

Equitable Distribution: When does a Trust have to be joined as a party?

In an earlier post, I wrote about LLCs and when the LLC as an entity must be joined as a party to the equitable distribution proceeding. <https://civil.sog.unc.edu/equitable-distribution-when-does-the-marital-llc-have-to-be-joined-as-a-party/>. The same issue arises when one or both parties have a beneficial interest in a Trust claimed to be marital property.

A beneficiary's interest in an express Trust varies significantly based on the specific provisions of the Trust. But, in most situations, the beneficiary of an express Trust has a property interest in the Trust that can be classified, valued, and distributed in equitable distribution. See e.g., *Lawrence v. Lawrence*, 100 NC App 1 (1990). See also discussion, Brett R. Turner, *Equitable Distribution of Property*, section 6.94, citing along with other cases, *Jenkins v. Jenkins*, 368 S.W.3d 363 (Mo. Ct. App. W.D. 2012); and *Fox v. Fox*, 592 N.W.2d 541 (N.D. 1999). [Turner also acknowledges that an interest in some trusts may be so contingent and speculative as to not amount to a recognizable property interest. That discussion is beyond the scope of this post].

This property interest is an interest separate and apart from property owned and held by the Trust. The person's status as a beneficiary is the property interest. If that interest is identified, classified as marital, and valued, it can be distributed as an asset in equitable distribution.

When does the Trust have to be named as a party?

As with a marital interest in an LLC, a trial court can distribute a marital property interest in a Trust without adding the Trust as a party to the action. For discussions of possible methods of distribution, see *Holte v. Holte*, 837 N.W.2d 894 (N.D., 2013)(marital interest in a Trust may be divided at the time of divorce by awarding the present value of the benefits or when present value is too speculative, by awarding a percentage of future payments), and *S.L. v. R.L.*, 774 N.E.2d 1179 (Mass, 2002)(approving deferred distribution of the marital interest in a Trust, the "if and when received" method of distribution).

However, a Trust must be a party before the trial court can consider distributing property owned by the Trust as part of the equitable distribution. In addition, there must be a legal basis for taking property from the Trust and vesting ownership in a party or both parties to the equitable distribution proceeding. See Brett R. Turner, *Equitable Distribution of Property*, section 6:95 (discussing various actions/claims against a Trust that would result in title to property being taken away from the Trustee and vested in the parties to the equitable distribution proceeding; for example, a claim that a fraudulent conveyance created the Trust).

There are two North Carolina appellate opinions illustrating this difference.

***Lawrence v. Lawrence*, 100 NC App 1 (1990)**

The defendant husband inherited an interest in an investment Trust from his father. Based on evidence provided by the President of the Trust, the trial court concluded that defendant's interest in the Trust was worth \$2,576.00 on the date of marriage and \$35,966 on the date of separation. During the marriage, the parties contributed \$10 per month to the Trust fund. The trial court concluded, and the court of appeals agreed, that 38.2% of defendant's interest in the Trust was marital property while the rest was separate property. The court of appeals concluded that the trial court erred in awarding the entire Trust interest to defendant, holding that plaintiff wife was "entitled to share in the distribution of the marital property portion of the Trust."

The Trust was not a party to the equitable distribution proceeding. The trial court did not distribute any property owned by the Trust. Rather, the trial court distributed only the value of husband's interest as beneficiary of the Trust.

***Nicks v. Nicks*, 241 NC App 487 (2015)**

During the marriage, as part of implementing an estate plan, the parties participated in the creation of an irrevocable Trust of which they were the sole beneficiaries. The Trust was funded with a monetary gift from plaintiff husband's father and with an LLC which held title to a significant amount of what would have been marital property if ownership of the property had not been transferred to the LLC. While both parties were beneficiaries of the Trust, plaintiff husband was the sole manager of the Trust property and had the right to make unlimited withdrawals from the Trust. Wife could only withdraw what husband allowed her to withdraw.

The trial court concluded that the LLC was marital property, distributed the LLC to the husband, and ordered the husband to pay wife a significant distributive award. The husband argued on appeal that the trial court erred in concluding that the LLC was marital property because the LLC was owned by the Trust and the court of appeals agreed. The court stated: "[m]arital property, as defined by [section 50-20](#) of our General Statutes, means all real and personal property acquired by either spouse or both spouses during the course of the marriage and before the date of the separation of the parties, and *presently owned*..." [N.C. Gen. Stat. § 50-20\(b\)\(1\) \(2013\)](#) (emphasis added). Here, the record indicates that on the date of separation, neither [husband] nor [wife] held legal title to either the Trust or [the LLC]."

The defendant wife argued, among other things, that the trial court had imposed a constructive trust on the assets held by the Trust and by the LLC after determining it would be inequitable to allow husband to remain in control of all the marital assets. The court of appeals rejected wife's claim, holding that "a trial court can only impose a constructive trust over a third party that holds legal title to purportedly marital property if that third party is joined as a party to the action" and the party seeking imposition of the trust proves by clear and convincing evidence that a trust should be imposed.

The court of appeals remanded the case to the trial court to give defendant wife the opportunity to add the Trust and the LLC to the action and to provide evidence to establish the propriety of the imposition of a constructive trust. The court of appeals also expressed the strong opinion that the Trust was being used for an improper purpose and that a remedy was available to the trial court, after the Trust was added as a party to defend against the wife's claims. The court stated:

"[W]e note that in spite of the errors discussed *supra*, the majority of the trial court's findings of fact regarding the Trust, [the LLC], and the control [husband] exercises over them are amply supported by the evidence in the record. Further, we find wholly incredible and without reasonable basis [husband's] argument that [the LLC] should not be distributed as marital property despite the trial court's well-supported factual findings that it is composed almost entirely of marital assets. The trial court's findings that [husband] engineered this elaborate scheme as an estate planning vehicle, effectively manages all the assets it conceals, and has the right to decide whether to make distributions of profits and assets from [the LLC] are similarly well supported. In short, it is clear from the record that once the Trust—which holds legal title to [the LLC] and the marital assets therein—is joined as a necessary party to this action, [wife] will have a strong claim for the imposition of a constructive trust. We remand this issue to the trial court for further findings and proceedings consistent with this opinion."