

Alabama Asset Protection Summary

State Exemptions:

Insurance:

§ 6-10-8. Rights of beneficiaries and assignees under life insurance policies.

If a policy of insurance, whether heretofore or hereafter issued, is effected by any person on his or her own life or on another life in favor of a person other than himself or herself or, except in cases of transfer with intent to defraud creditors, if a policy of life insurance is assigned or in any way made payable to any such person, the lawful beneficiary or assignee thereof, other than the insured or the person so effecting such insurance, or his or her executors or administrators, shall be entitled to its proceeds and avails against the creditors and representatives of the insured and of the person effecting the same, whether or not the right to change the beneficiary is reserved or permitted and whether or not the policy is made payable to the person whose life is insured if the beneficiary or assignee shall predecease such person; provided, that subject to the statute of limitations, the amount of any premiums for said insurance paid with intent to defraud creditors, with interest thereon, shall inure to their benefit from the proceeds of the policy; but the company issuing the policy shall be discharged of all liability thereon by payment of its proceeds in accordance with its terms unless, before such payment, the company shall have written notice, by or in behalf of a creditor, of a claim to recover for transfer made or premiums paid with intent to defraud creditors, with specifications of the amount claimed. A husband or a wife, in his or her own name or in the name of a trustee, may insure the life of his or her spouse for the benefit of himself or herself, or for the benefit of himself or herself and any child or children of the marriage; or a husband or a wife may insure his or her own life for the benefit of his or her spouse, or for the benefit of his or her spouse and children, or for the benefit of their children, either in the names of such children or in the name of a trustee; and such insurance and the proceeds and avails thereof, whether or not the right to change the beneficiary is reserved or permitted, is exempt from liability for the debts or engagements of the insured, or for the torts of the insured, or for any penalty or damages recoverable of the insured.

The following discussion is from Westlaw's Annotations:

“Purpose

The purpose of this section is not to set aside an exemption for the benefit of the debtor, but to provide for the maintenance and support of a class of people, primarily the spouse and children. While the benefit inures directly to the named beneficiary, it is an exemption of the debtor, which he can claim regardless of the power to change the named beneficiary. [Matter of Morris, 30 B.R. 392 \(Bkrcty.N.D.Ala.1983\)](#).

If the Legislature had intended to limit the life insurance exemption, it could have easily done so by amending or repealing this section. The cash surrender value of a life insurance policy is clearly personalty, and could be exempted under § 6-10-6 without the aid of this section, if the Legislature had so intended. Furthermore, in choosing to protect a separate class of people, the Legislature well understood that without an independent exemption statute for life insurance, a debtor could utilize his \$3,000 personalty exemption to his advantage and to the detriment of his beneficiaries. [Matter of Morris, 30 B.R. 392 \(Bkrtcy.N.D.Ala.1983\)](#).

Right to change beneficiaries

The provision of the policy reserving every right and benefit to the insured would not have the effect of taking away from the lawful beneficiary the right to receive, as against creditors of the insured, the “proceeds and avails” of the policy. This section itself gives this right to the lawful beneficiary, whether or not the right to change the beneficiary is reserved. [In re Beckman, 50 F.Supp. 339 \(N.D.Ala.1943\)](#).

Whether or not there is reserved a right to change the beneficiary or whether or not such beneficiary has contract rights or equities in the insurance, such insurance is no part of the estate of the insured, is not subject to administration and, except for fraud, is not subject to payment of debts. [Jennings v. Jennings, 250 Ala. 130, 33 So.2d 251 \(Ala.1947\)](#).”

Homestead:

§ 6-10-2. Homestead exemption -- Amount; area.


The homestead of every resident of this state, with the improvements and appurtenances, not exceeding in value \$5,000 and in area 160 acres, shall be, to the extent of any interest he or she may have therein, whether a fee or less estate or whether held in common or in severalty, exempt from levy and sale under execution or other process for the collection of debts during his or her life and occupancy and, if he or she leaves surviving him or her a spouse and a minor child, or children, or either, during the life of the surviving spouse and minority of the child, or children, but the area of the homestead shall not be enlarged by reason of any encumbrance thereon or of the character of the estate or interest owned therein by him or her. When a husband and wife jointly own a homestead each is entitled to claim separately the exemption provided herein, to the same extent and value as an unmarried individual. For purposes of this section and [Sections 6-10-38](#) and [6-10-40](#), a mobile home or similar dwelling if the principal place of residence of the individual claiming the exemption shall be deemed to be a homestead.

Tenancy By the Entirety:

It is uncertain whether Alabama recognizes tenancy by the entirety. *In Dougherty v. Hovater*, 447 So.2d 185 (Ala. 1984), the Alabama Supreme Court declined to rule on the issue finding that

resolution of the case did not depend on whether Alabama recognized tenancy by the entirety. Also see, See *Brown v. Andrews*, 288 Ala. 111, 257 So.2d 356 (1972), *Yates v. Guest*, 416 So.2d 973 (Ala 1982), *Nunn v. Keith*, 289 Ala. 518, 268 So.2d 792 (1972); *Durant v. Hamrick*, 409 So.2d 731 (Ala 1981); *Donegan v. Donegan*, 15 So. 823 (Ala. 1894). Denniston, *Joint Tenancy and Tenancy in Common of Real Property -- The Gulf Separating Them*, 44 Alabama Lawyer, p. 72 (March, 1983); Comment, *Muddy Waters: Concurrent Ownership with Right of Survivorship in Alabama After Durant v. Hamrick*, 34 Ala.L.R. 147 (1983).

Marital Property & Gifting

Although “marital property” generally includes property purchased or otherwise accumulated by the parties during the marriage, it may also include the property acquired before the marriage or received by gift or inheritance during the marriage when it is used, or income from it is used, regularly for the common benefit of the parties during their marriage. [Nichols v. Nichols, 824 So.2d 797 \(Ala.Civ.App.2001\)](#). [Divorce](#)  [252.3\(1\)](#)

From the Nichols Opinion:

” The trial judge is granted broad discretion in determining whether property purchased before the parties' marriage or received by gift or inheritance was used “regularly for the common benefit of the parties during the marriage.” See [§ 30-2-51, Ala.Code 1975](#). Even if the trial court determines that such property was regularly used for the common benefit of the parties during the marriage, the determination whether to include such property in the marital assets to be divided between the parties lies within the discretion of the trial court. [Durbin v. Durbin, 818 So.2d 404 \(Ala.2001\)](#). The record indicates that although the parties and the parties' children used and benefited from the Ward property inherited from the husband's mother during the parties marriage, the trial court determined that the inherited property was not regularly used for the common benefit of the parties and thus was the husband's separate estate. Even if the trial court had concluded that the property was regularly used for the benefit of the parties and their family, it is within the trial court's discretion to exclude the property from the marital estate. ***803** *Id.* Therefore, under *Durbin*, supra, we cannot say that the trial court abused its discretion in excluding the inherited portion of the Ward property from the marital estate.”

§ 30-2-51. Allowance upon grant of divorce; certain property not considered; retirement benefits.

(a) If either spouse has no separate estate or if it is insufficient for the maintenance of a spouse, the judge, upon granting a divorce, at his or her discretion, may order to a spouse an allowance out of the estate of the other spouse, taking into consideration the value thereof and the condition of the spouse's family. Notwithstanding the foregoing, the judge may not take into consideration

any property acquired prior to the marriage of the parties or by inheritance or gift unless the judge finds from the evidence that the property, or income produced by the property, has been used regularly for the common benefit of the parties during their marriage.

Note: The author was unable to find a case on whether inter spousal gifts are marital property. In this respect, it appears that an inter spousal gift would follow the general rule that it is non-marital property.

Alabama Discretionary Trust Law Before the Uniform Trust Code

Alabama discretionary trust law appears to be limited to primarily two cases: (1) *Howard v. Spragins*, 350 So. 2d 318 (Ala. 1977); and (2) *Boykin v. Boykin*, 656 So. 2d 821 (Ct. App. 1994). Both these cases recognize the common law distinction of a discretionary and support trust (i.e. spendthrift trust):

In Howard, the Alabama Supreme Court held:

“In a true discretionary trust, the general rule is that a beneficiary’s interest is not subject to a claim for child support. . . . A true discretionary trust must be distinguished from trusts where the discretion of the trustee pertains to the item or manner of the payments, or to the size of the payments needed to support the beneficiary. The trustee must be free to pay or apply or to totally exclude the beneficiary, if the trust is to be called “discretionary” in the technical sense.”

In Boykin, the Alabama Appellate Court held:

“A trust may be either a discretionary trust or a spendthrift trust. *Howard v. Spragins*, 350 So. 2d 318 (Ala. 1977). Regarding child support, our supreme court has held that, as a general rule, a true discretionary trust is not subject to a claim for child support. *Id.* A trust is a true discretionary trust only where the trustee has complete discretion to pay or totally exclude the beneficiary. *Id.* A spendthrift trust exists where the trustee must make payments to the beneficiary, but has discretion only as to the time or method of making those payments.”

It should be note that the Alabama Appellate Court inadvertently confused the term “spendthrift trust” with the term “support trust.” A spendthrift trust is any trust that has a spendthrift provision. Both discretionary and support trusts almost always both contain a spendthrift provision. Conversely, a support trust is where a beneficiary has an enforceable right to a distribution.

Alabama UTC Creditor Provisions

§ 19-3B-501. Rights of beneficiary's creditor or assignee.

To the extent a beneficiary's interest is not subject to a spendthrift provision, the court may authorize a creditor or assignee of the beneficiary to reach the beneficiary's interest by attachment of present or future distributions to or for the benefit of the beneficiary or other means. The court may limit the award to such relief as is appropriate under the circumstances.

§ 19-3B-502. Spendthrift provision.

(a) A spendthrift provision is valid only if it restrains both voluntary and involuntary transfer of a beneficiary's interest.

(b) A term of a trust providing that the interest of a beneficiary is held subject to a “spendthrift trust,” or words of similar import, is sufficient to restrain both voluntary and involuntary transfer of the beneficiary's interest.

(c) A beneficiary may not transfer an interest in a trust in violation of a valid spendthrift provision and, except as otherwise provided in this article, a creditor or assignee of the beneficiary may not reach the interest or a distribution by the trustee before its receipt by the beneficiary.

§ 19-3B-503. Exceptions to spendthrift provision.

(a) In this section, “child” includes any person for whom an order or judgment for child support has been entered in this or another state.

(b) A spendthrift provision is unenforceable against:

(1) a beneficiary's child, spouse, or former spouse who has a judgment or court order against the beneficiary for support or maintenance;

(2) a judgment creditor who has provided services for the protection of a beneficiary's interest in the trust; and

(3) a claim of this state or the United States to the extent a statute of this state or federal law so provides.

(c) A claimant against whom a spendthrift provision cannot be enforced may obtain from a court an order attaching present or future distributions to or for the benefit of the beneficiary. The court may limit the award to such relief as is appropriate under the circumstances.

§ 19-3B-504. Discretionary trusts; effect of standard.

(a) In this section, the terms “child”, “spouse”, or “former spouse” include any person for whom an order or judgment for child or spousal support has been entered in this or another state.

(b) Except as otherwise provided in subsection (c), whether or not a trust contains a spendthrift provision, a creditor of a beneficiary may not compel a distribution that is subject to the trustee's discretion, even if:

(1) the discretion is expressed in the form of a standard of distribution; or

(2) the trustee has abused the discretion.

(c) To the extent a trustee has not complied with a standard of distribution or has abused a discretion:

(1) a distribution may be ordered by the court to satisfy a judgment or court order against the beneficiary for support or maintenance of the beneficiary's child, spouse, or former spouse; and

(2) the court shall direct the trustee to pay to the child, spouse, or former spouse such amount as is equitable under the circumstances but not more than the amount the trustee would have been required to distribute to or for the benefit of the beneficiary had the trustee complied with the standard or not abused the discretion.

(d) This section does not limit the right of a beneficiary to maintain a judicial proceeding against a trustee for an abuse of discretion or failure to comply with a standard for distribution.

(e) A creditor may not reach the interest of a beneficiary who is also a trustee or co-trustee, or otherwise compel a distribution, if the trustee's discretion to make distributions for the trustee's own benefit is limited by an ascertainable standard.

UTC Comment Referred to in Alabama Code

Purpose and scope. This section addresses the ability of a beneficiary's creditor to reach the beneficiary's discretionary trust interest, whether or not the exercise of the trustee's discretion is subject to a standard. *This section, similar to the Restatement, eliminates the distinction between discretionary and support trusts, unifying the rules for all trusts fitting within either of the former categories. See [RESTATEMENT \(THIRD\) OF TRUSTS § 60](#) Reporter's Notes to cmt. a (Tentative Draft No. 2, approved 1999).* {Emphasis Added}

UTC 2005 Amended Comment in Response to Concerns

This section addresses the ability of a beneficiary's creditor to reach the beneficiary's discretionary trust interest, whether or not the exercise of the trustee's discretion is subject to a

standard. This section, similar to the Restatement, eliminates the distinction between discretionary and support trusts, unifying the rules for all trusts fitting within either of the former categories. *See* Restatement (Third) of Trusts Section 60 Reporter's Notes to cmt. a (Tentative Draft No. 2, approved 1999). By eliminating this distinction, the rights of a creditor are the same whether the distribution standard is discretionary, subject to a standard, or both. Other than for a claim by a child, spouse or former spouse, a beneficiary's creditor may not reach the beneficiary's interest. Eliminating this distinction affects only the rights of creditors. The affect of this change is limited to the rights of creditors. It does not affect the rights of a beneficiary to compel a distribution. Whether the trustee has a duty in a given situation to make a distribution depends on factors such as the breadth of the discretion granted and whether the terms of the trust include a support or other standard. *See* Section 814 comment.

§ 19-3B-505. Creditor's claim against settlor.

(a) Whether or not the terms of a trust contain a spendthrift provision, the following rules apply:

(1) During the lifetime of the settlor, the property of a revocable trust is subject to claims of the settlor's creditors.

(2) With respect to an irrevocable trust, a creditor or assignee of the settlor may reach the maximum amount that can be distributed to or for the settlor's benefit. If a trust has more than one settlor, then the amount the creditor or assignee of a particular settlor may reach may not exceed the settlor's interest in the portion of the trust attributable to that settlor's contribution.

(3) After the death of a settlor, and subject to the settlor's right to direct the source from which liabilities will be paid, the property of a trust that was revocable immediately prior to the settlor's death is subject to claims of the settlor's creditors, costs of administration of the settlor's estate, the expenses of the settlor's funeral and disposal of remains, and homestead allowance, exempt property and family allowance to a surviving spouse and children to the extent the settlor's probate estate is inadequate to satisfy those claims, costs, expenses, and homestead allowance, exempt property and family allowance.

(b) With respect to claims, expenses, and taxes in connection with the settlement of a trust that was revocable at the settlor's death:

(1) Any claim of a creditor which would be barred against the fiduciary of a decedent's estate, the estate of the decedent, or any creditor or beneficiary of the decedent's estate, shall be barred against the trustee, the trust property, and the creditors and beneficiaries of the trust.

(2) A trustee at any time may give notice to any person the trustee has reason to believe may have a claim against the settlor at death. The notice shall contain the name and address of the trustee to whom the claim must be presented. If the person fails to present the claim in writing within 90 days from the date of the notice, then the person shall be forever barred from asserting or recovering on the claim from the trustee, the trust property and the creditors and beneficiaries

of the trust. Any person who presents a claim on or before the date specified in the notice may not later increase the claim following the expiration of the 90-day period.

(3) If a claim is not presented in writing to the personal representative of the settlor's estate or to the trustee (i) within six months from the date of the appointment of the initial personal representative of the settlor's estate, or (ii) if no personal representative is appointed within six months from the settlor's date of death and a claim is not presented in writing to the trustee within six months from the settlor's date of death, then no trustee shall be chargeable for any assets that the trustee may pay or distribute in good faith in satisfaction of any lawful claims, expenses, or taxes or to any beneficiary before the claim was presented. A payment or distribution of assets by a trustee shall be deemed to have been made in good faith unless the creditor can prove that the trustee had actual knowledge of the claim at the time of the payment or distribution. The six-month period shall not be interrupted or affected by the death, resignation, or removal of a trustee, except that the time during which there is no trustee in office shall not be counted as part of the period.

(4) The provisions of [Section 43-2-371](#) dealing with the priority of payment of claims, expenses, and taxes from the probate estate of a decedent shall apply to a revocable trust to the extent the assets of the decedent's probate estate are inadequate.

(c) For purposes of this section:

(1) during the period the power may be exercised, the holder of a power of withdrawal is treated in the same manner as the settlor of a revocable trust to the extent of the property subject to the power; and

(2) upon the lapse, release, or waiver of the power, the holder is treated as the settlor of the trust only to the extent the value of the property affected by the lapse, release, or waiver exceeds the greater of the amount specified in [Section 2041\(b\)\(2\)](#), [2503\(b\)](#), or [2514\(e\) of the Internal Revenue Code of 1986](#), in each case as in effect on January 1, 2007, or as later amended.

§ 19-3B-506. Overdue distribution.

(a) In this section, “mandatory distribution” means a distribution of income or principal that the trustee is required to make to a beneficiary under the terms of the trust, including a distribution upon termination of the trust. The term excludes a distribution subject to the exercise of the trustee's discretion regardless of whether the terms of the trust (i) include a support or other standard to guide the trustee in making distribution decisions or (ii) provide that the trustee “may” or “shall” make discretionary distributions, including distributions pursuant to a support or other standard.

(b) Whether or not a trust contains a spendthrift provision, a creditor or assignee of a beneficiary may compel a mandatory distribution of income or principal to a beneficiary, including a distribution upon termination of the trust, if the trustee has not made the distribution to the beneficiary within a reasonable time after the mandated distribution date.

ALABAMA COMMENT

Comparison to Uniform Code. Alabama substitutes the word “compel” for the word “reach” in [Section 506\(b\) of the Uniform Trust Code \(2001\)](#). In addition, the prepositional phrase “to a beneficiary” is added for clarity. This change makes it clear that, while a creditor may force a mandatory distribution to be made, the distribution may still be made to the beneficiary and not necessarily directly to the creditor. A failure to make a required distribution within a reasonable period of time does not change the role of the trustee to that of a receiver or arbitrator of the claims and obligations of the beneficiary.

§ 19-3B-508. Qualified trusts under the Internal Revenue Code.

(a) Any benefits provided under a plan which includes a trust that constitutes a “qualified trust” may not be assigned or alienated, voluntarily or involuntarily, and shall be exempt from the operation of any bankruptcy or insolvency laws under [11 U.S.C. § 522\(b\)](#), as from time to time amended. This subsection may not be waived by a participant or beneficiary of any qualified plan.

(b) The securing of a loan made to a participant or beneficiary of such a plan shall not be treated as an assignment or alienation under subsection (a) if such loan is secured by the participant's accrued nonforfeitable benefit under the plan and is exempt from the tax imposed by Section 4975 of the code by reason of Section 4975(d)(1) of the code.

(c) Subsection (a) shall apply to the creation, assignment, or recognition of a right to any benefit payable with respect to a participant pursuant to a domestic relations order, as such term is defined in Section 414(p) of the code, except that subsection (a) shall not apply if the order is determined to be a “qualified domestic relations order” in accordance with Section 414(p) of the code. However, no domestic relations order shall be deemed a qualified domestic relations order except in accordance with the procedures for such determination set forth in Section 414(p) and the related provisions of the Employee Retirement Income Security Act of 1974, as from time to time amended.

(d) The provisions of this section shall be interpreted so as to provide restrictions on alienation and assignment to the extent, and only to the extent, the same are required for a trust within the definition of “qualified trust” herein to be a “qualified trust” under the applicable provisions of the code, notwithstanding any attempted assignment or alienation in violation of Section 401(a) or other applicable provisions of the code. It is intended that this section will constitute “a restriction of the transfer of a beneficial interest of the debtor in a trust that is enforceable under applicable nonbankruptcy law” for purposes of Section 541(c)(2) of the Federal Bankruptcy Code, [11 U.S.C. § 541\(c\)\(2\)](#), as from time to time amended. This section shall further be construed as a “state spendthrift trust law.” It is further intended for this section to provide an **exemption** from creditors' claims within [11 U.S.C. § 522](#).

(e) As used in this section:

(1) ASSIGNMENT or ALIENATION, and any conjugation thereof, includes any anticipation, assignment at law or in equity, alienation, attachment, garnishment, levy, execution, or other legal or equitable process. The term includes: (i) any arrangement providing for the payment to the employer or other sponsor of such plan of benefits that otherwise would be due the participant under the plan; (ii) any direct or indirect arrangement, whether revocable or irrevocable, whereby any person acquires from a participant or beneficiary of such plan a right or interest enforceable against the plan in, or to, all or any part of a plan benefit which is, or may become, payable to the participant or beneficiary; (iii) any attachment, execution, seizure, or the like, or under any form of legal process whatsoever; and (iv) the operation of any bankruptcy or insolvency laws under [11 U.S.C. § 522\(b\)](#) as from time to time amended. Notwithstanding the foregoing, the term does not include those items excluded from the definition by [Treasury Regulations § 1.401\(a\)-13\(c\)\(2\)](#).

(2) CODE means the Internal Revenue Code of 1986, as from time to time amended, or as at any time superseded by reenactment, recodification, or adoption of any other similar revenue law. Reference to specific sections of the code shall include references to their successor sections as a result of renumbering or recodification at any future date.

(3) TREASURY REGULATION means a valid regulation of the United States Department of Treasury codified at Title 26 of the Code of Federal Regulations. References to specific Treasury Regulations include references to amendments and future reenactments or recodifications of such regulations, regardless of how designated.

(4) QUALIFIED TRUST means a “qualified trust” as such term is used in Section 401(a) of the code, and includes any trust that would not be qualified but for this section. A “qualified trust” includes, without limitations, any trust that has received a favorable determination letter from the Internal Revenue Service of the United States Department of Treasury to the effect that such trust is, or will be upon the satisfaction of certain administrative conditions, a “qualified trust” under Section 401(a) of the code. “Qualified trust” also includes: (i) a “retirement annuity” described in Section 404(a)(2) of the code, including a retirement annuity that would not satisfy the requirements of Section 404(a)(2) of the code but for this section; (ii) an annuity described in Section 403(b) of the code, including an annuity that would not satisfy the requirements of Section 403(b) of the code but for this section; (iii) an individual **retirement plan** described in Section 7701(a)(37) of the code, including an individual **retirement plan** that would not satisfy the requirements of Section 7701(a) (37) of the code but for this section; (iv) a retirement bond described in Section 409 of the code, as in effect prior to January 1, 1984, including a retirement bond that would not satisfy the requirements of Section 409 of the code but for this section; (v) a governmental plan described in Section 414(d) of the code; (vi) a church plan described in Section 414(e) of the code; and (vii) a tax credit employee stock ownership plan described in Section 409 of the code, including a tax credit employee stock ownership plan that would not satisfy the requirements of Section 409 of the code but for this section.

(f) This section does not apply to the Employees' Retirement System of Alabama, Teachers' Retirement System of Alabama, and the Judicial Retirement Fund of Alabama.

Alabama Comment

Comparison to Uniform Code. Alabama adds Section 508, which is derived (without substantive change) from former ALA. CODE § 19-3-1(b), to the Alabama Trust Code.

§ 19-3B-603. Settlor's powers; powers of withdrawal.

(a) While a trust is revocable, rights of the beneficiaries are subject to the control of, and the duties of the trustee are owed exclusively to, the settlor.

(b) During the period the power may be exercised, the holder of a power of withdrawal has the rights of a settlor of a revocable trust under this section to the extent of the property subject to the power.

§ 19-3B-814. Discretionary powers; tax savings.

(a) Notwithstanding the breadth of discretion granted to a trustee in the terms of the trust, including the use of such terms as “absolute,” “sole,” or “uncontrolled,” the trustee shall exercise a discretionary power in good faith and in accordance with the terms and purposes of the trust and the interests of the beneficiaries.

UTC Comment – Referenced in Alabama Code

Purpose and scope. Despite the breadth of discretion purportedly granted by the wording of a trust, no grant of discretion to a trustee, whether with respect to management or distribution, is ever absolute. A grant of discretion establishes a range within which the trustee may act. The greater the grant of discretion, the broader the range. Pursuant to subsection (a), a trustee's action must always be in good faith, with regard to the purposes of the trust, and in accordance with the trustee's other duties, including the obligation to exercise reasonable skill, care and caution. See Sections 801 (duty to administer trust) and 804 (duty to act with prudence). The standard stated in subsection (a) applies only to powers which are to be exercised in a fiduciary as opposed to a nonfiduciary capacity. Regarding the standards for exercising discretion and construing particular language of discretion, see [RESTATEMENT \(THIRD\) OF TRUSTS § 50 \(Tentative Draft No. 2, approved 1999\)](#); [RESTATEMENT \(SECOND\) OF TRUSTS § 187 \(1959\)](#). See also Edward C. Halbach, Jr., *Problems of Discretion in Discretionary Trusts*, 61 COLUM. L. REV. 1425 (1961). An abuse by the trustee of the discretion granted in the terms of the trust is a breach of trust that can result in surcharge. See Section 1001(b) (remedies for breach of trust).

UTC 2005 Amended Comment in Response to Concerns Regarding the Good Faith Standard

Despite the breadth of discretion purportedly granted by the wording of a trust, no grant of discretion to a trustee, whether with respect to management or distribution, is ever absolute. A grant of discretion establishes a range within which the trustee may act. The greater the grant of discretion, the broader the range. Pursuant to subsection (a), a trustee's exercise of discretion must be in good faith. Consistent with the trustee's duty to administer the trust (*see* Section 801), the trustee's exercise must also be in accordance with the terms and purposes of the trust and the interests of the beneficiaries. "Interests of the beneficiaries" means the beneficial interests provided in the terms of the trust. *See* Section 103(8). Subsection (a) does not otherwise address the obligations of a trustee to make distributions, leaving that issue to the caselaw. Regarding the standards for exercising discretion and construing particular language of discretion, with numerous case citations, see Restatement (Third) of Trusts Section 50 (Tentative Draft No. 2, approved 1999); Restatement (Second) of Trusts Section 187 (1959). *See also* Edward C. Halbach, Jr., *Problems of Discretion in Discretionary Trusts*, 61 Colum. L. Rev. 1425 (1961). Under these standards, whether the trustee has a duty in a given situation to make a distribution depends on the exact language used, whether the standard grants discretion and its breadth, whether this discretion is coupled with a standard, whether the beneficiary has other available resources, and, more broadly, the overriding purposes of the trust. For example, distilling the results of scores of cases, the Restatement (Third) of Trusts concludes that there is a presumption that the "trustee's discretion should be exercised in a manner that will avoid either disqualifying the beneficiary for other benefits or expending trust funds for purposes for which public funds would otherwise be available." Restatement (Third) of Trusts Section 50 cmt. e & Reporter's Notes (Tentative Draft No. 2, 1999).

Subsection (a) requires a trustee exercise a discretionary power in good faith and in accordance with the terms and purposes of the trust and the interests of the beneficiaries. Similar to Restatement (Second) of Trusts Section 187 (1959), subsection (a) does not impose an obligation that a trustee's decision be within the bounds of a reasonable judgment, although such an interpretive standard may be imposed by the courts if the document adds a standard whereby the reasonableness of the trustee's judgment can be tested. Restatement (Second) of Trusts Section 187 cmt. f (1959).

The obligation of a trustee to act in good faith is a fundamental concept of fiduciary law although there are different ways that it can be expressed. Sometimes different formulations appear in the same source. Scott, in his treatise on trusts, states that the court *will not* interfere with the trustee's exercise of discretion if the trustee "acts in good faith and does not act capriciously," but Scott then states that the trustee *will* interfere if the trustee "acts dishonestly or in good faith, or where he acts from an improper motive." 3 Austin W. Scott & William F. Fratcher, *The Law of Trusts* Section 187.2 (4th ed. 1988).

Sometimes different formulations are used in the same case:

[If] the "sole discretion" vested in and exercised by the trustees in this case . . . were exercised fraudulently, in bad faith or in an abuse of discretion, it is subject to . . . review. Whether good faith has been exercised, or whether fraud, bad faith or an abuse of discretion has been committed is always subject to consideration by the court upon appropriate allegations and proof.

In re Ferrall's Estate, 258 P.2d 1009 (Cal. 1953).

An abuse by the trustee of the discretion granted in the terms of the trust is a breach of trust that can result in surcharge. *See* Section 1001(b) (remedies for breach of trust). The standard stated in subsection (a) applies only to powers which are to be exercised in a fiduciary as opposed to a nonfiduciary capacity.

Subsections (b) through (d) rewrite the terms of a trust that might otherwise result in adverse estate and gift tax consequences to a beneficiary-trustee. This Code does not generally address the subject of tax curative provisions. These are provisions that automatically rewrite the terms of trusts that might otherwise fail to qualify for probable intended tax benefits. Such provisions, because they apply to all trusts using or failing to use specified language, are often overbroad, applying not only to trusts intended to qualify for tax benefits but also to smaller trust situations where taxes are not a concern. Enacting tax-curative provisions also requires special diligence by state legislatures to make certain that these provisions are periodically amended to account for the frequent changes in federal tax law. Furthermore, many failures to draft with sufficient care may be correctable by including a tax savings clause in the terms of the trust or by seeking modification of the trust using one or more of the methods authorized by Sections 411-417. Notwithstanding these reasons, the unintended inclusion of the trust in the beneficiary-trustee's gross estate is a frequent enough occurrence that the drafters concluded that it is a topic that this Code should address. It is also a topic on which numerous States have enacted corrective statutes.

Richard Covey noted that the amended comment did not address the issues presented and was "not helpful." The author concurs with Richard Covey's statement.

Charging Order Protection

Partnership Act

§ 10-9B-703. Rights of creditor.

On application to a court of competent jurisdiction by any judgment creditor of a partner, the court may charge the partnership interest of the partner with payment of the unsatisfied amount of the judgment with interest. To the extent so charged, the judgment creditor has only the rights of an assignee of the partnership interest. This chapter does not deprive any partner of the benefit of any exemption laws applicable to his or her partnership interest.

Limited Liability Company Act

§ 10-12-35. Member's financial rights subject to charging order.

(a) On application to a court of competent jurisdiction by any judgment creditor of a member or assignee, the court may charge the interest of the member or assignee with payment of the unsatisfied amount of the judgment with interest. To the extent so charged, the judgment creditor has only the rights of an assignee of financial rights. This section shall be the sole and exclusive remedy of a judgment creditor with respect to the judgment debtor's membership interest.

(b) This chapter does not deprive any member of the benefit of any exemption laws applicable to the member's limited liability company interest.