

SPENDTHRIFT VERSUS DISCRETIONARY TRUST PROVISIONS

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Most trusts and Wills contain a clause or paragraph regarding a spendthrift provision. Some trust provisions also provide a sentence or statement about a trustee's ability to act in their sole discretion with regard to distribution of assets to a beneficiary. What is the difference between a spendthrift and a discretionary provision and which is better?

First let's describe in general terms what a Spendthrift clause creates. In general terms a Spendthrift clause prevents a beneficiary's creditors from garnishing a present or future distribution from an estate prior to the beneficiary receiving it. In addition, a Spendthrift clause prevents the Beneficiary from transferring their interest to another (e.g. assigning their trust income to a creditor). In layman's terms that means that a credit card company cannot attach a judgment debt owed them to a beneficiary's bequest from Mom or Dad until the beneficiary has taken actual possession of it.

A discretionary trust provision is one where the trustee is given sole or absolute discretion to provide either income or a bequest to a beneficiary. In many cases a discretionary trust provision provides a standard of how distributions of assets will occur. In a majority of cases the standards include the health, education, support and maintenance of a beneficiary. They can also include situations where the beneficiary is incapacitated, under a certain age (e.g. 25), substance abuse user or insolvent.

Under Florida's trust or probate code a Spendthrift clause does not provide protection against exception creditors. Exception creditors are typically spouses, former spouses or children of a beneficiary who have obtained a support judgment (e.g. alimony or child support) against a delinquent spouse or parent. Other exception creditors are the State of Florida, U.S. Government and any person who has provided services (e.g. Attorney) for the protection of a beneficiary's interest in a trust.

So what does that mean? If you are a parent and you want to provide income to your child via a trust instrument, but do not want it to become open to garnishment by the child's former spouse, then a Spendthrift trust or clause buried in the language of your trust may not help you. All that a former spouse needs to demonstrate is that he or she has exercised all other remedies to obtain their support income and if such exercise was fruitless, he or she may be able to garnish the amount of alimony or child support from the other spouse's trust that was prepared to provide him or her with an consistent income stream. That means that if Mom or Dad set up a trust to supply income to their child, and the former spouse of the child is unable to obtain support income from said child, the former spouse would be able to defeat Mom or Dad's spendthrift clause and garnish the child's income prior to the him or her receiving it.

Remember that the only creditors that can override a Spendthrift trust or clause are exception creditors, and not general creditors or judgment holders (e.g. credit card companies).

Florida's trust code provides that when a trust is discretionary, exception creditors cannot reach the beneficiary's bequest until the beneficiary takes actual possession of the devise. However, a case from Florida's Supreme Court states that if a trustee makes a distribution to a beneficiary, it may be subject to garnishment, even if a trustee has the discretion to make the distribution. Although, the case states that discretionary trusts are subject to garnishment, Florida's trust code, Chapter 736, Fla. Stat., states otherwise.

If Mom and Dad want to make a distribution to a beneficiary, such distribution might turn on who the beneficiary's devise is paid too. Thus, a trustee might consider paying a beneficiary's bills (e.g. electric, water, gas) directly to the source and not to the beneficiary who would then pay those bills themselves. In essence, the beneficiary does not take possession of the funds nor is there an intended payout to the Beneficiary which may avoid the subject of garnishment. Instead the Trustee pays the creditor directly out of the trust (think of it as automatic payment).

In the aforementioned comments, it would seem as if the primary issue to overcome is keeping the beneficiary from having any form of expectation of receiving his or her bequest. If this can be prevented, by and through the discretion of a trustee, then it is highly unlikely that a creditor would successfully be able to garnish a beneficiary's income stream especially if never paid directly to the beneficiary.

Getting back to the original question; which is better, a Spendthrift Trust/Clause or Discretionary Trust? If the intent is to prevent any and all creditors (except the IRS) from attaching to a beneficiary's interest, then clearly a discretionary trust provision is worthy of examination.

If you are considering leaving a legacy following your death, talk to the attorney of your choice who can explain what can happen to your assets should one of your beneficiaries come upon hard times and how best to protect your beneficiary's bequest from being garnished by creditors. It may be the best investment you make in the distribution of your assets following your death.

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