Michigan Law Review

Volume 47 | Issue 3

1949

FUTURE INTERESTS - POWERS OF APPOINTMENT- EFFECT OF BANKRUPTCY OF DONEE OF GENERAL TESTAMENTARY POWER

Albert B. Perlin, Jr.
University of Michigan Law School

FUTURE INTERESTS — POWERS OF APPOINTMENT — EFFECT OF BANKRUPTCY OF DONEE OF GENERAL TESTAMENTARY POWER—By her will, *X* established a spendthrift trust,[1] appointing *Y* and a trust company as co-trustees. In addition to receiving the income from the trust during his life, *Y* was given a general testamentary power to appoint the corpus; in default of appointment the corpus was to be divided equally among *Y*'s issue. After *X*'s death *Y* filed a voluntary petition in bankruptcy, listing the above interest as that of a beneficiary of a spendthrift trust, "value none." Before *Y*'s death the trustee in bankruptcy purported to sell to plaintiff, who was not a creditor of *Y*, all of *Y*'s right, title and interest in the trust. After *Y*'s death the plaintiff petitioned for assignment of the trust corpus. *Held*, plaintiff had no interest in the corpus. *In re Peck's Estate*, 320 Mich. 692, 32 N.W. (2d) 14 (1948).

The federal bankruptcy law[2] provides that the trustee in bankruptcy is vested with the title of the bankrupt, and it is settled that the determination of title under this provision depends upon the law of the place where the bankruptcy is adjudicated,[3] in this case, Michigan. Since at common law the mere grant of a general testamentary power of appointment did not carry title to the property

[1] See Roberts v. Michigan Trust Co., 273 Mich. 91, 262 N.W. 744 (1935), for previous litigation involving this trust.

[2] Sec. 70 (a), 30 Stat. L. 565 (1898), as amended by 44 Stat. L. 667 (1926), 11 U.S.C. (1946) § 110 (a). See also § 70(c). Cf. § 70(a)(3), which gives to the trustee in bankruptcy those powers which the bankrupt "might have exercised for his own benefit, but not those which he might have exercised solely for some other person," and principal case at 698.

[3] Horton v. Moore, (C.C.A. 6th, 1940) 110 F. (2d) 189, cert. den., 311 U.S. 692, 61 S.Ct. 75 (1940). For that reason this decision may be of some importance in jurisdictions with similar statutes on powers. Cf., for example, Wis. Stat. (1935) § 232.01; Minn. Stat. Ann. (1945) § 502.62; N.Y. Real Property Law (McKinney, 1945) § 153.

subject to the power,[4] it is clear that the plaintiff had no ground for recovery unless the Michigan statutes provided a basis therefor. The statute provides that the donee of a power is deemed to have a fee, with respect to his creditors and purchasers, "when an absolute power of disposition, not accompanied by any trust, shall be given to the owner of a particular estate, for life or for years. . . ."[5] An absolute power is first defined as one ". . . by means of which the grantee is enabled, in his lifetime, to dispose of the entire fee for his own benefit."[6] The court pointed out that in the principal case "the power of disposition was accompanied by a trust in favor of . . .[Y]," consequently, there was no ability to dispose of the corpus except at death. It seems beyond question that this power was not within the statutory definition of powers in trust;[7] therefore, it is possible that the court's finding on this point was based on a construction of the statutory definition of absolute powers as establishing three tests: the grantee must be able (1) to dispose of the fee (2) during his lifetime (3) for his own benefit.[8] Since this was a testamentary power, and in previous litigation the life interest had been characterized as unassignable and not subject to hypothecation,[9] this power clearly fails the second test and would not pass to the trustee in bankruptcy. However, the statute provides a second definition of absolute powers, which is fulfilled "when a general and beneficial power to devise the inheritance, shall be given to a tenant for life or for years. . . ."[10] Although the law of Michigan is quite clear that a life interest in a spendthrift trust is not the equivalent of a life estate for such a purpose,[11] the court based its decision upon a different ground. The statute provides that a beneficial power exists where ". . . no person other than the grantee has by the terms of its creation any interest in its execution."[12] Since, prior to Y's death, it had been held that the takers in default had sufficient interest to institute an action for alleged misuse of trust funds,[13] the court concluded that persons other than Y

[4] Eaton v. Boston Safe Deposit & Trust Co., 240 U.S. 427, 36 S.Ct. 391 (1916); Jones v. Clifton, 101 U.S. 225 (1880); Forbes v. Snow, 245 Mass. 85, 140 N.E. 418 (1923). But see 47 MICH. L. REV. 93 at 93 (1948).

[5] Mich. Comp. Laws (1929) § 13003; Mich. Stat. Ann. (1937) § 26.99.

[6] Mich. Comp. Laws (1929) § 13007; Mich. Stat. Ann. (1937) § 26.103.

[7] Mich. Comp. Laws (1929) § 13016; Mich. Stat. Ann. (1937) § 26.112, "A general power is in trust when any person or class of persons, other than the grantee, . . . is designated as entitled to the proceeds or other benefits to result from the alienation of the lands, according to the power." Note that the court did not describe the trust corpus although it applied these statutes which pertain only to powers affecting lands.

[8] This would be in accord with the analysis in Matter of Briggs, 101 Misc. 191 at 198, 167 N.Y.S. 632 (1917), decided under N.Y. Rev. Stat. (1829), Pt. II, c. I, tit. 2, art. 3, from which the Michigan Act was adopted.

[9] Supra, note 1. Since spendthrift trusts are recognized in Michigan, the life interest alone could not pass to the trustee in bankruptcy. Cummings v. Corey, 58 Mich. 494, 25 N.W. 481 (1885); Mich. Comp. Laws (1929) § 12985; Mich. Ann. Stat. (1937) § 26.69. Cf. Hull v. Palmer, 155 App. Div. 636 at 644, 140 N.Y.S. 811 (1913).

[10] Mich. Comp. Laws (1929) § 13006; Mich. Stat. Ann. (1937) § 26.102.

[11] Hunt v. Hunt, 124 Mich. 502, 83 N.W. 371 (1900).

[12] Mich. Comp. Laws (1929) § 13001; Mich. Stat. Ann. (1937) § 26.97.

[13] Roberts v. Michigan Trust Co., 273 Mich. 91 at 108, 109, 262 N.W. 744 (1935).

had an interest in the execution of the power; thus it was not a beneficial power.[14] It seems doubtful that the interest of the takers in default which was required to bring an action against *Y* as co-trustee is equivalent to the interest referred to in the statute. Furthermore, by this reasoning the existence of a beneficial interest in the donee of a general testamentary power would appear to depend upon whether or not the donor had made a gift over in default of appointment. If the power is not one in trust, the presence or absence of a gift over is of no importance in ascertaining the nature and scope of the control exercisable by the donee,[15] and if it is a power in trust it is expressly excluded from the operation of the statute.[16] The apparent intention of the statute is to permit creditors to seize that property in which the debtor enjoys the substantial equivalent of a fee;[17] therefore, it seems immaterial that the donee of a general testamentary power may be sued during his lifetime in his office of co-trustee. Clearly, the takers in default had no such interest as would permit them to demand that the power be exercised in a certain manner or that the proceeds of such an exercise be set aside for them. Furthermore, the fact that the takers in default had sufficient interest in the trust to maintain an action for misuse of funds against *Y* as co-trustee does not indicate that they had such an interest in the execution of the power as would allow them to question *Y*'s ability to dispose of the property solely for his benefit.[18] If the court in fact intended to hold that the power was in trust its reasoning might be more understandable, but it is difficult to support that interpretation of the decision since the instrument creating the trust directed that the property ". . . shall go and be disposed of as he [*Y*] may by his last will and testament appoint."[19] Despite some quarrel with the reasoning of the court in regard to the significance of the gift in default, the conclusion seems sound, for this donee did not have such interests as might be deemed to have merged to create a fee for any purpose; the life interest could be enjoyed only during his lifetime, and the power to appoint the remainder was exercisable only at his death. If it had been decided that the trustee in bankruptcy could take and pass *Y*'s power of appointment, the enforcement of the plaintiff's rights would have the anomalous effect of converting a testamentary power into one presently exercisable. This would be contrary to the donor's intent and to the widely-accepted doctrine that an inter vivos contract to exercise a testamentary power in a certain manner, even within the class of persons

[14] Cf. Lyon v. Alexander, 304 Pa. 288 at 291, 156 A. 84 (1931), where the court said, "No one has any interest in a general power of appointment except the donee of the power."

[15] See 47 MICH. L. REV. 93 at 99 (1948).

[16] Supra, note 5.

[17] Cutting v. Cutting, 86 N.Y. 522 at 538 (1881).

[18] See the principal case at 701. Cummings v. Corey, 58 Mich. 494, 25 N.W. 481 (1881).

[19] It is difficult to explain the recited finding of the trial court, which was not contested by the court here, to the effect that " 'Neither the exercise nor nonexercise of the power to designate in his will, would benefit [*Y*] or his estate in any way,' " (principal case at 698), unless there was a power in trust, but it is equally difficult to find circumstances giving rise to the trust. Cf., notes 2 and 7, supra.

contemplated by the donor, is void for all purposes although given for fair consideration.[20] Thus it should be immaterial that in the instant case the plaintiff gave substantial consideration for his purchase from the trustee in bankruptcy.[21]

Albert B. Perlin, Jr.

[20] Northern Trust Co. v. Porter, 368 Ill. 256, 13 N.E. (2d) 487 (1938); Mondell v. Thom, 79 App. D.C. 145, 143 F. (2d) 157 (1944).

[21] It is noteworthy that in this instance the plaintiff probably cannot recover the price paid. Hall v. McGehee, (C.C.A. 5th, 1930) 37 F. (2d) 854, cert. den., 281 U.S. 747, 50 S.Ct. 351 (1930). To the effect that a federal court has no jurisdiction to grant an injunction to protect a purchaser at a bankruptcy sale, see Piedmont Coal Co. v. Hustead, (C.C.A. 3d, 1923) 294 F. 247, cert. den., 264 U.S. 582, 44 S.Ct. 331 (1924).