

Trusts & Divorce: The Supreme Judicial Court Provides Clarity

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The Massachusetts Supreme Judicial Court recently issued its decision in the highly anticipated case of *Pfannenstiehl v. Pfannenstiehl*¹ providing clarity to the lower courts on whether a spouse's interest in a discretionary, spendthrift trust is subject to division in a divorce proceeding. The Supreme Judicial Court concluded that the husband's interest in an irrevocable spendthrift trust, created by the husband's father in 2004 for the benefit of the husband and his siblings and their children was so speculative as to constitute nothing more than an expectancy which is not assignable to the marital estate.

BACKGROUND

The parties were married for approximately ten years and had two disabled children. Between 2008 and 2010, the husband received distributions from the 2004 irrevocable trust in the amount of \$800,000. In the eight (8) months prior to the filing of the divorce action, the husband received monthly distributions of \$20,000. However, one (1) month prior to the husband filing the divorce complaint, the distributions to the husband ceased while distributions to the husband's siblings, also beneficiaries, continued. The trial court found that the family's expansive lifestyle was interconnected to the distributions from the 2004 trust. The trial court also found that the cutting off of distributions from the 2004 trust on the eve of the divorce "was a deliberate manipulation to erase a major component of the husband's annual income and to silence his interest in the trust for a convenient time while the divorce was ongoing."

THE 2004 TRUST

The 2004 trust at issue in *Pfannenstiehl* is an irrevocable, spendthrift trust that was established by the husband's father. The 2004 trust holds shares of stock in family-controlled private corporations which, in turn, own and operate private, for-profit colleges. The trust was valued at almost \$25,000,000 at the time of the divorce. The beneficiaries of the trust are the husband, his brother and sister, and their children (at the time of the divorce there were 11 beneficiaries but the class of beneficiaries remained open to expansion).

There are two trustees of the 2004 trust. The husband's brother is one trustee along with the family attorney. As an officer and director of the corporations owned by the trust along with

his father, the court found the husband's brother is able to manipulate what dividends are to be paid to the trust, thereby influencing the 2004 trust principal and income available for distributions. The family lawyer trustee, while allegedly an outside, independent trustee, was found by the trial court to be inextricably interconnected with and aligned with the husband's family. The trial court concluded that the 2004 trust had not been administered impartially by the two trustees, and upon the filing of the divorce, the "proverbial family wagons circled the family money."

The 2004 trust contains a standard "spendthrift clause". Specifically, it states, "neither the principal nor income of any trust created hereunder shall be subject to alienation, pledge, assignment or other anticipation by the person for whom the same is intended, nor attachment, execution, garnishment or other seizure under any legal, equitable or other process."

The 2004 trust also contains an "ascertainable standard" for distributions that reads as follows:

Until the division of the Trust into separate shares pursuant to Paragraph B below, the Trustee shall pay to, or apply for the benefit of, a class comprised of any one or more of the Donor's then living issue such amounts of income and principal as the Trustee, in its sole discretion, may deem advisable from time to time, whether in equal or unequal shares, to provide for the comfortable support, health, maintenance, welfare and education of each or all members of such class. In the exercise of such discretion, the Trustee may take into account funds available from other sources for such needs of each beneficiary. At the end of each taxable year, any net income which is not disposed of by the terms of this paragraph shall be added to the principal of the trust estate.

DECISION

In the lower courts, the wife had successfully argued that the irrevocable, spendthrift trust was an asset subject to division in divorce. The Appeals Court reasoned that the ascertainable standard in the 2004 trust supported the inclusion of the trust in the marital estate because the husband had a present, enforceable right to distributions from the trust. The trustees

¹*Pfannenstiehl v. Pfannenstiehl*, 2016 Mass. LEXIS 591 (2016)

were obligated to, and did, in fact, make distributions from the trust to the husband and other beneficiaries for such things as their comfortable support, health, maintenance, welfare, and education.

The Supreme Judicial Court rejected the Appeals Court's reliance on the ascertainable standard to support the inclusion of the trust in the marital estate and determined that the ascertainable standard restricts the discretion of the trustee to make distributions to a beneficiary based on objective guidelines. Given that he must rely on the trustees' exercise of discretion and has no authority to compel distributions, the husband has no present or enforceable right to the trust income or principal. More importantly, the fact that the husband was one of eleven beneficiaries and the class of beneficiaries could increase if additional grandchildren were born, the Court found that the husband has an expectancy which is too remote or speculative to be part of the marital estate.²

If the husband was the sole current beneficiary of his distinct trust fund (which is often the case in parents' estate plans) with the presence of the ascertainable standard it is quite possible that the Supreme Judicial Court would have included the trust fund, as an assignable marital asset.

²While the Supreme Judicial Court did not include this trust as a divisible marital asset, it did remand the case to the trial court to consider whether the husband's interest in the trust should be factored into the decision of how the actual marital assets get divided (the opportunity for the future acquisition of income as assets is a factor). Given the husband's expectancy under the 2004 trust, it is likely the trial court will allocate a greater share of marital assets to the wife or increase alimony accordingly.

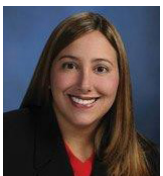


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PLANNING POINT

Taking a conservative approach, it may be preferable to allow the trustees to make distributions to beneficiaries in their sole, unfettered discretion, rather than directing them to make distributions under an ascertainable standard i.e., for health, education, support or maintenance (the most commonly used standard). Under current case law, this absolutely protects the trust assets from divorce and/or third party creditors in Massachusetts.

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