

## *Family Law: Treatment of Trust Interests in Divorce: An Overview*

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New Hampshire statutes and case law have evolved to provide some clarity to attorneys and Family Division judicial officers concerning the divisibility of a spouse's trust interests for property settlement purposes, particularly with the adoption of and amendments to the Uniform Trust Code (UTC), as well as the NH Supreme Court decisions in *Chamberlin* and *Goodlander*.

However, alimony, jurisdictional and discovery issues continue to bedevil some estate planners and family law practitioners.

Some trust interests in property settlements are categorically indivisible. Others are categorically divisible, and many remain uncertain and/or fact-specific.

Discretionary interests in third-party trusts (*Goodlander* and UTC §8-814(b)) are indivisible, whether the third party trustee's discretion is absolute or limited by an ascertainable standard. In one interpretation, this includes "beneficiary-controlled trusts" (e.g., beneficiary serves as co-trustee, has power to remove and replace third-party co-trustee, holds a limited power of appointment over trust assets, etc.).

Self-settled revocable trusts are equivalent to a general power of appointment and are divisible, as are general powers of appointment, including executor and "hanging" (*Crummey*) and "5 or 5" powers and other unrestricted withdrawal rights.

Mandatory income, annuity trust and unitrust interests (*Chamberlin*) are divisible in the absence of a "self-destruct" provision, unless a third party trustee/trust protector has power to terminate or suspend the interest.

Dissipation trusts (*Abrams*) are categorically divisible as assets placed in trust to intentionally reduce the marital assets.

It remains unclear whether remainder interests (*Flaherty*) can be divided. This determination often relies on the facts of a case. While some might be tempted to conclude that a remainder interest is divisible as a matter of law, when vested in the property law sense, *Flaherty* did not go that far, and the focus will be on whether, based on any particular facts, the interest represents a mere expectancy, or is too attenuated to be valued.

### **Alimony/Child Support**

UTC §503 allows certain "exception creditors" to reach a beneficiary's interest in a third-party spendthrift trust. They include, among others, the beneficiary's child, spouse or a former spouse who has a court order against the beneficiary that specifies the alimony amount attributable to the most basic food, shelter and medical needs of the spouse or former spouse.

An exception creditor may obtain a court order attaching imminent or future mandatory distributions to or for a beneficiary under UTC §503. However, this remedy is of limited utility in the context of a discretionary trust. It does not authorize an exception creditor to compel a distribution from a discretionary trust, regardless of whether the trust contains a spendthrift provision.

To compel a distribution, an exception creditor must first obtain an order from a family court that specifies and attaches only an alimony amount attributable to the most basic food, shelter and medical needs of the spouse or former spouse. The creditor must then petition a probate judge for a determination that the trustee's failure to distribute the amount specified would fail to comply with a standard or abused its discretion under §504, and an order that the trustee do so.

A trustee is required to exercise discretion in good faith and in accordance with the terms of the trust. In most cases it will be difficult to prove that a trustee has failed to comply with a standard and more difficult to prove bad faith with respect to a purely discretionary trust.

### **Jurisdiction and Disclosure/Privacy of Third Parties**

The family and probate divisions are courts of limited jurisdiction. In the *Matter of Muller*, decided in 2012, vacated the family division's order that would have effectively invalidated the husband's parents' claim to a mortgage interest the Mullers' marital home, on the basis that only a superior court judge can determine the parents' rights as donors or lenders.

Moreover, the family division has no personal jurisdiction over third parties who have not been joined as parties to the divorce proceedings. A trustee has duties to protect the trust's assets and avoid voluntarily submission to personal jurisdiction.

An alimony order that assumes that trust assets are available as a source of payment is enforceable only by a civil contempt remedy against the beneficiary spouse. However, if the beneficiary cannot compel distributions, impossibility of his or her performance is generally a defense to civil contempt.

Without personal jurisdiction over a trustee or subject matter jurisdiction over trust matters, gaining access to confidential third-party trust information is problematic. The beneficiary spouse's financial affidavit requires full disclosure under oath. But, he or she may not know the full extent of his or her interests in third-party trusts.

New Hampshire's UTC allows for "secret trusts" that can prohibit the trustee from giving access to trust information. Unlike in New Hampshire, a Massachusetts Vaughn Affidavit allows a court to require an in camera review of a third party's estate planning documents. In the absence of a similar procedure in New Hampshire, a trustee of a silent trust must protect certain trust information from voluntary or actual compelled disclosure to those looking to subvert its protection purposes.

### Choice/Conflicts of Law Issues

If a foreign divorce court is considering a spouse's interest in a New Hampshire trust and the trust agreement provides for New Hampshire governing law, the majority conflicts rule is that the foreign court should look to New Hampshire law to determine the nature of the beneficiary's interests.

This could give a beneficiary spouse a leg-up in a jurisdiction that does not offer the ironclad protection New Hampshire does for discretionary trust interests.

The New Hampshire courts follow this rule in divorce cases involving non-NH trusts; under *Flaherty*, New Hampshire law will be applied to determine whether a foreign trust interest is a property right. Foreign discretionary trust interests should not be considered property, even when the other state's governing law would allow for a different result, if the divorce were litigated there.

### Trust Provisions to Protect Against Divorce Risks

**Self-destruct provisions** provide that upon the commencement of a divorce proceeding to which a beneficiary is a party, the divorcing beneficiary's interests (other than a discretionary interest) and powers under the trust agreement are suspended or eliminated. The divorcing beneficiary also has no right to receive any trust records or asset information, and the trustee is directed to resist becoming a party to any divorce litigation, and refuse to voluntarily submit to personal jurisdiction or provide trust information.

**Favor third-party discretion.** These provisions can protect against divorce risks if drafted with strong precatory language encouraging (not directing) regular distributions of net income, for example, over mandatory distribution provisions.

Additionally, a “**crisis cause**” gives a trustee the discretion to prevent mandatory outright distributions and continue to hold in discretionary trust, if buzzards are circling.

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