

# The Decline and Fall of the Spendthrift Clause

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## I. HISTORY

The law has long recognized a settlor's right to restrict the use of trust assets by beneficiaries. These restrictive provisions are commonly called "spendthrift" provisions. As Professor Bogert explains in his treatise:

Subject to qualifications later noted, a spendthrift trust is one in which, by director of the settlor [trustor] or as a result of a statute, a trust beneficiary cannot alienate the right to payments, and the beneficiary's creditors may not subject the beneficiary's interest in the trust to the beneficiary's debts. The spendthrift clause protects the beneficiary's right to obtain benefits in the future, but not money or other property that the beneficiary has already received from the trustee. A spendthrift clause does not restrain the beneficiary's power to transfer the property that the trustee has already delivered over, or the creditor's power to reach that property for the collection of their claims.

Bogert & Shapo, *The Law of Trusts & Trustees* (3rd ed., Thompson West, 2007) §221, p. 385 ("**Bogert**").<sup>1</sup>

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1. The Bogert treatise notes that spendthrift trusts generally are enforceable in the United States; however, they are not enforced in England. Instead, the customary practice under English law is to provide substitutes for spendthrift trusts, such as a discretionary trust whereby the trustee is given absolute discretion as to payment of any benefit or as to the selection of beneficiary, or a protective trust which provides for the termination or forfeiture of a beneficiary's interests upon any purported transfer or creditor action. Such substitutes would be of dubious enforceability under the laws of the various United States, and certainly under California's laws. See, e.g., *Ells v. Order of United etc. Travelers* (1942) 20 Cal.2d 290, 301 (it is well settled that forfeitures are not favored by either courts of law or equity); California Probate Code §16080-16081 (a trustee who is given a discretionary power must act reasonably and be subject to court review).

Although the law of spendthrift trusts is generally codified, it is not uniform throughout the United States. Nevertheless, as Professor Bogert concludes, spendthrift trusts are generally enforceable throughout the United States, citing the Latin phrase of "*cujus est dare, ejus est disponere*" as the underlying principle, meaning 'he who gives anything can also direct how the gift is to be used.' See Bogert, at §222, p. 396. See also Black's Law Dictionary (7th ed. 1999), p. 1627 (interpreting the legal maxim to mean that the bestower of a gift has a right to regulate its disposal).

The corollary to the rules of spendthrift provisions is the principle that, once the money or property to be distributed is in the hands of the beneficiary, then it is no longer a trust asset and fair game for creditor action. As succinctly explained by Justice Seawall in the 1938 decision of *Kelly v. Kelly*:

It is of the essence of a spendthrift trust that it is not subject to voluntary alienation by the *cestui*, nor subject to involuntary alienation through attachment or other process at the suit of his creditors. But it is everywhere agreed that after the beneficiary has actually received the trust property his creditors may reach it and he may dispose of it as he wishes. A voluntary assignment executed before payment to the beneficiary confers on the assignee no right to demand payment or delivery from the trustee as it becomes due to the beneficiary.

*Kelly v. Kelly* (1938) 11 Cal.2d 356, 362-363. Hence, and at least historically, the spendthrift provision no longer has any effect, and does not protect against creditor action, once the funds are actually distributed by the trustee to a beneficiary.

## **II. RELATED TRUST CONCEPTS**

Spendthrift trusts provide that a beneficiary's interest may not be alienated, assigned to creditors, or otherwise anticipated by the beneficiary. With such trusts, the trustee might have no discretion over when to make payments or how much to pay. Note that a spendthrift trust need not be limited to providing only for a

beneficiary's needs, though such a purpose is presumed unless another is stated in the trust. *See, e.g.*, 60 Cal.Jur.3d, Trusts, §127.

A related concept is a "discretionary trust," which is customarily intended to provide for a beneficiary's support. Presumably some or all of the payments to the beneficiary will be mandated; in other words, not all distributions are left to the trustee's discretion. However, depending upon the terms of the trust, it may also allow a trustee discretion to make payments beyond, or regardless of, what is necessary for the beneficiary's support.<sup>2</sup>

Similarly, a "support trust" provides the trustee with discretion as to making payments and determining what the beneficiary needs. It differs from a discretionary trust in that the discretion is exercised pursuant to a standard set forth in the instrument or otherwise provided by law, rule, or regulation. Often times the trust instrument (or a statute) will require that certain minimum payments be made periodically regardless of the trustee's discretion.

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2. If trust distributions are solely in the trustee's discretion, the beneficiary's creditors cannot compel the trustee to make discretionary distributions to the beneficiary. *See* California Probate Code §15303. In general, a trustee who is given a discretionary power must act reasonably. California Probate Code §16080. The trustee's exercise of discretion is subject to review by the court. Even if a trustee is provided "sole," "absolute," or "uncontrolled" discretion, the trustee must nevertheless act in accordance with fiduciary principles and not in bad faith or in disregard of the purposes of the trust. California Probate Code §16081(a). The case of *Young v McCoy* (2007) 147 CA4th 1078 is instructive. In *Young v. McCoy*, the California Court of Appeal held that a trustee of discretionary support trust did not abuse her discretion in determining that no distributions should be made to beneficiary who was serving life sentence in prison for attempted murder. The facts are salacious, in that the trustee was the mother of the beneficiary, who had been incarcerated for attempting to kill the mother's other child, his brother. However, the Court of Appeal determined that the trustee had permissibly exercised her discretion to make no payments to the beneficiary of the trust, as he was incarcerated, enjoying the taxpayer's support, and not presently in need of monetary benefits. In the absence of a showing of bad faith, the trustee's actions were presumed valid. Consequently, there was no abuse of the trustee's discretion. Therefore, the trust beneficiary's judgment creditor (the victim brother) could not compel trustee (mom) to make discretionary payments to the beneficiary (the criminal brother), which payments would be used to satisfy the judgment.

California case law, much like other jurisdictions, sometimes conflates the discretionary and support trusts. And, of course, many if not all such trusts could and would include spendthrift provisions.

### III. CALIFORNIA'S SPENDTHRIFT LAWS

In California, the spendthrift laws are codified in California Probate Code §§15300 et seq. *See Canfield v. Security First National Bank* (1935) 8 Cal.App.2d 277, 282-283; *Estate of Johnston* (1967) 252 Cal.App.2d 923, 925.

See California Probate Code §§15300-15309 attached.
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Pursuant to those statutes, if a trust instrument provides that a beneficiary's interest in interest or principal is not subject to voluntary or involuntary transfer, then the beneficiary's interest may not be transferred and is not subject to enforcement of a money judgment until paid to the beneficiary. *See California Probate Code §§15300 & 15301.*

The validity of a spendthrift provision is predicated upon the idea that a person is free to dispose of their property as they see fit. *Seymour v. McAvoy* (1898) 121 Cal. 438, 442; *Estate of Johnston, supra*, 252 Cal.App.2d at 925. It is California's policy to effectuate intentions expressed in a trust or other testamentary instrument. California Probate Code §21102. *See Brown v. Labow* (2007) 157 Cal.App.4th 795, 812. As explained by the California Supreme Court in 1898:

By the great weight of authority in America, it is settled that the author of a trust to pay to or apply for the benefit of another the income of property, or a portion of such income, may lawfully provide that the interest of the beneficiary shall not be assignable, or shall not be subject to the claims of his creditors. []

It is also well settled in the jurisdictions where this doctrine prevails that such provisions need not be express, but may be implied from the general intention of the donor, to be gathered from the terms of the trust, in the light of all the circumstances. []

The decisions in England and in some of the American states limit this doctrine to cases where there is an express provision for a lesser or limitation of the estate upon any alienation, or upon bankruptcy, levy of execution, or the like. But we think that the rule established by the decisions we have cited is more consonant with the rules of law and with the principles of reason. *Alienability is not an essential attribute of an equitable life estate in property; and there is nothing in the policy of the law prohibiting a donor from providing that his bounty shall be enjoyed only by those to whom he intends to extend it, and that property devoted by him to a trust otherwise valid shall not be diverted from its appointed destination.*

*Seymour v. McAvoy, supra*, 121 Cal. at 442-443. The case of *Seymour v. McAvoy* provided one of the first expositions as to the validity of spendthrift clauses under California law. It was also the first published case in California to clearly adopt the principle that such provisions need not be explicitly stated in the subject trust instrument but may be, essentially, presumed from less explicit expressions set forth in that instrument.

Thus, we have the modern principle of law of which most estate planners and related professions are aware: the interest(s) of each beneficiary in a spendthrift trust, both as to income and principal, are protected from the claims of creditors taken or to be taken by any legal or equitable process. Because the subject of the creditor's action is money or property belonging to the trustor(s), not the beneficiary, and the trustor(s) wanted their beneficiary protected from that beneficiary's own improvidence, then those trust assets are protected from attack by the beneficiary's creditors.

The primary statutory expression of modern California spendthrift rule is set forth in California Probate Code §§15300 and 15301, which state as follows:

California Probate Code 15300:

Except as provided in Sections 15304 to 15307, inclusive, if the trust instrument provides that a beneficiary's interest in income is not

subject to voluntary or involuntary transfer, the beneficiary's interest in income under the trust may not be transferred and is not subject to enforcement of a money judgment until paid to the beneficiary.

California Probate Code §15301:

(a) Except as provided in subdivision (b) and in Sections 15304 to 15307, inclusive, if the trust instrument provides that a beneficiary's interest in principal is not subject to voluntary or involuntary transfer, the beneficiary's interest in principal may not be transferred and is not subject to enforcement of a money judgment until paid to the beneficiary.

#### **IV. EXCEPTIONS AND LIMITATIONS**

##### **A. The decline of Protections Offered by the Spendthrift Rule**

California, like almost all other jurisdictions, has over time expanded the class of persons permitted to avoid operation a spendthrift clause in satisfaction of obligations owed by beneficiaries. A natural consequence of that expansion has, in some cases, frustrated the intent of the trustors. This expansion in favor of creditors has, out of necessity, led to a corresponding decline in the protections offered to beneficiaries (and trustors) by the spendthrift rules.

As previously mentioned, California has codified its spendthrift rules and exceptions in California Probate Code §§15300 et seq. Many but not all of the exceptions are based on public policy considerations. For instance:

- ***Settlor as a Beneficiary (aka Self-Settled Trust)*** — This is probably the best-known exception to the spendthrift rule. Although such a trust is not deemed void, California will not give effect to spendthrift provisions in a self-settled trust so as to prevent individuals from placing their property beyond the reach of their creditors while at the same time still reaping the bounties of such property. *See* California Probate Code §15304(a). It is against public policy to permit a person to tie up their property in trust in such a way that he can enjoy it but prevent his

creditors from reaching it. *Nelson v. California Trust Co.* (1949) 33 Cal.2d 501 (where the person makes himself a beneficiary of such a trust, then any restraints in the instrument on the involuntary transfer or alienation of the person's interest in the trust are invalid and ineffective).

- ***Claims for Child and Spousal Support*** — The obligation to support both minor children and former spouses is based on clear legislative directives and public policy in California. *See, e.g.,* California Family Code §§3900 & 4053 ("[a] parent's first and principal obligation is to support his or her minor children"); *Marriage of Smith* (1990) 225 Cal.App.3d 469, 480-481 (spousal support). Not surprisingly, this policy finds expression in the area of spendthrift trusts, such that a beneficiary of a trust cannot avoid his duties of support. California Probate Code §§15305 and 15306 provide support claimants certain preferences and exemptions from spendthrift rules.

- ***Restitution Judgments*** — *See* California Probate Code §15305.5, which excepts from the spendthrift rule certain judgments awarding restitution for certain damages arising from acts upon which a defendant was convicted of a felony.

IMPORTANT: For purposes of this discussion, it is important to review following statutes which we will soon see appeared to conflict and therefore flummoxed our good friends sitting at the Ninth Circuit Court of Appeals:

California Probate Code §15301:

...

**(b) After an amount of principal has become due and payable to the beneficiary under the trust instrument, upon petition to the court under Section 709.010 of the Code of Civil Procedure by a judgment creditor, the court may make an order directing the trustee to satisfy the money judgment out of that principal amount. The court in its discretion may issue an order directing the trustee to satisfy all or part of the judgment out of that principal amount.**

California Probate Code §15306.5:

(a) Notwithstanding a restraint on transfer of the beneficiary's interest in the trust under Section 15300 or 15301, and subject to the limitations of this section, upon a judgment creditor's petition under Section 709.010 of the Code of Civil Procedure, the court may make an order directing the trustee to satisfy all or part of the judgment out of the payments to which the beneficiary is entitled under the trust instrument or that the trustee, in the exercise of the trustee's discretion, has determined or determines in the future to pay to the beneficiary.

**(b) An order under this section may not require that the trustee pay in satisfaction of the judgment an amount exceeding 25 percent of the payment that otherwise would be made to, or for the benefit of, the beneficiary.**

California Probate Code 15307

Notwithstanding a restraint on transfer of a beneficiary's interest in the trust under Section 15300 or 15301, **any amount to which the beneficiary is entitled under the trust instrument or that the trustee, in the exercise of the trustee's discretion, has determined to pay to the beneficiary in excess of the amount that is or will be necessary for the education and support of the beneficiary may be applied to the satisfaction of a money judgment against the beneficiary.** Upon the judgment creditor's petition under Section 709.010 of the Code of Civil Procedure, the court may make an order directing the trustee to satisfy all or part of the judgment out of the beneficiary's interest in the trust.

**B. Judgment Creditors and the *Carmack/Frealy* Cases**

So, as we have seen, notwithstanding a valid restraint on the transfer of a beneficiary's interest in a trust, and subject to the limitations of California Probate Code §§15300-15307, a judgment creditor may apply to, move, or petition a court pursuant to California Code of Civil Procedure §709.010 for an order directing the trustee of a trust to satisfy all or part of the judgment out of the payments to which a judgment debtor beneficiary is entitled pursuant to the trust instrument.



These procedures are the **only** means available for a judgment creditor to enforce a money judgment against a judgment debtor's interest in a trust. California Code of Civil Procedure §§709.010(b) & (c). However, the judgment creditor's rights remain expressly subject to the limitations of California Probate Code §§15300 *et seq.* & 15306.5. *See generally* California Code of Civil Procedure §709.010(c).

<p><i>See California Code of Civil Procedure §709.010 attached.</i></p>
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The California Supreme Court recently (2017) clarified the extent of those exceptions and limitations in *Carmack v. Reynolds* (2017) 2 Cal.5th 844 ("**Carmack**"). The *Carmack* ruling was then applied in the Ninth Circuit Court of Appeals proceeding of *Frealy v. Reynolds (In re Reynolds)* (9th Cir., Aug. 15, 2017) 867 F.3d 1119 ("**Frealy**"). The background is important to understand:

*First – Spendthrift Trust Created*

Mr. and Mrs. Reynolds created the Reynolds Family Trust in 2005. The couple resided in California. The Reynolds Family Trust instrument was revocable, and it named Mr. and Mrs. Reynolds themselves as the original trustees. The instrument also contained a typical spendthrift provision, which stated:

*"no interest in the income or principal of any trust created under this instrument shall be voluntarily or involuntarily anticipated, assigned, encumbered, or subjected to creditor's [sic] claim or legal process before actual receipt by the beneficiary."*

Ms. Reynolds died a few years after the trust was created. And a few years after that, Mr. Reynolds also died. One of the named beneficiaries was their child Rick, who was to receive \$250,000 so long as he survived his father by 30 days. He would also receive another \$100,000 per year for the next 10 years, and then one-third of whatever was left in the Reynolds Family Trust by that time. It was expected that those payments were to be made from the Trust's principal since, at the time of Mr. Reynold's death, the trust assets were mostly in undeveloped real estate estimated to be worth several million dollars but which otherwise produced little income.

*Second – Debtor Bankruptcy*

Because he had creditors, Rick filed a voluntary bankruptcy petition under Chapter 7 the day after his father passed away. Unlike a Chapter 11

reorganization, or Chapter 13 wage earner rehabilitation, a Chapter 7 bankruptcy is traditional bankruptcy case (i.e., liquidation). This means that a bankruptcy estate is created as of the date of the filing for relief, comprised of all legal and equitable interests of the debtor, which is then held by a trustee appointed by the federal bankruptcy court (i.e., "Bankruptcy Trustee") who seeks to sell, dispose of the debtor's valuable assets, if any, after providing for all legal exemptions, which the goal of providing net proceeds to the creditors and other interested persons in accordance with priorities established under applicable bankruptcy and non-bankruptcy laws. Under applicable bankruptcy law, the Bankruptcy Trustee stands in the shoes of a hypothetical judgment creditor with respect to any and all assets of the judgment debtor-beneficiary.

Rick's bankruptcy schedules showed \$1.744 million in liabilities against \$1.370 million in assets.

### *Third – Bankruptcy Court Decision*

The Trustees of the Reynolds Family Trust sought a declaratory judgment as to the Bankruptcy Trustee's interest in the trust, asserting that the Bankruptcy Trustee was limited to 25% of payments from the trust to Rick pursuant to California Probate Code §15306.5.<sup>3</sup>

The bankruptcy judge ruled that the Bankruptcy Trustee was entitled to no more than the 25% cap provided by California Probate Code §15306.5.

The Bankruptcy Appellate Panel ("BAP") of the Ninth Circuit Court of Appeals affirmed the decision in 2011, ruling that California Probate Code §15307 applied only to distributions of income, and was therefore inapplicable. Notably, the BAP ruling did not address the Bankruptcy Trustee's contentions with respect to California Probate Code §15301(b), discussed more fully below.

### *Fourth – Appeals within Ninth Circuit*

A further appeal was taken by the Bankruptcy Trustee to the Ninth Circuit Court of Appeals as a whole, which declared that it was unable to decide the issue (stating that California's spendthrift statutes were "opaque"). Instead, in February of 2015, it certified a question to the California Supreme Court to decide how to interpret and apply the apparently-conflicting provisions of

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3. This set up an interpretation as to how to interpret and apply the various provisions of the California Probate Code regarding spendthrift provisions. In particular, the bankruptcy judge was called upon to determine how California Probate Code §§15301 and 15306.5 were to be interpreted. In other words, were Rick's creditors completely shut out from recovering against Rick's interests in the assets in the Reynolds Family Trust under §15301, or were they entitled to 25% of the amount to which Rick is himself entitled under §15306.5?

California Probate Code §§15301(b), 15306.5 and 15307, which the Ninth Circuit was unable to reconcile. The Ninth Circuit's question was as follows:

**Does section 15306.5 of the California Probate Code impose an absolute cap of 25 percent on a bankruptcy estate's access to a beneficiary's interest in a spendthrift trust that consists entirely of payments from principal, or may the bankruptcy estate reach more than 25 percent under other sections of the Probate Code?**  
[presumably "other sections" here means California Probate Code §§15301(b), 15306.5, and 15307 which seem to conflict on their face]

The California Supreme Court subsequently decided to accept the question.

*Fifth – Decision by the California Supreme Court*

After a few years (!) of waiting, the Court finally attempted to provide an answer in March of 2017.

After a lengthy review of the legislative history of California Probate Code §§15306.5 and 15307, the Court decided that §15307 "reflects a drafting error" and that the 25% limitation should have been applied to §15307 as well but was inadvertently omitted. Nevertheless, considering the provisions of §15301(b), which provides that once a distribution of principal has become due and payable, all of the said distribution may be ordered to the creditor, the Court concluded that the 25% limitation did not apply where a distribution had *already* come due to a beneficiary. Instead, the 25% limitation only applied to an order that sought to obtain distributions, including *future* distributions, for principal and income that remain subject to trust (i.e., not currently "due and payable"). The Court reasoned that once a distribution has become due and payable to the beneficiary, it is now the beneficiary's asset and therefore the spendthrift protection should no longer apply.

The Court held as follows:

"In sum, after an amount of principal has become due and payable (but has not yet been distributed), a creditor can petition to have the trustee pay directly to the creditor a sum up to the full amount of that distribution (sec. 15301(b)) unless the trust instrument specifies that the distribution is for the beneficiary's support or education and the beneficiary needs the distribution for those purposes (sec. 15302). If no such distribution is pending or if the distribution is not adequate to satisfy a judgment, a general creditor can petition to levy up to 25 percent of the payments expected to be made to the beneficiary, reduced by the amount other creditors have already obtained and subject to the support needs of the beneficiary and any dependents. (sec. 15306.5.)

"As an illustration, suppose a trust instrument specified that a beneficiary was to receive distributions of principal of \$10,000 on March 1 of each year for 10 years. Suppose further that a general creditor had a money judgment of \$50,000 against the beneficiary and that the trust distributions are neither specifically intended nor required for the beneficiary's support. On March 1 of the first year, upon the creditor's petition a court could order the trustee to remit the full distribution of \$10,000 for that year to the creditor directly if it has not already been paid to the beneficiary, as well as \$2,500 from each of the nine anticipated payments (a total of \$22,500) as they are paid out. If the creditor were not otherwise able to satisfy the remaining \$17,500 balance on the judgment, then on March 1 of the following years, upon the general creditor's petition the court could order the trustee to pay directly to the creditor a sum up to the remainder of that year's principal distribution (\$7,500), as the court in its discretion finds appropriate, until the judgment is satisfied."

And so the Court then answered the certified question by the Ninth Circuit and returned the case to the federal court system for further proceedings.

#### *Sixth – Application by Bankruptcy Court System*

The ruling meant that the Bankruptcy Trustee could reach 100% of any distributions that were already due and payable to Rick, meaning the \$250,000. Second, it meant that the Bankruptcy Trustee could also reach future payments to be made to Rick, but that it was limited to 25% of those payments and with support payments excluded (in other words, the Bankruptcy Trustee would be able to reach 25 percent of expected future trust distributions, reduced by amounts needed by the beneficiary to support and support of any dependents).

### **C. What Does this Mean?**

The drastic revision in California law delivered by the *Carmack* and *Frealy* cases are summarized as follows:

- **As to amounts which are "due and payable" to a judgment debtor from a spendthrift trust:**

Applying *Carmack* and *Frealy*, the rule now is that the spendthrift restraints no longer apply to prohibit a judgment creditor's ability to obtain an order applying any amounts which are already "due and payable" to a

judgment debtor. That is, after an amount of principal has become due and payable, but has not yet been distributed, a creditor can petition to have the trustee pay directly to the creditor a sum up to the 100 percent of that distribution unless the subject trust instrument expressly specifies that the distribution is for the beneficiary's support or education and, also, that the beneficiary actually needs the distribution for those specific purposes.

The California Supreme Court reasoned that once a distribution has become due and payable to the beneficiary, it is now the beneficiary's asset, and not a trust asset, and so, therefore, the spendthrift protection should no longer apply.

- **As to amounts which are NOT already "due and payable" to a judgment debtor from a spendthrift trust (i.e., "future" payments):**

Applying *Carmack* and *Frealy*, the rule now is that the spendthrift restraint applies to prohibit a judgment creditor's ability to obtain an order applying any amounts which are NOT already "due and payable" to a judgment debtor. As to any such "future" payments, the statutory spendthrift rules remain applicable. Hence, a judgment creditor is entitled to satisfy its judgment out of the payments to which a judgment debtor beneficiary is entitled -- so long as the payment does not exceed 25 percent of the payment that otherwise would be made to the beneficiary. California Probate Code §15306.5(b). In other words, as to future payments, the spendthrift provision completely protects 75 percent of the beneficiary's interest in the trust; the remaining 25 percent, subject to limitation, could be available to the judgment creditor.

Moreover, the court may not order the trustee to withhold from a distribution due to a beneficiary any more than 25 percent thereof for the

benefit of all judgment creditor(s) who have obtained a remedy pursuant to California Probate Code §15306.5(b) and California Code of Civil Procedure §709.010. See California Probate Code §15306.5(f).

In addition, again as to such "future" payments, the judgment creditor cannot receive any amount required to support the beneficiary or the beneficiary's dependents. California Probate Code §15306.5(c).

- **What *Carmack* and *Frealy* did not determine:**

The logical result of the scheme set out by the court, which is that a judgment creditor appears to have to make a choice:

Choice 1 -- Wait until a distribution becomes due and payable, and thereafter apply, move, or petition for an order for that distribution, with the hope to receive 100 percent of it;

Choice 2 -- Apply, move, or petition a court for an order regarding future payments, which are subject to the 25 percent restriction.

The former, of course, risks the distribution being made to the debtor in the short time between the distribution coming due, and the creditor obtaining the order—but *Carmack* and *Frealy* did not resolve that issue.

Why did neither *Carmack* or *Frealy* resolve that issue? It was unnecessary to do so because the case arose in the context of a Chapter 7 bankruptcy case. In that context, the judgment debtor's assets were 'frozen' in time at the date of the creation of a bankruptcy estate as per 11 U.S.C. §541. However, the freeze and creation of a bankruptcy estate occurred after the judgment debtor's trust distribution came due but before the distribution was paid.

Also, *Carmack* and *Frealy* made no determinations as to the effect or impact of any laws or doctrines other than the particular spendthrift issue. Thus, for instance:

1. We presume but do not know if a **discretionary trust** would have resolved the issue; if a trustee has discretion to make payment of principal, then are such discretionary amounts ever become "due and payable?" Or do they remain protected by California Probate Code §15303?

2. What if a distribution is **accrued income** rather than solely being principal?

3. **What** is "due and payable"? What is the scope, nature, and extent of the newly minted "15301(b) Assets?" If a trust does not mandate when principal should be paid to a beneficiary (which many do not), then when will such principal distributions be deemed "due and payable?"

4. **When** can a petition or motion pursuant to California Code of Civ. Proc. §709.010 be filed? California Code of Civil Procedure §709.010 is the only authorized method to obtain an order directing the trustee of a trust to satisfy all or part of the judgment out of the payments to which a judgment debtor beneficiary is entitled pursuant to the trust instrument. However, *Carmack* states that a creditor may do so "after an amount of principal has become due and payable (but has not yet been distributed)...." So, when can a petition be filed or an order issued, authorizing payment of principal to a creditor? If an order cannot be issued until after such principal becomes due and payable, then a

trustee can seemingly avoid the effect of *Carmack* by making distribution immediately after principal becomes due and payable. And will this increase trustee liability?

5. Does California Probate Code §15307 exist anymore? Under the *Carmack* ruling, the answer is "no." It is a mere drafting error and inadvertent. **But is this dicta?**

**D. Summary of Authorized Remedies Post-*Carmack* and *Frealy*:**

As is clear, when faced with a request for relief by a judgment creditor pursuant to California Code of Civil Procedure §709.010 to apply a judgment debtor beneficiary's interest in a spendthrift trust towards satisfaction of a judgment, a trial court may apply up to 100 percent of the amounts for any distribution that is "due and payable." But, as to "future" payments, the trial court has no authority to order the trustee to withhold from a beneficiary's future distribution any more than 25 percent thereof, in the aggregate, as to all judgment creditors.





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**CODE OF CIVIL PROCEDURE - CCP**

**PART 2. OF CIVIL ACTIONS [307 - 1062.20]** ( Part 2 enacted 1872. )

**TITLE 9. ENFORCEMENT OF JUDGMENTS [680.010 - 724.260]** ( Title 9 repealed and added by Stats. 1982, Ch. 1364, Sec. 2. )

**DIVISION 2. ENFORCEMENT OF MONEY JUDGMENTS [695.010 - 709.030]** ( Division 2 added by Stats. 1982, Ch. 1364, Sec. 2. )

**CHAPTER 6. Miscellaneous Creditors' Remedies [708.010 - 709.030]** ( Chapter 6 added by Stats. 1982, Ch. 1364, Sec. 2. )

**ARTICLE 10. Other Enforcement Procedures [709.010 - 709.030]** ( Article 10 added by Stats. 1982, Ch. 1364, Sec. 2. )

**709.010.** (a) As used in this section, "trust" has the meaning provided in Section 82 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 having jurisdiction over administration of the trust as prescribed in Part 5 (commencing with Section 17000) of Division 9 of the Probate Code. 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 property by the trustee.

(c) Nothing in this section affects the limitations on the enforcement of a money judgment against the judgment debtor's interest in a trust under Chapter 2 (commencing with Section 15300) of Part 2 of Division 9 of the Probate Code, and the provisions of this section are subject to the limitations of that chapter.

*(Amended by Stats. 1986, Ch. 820, Sec. 18. Operative July 1, 1987, by Sec. 43 of Ch. 820.)*

**709.020.** The judgment creditor may apply to the court on noticed motion for an order applying to the satisfaction of a money judgment a contingent remainder, executory interest, or other interest of the judgment debtor in property that is not vested in the judgment debtor. The interest of the judgment debtor may be applied to the satisfaction of the money judgment by such means as the court, in its discretion, determines are proper to protect the interests of both the judgment debtor and judgment creditor, including but not limited to the imposition of a lien on or the sale of the judgment debtor's interest.

*(Added by Stats. 1982, Ch. 1364, Sec. 2. Operative July 1, 1983, by Sec. 3 of Ch. 1364.)*

**709.030.** Property in a guardianship or conservatorship estate is not subject to enforcement of a money judgment by a procedure provided in this division, but the judgment creditor may apply to the court in which the guardianship or conservatorship proceeding is pending under Division 4 (commencing with Section 1400) of the Probate Code for an order requiring payment of the judgment.

*(Added by Stats. 1982, Ch. 1364, Sec. 2. Operative July 1, 1983, by Sec. 3 of Ch. 1364.)*



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**PROBATE CODE - PROB**

**DIVISION 9. TRUST LAW [15000 - 19403]** (*Division 9 enacted by Stats. 1990, Ch. 79.*)

**PART 2. CREATION, VALIDITY, MODIFICATION, AND TERMINATION OF TRUSTS [15200 - 15414]** (*Part 2 enacted by Stats. 1990, Ch. 79.*)

**CHAPTER 2. Restrictions on Voluntary and Involuntary Transfers [15300 - 15309]** (*Chapter 2 enacted by Stats. 1990, Ch. 79.*)

**15300.** Except as provided in Sections 15304 to 15307, inclusive, if the trust instrument provides that a beneficiary's interest in income is not subject to voluntary or involuntary transfer, the beneficiary's interest in income under the trust may not be transferred and is not subject to enforcement of a money judgment until paid to the beneficiary.

(Enacted by Stats. 1990, Ch. 79.)

**15301.** (a) Except as provided in subdivision (b) and in Sections 15304 to 15307, inclusive, if the trust instrument provides that a beneficiary's interest in principal is not subject to voluntary or involuntary transfer, the beneficiary's interest in principal may not be transferred and is not subject to enforcement of a money judgment until paid to the beneficiary.

(b) After an amount of principal has become due and payable to the beneficiary under the trust instrument, upon petition to the court under Section 709.010 of the Code of Civil Procedure by a judgment creditor, the court may make an order directing the trustee to satisfy the money judgment out of that principal amount. The court in its discretion may issue an order directing the trustee to satisfy all or part of the judgment out of that principal amount.

(Enacted by Stats. 1990, Ch. 79.)

**15302.** Except as provided in Sections 15304 to 15307, inclusive, if the trust instrument provides that the trustee shall pay income or principal or both for the education or support of a beneficiary, the beneficiary's interest in income or principal or both under the trust, to the extent the income or principal or both is necessary for the education or support of the beneficiary, may not be transferred and is not subject to the enforcement of a money judgment until paid to the beneficiary.

(Enacted by Stats. 1990, Ch. 79.)

**15303.** (a) If the trust instrument provides that the trustee shall pay to or for the benefit of a beneficiary so much of the income or principal or both as the trustee in the trustee's discretion sees fit to pay, a transferee or creditor of the beneficiary may not compel the trustee to pay any amount that may be paid only in the exercise of the trustee's discretion.

(b) If the trustee has knowledge of the transfer of the beneficiary's interest or has been served with process in a proceeding under Section 709.010 of the Code of Civil Procedure by a judgment creditor seeking to reach the beneficiary's interest, and the trustee pays to or for the benefit of the beneficiary any part of the income or principal that may be paid only in the exercise of the trustee's discretion, the trustee is liable to the transferee or creditor to the extent that the payment to or for the benefit of the beneficiary impairs the right of the transferee or creditor. This subdivision does not apply if the beneficiary's interest in the trust is subject to a restraint on transfer that is valid under Section 15300 or 15301.

(c) This section applies regardless of whether the trust instrument provides a standard for the exercise of the trustee's discretion.

(d) Nothing in this section limits any right the beneficiary may have to compel the trustee to pay to or for the benefit of the beneficiary all or part of the income or principal.

*(Enacted by Stats. 1990, Ch. 79.)*

**15304.** (a) If the settlor is a beneficiary of a trust created by the settlor and the settlor's interest is subject to a provision restraining the voluntary or involuntary transfer of the settlor's interest, the restraint is invalid against transferees or creditors of the settlor. The invalidity of the restraint on transfer does not affect the validity of the trust.

(b) If the settlor is the beneficiary of a trust created by the settlor and the trust instrument provides that the trustee shall pay income or principal or both for the education or support of the beneficiary or gives the trustee discretion to determine the amount of income or principal or both to be paid to or for the benefit of the settlor, a transferee or creditor of the settlor may reach the maximum amount that the trustee could pay to or for the benefit of the settlor under the trust instrument, not exceeding the amount of the settlor's proportionate contribution to the trust.

*(Enacted by Stats. 1990, Ch. 79.)*

**15305.** (a) As used in this section, "support judgment" means a money judgment for support of the trust beneficiary's spouse or former spouse or minor child.

(b) If the beneficiary has the right under the trust to compel the trustee to pay income or principal or both to or for the benefit of the beneficiary, the court may, to the extent that the court determines it is equitable and reasonable under the circumstances of the particular case, order the trustee to satisfy all or part of the support judgment out of all or part of those payments as they become due and payable, presently or in the future.

(c) Whether or not the beneficiary has the right under the trust to compel the trustee to pay income or principal or both to or for the benefit of the beneficiary, the court may, to the extent that the court determines it is equitable and reasonable under the circumstances of the particular case, order the trustee to satisfy all or part of the support judgment out of all or part of future payments that the trustee, pursuant to the exercise of the trustee's discretion, determines to make to or for the benefit of the beneficiary.

(d) This section applies to a support judgment notwithstanding any provision in the trust instrument.

*(Enacted by Stats. 1990, Ch. 79.)*

**15305.5.** (a) As used in this section, "restitution judgment" means a judgment awarding restitution for the commission of a felony or a money judgment for damages incurred as a result of conduct for which the defendant was convicted of a felony.

(b) If the beneficiary has the right under the trust to compel the trustee to pay income or principal or both to or for the benefit of the beneficiary, the court may, to the extent that the court determines it is equitable and reasonable under the circumstances of the particular case, order the trustee to satisfy all or part of the restitution judgment out of all or part of those payments as they become due and payable, presently or in the future.

(c) Whether or not the beneficiary has the right under the trust to compel the trustee to pay income or principal or both to or for the benefit of the beneficiary, the court may, to the extent that the court determines it is equitable and reasonable under the circumstances of the particular case, order the trustee to satisfy all or part of the restitution judgment out of all or part of future payments that the trustee, pursuant to the exercise of the trustee's discretion, determines to make to or for the benefit of the beneficiary.

(d) This section applies to a restitution judgment notwithstanding any provision in the trust instrument.

*(Added by Stats. 1991, Ch. 175, Sec. 1.)*

**15306.** (a) Notwithstanding any provision in the trust instrument, if a statute of this state makes the beneficiary liable for reimbursement of this state or a local public entity in this state for public support furnished to the beneficiary or to the beneficiary's spouse or minor child, upon petition to the court under Section 709.010 of the Code of Civil Procedure by the appropriate state or local public entity or public official, to the extent the court determines it is equitable and reasonable under the circumstances of the particular case, the court may do the following:

(1) If the beneficiary has the right under the trust to compel the trustee to pay income or principal or both to or for the benefit of the beneficiary, order the trustee to satisfy all or part of the liability out of all or part of the payments as they become due, presently or in the future.

(2) Whether or not the beneficiary has the right under the trust to compel the trustee to pay income or principal or both to or for the benefit of the beneficiary, order the trustee to satisfy all or part of the liability out of all or part of the future payments that the trustee, pursuant to the exercise of the trustee's discretion, determines to make to or for the benefit of the beneficiary.

(3) If the beneficiary is a settlor or the spouse or minor child of the settlor and the beneficiary does not have the right under the trust to compel the trustee to pay income or principal or both to or for the benefit of the beneficiary, to the extent that the trustee has the right to make payments of income or principal or both to or for the beneficiary pursuant to the exercise of the trustee's discretion, order the trustee to satisfy all or part of the liability without regard to whether the trustee has then exercised or may thereafter exercise the discretion in favor of the beneficiary.

(b) Subdivision (a) does not apply to any trust that is established for the benefit of an individual who has a disability that substantially impairs the individual's ability to provide for his or her own care or custody and constitutes a substantial handicap. If, however, the trust results in the individual being ineligible for needed public social services under Division 9 (commencing With Section 10000) of the Welfare and Institutions Code, this subdivision is not applicable and the provisions of subdivision (a) are to be applied.

*(Enacted by Stats. 1990, Ch. 79.)*

**15306.5.** (a) Notwithstanding a restraint on transfer of the beneficiary's interest in the trust under Section 15300 or 15301, and subject to the limitations of this section, upon a judgment creditor's petition under Section 709.010 of the Code of Civil Procedure, the court may make an order directing the trustee to satisfy all or part of the judgment out of the payments to which the beneficiary is entitled under the trust instrument or that the trustee, in the exercise of the trustee's discretion, has determined or determines in the future to pay to the beneficiary.

(b) An order under this section may not require that the trustee pay in satisfaction of the judgment an amount exceeding 25 percent of the payment that otherwise would be made to, or for the benefit of, the beneficiary.

(c) An order under this section may not require that the trustee pay in satisfaction of the judgment any amount that the court determines is necessary for the support of the beneficiary and all the persons the beneficiary is required to support.

(d) An order for satisfaction of a support judgment, as defined in Section 15305, has priority over an order to satisfy a judgment under this section. Any amount ordered to be applied to the satisfaction of a judgment under this section shall be reduced by the amount of an order for satisfaction of a support judgment under Section 15305, regardless of whether the order for satisfaction of the support judgment was made before or after the order under this section.

(e) If 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 in any manner. The trustee has no duty to oppose a petition to satisfy a judgment under this section or to make any claim for exemption on behalf of the 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) Subject to subdivision (d), the aggregate of all orders for satisfaction of money judgments against the beneficiary's interest in the trust may not exceed 25 percent of the payment that otherwise would be made to, or for the benefit of, the beneficiary.

*(Enacted by Stats. 1990, Ch. 79.)*

**15307.** Notwithstanding a restraint on transfer of a beneficiary's interest in the trust under Section 15300 or 15301, any amount to which the beneficiary is entitled under the trust instrument or that the trustee, in the exercise of the trustee's discretion, has determined to pay to the beneficiary in excess of the amount that is or will be necessary for the education and support of the beneficiary may be applied to the satisfaction of a money judgment against the beneficiary. Upon the judgment creditor's petition under Section 709.010 of the Code of Civil Procedure, the court may make an order directing the trustee to satisfy all or part of the judgment out of the beneficiary's interest in the trust.

*(Enacted by Stats. 1990, Ch. 79.)*

**15308.** Any order entered by a court under Section 15305, 15306, 15306.5, or 15307 is subject to modification upon petition of an interested person filed in the court where the order was made.

*(Enacted by Stats. 1990, Ch. 79.)*

**15309.** A disclaimer or renunciation by a beneficiary of all or part of his or her interest under a trust shall not be considered a transfer under Section 15300 or 15301.

*(Enacted by Stats. 1990, Ch. 79.)*

**FOR PUBLICATION**  
**UNITED STATES COURT OF APPEALS**  
**FOR THE NINTH CIRCUIT**

<p>IN RE RICK H. REYNOLDS, <i>Debtor.</i></p> <hr/> <p>TODD A. FREALY, Attorney, Chapter 7 Trustee of Estate of Rick Reynolds, <i>Appellant,</i></p> <p style="text-align:center">v.</p> <p>RICK H. REYNOLDS; JOHN M. CARMACK, Co-Trustee of the Reynolds Family Trust and Co- Trustee of The Reynolds Family Trust - Survivor's Trust, as amended; JOHN MORRIS, Co-Trustee of the Reynolds Family Trust and Co-Trustee of The Reynolds Family Trust - Survivor's Trust, as amended, <i>Appellees.</i></p>	<p>No. 12-60068</p> <p>BAP No. 11-1433</p> <p>OPINION</p>
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Appeal from the Ninth Circuit  
Bankruptcy Appellate Panel  
Hollowell, Pappas, and Dunn, Bankruptcy Judges,  
Presiding

Argued and Submitted March 7, 2014  
Pasadena, California

Filed August 15, 2017

Before: Alex Kozinski and Susan P. Graber, Circuit  
Judges, and Charles R. Breyer,\* District Judge.

Per Curiam Opinion

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## SUMMARY\*\*

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### **Bankruptcy**

The panel reversed a decision of the Bankruptcy Appellate Panel following the California Supreme Court's opinion answering a certified question regarding whether the creditors of the beneficiary of a spendthrift trust may reach the trust distributions.

The panel held that a bankruptcy estate is entitled to the full amount of spendthrift trust distributions due to be paid as of the date of the bankruptcy petition. But the estate may not access any portion of that money the beneficiary needs for his support or education, as long as the trust instrument specifies that the funds are for that purpose. The estate may also reach

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\* The Honorable Charles R. Breyer, United States District Judge for the Northern District of California, sitting by designation.

\*\* This summary constitutes no part of the opinion of the court. It has been prepared by court staff for the convenience of the reader.

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25 percent of expected future payments from the spendthrift trust, reduced by the amount the beneficiary needs to support himself and his dependents.

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### COUNSEL

Jesse S. Finlayson (argued), Finlayson Williams Toffer Roosevelt & Lilly LLP, Irvine, California, for Appellant.

David W. Meadows (argued), Law Offices of David W. Meadows, Los Angeles, California, for Appellees.

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### OPINION

PER CURIAM:

Debtor is the beneficiary of a spendthrift trust. The trust payments he receives come entirely from trust principal. The California Probate Code is unclear as to whether and to what extent his creditors may reach the trust distributions, so we certified the question to the California Supreme Court. *Frealy v. Reynolds*, 779 F.3d 1028, 1030 (9th Cir. 2015). That court answers us in the attached opinion.

In our order certifying the question, we recounted the facts of this case. *Id.* at 1031–32. Based on the California Supreme Court opinion, we now hold that a bankruptcy estate is entitled to the full amount of spendthrift trust distributions due to be paid as of the petition date. *See Carmack v. Reynolds*, 391 P.3d 625, 628 (Cal. 2017); Cal. Prob. Code § 15301(b). But the estate may not access any portion of that money the beneficiary needs for his support or education, as



long as the trust instrument specifies that the funds are for that purpose. *See Carmack*, 391 P.3d at 629; Cal. Prob. Code § 15302. The estate may also reach 25 percent of expected future payments from the spendthrift trust, reduced by the amount the beneficiary needs to support himself and his dependents. *See Carmack*, 391 P.3d at 632; Cal. Prob. Code § 15306.5.

We remand so that the bankruptcy court can apply the teachings of *Carmack*.

**REVERSED and REMANDED.**

**APPENDIX**

215 Cal.Rptr.3d 749

**John M. CARMACK, as Trustee, etc., et al., Plaintiffs and Respondents,**

v.

**Rick H. REYNOLDS, Defendant;**

**Todd A. Frealy, as Trustee in Bankruptcy, etc., Claimant and Appellant.**

S224985

Supreme Court of California.

Filed 3/23/2017

**Background:** Chapter 7 trustee brought adversary proceeding, seeking to compel turnover of the undistributed principal to which debtor was entitled under spendthrift trust established by his late father. The United States Bankruptcy Court for the Central District of California, Meredith A. Jury, J., granted debtor's motion for summary judgment, and trustee appealed. The Bankruptcy Appellate Panel (BAP), Hollowell, J., 479 B.R. 67, affirmed, and trustee appealed, and the Court of Appeals, 2017 WL 1131882, certified question to the California Supreme Court as to the extent to which a bankruptcy estate may reach a beneficiary's interest in spendthrift trust.

**Holding:** The Supreme Court, Liu, J., held that creditor may petition for pending distribution of principal as well as up to 25 percent of future payments.

Question answered.

### 1. Trusts ⇌141

A "spendthrift trust" is a trust that provides that the beneficiary's interest cannot be alienated before it is distributed to the beneficiary.

See publication Words and Phrases for other judicial constructions and definitions.

### 2. Trusts ⇌152

Creditors of the beneficiary of a spendthrift trust generally cannot reach trust assets while those assets are in the hands of

the trustee, even if they have secured a judgment against the beneficiary; rather, creditors must wait until the trustee makes distributions to the beneficiary.

### 3. Trusts ⇌12

The law permits spendthrift trusts because donors have the right to choose the object of their bounty and to protect their gifts from the donees' creditors.

### 4. Statutes ⇌1076

Court interpreting a statute seeks to ascertain the intent of the lawmakers so as to effectuate the purpose of the statute.

### 5. Statutes ⇌1079

Court interpreting a statute begins by looking to the statutory language.

### 6. Statutes ⇌1091, 1151

Court interpreting a statute must give the language its usual, ordinary import and accord significance, if possible, to every word, phrase and sentence in pursuance of the legislative purpose.

### 7. Statutes ⇌1156

A construction of a statute making some words surplusage is to be avoided.

### 8. Statutes ⇌1153, 1155, 1216(2)

The words of the statute must be construed in context, keeping in mind the statutory purpose, and statutes or statutory sections relating to the same subject must be harmonized, both internally and with each other, to the extent possible.

### 9. Statutes ⇌1105, 1183, 1242

If the statutory language is susceptible of more than one reasonable interpretation, court must look to additional canons of statutory construction to determine the Legislature's purpose; both the legislative history of the statute and the wider historical circumstances of its enactment may be considered in ascertaining the legislative intent.

### 10. Trusts ⇌152

The general rule is that principal held in a spendthrift trust may not be touched by creditors until it is paid to the beneficiary. Cal. Prob. Code § 15301(a).

**11. Trusts** ⇨152

Where trust assets are not protected by a spendthrift provision, the default rule is that creditors may reach those assets. Cal. Civ. Proc. Code § 709.010(b).

**12. Trusts** ⇨152

After an amount of principal of a spendthrift trust has become due and payable, but has not yet been distributed, a creditor can petition to have the trustee pay directly to the creditor a sum up to the full amount of that distribution unless the trust instrument specifies that the distribution is for the beneficiary's support or education and the beneficiary needs the distribution for those purposes; if no such distribution is pending or if the distribution is not adequate to satisfy a judgment, a general creditor can petition to levy up to 25 percent of the payments expected to be made to the beneficiary, reduced by the amount other creditors have already obtained and subject to the support needs of the beneficiary and any dependents. Cal. Prob. Code §§ 15301(b), 15306.5, 15307.

*See 13 Witkin, Summary of Cal. Law (10th ed. 2005) Trusts, § 151 et seq.*

9th Cir. No. 12-60068, BAP No. CC-11-1433-HPaD, C.D. Cal. Bankr. Nos. 09-14039-MJ, 09-01205-MJ

Finlayson Toffer Roosevelt & Lilly, Jesse S. Finlayson and Matthew E. Lilly, Irvine, for Claimant and Appellant.

Law Offices of David W. Meadows and David W. Meadows, Los Angeles, for Defendant.

The Eroen Law Firm and Robert C. Eroen for Plaintiffs and Respondents.

Liu, J.

Under the terms of a spendthrift trust established by his parents, defendant Rick H. Reynolds is entitled to receive over a million dollars, all to be paid out of trust principal. Reynolds filed for bankruptcy before the trust's first payment, and the bankruptcy trustee seeks to determine what interest the bankruptcy estate has in the trust. The trust is governed by California law, and as the United States Court of Appeals for the Ninth Circuit observed, the relevant statutory pro-

visions are "opaque." (*Frealy v. Reynolds* (9th Cir. 2015) 779 F.3d 1028, 1029 (*Frealy*)). Probate Code section 15306.5 appears to limit the bankruptcy estate to 25 percent of the beneficiary's interest; other provisions of the Probate Code suggest no such limitation. The Ninth Circuit asked us whether the Probate Code limits a bankruptcy estate's access to a spendthrift trust to 25 percent of the beneficiary's interest, where the trust pays the beneficiary entirely out of principal. We hold that the Probate Code does not impose such an absolute limit on a general creditor's access to the trust. With limited exceptions for distributions explicitly intended or actually required for the beneficiary's support, a general creditor may reach a sum up to the full amount of any distributions that are currently due and payable to the beneficiary even though they are still in the trustee's hands, and separately may reach a sum up to 25 percent of any payments that are anticipated to be made to the beneficiary.

**I.**

Reynolds's parents established the Reynolds Family Trust in 2005. The trust contains a spendthrift clause, providing that "no interest in the income or principal of any trust created under this instrument shall be voluntarily or involuntarily anticipated, assigned, encumbered, or subjected to creditor's [*sic*] claim or legal process before actual receipt by the beneficiary." Reynolds's mother Patsy died in 2007. Following her death, Reynolds's father Freddie received all the trust's distributions until Freddie died in 2009.

The trust provides that at Freddie's death, Reynolds is entitled to \$250,000 from the trust if he survives Freddie by 30 days. In addition, Reynolds is entitled to receive \$100,000 a year for 10 years and then one-third of the remainder. All payments are expected to be made from principal; the trust's assets are in undeveloped real estate that do not produce income. Those assets are estimated to be worth several million dollars, although their exact value will not be known until the trust assets are liquidated.

The day after his father died, Reynolds filed for voluntary bankruptcy under chapter

7 of the United States Bankruptcy Code. The trustees of the Reynolds Family Trust sought a declaratory judgment on the extent of the bankruptcy trustee's interest in the trust. The bankruptcy court held that under the California Probate Code, the bankruptcy trustee standing as a hypothetical lien creditor could reach 25 percent of Reynolds's interest in the trust. The bankruptcy appellate panel affirmed. The bankruptcy trustee appealed to the Ninth Circuit, which asked us to clarify if Probate Code section 15306.5 caps a bankruptcy estate's access to a spendthrift trust at 25 percent of the beneficiary's interest where the trust pays entirely from principal. We granted the Ninth Circuit's request.

## II.

[1–3] A spendthrift trust is a trust that provides that the beneficiary's interest cannot be alienated before it is distributed to the beneficiary. Creditors of the beneficiary generally cannot reach trust assets while those assets are in the hands of the trustee, even if they have secured a judgment against the beneficiary. Rather, creditors must wait until the trustee makes distributions to the beneficiary. The law permits such trusts because donors have “the right to choose the object of [their] bounty” and to protect their gifts from the donees' creditors. (*Canfield v. Security-First Nat. Bank* (1939) 13 Cal.2d 1, 11, 87 P.2d 830 (*Canfield*)). Providing donors some measure of control over their gifts encourages donors to make those gifts, to the benefit of the donor, the beneficiary, and ultimately the beneficiary's creditors.

Under the Probate Code, spendthrift provisions are generally valid as to both trust income and trust principal. (Prob. Code, §§ 15300 [trust income], 15301, subd. (a) [trust principal]; all statutory references are to the Probate Code unless otherwise noted.) Yet creditors need not always wait for distributions to reach the debtor's hands. Spendthrift provisions are invalid when grantors name themselves beneficiaries. (§ 15304, subd. (a).) When a trust includes a valid spendthrift provision, certain creditors may reach into the trust. Such creditors include those with claims for spousal or child support

(§ 15305) and those with restitution judgments (§ 15305.5). In addition, a state or local public entity can reach trust assets when the beneficiary owes money for public support (§ 15306, subd. (a)) unless distributions from the trust are required to care for a disabled beneficiary (§ 15306, subd. (b)).

Even general creditors, including a bankruptcy trustee standing as a hypothetical lien creditor, have some recourse under three provisions: section 15301, subdivision (b) (section 15301(b)), section 15306.5, and section 15307. The question here is how much access to trust principal a general creditor has under these provisions.

[4–9] This is a question of statutory construction. We seek to “ascertain the intent of the lawmakers so as to effectuate the purpose of the statute.” (*Day v. City of Fontana* (2001) 25 Cal.4th 268, 272, 105 Cal.Rptr.2d 457, 19 P.3d 1196.) “[W]e begin by looking to the statutory language. [Citation.] We must give ‘the language its usual, ordinary import and accord[ ] significance, if possible, to every word, phrase and sentence in pursuance of the legislative purpose. A construction making some words surplusage is to be avoided. The words of the statute must be construed in context, keeping in mind the statutory purpose, and statutes or statutory sections relating to the same subject must be harmonized, both internally and with each other, to the extent possible.’ [Citation.] If the statutory language is susceptible of more than one reasonable interpretation, we must look to additional canons of statutory construction to determine the Legislature's purpose. [Citation.] ‘Both the legislative history of the statute and the wider historical circumstances of its enactment may be considered in ascertaining the legislative intent.’” (*McCarther v. Pacific Telesis Group* (2010) 48 Cal.4th 104, 110, 105 Cal.Rptr.3d 404, 225 P.3d 538.)

In construing the provisions at issue, we are mindful that the Reynolds Family Trust is distinctive in directing all disbursements to be made from principal. In other trusts, productive assets produce periodic income payments during the life of the trust, and preserving principal is one of the trustee's paramount duties. (See 76 Am.Jur.2d (2016)

Trusts, § 429.) It is common for trusts to specify that the principal may not be distributed for many years, and liquidating principal may signal that the trust's purpose has been fulfilled. We are also mindful that this case arises out of a bankruptcy proceeding. Ordinarily, a judgment creditor who is unable to satisfy all of the judgment out of the beneficiary's trust interest may continue to attempt to collect on the balance of the judgment from whatever other assets the beneficiary may have. Here, however, the amount Reynolds's creditors will receive depends on the reach of the bankruptcy trustee. Any remaining debts after the bankruptcy process will be extinguished, and any further distributions will be unencumbered. (11 U.S.C. § 541(c)(2).) That spendthrift provisions can work to beneficiaries' advantage in bankruptcy in this way has long been recognized as a characteristic of such provisions. (See Rest.3d Trusts, § 58, com. a ["An important byproduct of the limited spendthrift protection, however, is the again limited but nevertheless important insulation that may result from a discharge in bankruptcy."].)

#### A.

We begin with section 15301(b), which provides in pertinent part: "After an amount of principal has become due and payable to the beneficiary under the trust instrument, upon petition to the court under Section 709.010 of the Code of Civil Procedure by a judgment creditor, the court may make an order directing the trustee to satisfy the money judgment out of that principal amount." Section 709.010 of the Code of Civil Procedure (section 709.010) sets forth the procedure for a judgment creditor to petition a court to satisfy the judgment out of the debtor's trust interests.

As the Ninth Circuit observed, the statute does not define "due and payable." (*Frealy, supra*, 779 F.3d at p. 1033.) The phrase is used in other provisions such as section 15305, which provides that creditors with judgments for child or spousal support may petition a court to satisfy their judgments out of disbursements of either income or principal "as they become due and payable, presently or in the future." (§ 15305, subd. (b).)

Any disbursement from the trust would appear to be due and payable in the sense the phrase is used in section 15305. But, as the Ninth Circuit recognized, applying such a reading to section 15301(b) could mean that creditors have "immediate access to all of a beneficiary's trust principal," which would eliminate spendthrift protections as to principal entirely. (*Frealy*, at p. 1033.)

We do not think the Legislature intended to remove all protections from trust principal immediately after specifying that spendthrift provisions are generally valid as applied to principal. (§ 15301, subd. (a).) Instead, the Legislature provided the limiting principle in the introductory clause of section 15301(b): "After an amount of principal *has become* due and payable . . ." (Italics added.) This clause indicates that timing is critical: section 15301(b) reaches only those amounts which are presently set to be paid to the beneficiary. The provision thus requires an amount of principal to "ha[ve] become" due to the beneficiary, at which point upon a creditor's petition the court may enter an order "directing the trustee to satisfy the money judgment out of *that principal amount*." (§ 15301(b), italics added.) In other words, under this provision creditors may reach the principal already set to be distributed and only up to the extent of that distribution. Such principal has served its trust purposes, and in many (but not all) cases, the distribution may signal that the trust is ending. Section 15301(b) makes these assets, and these assets only, fair game to creditors.

[10] In this light, section 15301(b) is properly viewed not as an exception to the general spendthrift protections but as a corollary. The general rule is that principal held in a spendthrift trust may not be touched by creditors until it is paid to the beneficiary. (§ 15301, subd. (a).) Section 15301(b) adds that once an amount of principal has become due and payable, the court can order the trustee to pay that amount directly to the beneficiary's creditors instead. A distribution of principal is reasonably understood to signify that the amount distributed has satisfied its trust purposes. Because the beneficiary's interest in those assets has effectively vested, the law no longer has any interest in protect-

ing them (except as provided in section 15302, as explained below).

The legislative history points the same way. The provisions at issue date from the Law Revision Commission's 1986 proposed revisions to the Probate Code. (See Selected 1986 Trust and Probate Legislation (Sep. 1986) 18 Cal. Law Revision Com. Rep. (1986) pp. 1321–1479 (1986 Report); Stats. 1986, ch. 820, § 40, as reenacted by Stats 1990, ch. 79, § 14.) The revisions were designed to remedy the patchwork nature of the prior statutory framework while largely continuing existing law. (1986 Report, *supra*, at pp. 1221–1222, 1302–1306.) Prior California statutes had not made clear that spendthrift provisions were valid as applied to principal, though case law generally suggested they were. (*Id.* at p. 1302; see *Seymour v. McAvoy* (1898) 121 Cal. 438, 444, 53 P. 946; *San Diego Trust etc. Bank v. Heustis* (1932) 121 Cal. App. 675, 683–684, 10 P.2d 158.) The Commission's report, to which we give “substantial weight” (*Van Arsdale v. Hollinger* (1968) 68 Cal.2d 245, 249, 66 Cal.Rptr. 20, 437 P.2d 508, overruled on other grounds in *Privette v. Superior Court* (1993) 5 Cal.4th 689, 21 Cal. Rptr.2d 72, 854 P.2d 721), notes that the drafters sought to codify the validity of spendthrift provisions as applied to trust principal in section 15301, subdivision (a) (section 15301(a)). (1986 Report, *supra*, at p. 1302.) But the drafters also sought to clarify that once principal was due and payable, creditors could reach it both “in the hands of the trustee and after payment to the beneficiary.” (*Id.* at pp. 1302–1303.) In other words, spendthrift protections do not apply to section 15301(b) assets.

Importantly, creditors' access under section 15301(b) is not unlimited. Section 15302 explains that where the trust instrument specifies that a distribution, whether from income or principal, is for the beneficiary's support or education, the amount the beneficiary actually needs for either purpose may not be reached by creditors until in the hands of the beneficiary. Section 15302 explicitly provides that it does not apply where creditors seek access under sections 15304 through 15307, but section 15302 does not exclude orders under section 15301(b). Sec-

tion 15302 thus provides limited continued protection to former trust assets where the donor specifically intended the distribution to support the beneficiary. This protection encourages donors to provide for beneficiaries' support and helps to prevent beneficiaries from becoming public charges. (See *Canfield, supra*, 13 Cal.2d at p. 11, 87 P.2d 830.)

## B.

We now turn to sections 15306.5 and 15307. Both provisions are exceptions to the general validity of spendthrift provisions as applied to trust principal established by section 15301(a). Section 15306.5, subdivision (a) (section 15306.5(a)) provides that any judgment creditor can petition a court to order the trustee to satisfy the judgment out of payments to which the beneficiary is entitled. But those orders are limited to “25 percent of the payment that otherwise would be made to, or for the benefit of, the beneficiary” (§ 15306.5, subd. (b)), and they cannot cut into any amount required to support the beneficiary or the beneficiary's dependents (§ 15306.5, subd. (c)). Section 15307, for its part, provides: “Notwithstanding a restraint on transfer of a beneficiary's interest in the trust under Section 15300 or 15301, any amount to which the beneficiary is entitled under the trust instrument . . . in excess of the amount that is or will be necessary for the education and support of the beneficiary may be applied to the satisfaction of a money judgment against the beneficiary. Upon the judgment creditor's petition under Section 709.010 of the Code of Civil Procedure, the court may make an order directing the trustee to satisfy all or part of the judgment out of the beneficiary's interest in the trust.”

Section 15307 thus appears to allow any creditor to access all of a beneficiary's interest in a spendthrift trust besides what is necessary for the beneficiary's education and support, whereas section 15306.5 limits creditors to only 25 percent of the same interest. How are these two provisions to be reconciled?

One possibility is that section 15307 is only meant to apply to income, not principal. It is true that the Law Revision Commission titled this provision “Income in excess of

amount for education and support subject to creditors' claims." (1986 Report, *supra*, 18 Cal. Law Revision Com. Rep. at p. 1340; see also Cal. Law Revision Com. com., 54 West's Ann. Prob. Code (1991 ed.) foll. § 15307, p. 562 (West's Annotated Code) ["Section 15307 permits an ordinary creditor to reach income under limited circumstances."]; 13 Witkin, Summary of Cal. Law (10th ed. 2005) Trusts, § 155 ["Under the Trust Law, surplus income may be reached to satisfy creditors' claims."].) But this title was not part of the official legislative enactments (see Stats. 1986, ch. 820, § 40) and therefore cannot have any bearing on the interpretation of the statute (58 Cal.Jur.3d (2017) Statutes, § 177). Moreover, section 15301(a), which applies only to principal, specifically refers to section 15307, and section 15307 provides that it applies "[n]otwithstanding . . . [section] 15301." Both references would be unnecessary if section 15307 only applied to income. (See also 1986 Report, *supra*, at p. 1305 [§ 15307 applies "notwithstanding a restraint on transfer of income *or principal* in the trust instrument" (italics added)].) In any event, excluding principal from section 15307 would not resolve the tension between sections 15306.5 and 15307 for income. We thus conclude that section 15307 applies to both income and principal, as its text plainly says.

The bankruptcy trustee suggests that section 15307 serves a different purpose from section 15306.5 by setting a higher bar for creditors than section 15306.5. Under this theory, general creditors have "automatic" access to 25 percent of beneficiaries' trust interest under section 15306.5, with the burden on the beneficiaries to prove that this should be reduced in light of their support needs and those of their dependents. But in exceptional circumstances, the argument goes, general creditors can turn to section 15307 to reach beyond the 25 percent cap if they can show that exceeding the cap would be equitable and would not cut into the beneficiaries' support or education needs.

The bankruptcy trustee's theory might reflect sensible policy and may find some support in the Law Revision Commission's unelaborated comment that section 15307 applies "under limited circumstances." (West's Ann.

Prob. Code, *supra*, at p. 562.) However, nothing in the statutes suggests that obtaining an order under section 15307 involves any different burden or standard of proof than obtaining an order under any other section. On the contrary, section 15307 contains the same reference to section 709.010 of the Code of Civil Procedure as does section 15306.5(a). Section 709.010, for its part, does not specify any special burdens or procedures for orders under section 15307. The bankruptcy trustee does not cite any authority in support of its theory.

Instead, the more likely answer is that section 15307 reflects a drafting error. Before the 1986 revisions, spendthrift trusts were governed by three key provisions. The first was former section 867 of the Civil Code, which generally permitted spendthrift provisions as applied to income. (Recommendation Proposing the Trust Law (Dec. 1985) 18 Cal. Law Revision Com. Rep. (1985) p. 596 (1985 Report).) The second provision was former section 859 of the Civil Code, which allowed creditors to reach the "surplus" beyond the beneficiary's education and support in the limited instances where the trust instrument did not specify what to do with accumulating income. (1985 Report, *supra*, at p. 597, fn. 390, quoting Civ. Code, former § 859; see *Estate of Lawrence* (1968) 267 Cal.App.2d 77, 82, 72 Cal.Rptr. 851 [trust provision specifying that "[a]ll unexpended portions of the net income . . . shall be accumulated, added to, and become a part of the principal" is valid direction for the accumulation of income].) Moreover, former section 859 said it applied "as provided in Section 709.010 of the Code of Civil Procedure," the third key provision governing spendthrift trusts. (1985 Report, *supra*, at p. 597, fn. 390.) At the time, former section 709.010 applied by reference the principles of the wage garnishment statute to periodic trust payments, capping payments at 25 percent for general creditors and 50 percent for support creditors. (1985 Report, *supra*, at pp. 597-599, fn. 392, quoting former § 709.010.) So, where former section 859 applied, general creditors were capped at 25 percent of periodic payments to beneficiaries.



The Commission's original proposal reworked those provisions into the current framework. Former section 867 of the Civil Code was the basis for proposed section 15300. (1985 Report, *supra*, 18 Cal. Law Revision Com. Rep. at p. 625.) Former section 859 of the Civil Code formed the basis for proposed section 15307, though section 15307's scope is much broader as it seemingly applies to all trust assets and not just undirected accumulations of income. (See 1985 Report, *supra*, at p. 633.) And although section 15307, like former section 859, retained a reference to section 709.010 of the Code of Civil Procedure, that reference would have been to a much changed provision, for the proposal also contemplated amending former section 709.010 to remove its references to the wage garnishment statute. (1985 Report, *supra*, at p. 766.) Some of the removed provisions were given new homes; for example, the provision giving preferred access to support creditors became proposed section 15305, which also removed the 50 percent cap. (1985 Report, *supra*, at pp. 630–631.) The 25 percent cap that had applied to general creditors was not retained anywhere; if the 1985 proposal had been enacted as written, the new law would have dramatically increased the reach of general creditors.

But the revised draft of the Trust Law in 1986, which was ultimately enacted, included for the first time section 15306.5. (1986 Report, *supra*, 18 Cal. Law Revision Com. Rep. at p. 1339; see Stats. 1986, ch. 820, § 40.) This new section drew on former section 709.010 and the wage garnishment statute to create an explicit 25 percent cap on trust interests comparable to the cap protecting wages. (1986 Report, *supra*, at p. 1339.) In the process, the Commission did not meaningfully revise its proposal for section 15307 (compare 1985 Report, *supra*, 18 Cal. Law Revision Com. Rep. at p. 633, with 1986 Report, *supra*, at p. 1340), nor did the Commission clarify the role of section 15307 in light of section 15306.5. The result is that unlike Civil Code former section 859, which it purportedly replaced, section 15307 refers to a version of section 709.010 that no longer imposes a cap on general creditors, even as it follows a new provision, section 15306.5, that

reestablishes that same cap. In light of this history, we decline to adopt an interpretation of section 15307 that simply undoes the limitations on general creditors that section 15306.5 sets forth in a set of specific and carefully calibrated provisions. We conclude instead that the ultimate enactment of section 15307 without apparent limitations on the reach of general creditors was inadvertent. The Legislature plainly intended general creditors to be limited to 25 percent of distributions from the trust.

### C.

The final issue we must address is whether the 25 percent limitation of section 15306.5 applies to section 15301(b). Section 15306.5, subdivision (f) (section 15306.5(f)) provides: “Subject to subdivision (d), the aggregate of all orders for satisfaction of money judgments against the beneficiary’s interest in the trust may not exceed 25 percent of the payment that otherwise would be made to, or for the benefit of, the beneficiary.” Unlike section 15306.5(b)’s reference to “[a]n order under this section,” the language of section 15306.5(f)—“all orders for satisfaction of money judgments”—is not limited to orders under section 15306.5. One possibility, therefore, is that section 15306.5(f)’s cap extends to all orders under any provision of the Probate Code.

We need not decide the full reach of the 25 percent cap under 15306.5(f) as this case involves only the scope of sections 15301(b) and 15306.5. Whatever other orders may be subject to section 15306.5(f)’s cap, we conclude that the cap does not apply to orders under section 15301(b). As explained above, section 15306.5 was modeled on the wage garnishment statute then in force (Code Civ. Proc., former § 706.050 et seq., as enacted by Stats. 1982, ch. 1364, § 2) and provides creditors a limited exception to spendthrift protections on the beneficiary’s continuing interest in the trust. As the use of the conditional in section 15306.5(f) suggests, “the payment that otherwise *would be* made to” the beneficiary is best understood as referring to ongoing payments the beneficiary stands to receive. (Italics added.) The cap thus operates to limit the sum of orders subject to section

15306.5(f)'s cap to 25 percent of any individual expected distribution.

[11] By contrast, section 15301(b) makes clear that spendthrift protections do not apply to distributions of principal that have become due and payable. Where trust assets are not protected by a spendthrift provision, the default rule is that creditors may reach those assets. (See § 709.010, subd. (b).) By crafting a specific rule for this narrow class of assets, the Legislature indicated its intent that those assets be treated differently. (See *Miller v. Superior Court* (1999) 21 Cal.4th 883, 895, 89 Cal.Rptr.2d 834, 986 P.2d 170 [““A specific provision relating to a particular subject will govern in respect to that subject, as against a general provision, although the latter, standing alone, would be broad enough to include the subject to which the more particular provision relates.”” [Citation.]”].) Applying section 15306.5(f)'s cap to section 15301(b) assets would defeat the Legislature's specific intent to treat due and payable principal “in the hands of the trustee” on par with such principal “after payment to the beneficiary.” (See 1986 Report, *supra*, 18 Cal. Law Revision Com. Rep. at pp. 1302–1303.)

[12] In sum, after an amount of principal has become due and payable (but has not yet been distributed), a creditor can petition to have the trustee pay directly to the creditor a sum up to the full amount of that distribution (§ 15301(b)) unless the trust instrument specifies that the distribution is for the beneficiary's support or education and the beneficiary needs the distribution for those purposes (§ 15302). If no such distribution is pending or if the distribution is not adequate to satisfy a judgment, a general creditor can petition to levy up to 25 percent of the payments expected to be made to the beneficiary, reduced by the amount other creditors have already obtained and subject to the support needs of the beneficiary and any dependents. (§ 15306.5.)

As an illustration, suppose a trust instrument specified that a beneficiary was to receive distributions of principal of \$10,000 on March 1 of each year for 10 years. Suppose further that a general creditor had a money judgment of \$50,000 against the beneficiary

and that the trust distributions are neither specifically intended nor required for the beneficiary's support. On March 1 of the first year, upon the creditor's petition a court could order the trustee to remit the full distribution of \$10,000 for that year to the creditor directly if it has not already been paid to the beneficiary, as well as \$2,500 from each of the nine anticipated payments (a total of \$22,500) as they are paid out. If the creditor were not otherwise able to satisfy the remaining \$17,500 balance on the judgment, then on March 1 of the following years, upon the general creditor's petition the court could order the trustee to pay directly to the creditor a sum up to the remainder of that year's principal distribution (\$7,500), as the court in its discretion finds appropriate, until the judgment is satisfied.

#### CONCLUSION

We conclude that a bankruptcy trustee, standing as a hypothetical judgment creditor, can reach a beneficiary's interest in a trust that pays entirely out of principal in two ways. It may reach up to the full amount of any distributions of principal that are currently due and payable to the beneficiary, unless the trust instrument specifies that those distributions are for the beneficiary's support or education and the beneficiary needs those distributions for either purpose. Separately, the bankruptcy trustee can reach up to 25 percent of any anticipated payments made to, or for the benefit of, the beneficiary, reduced to the extent necessary by the support needs of the beneficiary and any dependents.

We Concur:

Cantil-Sakauye, C.J.

Werdegar, J.

Chin, J.

Corrigan, J.

Cuellar, J.

Kruger, J.

