

Memorandum 83-60

Subject: Study L-641 - Creditor's Right to Reach Payments From Trust

Attached is a draft of a tentative recommendation that effectuates the Commission's decisions with respect to garnishment of amounts payable to a trust beneficiary. The draft has been distributed for review and comment. We will review the draft and any comments we have received at the September meeting.

Respectfully submitted,

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STATE OF CALIFORNIA
CALIFORNIA LAW
REVISION COMMISSION

TENTATIVE RECOMMENDATION

relating to

GARNISHMENT OF AMOUNTS PAYABLE TO TRUST BENEFICIARY

August 1, 1983

Important Note: This tentative recommendation is being distributed so that interested persons will be advised of the Commission's tentative conclusions and can make their views known to the Commission. Any comments sent to the Commission will be considered when the Commission determines what recommendation, if any, it will make to the California Legislature. It is just as important to advise the Commission that you approve the tentative recommendation as it is to advise the Commission that you object to the tentative recommendation or that you believe that it needs to be revised. COMMENTS ON THIS TENTATIVE RECOMMENDATION SHOULD BE SENT TO THE COMMISSION NOT LATER THAN SEPTEMBER 8, 1983.

The Commission often substantially revises tentative recommendations as a result of the comments it receives. Hence, this tentative recommendation is not necessarily the recommendation the Commission will submit to the Legislature.

CALIFORNIA LAW REVISION COMMISSION
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TENTATIVE RECOMMENDATION

relating to

GARNISHMENT OF AMOUNTS PAYABLE TO TRUST BENEFICIARY

Existing law does not permit a judgment creditor to levy on the amounts payable to the judgment debtor from a trust.¹ Instead, the creditor must petition the probate court for an order that payments from the trust be applied to the satisfaction of the judgment by such means as the court, in its discretion, determines are proper.² If the trust is a spendthrift trust, the court must also determine the amount necessary for the education and support of the beneficiary which is protected from the creditor.³ A station-in-life test is used to determine the protected amount.⁴ The "surplus" income over the protected amount is subject to the creditor's claim.⁵

1. Code Civ. Proc. § 699.070(a)(8).
2. Code Civ. Proc. § 709.010.
3. See, e.g., Canfield v. Security-First Nat'l Bank, 13 Cal.2d 1, 11-12, 87 P.2d 830 (1939); see generally 7 B. Witkin, Summary of California Law Trusts § 94, at 5452-54 (8th ed. 1974).
4. See Canfield v. Security-First Nat'l Bank, 13 Cal.2d 1, 21-24, 87 P.2d 830 (1939); Magner v. Crooks, 139 Cal. 640, 642, 73 P. 585 (1903). Use of the station-in-life test has seldom given a creditor payment on a claim. Powell, The Rule Against Perpetuities and Spendthrift Trusts in New York: Comments and Suggestions, 71 Colum. L. Rev. 688, 699 (1971). The California Supreme Court has rejected the more extreme New York cases, but has continued to embrace the station-in-life test which considers factors such as the social background of the beneficiary and the need for servants. See, e.g., Canfield v. Security-First Nat'l Bank, 13 Cal.2d 1, 24-28, 87 P.2d 830 (1939). For criticisms of the station-in-life test, see Costigan, Those Protective Trusts Which Are Miscalled "Spendthrift Trusts" Reexamined, 22 Calif. L. Rev. 471, 484 (1934); Evans, "Observations on the State, Etc., of the California Laws of Uses and Trusts", 28 S. Cal. L. Rev. 111, 112-13 (1955); Note, 40 Calif. L. Rev. 441, 446-47 (1952).
5. Civil Code § 859. See also Code Civ. Proc. §§ 699.720(a)(8) (interest of trust beneficiary not subject to levy of execution), 709.010 (judicial procedure for reaching interest of trust beneficiary). If the trustee has discretion to determine the disposition of the trust income, the trustee may defeat the creditor's attempt to reach the "surplus" by reducing the amount to be paid to the beneficiary to the amount determined by the court to be necessary for the support and education of the beneficiary. See Estate of Canfield, 80 Cal. App.2d 443, 181 P.2d 732 (1947); E. Griswold, Spendthrift Trusts § 428 (2d ed. 1947).

The Commission recommends that the amounts payable to a trust beneficiary be made subject to garnishment under a writ of execution to the same extent as earnings. This will avoid the need to obtain a court determination that garnishment is an appropriate means to reach these amounts. In addition, adoption of the wage garnishment standard will provide detailed rules for determining the amount to be paid to the creditor by the trustee.

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,⁶ \$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 or her dependents, a hardship claim may be made.⁷ Where the garnishment is to collect delinquent amounts payable under a judgment for the support of a child or spouse or former spouse of the debtor, the creditor can reach one-half of the amount payable,⁸ but any party may apply to the court for an equitable division that varies this 50-50 division rule.⁹

The wage garnishment rules would replace the existing rule that permits a creditor of the beneficiary of a spendthrift trust to reach the surplus over the amount necessary for education and support of the beneficiary. Under existing law, it is necessary to obtain a court determination of the amount of the surplus in every case. Adoption of the wage garnishment rules would avoid the need for a court determination except in an unusual case.

6. Code Civ. Proc. § 706.050. This provision incorporates the federal standard provided in 15 U.S.C. § 1673(a) (1976) which protects an amount of disposable earnings per week equal to 30 times the federal minimum wage (currently \$3.35). Disposable earnings are earnings remaining after the deduction of taxes and other amounts required by law to be deducted. 15 U.S.C. § 1672(b) (1976).
7. Code Civ. Proc. § 706.051.
8. Code Civ. Proc. § 706.052.
9. 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.

The most convincing modern justification for protecting amounts payable from a spendthrift trust is that the "protection of impecunious beneficiaries is in accord with public policy, at least to the extent of keeping such beneficiaries from becoming public charges."¹⁰ The exemptions governing wage garnishment represent a balancing of the interest of the creditor and the interest of the debtor and are designed to minimize the need for judicial determinations. Wage garnishment exemptions are also applied when certain private retirement benefits or periodic payments of damages for personal injury or wrongful death are garnished.¹¹ It is appropriate to apply the same standards to the garnishment of payments from a spendthrift trust.

In the case of a spendthrift trust, the recommended legislation limits the amounts payable to the beneficiary that can be reached by the creditor to the amounts that could be reached on a like amount of earnings regardless of whether the creditor uses a writ of execution or some other procedure. The creditor of a beneficiary of a nonspendthrift trust can reach this same amount by garnishment under a writ of execution and will continue to have the right provided by existing law to apply for a court order to reach the entire interest of the beneficiary in the trust.

The recommended legislation would apply to all trusts, whether created before or after the date the legislation goes into effect.¹²

10. *Canfield v. Security-First Nat'l Bank*, 13 Cal.2d 1, 11, 87 P.2d 830 (1939). A similar policy supports the various exemptions from enforcement of a money judgment. See *Holmes v. Marshall*, 145 Cal. 777, 778-79, 79 P. 534 (1905); Tentative Recommendation Proposing the Enforcement of Judgments Law, 15 Cal. L. Revision Comm'n Reports 2001, 2075-76 (1980).
11. Code Civ. Proc. §§ 704.115(f) (retirement), 704.140(d) (personal injury), 704.150(c) (wrongful death).
12. It has long been settled that debtors have no vested right in exemption laws. See E. Griswold, *Spendthrift Trusts* § 391, at 483 (2d ed. 1947); Vukowich, Debtors' Exemption Rights, 62 Geo. L.J. 779, 865 (1974); 35 C.J.S. Exemptions § 6 (1960). See also Code Civ. Proc. §§ 703.050, 703.060. Application of a 10 percent garnishment statute to existing trusts was upheld in *New York. Brearly School v. Ward*, 201 N.Y. 358, 94 N.E. 1001 (1911).

Proposed Legislation

The Commission's recommendation would be effectuated by enactment of the following measure:

An act to amend Sections 699.720 and 709.010 of the Code of Civil Procedure, relating to trusts.

The people of the State of California do enact as follows:

405/930

Code of Civil Procedure § 699.720 (technical amendment). Property not subject to execution

SECTION 1. Section 699.720 of the Code of Civil Procedure is amended to read:

699.720. (a) The following types of property are not subject to execution:

(1) An alcoholic beverage license that is transferable under Article 5 (commencing with Section 24070) of Chapter 6 of Division 9 of the Business and Professions Code.

(2) The interest of a partner in a partnership where the partnership is not a judgment debtor.

(3) A cause of action that is the subject of a pending action or special proceeding.

(4) A judgment in favor of the judgment debtor prior to the expiration of the time for appeal from such judgment or, if an appeal is filed, prior to the final determination of the appeal.

(5) A debt (other than earnings) owing and unpaid by a public entity.

(6) The loan value of an unmaturing life insurance, endowment, or annuity policy.

(7) A franchise granted by a public entity and all the rights and privileges thereof.

(8) The interest of a trust beneficiary, other than amounts subject to execution under subdivision (c) of Section 709.010.

(9) A contingent remainder, executory interest, or other interest in property that is not vested.

(10) Property in a guardianship or conservatorship estate.

(b) Nothing in subdivision (a) affects or limits the right of the judgment creditor to apply property to the satisfaction of a money judgment pursuant to any applicable procedure other than execution.

Comment. Subdivision (a)(8) of Section 699.720 is amended to conform to subdivision (c) of Section 709.010 which permits execution on amounts payable to a judgment debtor as beneficiary under a trust.

405/939

Code of Civil Procedure § 709.010 (amended). Enforcement against trusts

SEC. 2. Section 709.010 of the Code of Civil Procedure is amended to read:

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 Except as provided in subdivision (c), 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 the judgment creditor to the 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) If payments in the form of cash or its equivalent are being made to the beneficiary from the trust or are to be made in the future, the amounts payable are subject to execution before payment. The amount of the payments that may be applied to the satisfaction of a money judgment by levy under a writ of execution is the amount that may be withheld from a like amount of earnings under Chapter 5 (commencing with Section 706.010) (Wage Garnishment Law). Any court determinations in connection with a levy under this subdivision, including but not limited to an exemption claim under Section 706.051 or a motion under Section 706.052, shall be made by the court where the judgment sought to be enforced was entered unless the levy is made pursuant to a court determination made under subdivision (b).

(d) Amounts payable to a beneficiary from a spendthrift trust may be applied to the satisfaction of a money judgment only in the amount determined as provided in subdivision (c), whether the amounts are

sought to be applied to the satisfaction of the judgment in a proceeding under subdivision (b) or by execution under subdivision (c) or both. If the trust is not a spendthrift trust, the amount that may be applied to the satisfaction of a money judgment in a proceeding under subdivision (b) is not limited to the amount determined as provided in subdivision (c).

~~(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~~

(e) Subject to subdivision (d), 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.

Comment. Subdivision (c) is added to Section 709.010 to make amounts payable to a trust beneficiary subject to garnishment under a writ of execution. This avoids the need to commence a proceeding under subdivision (b) to apply the beneficiary's interest to satisfaction of the money judgment. If levy is made under a writ of execution as provided in subdivision (c), the trustee is required to pay to the levying officer the nonexempt portion of payments that would otherwise be made to the beneficiary, regardless of the nature of the trust. See Sections 700.170 (levy on general intangibles), 701.010 (duty of garnishee), 701.050 (duty of account debtor). This duty continues during the period of the execution lien. See Sections 697.710 (duration of execution lien), 701.010 (duty of garnishee).

The amount to be applied to the satisfaction of the money judgment under a levy pursuant to subdivision (c) is the amount that could be withheld under the Wage Garnishment Law. The Wage Garnishment Law provides a formula for determining the amount to be paid to the judgment creditor. In the case of an ordinary judgment, the amount is determined by Section 706.050. Where the trust beneficiary can show that a greater amount is necessary for his or her support or the support of his or her dependents, the trust beneficiary may claim an exemption under Section 706.051. Where the execution is to collect delinquent amounts payable under a judgment for the support of a child, or spouse or former spouse, of the judgment debtor, the amount to be withheld is determined by Section 706.052. See also Sections 706.074 and 706.076.

In the case of a spendthrift trust, subdivision (c) provides the standard for determining the entire amount of payments that may be reached in the hands of the trustee. See subdivision (d). No greater amount of payments from such trusts may be subjected to enforcement of a money judgment. If the trust is not a spendthrift trust, the creditor may first levy on the amount permitted by subdivision (c) and also apply for a court order under subdivision (b) to reach the remainder of any payments. As an alternative, the creditor may apply to the court under subdivision (b) at the outset and the amount of payments subject to enforcement is determined under subdivision (d). The court in a hearing under subdivision (b) may determine any issue concerning whether the trust is a spendthrift trust and, if it is, the applicable exemption.

Application to existing trusts

SEC. 3. This act applies to all trusts, whether the trust is created before or after the operative date of this act.