

UNITED STATES BANKRUPTCY COURT  
EASTERN DISTRICT OF WISCONSIN

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In re

CASEY R. WILBUR,

Debtor.

Case No. 03-37383

Chapter 7

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MEMORANDUM DECISION ON TRUSTEE'S MOTION TO TURN OVER ASSETS

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The debtor filed a chapter 7 petition on November 24, 2003, and listed his interest as beneficiary of an inter vivos trust created by his grandparents of approximately \$147,000, noting it was not part of the bankruptcy estate. The chapter 7 trustee subsequently moved the court for an order determining that the debtor's interest in the trust is included in the bankruptcy estate and for turnover. Bank One Trust Company, the designated trustee of the subject trust, intervened in the matter and opposed the motion for turnover. The parties agreed the matter could be decided as a matter of law and fully briefed the issue.

BACKGROUND

The debtor is the grandson of the donors of the trust, C.R. and Mary Margaret Wilbur. Both donors are deceased, and the debtor is the son of a deceased child of the donors. As such, the debtor was given the following rights under the trust:

Separate Trusts for Issue of a Deceased Child of the Donors. Each share so created for an issue of a deceased child of the Donors shall be held in a separate trust hereunder for the benefit of such issue. All of the assets of such separate trust shall be distributed to such issue upon attainment of thirty (30) years of age.

Trust Agreement of C.R. and Mary Margaret Wilbur 1991 Trust, Part I - Art. 7(c)(iii). The debtor has not yet turned 30 years of age.

Additionally, the trustee of the trust can make discretionary distributions of principal and income to the debtor in the trustee's sole discretion:

Distributions of Income and Principal From Separate Trusts. With respect to any separate trust created for a child or issue of a deceased child of the Donors, the Trustees, in their discretion, may distribute to or for the benefit of the beneficiary for whom such separate trust was created, or any issue of such beneficiary, such amounts of the income of the separate trust as the Trustees determine, or the Trustees may accumulate the income and add it to principal. The Trustees may also distribute to or for the benefit of any beneficiary who may receive net income, such amounts from the principal of such separate trust as the Trustees determine advisable for such person's education, health, maintenance in reasonable comfort or support in such person's accustomed manner of living. In the case of distributions of principal to a child of the Donors, the Trustees, in their discretion, may distribute principal which will increase the child's standard of living. The Trustees may also make principal distributions for the purposes set forth in subparagraph 7(b)(A) through (D).

Trust Agreement of C.R. and Mary Margaret Wilbur 1991 Trust, Part I - Art. 7(c)(iv). The debtor's interest in the trust is protected by a spendthrift provision:

[T]his Trust Agreement is intended for the personal protection and welfare of the beneficiaries of the trusts hereunder, and no interest in any trust hereunder shall be susceptible of assignment, anticipation, hypothecation or seizure by legal process.

Trust Agreement of C.R. and Mary Margaret Wilbur 1991 Trust, Part II - Art. 11(a).

## ARGUMENTS

Because the debtor has a present right to discretionary distributions of income and principal and an unconditional right to all assets in the trust, contingent upon his survival to age 30, the bankruptcy trustee's position is that Wis. Stats. § 701.06(2) authorizes an order directing payment of those funds to the bankruptcy trustee whenever the right to distribution arises. Accordingly, the trustee seeks an order

from this court requiring Bank One to turn over the funds in the trust on the date the debtor turns 30 years of age, as well as any discretionary distributions prior to age 30. The bankruptcy estate would remain open until all funds were collected and distributed pursuant to bankruptcy law.

Bank One, as trustee of the trust, argues the future interest of the debtor should be excluded from the bankruptcy estate because the applicable spendthrift provision in the trust restricts alienation of that future interest. Section 701.06(2), Wis. Stats., only allows a judgment creditor to apply for a court order for payment from a spendthrift trust *after* any payments of principal have become due or payable to the beneficiary. Distributions from the trust are discretionary with the trustee, and the debtor cannot control those distributions. Because the debtor has not yet turned 30, neither the debtor nor the bankruptcy trustee have any right to the trust corpus.

#### DISCUSSION

Traditionally, there are three requirements for a spendthrift trust: (1) The settlor may not be a beneficiary of the trust; (2) The trust must contain a clause barring any beneficiary from voluntarily or involuntarily transferring his interest in the trust; and (3) The debtor-beneficiary must have no present dominion or control over the trust corpus. *See* Restatement (Third) of Trusts § 58 (2003). All three of these conditions are met by the subject trust.

The issue of whether a spendthrift trust is property of the estate is affected by the operation of 11 U.S.C. § 541(c)(2) and, in some instances not applicable here, 11 U.S.C. § 541(a)(5). Property of the debtor held in trust becomes property of the estate under 11 U.S.C. § 541(a)(1), except to the extent that a restriction on transfer of a spendthrift trust is enforceable under applicable nonbankruptcy law. Relevant state law provides:

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 of part or all of the judgment.

Wis. Stat. § 701.06(2).

The restriction in the debtor's grandparents' trust complies with this statutory provision regarding alienation of the beneficiary's interest. There is no indication that the trust provisions which prevent the debtor from voluntarily transferring his beneficial interest and which prevent creditors from enforcing judgments against his interest in principal or income are in any way unenforceable under applicable Wisconsin law. If the statute stopped at the point regarding restrictions on alienation, 11 U.S.C. § 541(c)(2) clearly excludes the debtor's interest in the trust from property of the bankruptcy estate. However, the same statute goes on to provide "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." Wis. Stat. § 701.06(2) (emphasis added). The bankruptcy trustee wishes to use this provision to bring the trust assets into the estate after the date of filing when the debtor turns 30 or receives other distributions.

The trustee cites *In re Calaway*, No. 99-54197-7 (Bankr. W.D. Wis. June 30, 2000) (full text available at 2000 WL 33950024), in support of his motion for turnover. In that case, the chapter 7 debtor was the beneficiary of a trust which provided for an ultimate distribution of the trust res at the time the youngest grandchild of the grantor attained the age of 30, approximately seven years after the

date of the petition. The *Calaway* court found support in *Meyer v. Reif*, 217 Wis. 11, 258 N.W. 391 (1935), which held that a creditor's judgment could be satisfied from a beneficiary's interest in the principal of a trust, despite the fact that the beneficiary would not receive the principal until age 25. The *Meyer* court's conclusion was based on previous statutory authority which declared that "the rights and interests of every person for whose benefit a trust for the payment of a sum in gross is created are assignable." *Meyer*, 258 N.W. at 392 (citing Wis. Stat. § 231.19, which was repealed and renumbered by L.1969, c. 283, §§ 2 to 4, eff. July 1, 1971). Such reliance undercuts the *Calaway* reasoning as the current statute allows a restriction on assignment. The bankruptcy court also found that the trust language, stating the trust would not terminate if a beneficiary's share was threatened with recovery by a creditor, did not overcome the express statutory directive in Wis. Stat. § 701.06(2) that allows a creditor to pursue the trust principal when it became subject to distribution. Therefore, the court held that the trust *was* subject to the claims of creditors, which removed it from the exclusionary protection of 11 U.S.C § 541(c)(2). While the trust termination language is different in the present case, this court is not persuaded that Wis. Stat. § 701.06(2) assists the bankruptcy trustee in bringing the trust into the estate.

Property of the estate is determined at the time of filing. 11 U.S.C. § 541(a). If the trust was excluded from property of the estate as of the date of filing by § 541(c)(2), it follows that any future interest in the excluded asset is likewise excluded. Section 541(a)(5) provides that specific types of property acquired by the debtor within 180 days of filing can be brought into the estate, but the

termination and distribution of a spendthrift inter vivos trust is not one of them.<sup>1</sup> The passage of time, coupled with the debtor's continuing to survive, does not turn an excluded asset into property of the estate. The assets of the trust are not the debtor's property at the time of filing, and unless the debtor survives the age of mandatory distribution which occurs after the date of filing, the assets will never be his property. The donors provided for disposition of the assets if he fails to survive the date of distribution.

Although other courts have not specifically applied Wisconsin law to future interests in spendthrift trusts, as this court is obligated to, they have come to similar conclusions under similar state laws. In *In re Schauer*, 246 B.R. 384 (Bankr. D. N.D. 2000), the chapter 7 debtor's future interest in receiving, after his mother died, a distributive share of the corpus of a trust created by his father was excluded from the bankruptcy estate. The language of the trust's spendthrift provision effectively prohibited alienation of the debtor's future interest in the trust corpus as well as his interest in income from the trust. The court's interpretation of the spendthrift provision was consistent with the settlor's intent to prohibit alienation of the debtor's interests, and there was no indication that the spendthrift provision was unenforceable under applicable North Dakota law. *Id.* at 389; *see also In re Conner*, 233 B.R. 358 (Bankr. N.D. W. Va. 1999) (holding to extent that spendthrift trust had not terminated prepetition, debtor-beneficiary's interest therein, being subject to restriction on transfer which was enforceable under applicable nonbankruptcy law, was not included in property of chapter 7 estate).

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<sup>1</sup>Even if the debtor's 30<sup>th</sup> birthday fell within 180 days after filing, which it does not, the termination and distribution of an inter vivos trust would not result in acquisition by the beneficiary by "bequest, devise, or inheritance" and therefore would not fall within one of the categories of included property. *See In re Spencer*, 306 B.R. 328 (Bankr. C.D. Cal. 2004).

In *Matter of Newman*, 903 F.2d 1150 (7<sup>th</sup> Cir. 1990), the debtor had been named beneficiary of two inter vivos trusts that provided for payments to be made to him until his 50<sup>th</sup> birthday, at which time the trust would terminate, and he would receive its corpus. The trust agreements also contained spendthrift provisions that were effective under applicable state (Missouri) law. The debtor filed his bankruptcy case when he was 45 years old, and the trustee argued that because the debtor would receive the trust corpus in five years, the court should include the present value of this amount as part of the debtor's estate. The court rejected this argument, noting that "[t]he point of a spendthrift trust ... is to prevent exactly this sort of anticipation by beneficiaries and their creditors," and that "[t]he Bankruptcy Code is designed to further that goal." *Id.* at 1153.

In *In re Baydush*, 171 B.R. 953, 958 (E.D.Va. 1994), the debtor was the beneficiary of two testamentary spendthrift trusts created by his grandparents. The language of the trusts provided that the corpus of the trusts would not be distributed to the debtor until his parents, his aunt, and his uncle died, and all grandchildren living at the time of the testator's death either themselves died or reached the age of 25. At the time of the debtor's filing for bankruptcy, neither of the debtor's parents, his aunt, nor his uncle had died. Therefore, his interest in the trust corpus was held to be a future interest, i.e., a contingent remainder. The court held that the debtor's contingent remainder interests in the corpus of the trusts were subject to the spendthrift provisions of the trusts, and therefore were nontransferable. *Id.* at 956-59. Thus, pursuant to § 541(c)(2), the trusts were not included in the debtor's bankruptcy estate. *Id.* at 958.

The Wisconsin statute quoted above does not bring a future interest into the estate. The statute addresses what happens when a judgment creditor's rights have been determined at the time of

distribution of trust principal. The creditor cannot acquire an interest prior to that time. Nevertheless, the judgment creditor could wait out the termination of a trust and have a court direct distribution to the creditor at that time, as long as the judgment is enforceable. The longevity of this provision under state law does not nullify the fact that we must determine property of the bankruptcy estate at a particular time and that a wealth of bankruptcy law supports the right of trust donors to determine how their assets are to be used.

There is no evidence whether Bank One has made discretionary distributions of income or principal since the bankruptcy was filed, but the bankruptcy trustee has demanded turnover of any current distributions in addition to his demand for the mandatory age 30 distribution when the time comes. However, if the right to discretionary distributions of income and principal is considered an interest in the trust, and this court holds that it is, the spendthrift clause covers *all* interests. The clause prevents assignment, anticipation, hypothecation or seizure of the debtor's current interest as well as his future interest. In sum, § 541(c)(2) of the Bankruptcy Code thus excludes the debtor's beneficial present and future interest in the trust from property of the estate. The bankruptcy trustee can only demand turnover of certain enumerated property under § 542(a). As the court has held the trust is not property of the estate, it follows that the trustee cannot use, sell, or lease the trust or trust assets under § 363. The debtor cannot claim his interest in the trust exempt under § 522(b) because that section only applies to property of the estate. Furthermore, the trust and its assets are not property of



the debtor because the debtor has no ownership or control over them. Therefore, the trust meets none of the requirements for turnover to the bankruptcy trustee under 11 U.S.C. § 542(a).<sup>2</sup>

The trustee's motion for turnover is denied. A separate order will be entered accordingly.

Dated: March 11, 2005.

BY THE COURT:

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Honorable Margaret Dee McGarity  
Chief United States Bankruptcy Judge

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<sup>2</sup>In its motion to intervene, BankOne Trust Company referred to itself as a "custodian" of the trust assets. However, the trustee of an inter vivos trust is not a custodian under 11 U.S.C. § 101(11), and the turnover section applicable to custodians, 11 U.S.C § 543, does not apply.

UNITED STATES BANKRUPTCY COURT  
EASTERN DISTRICT OF WISCONSIN

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CASEY R. WILBUR,

Debtor.

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ORDER DENYING TRUSTEE'S MOTION TO TURN OVER ASSETS

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For the reasons stated in the court's memorandum decision entered on this date,

IT IS ORDERED the trustee's motion to turn over assets is denied.

Dated: March 11, 2005.

BY THE COURT:

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Honorable Margaret Dee McGarity  
Chief United States Bankruptcy Judge