

IN THE UNITED STATES BANKRUPTCY COURT  
FOR THE DISTRICT OF NEBRASKA

IN THE MATTER OF: )  
)  
GREGORY & BRENDA RATHE, ) CASE NO. BK03-81956  
)  
Debtor(s). ) CH. 7

MEMORANDUM

Hearing was held in Omaha, Nebraska, on November 20, 2003, on the Chapter 7 trustee's objection to the debtors' amended claim of exemptions (Fil. #32) and resistance by the debtors (Fil. #34). Frank Skrupa appeared for the debtor, and Richard Myers appeared as the Chapter 7 trustee. This memorandum contains findings of fact and conclusions of law required by Federal Rule of Bankruptcy Procedure 7052 and Federal Rule of Civil Procedure 52. This is a core proceeding as defined by 28 U.S.C. § 157(b)(2)(B).

The objection is overruled as moot.

The parties dispute the exemptibility of the debtor's right to receive a distribution from a testamentary trust. The debtors listed Mr. Rathe's interest in the trust on their amended Schedule B (Fil. #31). The interest, valued at \$1.00, is as follows:

21.1326 % of Testamentary Trust Fund from Linda R. Rathe Payable to Debtor upon the age of 35 which is in 4 years. Two brothers are also beneficiaries of the Trust Fund. Not yet vested. Value is unknown.  
(Please note) this Trust was previously valued at \$12,000, however that was the best guess as to the value 4 years hence.

The debtors claimed the interest as exempt on their amended Schedule C under Neb. Rev. Stat. § 44-371(1)(a):

All proceeds, cash values, and benefits accruing under any annuity contract, under any policy or certificate of life insurance payable upon the death of the insured to a beneficiary other than the estate of the insured, or under any accident or health insurance policy shall be exempt from attachment, garnishment, or other legal or equitable process and from all claims of creditors of the insured and of the beneficiary if related to the insured by blood or

marriage, unless a written assignment to the contrary has been obtained by the claimant.

The trustee argues that the exemption should be disallowed because the statutory section under which it is claimed is inapplicable.<sup>1</sup> In response to the trustee's objection, the debtors assert that the asset is not property of the bankruptcy estate because disbursement to the debtor will not occur until 2005, well after the 180-day timeframe in 11 U.S.C. § 541(a)(5).

The trustee appears to be correct that the claimed exemption does not come under Neb. Rev. Stat. § 44-371(1)(a). Nonetheless, the appropriate basis for an exemption is not relevant here because the property is not property of the bankruptcy estate.

The trust at issue was created in 1986 by Mr. Rathe's mother, as part of her last will and testament, to provide for her three children. Upon the youngest child reaching 21 years of age, the trust res was divided into thirds. Each child's share was to be distributed incrementally – one-fourth upon turning 25, one-half of the balance upon turning 30, and the remainder upon turning 35. The trust was also intended to keep each beneficiary's interest from his creditors. The balance of the debtor's share of the trust is scheduled to be paid in approximately two years when he reaches age 35.

The debtor argues that § 541(c)(2) excepts this interest from property of the estate. That section generally excludes a debtor's interest in a spendthrift trust to the extent the trust is protected from creditors under applicable state law. Markmueller v. Case (In re Markmueller), 51 F.3d 775, 776 (8th Cir. 1995).

"Property of the bankruptcy estate" is extensive in scope, covering "all legal or equitable interests of the debtor in property as of the commencement of the case", § 541(a)(1), with exceptions set out in §§ 541(b) and (c)(2). Property of the estate therefore includes a debtor's beneficial interest under

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<sup>1</sup>The debtors had previously attempted to exempt the interest under Neb. Rev. Stat. § 25-1563.01 as a stock bonus, pension, profit-sharing, or similar plan. That claimed exemption was objected to by the trustee and a creditor. The objection was unresisted, so it was granted in August 2003. In September, the debtors filed their amended schedules, giving rise to the present objection.

a trust, unless valid restrictions on the transfer of such an interest exist. See Potter v. Drewes (In re Potter), 228 B.R. 422 (B.A.P. 8th Cir. 1999) (debtor's contingent remainder interest in trust corpus was property of the estate and would be subject to administration when the full value of the asset was realized); Lonstein v. Rockman (In re Lonstein), 950 F.2d 77 (1st Cir. 1991) (debtor's right to an undistributed bequest on the petition date was property of the estate); Yorke v. Bank One Wisconsin Trust Co. (In re Smith), 189 B.R. 8 (N.D. Ill. 1995) (debtor's beneficial interest in a trust was property of the estate even though the debtor's interest was unvested and contingent on the petition date); In re Grieves, 250 B.R. 405 (Bankr. M.D. Fla. 2000) (debtor's right to receive trust assets in two years when she turned 25 was a present vested equitable interest subject to possible future divestment and was property of the estate).

Generally, a spendthrift trust is one in which the right of the beneficiary to future payments of income or capital cannot be voluntarily transferred by the beneficiary or reached by his or her creditors. See, e.g., Lancaster County Bank v. Marshel, 130 Neb. 141, 264 N.W. 470, 476 (1936); Aetna Life Ins. Co. v. Leimer (In re Leimer), 54 B.R. 587, 590 (D. Neb. 1985). "No particular form of words is necessary to create restrictions rendering the interest of a beneficiary of a testamentary trust inalienable and placing the same beyond the reach of his creditors[.]" Marshel, 264 N.W. at 475-76.

The fourth paragraph of the last will and testament states:

FOURTH: No interest hereunder shall be assignable or transferable by any beneficiary or be subject during his or her lifetime to the claims of his or her creditors. However, this provision shall not be construed as restricting the exercise of any power of appointment granted hereunder or any provision granting rights to withdraw principal.

Ex. A to Debtors' Resistance at 8 (Fil. #34).

The language of the trust document clearly and unambiguously evidences the settlor's intent to protect the beneficiaries' interest from their creditors, which is sufficient to constitute a spendthrift trust. The trustee advanced an argument suggesting that the manner of distribution called for in the document (mandatory rather than discretionary) removed it from the realm of spendthrift trusts. However, no support for that argument was

provided to or found by the court.

The trustee's primary argument is that the debtor's prepetition "present expectancy" of receiving the trust distribution is a current asset and should be considered property of the estate. That position would be viable if the trust at issue were not a spendthrift trust. See Potter, 228 B.R. at 424 ("Unless there is a valid spendthrift provision which excludes the debtor's trust interest pursuant to Section 541(c)(2), 'every right of the debtor under the trust becomes property of the estate.'")

Here, under the terms of the trust the debtor has a present interest in the annual distribution of income from the trust,<sup>2</sup> as well as a vested interest in the final distribution of the trust assets to him in two years.<sup>3</sup> That interest in the future

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<sup>2</sup>The trust document, at 2, states, "The trustee is hereby directed to pay to each of the beneficiaries the income to each of my said beneficiaries on at least an annual basis from and after my youngest son's attaining the age of 21 years."

<sup>3</sup> The interest is arguably vested because the right to distribution of the trust assets is his, subject only to him surviving to age 35. See Shackley v. Homer, 87 Neb. 146, 127 N.W. 145 (1910):

Where real estate is devised to executors, to be held by them in trust until C. shall attain the age of 25 years, when the same shall be conveyed to him in fee, . . . this will confer on C. a vested estate in fee simple, . . . subject to defeasance in the event of his death before attaining such age.

See also In re Estate of Darling, 219 Neb. 705, 365 N.W.2d 821 (1985), in a discussion of when future interests vest for purposes of the rule against perpetuities:

"Whenever it is possible the future interest will be construed as vested [rather than contingent]. It is not so much the certainty or uncertainty of the enjoyment of the fee in remainder after the life estate ends as the uncertainty of the person who has a present right to enjoy the future estate if the particular estate came to an end now, which determines  
(continued...)

distribution of the remaining portion of the trust corpus is not available to the debtor's creditors by operation of the anti-alienation provision in the trust document whereby "[n]o interest hereunder shall be assignable or transferable by any beneficiary or be subject during his or her lifetime to the claims of his or her creditors."

In First Nat'l Bank of Omaha v. First Cadco Corp., 189 Neb. 734, 205 N.W.2d 115 (1973), the Nebraska Supreme Court held that a purported assignment, as security for a loan, of a beneficiary's interest in the trust corpus, to be distributed to her when she turned 70, violated the trust's anti-alienation provision and was void ab initio because it "disappoint[ed] the purpose of the settlor by diverting a property or income from the purpose named," as it was executed before the beneficiary had any right to demand the trust corpus. 189 Neb. at 737 (quoting Marshel, supra).

Although the debtor here holds an equitable interest in the corpus of the trust set up by his late mother, the proceeds of which will be distributed to him at age 35, his ability to sell, encumber, or otherwise alienate that interest is prevented by the terms of the trust. For that reason, his equitable interest in that distribution is not property of the bankruptcy estate and may not be claimed by the trustee for the estate's creditors.

Separate order will be entered.

DATED: February 3, 2004

BY THE COURT:

/s/ Timothy J. Mahoney  
Chief Judge

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<sup>3</sup>(...continued)

the character of the remainder. A remainder is vested if the remainderman, being alive, will take at once if the life tenant were to die. *The fact that his enjoyment is postponed, and, on a certain event, as on his death, may never take place at all, does not make the remainder contingent.*

219 Neb. at 709-10, 365 N.W.2d at 824-25 (quoting Wilkins v. Rowan, 107 Neb. 180, 186-87, 185 N.W. 437, 440 (1921) (emphasis supplied)).

Notice given by the Court to:

Frank Skrupa

\*Richard Myers

United States Trustee

\*Movant to give notice of this order to all parties not listed if required by rule or statute.

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ORDER

Hearing was held in Omaha, Nebraska, on November 20, 2003, on the Chapter 7 trustee's objection to the debtors' amended claim of exemptions (Fil. #32) and resistance by the debtors (Fil. #34). Frank Skrupa appeared for the debtor, and Richard Myers appeared as the Chapter 7 trustee.

IT IS ORDERED the Chapter 7 trustee's objection to the debtors' amended claim of exemptions (Fil. #32) is overruled as moot, because the property is not property of the estate. See Memorandum entered this date.

DATED: February 3, 2004

BY THE COURT:

/s/ Timothy J. Mahoney  
Chief Judge

Notice given by the Court to:  
Frank Skrupa  
\*Richard Myers  
United States Trustee

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