from the text and include it in the commentary as in the Restatement. There should be a cross-reference to the trust garnishment provision (C.C.P. 709.010) which specifically applies to trusts for support.

#### § 7. Discretionary Trusts.

(1) Except as stated in § 8, if by the terms of a trust it is provided that the trustee shall pay to or apply for a beneficiary only so much of the income and principal or either as the trustee in his uncontrolled discretion shall see fit to pay or apply, a transferee or creditor of the beneficiary cannot compel the trustee to pay any part of the income or principal.

(2) Unless a valid restraint on alienation has been imposed in accordance with the rules stated in §§ 3 and 5, if the trustee pays to or applies for the beneficiary any part of the income or principal with knowledge of the transfer or after he has been served with process in a proceeding by a creditor to reach it, he is liable to such transferee or creditor.

Comment: This section is based on Rest.T.2d § 155. Comments to the section should be similar to the Comments in Rest.T.2d § 155.

The Wisconsin statute is essentially the same and is somewhat briefer.

#### § 8. Where the Settlor is Beneficiary.

(1) Where a person creates for his own benefit a trust with a provision restraining the voluntary or involuntary transfer of his interest, his transferee or creditors can reach his interest.

(2) Where a person creates for his own benefit a trust for support or a discretionary trust, his transferee or creditors can reach the maximum amount which the trustee under the terms of the trust could pay to him or apply for his benefit.

Comment: It is at this point that the Rest.Trusts, 2d permits the credition of a self-settled trust to reach the trust fund if the settlor retains the income and the power to appoint. If the Commission accepts the rule that creditors of the settlor may reach the trust fund of any revocable trust, even after the death of the settlor but within the non-claim period, then this would be the place to refer to the relevant provision.

Self-settled pension trusts are "exempt" under C.C.P. § 104.115(b) and therefore a cross-reference should be included here.

#### § 9. Particular Classes of Claimants.

Although a trust is a spendthrift trust or a trust for support, the interest of the beneficiary can be reached in satisfaction of an enforceable claim against the beneficiary,

(a) by the spouse or child of the beneficiary for support.

(b) for necessary services rendered to the beneficiary or necessary supplies furnished to him.

Comment: There should be a cross-reference to C.C.P. § 709.010. This section is more limited than Rest. Trusts 2d. § 157 and needs further study.