Is an Irrevocable Spendthrift Trust Subject to Division in Divorce?

Good estate planning can oftentimes revolve around asset protection – will the assets left for the benefit of children be subject to the creditors of the children or be subject to seizure by an ex-spouse. A recent case from the Massachusetts Supreme Court held that assets in an irrevocable trust could not be divided in a divorce proceeding between one of the beneficiaries and that beneficiary's spouse.

In Pfannenstiehl v. Pfannenstiehl, 475 Mass. 105, 55 N.E.3d 933 (2016), the Massachusetts Supreme Court unanimously overturned a lower court decision that had ordered that assets in an irrevocable discretionary trust created by the husband's father be split in a divorce.

The husband's father created an irrevocable trust for the husband, his siblings, and their children. At the time of the divorce proceeding, the trust held property valued at $25 million and there were 11 beneficiaries.

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The irrevocable trust instrument states that distributions shall be made as follows:

[The trustees] shall pay to, or apply for the benefit of, a class composed of any one or more of the Donor's then living issue such amounts of income and principal as the Trustee, in its sole discretion, may deem advisable from time to time, whether in equal or unequal shares, to provide for the comfortable support, health, maintenance, welfare and education of each or all members of such class.

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The irrevocable trust also contains a spendthrift clause:

Neither the principal nor income of any trust created hereunder shall be subject to alienation, pledge, assignment or other anticipation by the person for whom the same is intended, nor to attachment, execution, garnishment or other seizure under any legal, equitable or other process.

The Massachusetts Supreme Court held that the husband's interest in the irrevocable trust should not have been awarded to the wife in the divorce, because the husband does not have sufficient ownership and control over the trust. As explained (citations omitted):

Interests in discretionary trusts generally are treated as expectancies and as too remote for inclusion in a marital estate, because the interest is not "present [and] enforceable"; the beneficiary must rely on the trustee's exercise of discretion, does not have a present right to use the trust principal, and cannot compel distributions. Diane attempts to distinguish the 2004 trust from a "pure" discretionary trust, however, by noting that distributions from the 2004 trust are subject to an "ascertainable standard" which governs the trustee's discretion. Under § 103 of the Uniform Trust Code, an "ascertainable standard" refers to a trust provision that requires a trustee to distribute funds to support a beneficiary's needs "relating to an individual's health, education, support or maintenance." See G. L. c. 203E, § 103. This standard limit's the discretion of the trustee, who is obligated to make distributions with an eye toward maintaining the beneficiary's standard of living in existence at the time the trust was created.

The trustee of a trust that contains an ascertainable standard must engage in a detailed inquiry into each beneficiary's needs and finances, and must "give serious and responsible consideration both as to the propriety of the amounts and as to their consistency with the terms and purposes of the trust." Such consideration must be "viewed in light of [the beneficiaries'] assets and needs, when measured against the assets of the trust." See G. L. c. 203E, § 803 (if trust has more than one beneficiary, trustee must give "due regard to the beneficiaries' respective interests").

The wife argues that, because the trustees of the 2004 trust must take the husbands standard of living into account when determining whether to make distributions, the husband has a present enforceable property right to compel distributions when he needs them. Her argument relies in large part on the Appeals Court's decision in Comins v. Comins, 33 Mass. App. Ct. 28 , 30-31 (1992), in which an interest in a discretionary trust with an ascertainable standard was deemed sufficiently certain to include the trust in the marital estate. In that case, the wife was the sole beneficiary of the trust. She received all of the trust income and held power of appointment over the trust upon her death. Unlike the spouse in Comins, however, the husband is one of eleven living beneficiaries among an open class of beneficiaries. The trustees of the 2004 trust are required to take into account the trust's long-term needs and assets, unpredictability in the stocks that fund it (which the judge found at times in the past have provided no income or have incurred a loss), the changing needs of the eleven current beneficiaries, and the possibility of additional beneficiaries.

The husband's present right to distributions from the 2004 trust is speculative, because the terms of the trust permit unequal distributions among an open class that already includes numerous beneficiaries, and because his right "to receive anything is subject to the condition precedent of the trustee having first exercised his discretion" in determining the needs of an unknown number of beneficiaries.