COURT OF COMMON PLEAS OF PHILADELPHIA
ORPHANS' COURT DIVISION

Residuary Trust Established Under the Will of George M. Rintz,
Deceased
No. 1652 ST of 2006
Control No. 066026

Sur First and Final Account stated by Kathryn Walker (formerly Uhlmann), Trustee
The account was called for audit December 4, 2006 **Before: Herron, J.**
Counsel appeared as follows:
Paul A. Coghlan, Esquire for the Accountant
Pamela Fingerhut, Esquire, for Office of the
Attorney General
Notice: Terry A. Dake, Esquire, for Trustee in Bankruptcy,
Charles Riley

ADJUDICATION

George M. Rintz died on May 26, 1998. By Will dated June 22, 1992, he left the residue of his estate in trust for the benefit of his wife, Willetta Rintz, during her lifetime, and upon her death to designated beneficiaries.[1] George Rintz named Katherine Uhlmann, presently Kathryn Walker, as Trustee.[2] The decedent's Will was probated by the Register of Wills for Philadelphia County on June 17, 1998, and Letters Testamentary were issued to Willetta E. Rintz and Kathryn Uhlmann (presently Walker).[3] On October 31, 2006, the trustee, Kathryn Walker, filed an account for the period June 30, 2000 to September 30, 2006. The reason for filing the account was the termination of the Trust due to the death of the income beneficiary, Willetta E. Rintz on October 10, 2005.

The dispositive terms of the Trust are set forth at length in the petition for adjudication as well as in the annexed Will. The Will provides that during her lifetime the decedent's wife,

1 Will of George M. Rintz, Article THIRD.
2 Will of George M. Ritntz, Article ELEVENTH.

Willetta E. Rintz, would receive all income and as much principal as the Trustee considered desirable for her health, support, maintenance or education. Mrs. Rintz was also given the right to withdraw annually from the trust principal $5,000 or 5% of trust principal. Upon the death of Willetta Rintz, the Will provided that the remaining trust principal would be paid in specified percentages to individual beneficiaries.

The accountant initially raised two questions for adjudication, but was able to resolve the first question relating to a bequest to Wilkey Memorial Presbyterean (sic) Church with the Attorney General's office and William H. Bradbury, III, Esquire on behalf of the Church. The second issue concerns distribution of a specific bequest to a remainder beneficiary, James Haddon, who filed a Chapter 7 bankruptcy petition on October 14, 2005. After the death of Willetta Rintz, written notices were sent to the remainder beneficiaries concerning their interest in the trust. Subsequently, the accountant received a letter dated May 20, 2006 from Terry A. Dake, Esquire, who stated that he represented Charles L. Riley Jr., the trustee in the federal bankruptcy proceeding involving one of the remainder beneficiaries, James Haddon, in Phoenix, Arizona. According to Mr. Dake, any property due to James Haddon under the Will of George Rintz is property of the bankruptcy estate. Consequently, Mr. Dake requested that James Haddon's share of the trust be paid to the bankruptcy trustee.[4]

The accountant thereafter filed her account, and sent notice of the audit to Mr. Dake as attorney for the bankruptcy trustee. In her notice letter, the accountant stated that the court would be asked to decide whether James Haddon's share should be paid directly to him or to the bankruptcy trustee. More specifically, the notice to Mr. Dake for the bankruptcy trustee

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3 1/2/2007 Accountant's Memorandum of Law. See 5/20/2006 letter (Dake to Coghlan).

indicated that he should file an objection if he opposed payment directly to James Haddon. Upon consideration of the complex questions raised in the petition, this court directed the accountant to file a memorandum of law to address the issue of the proper distribution of James Haddon's share of the Trust in light of the spendthrift clause in the Will creating the Trust and the bankruptcy proceedings.[5] Counsel for the accountant certifies that a copy of the Memorandum and Supplemental Memorandum were served on Mr. Dake, who has submitted no response.

Article EIGHT of George Rintz's last will sets forth the following broad spendthrift provision:

> To the greatest extent permitted by law, before actual payment to a beneficiary no interest in income or principal shall be (i) assignable by a beneficiary or (ii) available to anyone having a claim against a beneficiary. Exceptions may be made if all my trustees, in their sole discretion, approve.

The accountant takes the position in her memorandum and a supplemental memorandum that under the broad terms of the Will's spendthrift provision, James Haddon's share of the trust should be paid to directly to him and not to the trustee in bankruptcy. To support this conclusion, the accountant focuses first on various provisions of the bankruptcy code, and then on Pennsylvania precedent on the enforceability of spendthrift provisions as well as the Pennsylvania Uniform Trust Act. This is also the general approach adopted by the various federal bankruptcy courts that have addressed the issue of the effect of a spendthrift provision on distributions where the beneficiary of a trust or will has filed a petition in bankruptcy. See generally In re Schauer, 246 B.R. 384, 388-89 (D. N. D. 2000); In re Esterson, 150 B.R. 72, 74 (M.D. Fla. 1993) This inquiry is critical because it is well established that valid "spendthrift

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4 See 1/2/2007 Accountant's Memorandum of Law at 6.

trusts are excluded entirely from bankruptcy estates." In re Katz, 220 B.R. 556, 565 (E.D. Pa. 1998).

A threshold jurisdictional issue, however, must first be addressed. There is a zone of concurrent jurisdiction for Orphans' Court that is not always clearly defined. As one commentator has observed, "[b]y far the most controversial area of so-called concurrent jurisdiction is the broad field of claim of creditors against decedent's estates, a zone which, for some inexplicable reason, was never clearly defined by statute…."[6] This area of concurrent jurisdiction is particularly murky in claims involving bankruptcy proceedings. The United States Supreme Court recently clarified the scope of the "probate exception" in the context of a bankruptcy proceeding in its recent opinion Marshall v. Marshall, 126 S. Ct. 1735 (2006), popularly known as the "Anna Nicole Smith" decision.[7] In mapping out the boundaries of the jurisdiction of a state probate court and a bankruptcy court, the Marshall court reiterated the "general principle that, when one court is exercising *in rem* jurisdiction over a *res*, a second court will not assume *in rem* jurisdiction over the same *res*."[8] More specifically, the court observed:

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5 1/2/2007 Accountant's Memorandum of Law.

6 VI Partridge-Remick, Practice and Procedure in the Orphans' Court Division, § 44.03(a)(2) at 27.

7 The facts of Marshall involve two proceedings: while the will of decedent E. Pierce Marshall was being probated in a Texas court, his wife filed for bankruptcy in the United States Bankruptcy Court in the Central District of California. The Decedent's son filed a claim in the bankruptcy court, alleging that the wife had defamed him when she told members of the press that he had engaged in fraud to gain access to his father's assets. This prompted an answer and counterclaim by the wife that the son had tortiously interfered with the decedent's intended gift to her. The bankruptcy court found in favor of the wife on this claim. The District Court after an independent review likewise concluded that the wife's tortious interference with expectancy claim had merit and awarded her $44.3 million in compensatory damages. The son appealed, asserting, inter alia, that the District court lacked jurisdiction to decide this issue which should have been decided instead by the state Probate Court. The United States Supreme Court concluded that the District court properly exercised jurisdiction over this claim for tortious interference with an intended gift. 126 S.Ct. at 1750 (citations omitted).

8 Marshall, 126 S.Ct. at 1748.

> Thus, the probate exception reserves to state probate courts the probate or annulment of a will and the administration of a decedent's estate; it also precludes federal courts from endeavoring to dispose of property that is in the custody of a state probate court. But it does not bar federal courts from adjudicating matters outside those confines and otherwise within federal jurisdiction.
> Mitchell, 126 S.Ct. at 1748.

This analysis of jurisdictional deference set forth in Marshall based on the priority of *in rem* jurisdiction over a *res* was articulated more than 70 years ago by the Pennsylvania Supreme Court in McCahan's Estate, 312 Pa. 515, 168 A. 685 (1933). In that case, the Pennsylvania court concluded that the Orphans' court had jurisdiction to consider the conflicting claims of a trustee in bankruptcy and an executor and that such a dispute did not fall within the exclusive jurisdiction of federal courts. McCahan's Estate, 312 Pa. at 518, 168 A. at 686. In explaining this conclusion, the court observed:

> The rule of the federal courts as to this question may be summarized as follows: The jurisdiction conferred upon the federal courts for the benefit of an assignee in bankruptcy is concurrent with and does not divest that of the state courts in suits of which the latter had full cognizance. Where a state court has, in a proper case, taken jurisdiction of the subject-matter there involved prior to the filing of a petition in bankruptcy, it has complete and effective power to determine finally all rights and title in and to such property….
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> Our own decisions substantiate this conclusion. Recently in the case Dalton & Dalton v. Supplee, we said: "The general rule of law that the court first obtaining jurisdiction over the res retains it to the end, prevails in the law of bankruptcy….A state court distributing a fund in its hands raised by it on its process, or in the possession of the res, is entitled to retain jurisdiction for the purpose of enforcing a lien, even though bankruptcy intervenes.
> McCahan's Estate, 312 Pa. at 519, 168 A. at 687(citations omitted).

Under Marshall and McCahan, therefore, the proper inquiry for determining jurisdiction would focus initially on which court first obtained jurisdiction over the *res*. It is not clear, however, what benchmarks should be employed. In the instant case, for instance, George Rintz's will was probated on June 17, 1998, while the petition in bankruptcy at issue was not

filed until October 14, 2005.[9] The trustee in bankruptcy, moreover, has filed no formal objection to the account to assert a claim or clarify this threshold issue. Consequently, on the present record this court has jurisdiction to decide the substantive issue of the validity of the spendthrift provision in Mr. Rintz's Will and its effect on distribution to a beneficiary who has filed a bankruptcy petition.

Under section 452 of the federal bankruptcy code, an entity in possession of a debtor's property that is part of his bankruptcy estate "shall deliver to the trustee [in bankruptcy], and account for, such property or the value of such property," unless the property is "of inconsequential value or benefit to the estate." 11 U.S.C. § 542. An inheritance, bequest or devise "that a debtor acquires or becomes entitled to acquire within 180 days" of filing his petition would typically fall within the bankruptcy estate. See 11 U.S.C. § 541(a)(5)(A). The accountant maintains, however, that because George Rintz's Will contains a spendthrift provision, section 541 (c)(2) comes into play.[10] This section "is commonly referred to as the 'spendthrift provision.'" In re Esterson, 150 B.R. at 73. Section 541(c)(2) provides as follows:

> (c)(1)Except as provided in paragraph (2) of this subsection, an interest of the debtor in property becomes property of the estate under subsection (a)(1), (a)(2) or (a)(5)of this section notwithstanding any provision in an agreement, transfer instrument or applicable nonbankruptcy law—
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> (2) A restriction on the transfer of a beneficial interest of the debtor in a trust that is enforceable under applicable nonbankruptcy law is enforceable in a case under this title.

The reference to "applicable nonbankruptcy law" has been interpreted as the relevant state law on spendthrift trusts. See, e.g., In re Schauer, 246 B.R. at 388 (interpreting 11 U.S.C. §

9 1/2/2007 Accountant's Memorandum of law at 3.

541(c)(2) in light of North Dakota law which generally recognizes the validity of spendthrift trust provisions); Drewes v. Schonteich, 31 F.3d 674, 676 n.4 ("Neither party disputes the bankruptcy court's use of California and Minnesota law, the situs of the trust funds, in analyzing whether these agreements are excludable under the applicable nonbankruptcy law" as valid spendthrift trusts).

Determining whether James Haddon's share of the trust should be turned over to the bankruptcy trustee thus requires analysis of both the terms of the spendthrift provision and applicable Pennsylvania law. Pennsylvania Courts have long recognized the validity of spendthrift trusts. See Heyl Estate, 352 Pa. 407, 43 A.2d 130 (1945). The rationale for enforcing spendthrift trusts is to protect the intent of the settlor, as the Pennsylvania Supreme Court emphasized in Morgan's Estate, 223 Pa. 228, 72 A. 498 (1909):

> The law rests its protection of what is known as a spendthrift trust fundamentally on the principle of cujus est dare, ejus est disponere. It allows the donor to condition his bounty as suits himself, so long as he violates no law in so doing. When a trust of this kind has been created, the law holds that the donor has an individual right of property in the execution of the trust; and to deprive him of it would be a fraud on his generosity. For the law to appropriate a gift of a person not intended would be an invasion of the donor's private dominion. It is always to be remembered that consideration for the beneficiary does not even in the remotest way enter into the policy of the law; it is regard solely to the rights of the donor. Morgan's Estate, 223 Pa. 228, 230, 72 A. 498, 499 (1909)(citations omitted).

Consequently, Pennsylvania courts "uphold the spendthrift provisions as a means to enforce the settlor's right to dispose of his property as he so chooses." In re Trust Under Agreement of John Ware, 814 A.2d 725, 731 (Pa. Super 2002). Not all attempts to create a spendthrift trust are enforceable. See,e.g. Taubel Estate, 34 Pa. D & C 2d 642, 649(Phila. O.C. 1965)(A settlor cannot

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10 1/2/2007 Accountant's Memorandum of law at 4 (citing 11 U.S.C. § 541(c)(2)).

use a spendthrift clause to protect his assets). To determine whether a spendthrift trust is valid, a court must consider, inter alia, the settlor's intent as expressed in the language of the trust. In re Trust Agreement of John Ware, 814 A.2d at 731.

Guidance on the enforceability of spendthrift provisions in the context of bankruptcy proceedings is provided by Section 58 of the Restatement, Third, of Trusts, which notes that "the rules of this Section have long been recognized under federal bankruptcy law,"[11] in particular Bankruptcy Code section 541(c)(2). A spendthrift trust is defined by Section 58 of the Restatement as a restraint on "voluntary and involuntary alienation of all or any of the beneficiaries' interests."[12] One prerequisite for a valid spendthrift trust for purposes of the bankruptcy code is that the settlor of the trust is not the trust beneficiary. Similarly, a spendthrift trust would be invalid if the beneficiary has the "equivalence of ownership," and can demand immediate distribution of the property.[13] The rationale for these rules is that a valid spendthrift trust restrains both voluntary and involuntary attachments or distributions of a trust. It not only prevents creditors from attaching the beneficiaries' assets, but restrains the beneficiary from distributing assets as well. Such a valid spendthrift trust would thus not "become an asset of the beneficiary's bankruptcy estate under Section 541 of the Bankruptcy Code."[14]

Several ancient Pennsylvania cases have likewise recognized the effect of spendthrift clauses in keeping a debtor's inheritance out of the bankruptcy estate. In Jacobs' Estate, 45 York Legal Record 17 (York O.C. 1931), for instance, the York County Orphans' Court concluded that a

11 Restatement, Third, of Trusts, Section 58, Comments & Illustrations (a).
12 Restatement, Third, of Trusts, Section 58, Comments & Illustrations (a).
13 Restatement , Third, of Trusts, Section 58, Comment on Subsection (1) b & b(1)
14 Restatement, Third, of Trusts, Section 58, Comment on Subsection(1)b(2) & d (2).

decedent's heir who had filed for bankruptcy should nonetheless receive his inheritance under a Will that contained a spendthrift clause, providing that "nothing herein given to my wife or any of my children shall in any manner or under any form of proceedings be subject to or liable for their debts, contracts or ingagements—present or future, of them or either of them, or be subject to or taken in execution or attachment at any suit of any creditor of them or either of them, but said share and income thereof shall be absolutely free from the same." Similarly, in Fulmer's Estate, 34 Berks Cty. L. J.l 1 (Berks Cty. O.C. 1933), the Orphans' Court concluded that where a Will creating a residuary trust contained a spendthrift provision, the interest of the beneficiary who had filed for bankruptcy did not pass to his trustee in bankruptcy. As the Fulmer court explained:

> Spendthrift trusts are recognized under the law of this commonwealth. The law does not fix or require set words or specific stipulations in order that a testamentary trust may be and become a spendthrift trust…..We find in the testamentary disposition under consideration a clearly defined and established spendthrift trust. It is well established that in jurisdictions where spendthrift trusts are valid as against creditors of interest of the beneficiary does not pass to his trustee in bankruptcy.
> Fulmer's Estate, 34 Berks Cty.L.J. at 2-3.

In support of the conclusion that the beneficiary's interest in the trust should not be distributed to the trustee in bankruptcy, the Fulmer court noted that the estate had been under its jurisdiction more than 10 years prior to the filing of the bankruptcy petition. Consequently, the "bankruptcy proceeding of the life tenant did not cut off this power nor remove all questions of distribution into the sphere of federal jurisdiction." The court concluded: "When the orphans' court has once acquired control over property, the jurisdiction of all other courts, though concurrent, is subject thereto." Fulmer Estate, 34 Berks Cty. L. J. at 3.

The Pennsylvania Uniform Trust Act which became effective on November 6, 2006 both

as to existing trusts and to trusts created after that date is also relevant. Section 7705(b)(5) of the Act provides that the effect of a spendthrift provision is governed by Subchapter E, which encompasses section 7741 through 7748. Under Section 7742, a spendthrift provision is effective "only if it restrains both voluntary and involuntary transfer of a beneficiary's interest." 20 Pa.C.S. §7742. The spendthrift provisions in Article VIII of George M. Rintz's Will would satisfy this requirement since it states that distributions to a beneficiary should not be either "assignable by a beneficiary" or "available to anyone having a claim against a beneficiary." Based on this precedent—and the failure of the trustee in bankruptcy to participate in this adjudicatory process-the proposed distribution of 6.25% of the income and 6.25% of the principal to James Haddon is approved.

The accountant states that no Pennsylvania Inheritance Tax was paid during the accounting period because the inheritance tax on future interests was paid by the decedent's estate pursuant to a § 9113 (a) election by the decedent's personal representatives. A Charitable Gift Clearance Certificate was submitted stating that the Attorney General of the Commonwealth of Pennsylvania as parens patriae has no objection to the confirmation of the Account based on the facts contained in the Notice. Finally, the accountant requests a reserve of $15,000 for any taxes that may be due.

No objections were filed to the account. According to the Account for the period June 30, 2006 through September 30, 2006, the balance of principal before distribution is $745,768.73 while the balance of income before distribution is $ 143,445.30 for a total of $ 889,214.03. This sum, composed as stated in the account, plus income received since the filing thereof and subject to distributions already properly made, the entry of appearance slip claim for $1,083.60 in filing

fees, or transfer inheritance tax which may be due, is awarded as set forth in the accountant' petition and statement of proposed distribution:

Income

Proposed Distributee(s)	Amount/Proportion
Kathryn (Uhlmann) Walker	12.50%
Joan Squiccimarra	31.25%
Patricia Jarvis	6.25%
James Haddon	6.25%
Katherine Haddon Fuller	6.25%
Barbara Haddon	6.25%
Timothy Haddon	6.25%
Ruth Stewart	12.50%
Janet Shepherd	12.50%

Principal

Kathryn (Uhlmann) Walker	12.50%
Joan Squiccimarra	31.25%
Patricia Jarvis	6.25%
James Haddon	6.25%
Katherine Haddon Fuller	6.25%
Barbara Haddon	6.25%
Timothy Haddon	6.25%
Ruth Stewart	12.50%
Janet Shepherd	12.50%

Leave is hereby granted to the accountants to make all transfers and assignments necessary to effect distribution in accordance with this adjudication.

AND NOW, this _____ day of JUNE 2007, the account is confirmed absolutely.

Exceptions to this Adjudication may be filed within twenty (20) days from the date of the issuance of the Adjudication. An Appeal from this Adjudication may be taken to the appropriate Appellate Court within thirty (30) days from the issuance of the Adjudication. See Phila. O.C.

Rule 7.1.A and Pa. O.C. Rule 7.1 as amended, and Pa.R.A.P. 902 and 903.

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John W. Herron, J.