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Death and Bankruptcy: Probate, Trusts, IRAs, and Inheritance Issues

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Chapter 4

Dealing with Death in Bankruptcy: Trusts, Estates, and Inheritances

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I. What Happens When a Debtor Dies?

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If a potential debtor dies prior to filing a bankruptcy petition, the individual would be unable to voluntarily file a petition, for the obvious reasons (including that physically signing the bankruptcy petition is necessary).

Bankruptcy was not created for the benefit of deceased individuals. (As an irreverent side-note that will utilize your newfound bankruptcy terminology, it should be noted that bankruptcy isn't necessary. Many religions would consider a decedent as having obtained the ultimate "fresh start." Meanwhile, science says that death provides the truest form of "automatic stay." And relief from that ultimate form of "stay" is not something our bankruptcy bench, however powerful, is able to grant.)

ii. The Estate of the Decedent

After the death of an individual, state law creates an estate of the decedent, for the benefit of everyone else remaining in the mortal realm. That estate will generally bear the debts of the individual. However, the decedent's estate will be unable to utilize the Bankruptcy Code to discharge those debts. A decedent's estate is not eligible to be a "debtor" in bankruptcy under 11 U.S.C. § 109. That is because a probate estate is not considered a "person" under 11 U.S.C. § 101(41).

Section 101(41) provides that "'person' includes individual, partnership, and corporation," and it does not include an estate. *See, e.g., In re Goerg*, 844 F.2d 1562, 1565-66 (11th Cir. 1988) (holding that decedents' estates are ineligible for relief under the Bankruptcy Code); *In re Estate of Whiteside by Whiteside*, 64 B.R. 99, 101 (Bankr. E.D. Cal. 1986) (concluding that a probate estate is ineligible for relief under the Bankruptcy Code).

Note that this eligibility analysis might be sidestepped by arguing that a personal representative of a decedent is an "individual" who would qualify. *See, e.g., In re Stewart*, 2004 Bankr. LEXIS 1042, at *1-2 (Bankr. D. Or., Mar. 2, 2004) (Now-retired Eugene, Oregon-based Bankruptcy Judge Frank Alley's opinion, allowing the heirs of the deceased debtor to complete the remaining 11 months of the chapter 13 plan by allowing a personal representative appointed by the probate court to stand in the shoes of the debtor). However, that situation will be distinguishable from most, in that the death arose post-petition, and the bankruptcy court – by wrapping up the prior chapter 13 plan – was not supplanting the probate court's duties. In comparison, see *Bunch v. Hopkins Savs. Bank (In re Bunch)*, 249 B.R. 667, 671 (Bankr. D. Md. 2000) (noting that probate estates are unable to be debtors, even through a personal representative). The *Bunch* court held that, where the debtor served as a personal representative of a probate estate, the debtor was still eligible to file a chapter 13 bankruptcy petition as an individual. However, the debtor was prohibited from filing a chapter 13 petition as a personal representative on behalf of the probate estate. *Id.*

b. Death of the Debtor After the Bankruptcy Filing

i. Under FRPB 1016, chapter 7 cases are not dismissed; other chapters can proceed after death of the debtor, if possible.

If a debtor dies during a bankruptcy case, the case is not necessary dismissed. Rule 1016 directs how the case shall proceed.

Chapter 7 cases are definitely not dismissed when the debtor dies. Cases under other chapters can proceed, but dismissal is also possible. FRBP 1016 provides:

> Death or incompetency of the debtor shall not abate a liquidation case under chapter 7 of the Code. In such event the estate shall be administered and the case concluded in the same manner, so far as possible, as though the death or incompetency had not occurred.
>
> If a reorganization, family farmer's debt adjustment, or individual's debt adjustment case is pending under chapter 11, chapter 12, or chapter 13, the case may be dismissed; or if further administration is possible and in the best interest of the parties, the case may proceed and be concluded in the same manner, so far as possible, as though the death or incompetency had not occurred.

FRBP 1016 (emphasis & paragraph break added).

It appears that the Washington bankruptcy courts addressed FRBP 1016 most recently in the bankruptcy case of Lee and Ann Kandu, the joint same-sex debtors who challenged the Defense of Marriage Act (DOMA), 1 U.S.C. § 7. *In re Kandu*, 315 B.R. 123, 130 (Bankr. W.D. Wash. 2004). Judge Snyder ultimately determined that DOMA did not violate the principles of comity, or the Fourth, Fifth, or Tenth Amendments to the U.S. Constitution, and he required bifurcation of the cases or dismissal. Sadly, during the proceedings, joint debtor Ann Kandu died. However, Judge Snyder did not dismiss nor find that the death rendered the issues moot. *Id.* at 130 n.1 ("Pursuant to Fed. R. Bankr. P. 1016, the death of Ann C. Kandu did not abate the Debtors' case under Chapter 7, nor did her death render the issues moot. Rather, in accordance with Fed. R. Bankr. P. 1016, the estate 'shall be administered and the case concluded' in the same manner as though the death did not occur.").

Practically speaking, FRBP 1016 does not explain how a bankruptcy case is to proceed after the debtor dies. Therefore, courts exercise discretion based on the equities and practicalities of the situation, including the state court probate process.

ii. The interplay of bankruptcy and probate estates

Some bankruptcy courts have ruled that if a person wishes to appear on the debtor's behalf, that person must have the legal authority to do so – generally a personal representative of the debtor's estate.

For example, one bankruptcy court concluded that it was not appropriate for the deceased debtor's daughter – despite her having power of attorney and extensive knowledge of the chapter 7 debtor's affairs – to testify at the Meeting of Creditors. The chapter 7 trustee had requested that the court dismiss the case, because the debtor had died and could not appear to testify. The court refused to dismiss the case. Instead, the court directed that the Meeting of Creditors be abated until a personal representative of the debtor's probate estate could be appointed by the state court and could then appear and testify. *In re Lucio*, 251 B.R. 705 (Bankr. W.D. Tex. 2000).

Probate and bankruptcy proceedings generally can proceed simultaneously, but they remain independent. For example, in the chapter 7 context, the only assets that would go into the probate estate are (1) any property claimed as exempt in the debtor's bankruptcy case (assuming no objections to those exemption claims are sustained) and (2) any property acquired by the debtor after the commencement of the bankruptcy case.

In regards to liabilities, the only debts for which the probate estate is liable are those incurred by the decedent after the filing of the bankruptcy petition. *See In re Gridley*, 131 B.R. 447, 451 (Bankr. D. S.D. 1991). The result is that the deceased debtor's pre-bankruptcy debts are discharged in the bankruptcy, and the deceased debtor's exempt assets are passed to the probate estate free of that debt. *See In re Combs*, 166 B.R. 417, 420 (Bankr. N.D. Cal. 1994).

The bankruptcy court has exclusive jurisdiction to determine the debtor′s exemptions as of the date of filing, but it would not have jurisdiction to determine exemptions in the probate estate. *In re Lucio*, 251 B.R. 705, 709-10 (Bankr. W.D. Tex. 2000). Conversely, the probate estate has no authority to supervene the bankruptcy trustee's exclusive control over property of the bankruptcy estate. *Id.* at 710, citing 28 U.S.C. § 1334(d). Neither can the probate estate entertain collateral attacks on the claims allowance process of the bankruptcy case. In other words, "everything up to the commencement of the bankruptcy case is handled by the bankruptcy court and everything post-petition and after death is administered by the probate court." *In re Gridley*, 131 B.R. 447, 451 (Bankr.D. S.D. 1991).

As summarized in the Bankruptcy Code's legislative history:

> Once the estate is created, no interests in property of the estate remain in the debtor. Consequently, if the debtor dies during the case, only property exempted from property of the estate or acquired by the debtor after the commencement of the case and not included as property of the estate will be available to the representative of the debtor's probate estate. The bankruptcy proceeding will continue in rem with respect to property of the

> [e]state *[sic]*, and the discharge will apply in personam to relieve the debtor, and thus his probate representative, of liability for dischargeable debts.

H.R. Rep. No. 595, 95th Cong., 1st Sess. 367-68 (1977); S. Rep. No. 989, 95th Cong., 2d Sess. 82-83 (1978).

iii. Possibilities for chapter 13 cases: dismissal, completion of plan, or hardship discharge, but probably not conversion.

Dismissal of a chapter 13 debtor's case appears to be the most common result when the debtor dies. However, chapter 13 cases do not necessarily need to be dismissed when the debtor dies. For example, in a 2004 Oregon bankruptcy case, Judge Alley allowed the heirs of the deceased debtor to complete the remaining 11 months of the debtor's chapter 13 plan. *In re Stewart*, No. 01-66434-fra13, 2004 Bankr. LEXIS 1042, at *1-2 (Bankr. D. Or., Mar. 2, 2004).

Applying FRBP 1016, Judge Alley evaluated the equities of the situation, which weighed in favor of continuing administration. *Id.* at *3 ("The Debtor could have filed under Chapter 7, with the likely result of a smaller distribution to creditors. Instead, he chose to proceed under Chapter 13, and complied with the plan in every respect until his death. The Debtor's family should not be deprived of the benefits of these efforts: to do so would effectively penalize the debtor for having elected to reorganize.") The court's ruling required appointment of a personal representative for the debtor by the state court. The personal representative would then substitute in for the debtor and fulfill all duties of the debtor. *Id.*

Under some circumstances, courts will grant a hardship discharge upon death under Section 1328(b). *See, e.g., In re Hoover*, 2015 Bankr. LEXIS 924, at *4-5 (Bankr. N.D. Cal. Mar. 24, 2015) (granting hardship discharge where debtor died with one final payment due under his five-year plan). In this 2015 case, the California bankruptcy court surveyed courts that had considered granting a hardship discharge upon death of a chapter 13 debtor:

> Some courts have found that because the Bankruptcy Code section authorizing a hardship discharge does not provide for the debtor's death, and the language of Rule 1016 does not mention a hardship discharge, granting one is impermissible. *See In re Hennessy*, No. 11-13793, 2013 Bankr. LEXIS 3034, 2013 WL 3939886, at *1 (Bankr. N.D. Cal. July 29, 2013). *See also, In re Miller*, AP No. 13-cv-03043-REB, Bankruptcy Case No. 09-12146 ABC, 526 B.R. 857, 2014 U.S. Dist. LEXIS 133435, 2014 WL 4723881, at *3 (D. Colo. Sept. 23, 2014) (finding no error in bankruptcy court's holding that hardship discharge was not contemplated by the drafters of Rule 1016 and upholding denial of a hardship discharge for deceased debtor).

> While § 1328(b) does not contemplate the death of the debtor, other courts have chosen to include death as a circumstance for which the debtor should not justly be held accountable. *See, e.g., In re Perkins*, 381 B.R. 530, 532 (Bankr. S.D. Ill. 2007); *In re Graham*, 63 B.R. 95, 96 (Bankr. E.D. Pa. 1986). These courts have found that granting a hardship discharge is permissible under Rule 1016 when the rule is read to allow the deceased debtor's representative to perform any appropriate action under the Bankruptcy Code that is in the best interest of the parties in the "further administration" of the deceased debtor's case, including disposing of a case via a hardship discharge. *See, e.g., In re Kosinski*, No. 10 bk 28949, 2015 Bankr. LEXIS 779, at *4 (Bankr. N.D. Ill. Mar. 5, 2015); *In re Bevelot*, No. 05-36051, 2007 Bankr. LEXIS 3970, 2007 WL 4191926, at *2 (Bankr. S.D. Ill. Nov. 21, 2007); *In re Maxx Redwine*, No. 09-84032-JB, 2011 Bankr. LEXIS 946, 2011 WL 1116783, at *2 (Bankr. N.D. Ga. Mar. 8, 2011).
>
> This Court concludes that the latter interpretation of Rule 1016 is a fair reading of the rule. In the case of a deceased debtor, further administration of the case can encompass a hardship discharge when the equities in the case so merit, and when the requirements of § 1328(b) are met.

Hoover, 2015 Bankr. LEXIS 924, at *4-5 (paragraph breaks added).

Regarding conversion from chapter 13 to chapter 7 upon death, at least one bankruptcy court has rejected the idea – concluding that Section 1307(f) would not allow it because a probate estate is not eligible to be a debtor under Section 109. *In re Spiser*, 232 B.R. 669 (Bankr. N.D. Tex. 1999). Another court has suggested that conversion would not be equitable because it would prevent creditors from reaching assets that they could otherwise pursue upon dismissal. *In re Hancock*, 2009 Bankr. LEXIS 2174 (Bankr. N.D. Okla. Aug. 10, 2009).

iv. <u>Chapter 11 cases can continue after death, depending on the need for decedent's involvement in the case.</u>

In chapter 11 cases, the outcome will generally depend on whether the chapter 11 plan depends on future earnings or other involvement of the debtor, such as when a trustee is involved. *See, e.g., Wills v. Heritage Bank (In re Wills)*, 226 B.R. 369 (Bankr. E.D. Va. 1998) (concluding that an adversary proceeding could continue in chapter 11 case administered by trustee because debtor's participation was unnecessary). However, because any party in interest may file a reorganization plan under Section 1121(c), it is possible for a debtor's estate to be administered notwithstanding the death (or insanity) of the debtor. *See* COLLIER ON BANKRUPTCY ¶ 1016.03 (16th Ed. 2016) (describing cases allowing guardians and "next friends" to stand in for debtors who become incompetent during their case under FRBP 1016).

II. What Happens to an Inheritance in Bankruptcy?: How to Apply the 180-day "Dragnet" Period under § 541(a)(5) of the Bankruptcy Code

Section 541(a) establishes the scope of the "estate," which includes any property interest that the debtor acquires or becomes entitled to within 180 days after the petition is filed:

- by bequest, devise or inheritance;
- as a result of a property settlement agreement with the debtor's spouse, or of an interlocutory or final divorce decree; or
- as the beneficiary of a life insurance policy or death benefit plan.

11 U.S.C. § 541(a)(5).

This subsection is supplemented by Bankruptcy Rule 1007(h), which requires the debtor to file a supplemental schedule regarding interests acquired or arising after the filing of the petition. This Supplemental Schedule B is to be filed within 14 days after the information comes to the debtor's knowledge or within such further time as the bankruptcy court may allow.

Remarkably, this Supplemental Schedule B must be filed even if the case has been closed. FRBP 1007(h) ("The duty to file a supplemental schedule in accordance with this subdivision continues notwithstanding the closing of the case, except that the schedule need not be filed in a chapter 11, chapter 12, or chapter 13 case with respect to property acquired after entry of the order confirming a chapter 11 plan or discharging the debtor in a chapter 12 or chapter 13 case."). To the extent the debtor wishes to claim an exemption, a Supplemental Schedule C can be filed at the same time. FRBP 1007(h).

a. Section 541(a)'s general scope is intended to bring everything of value into the estate, and it is interpreted expansively.

This scope of Section 541 is interpreted expansively by bankruptcy courts. For example, our Ninth Circuit Court of Appeals recently revisited the broad scope of Section 541(a) in a January 2016 opinion that relates to the subject of this CLE: *Gladstone v. U.S. Bancorp*, 811 F.3d 1133 (9th Cir. 2016). The Ninth Circuit considered whether unmatured term life insurance policies are property of the estate prior to death (*i.e.,* maturity). These unmatured policies can be sold or "settled" before the measuring life dies. Called "viatical settlement" or "life" settlement transactions, the policyholder receives a lump-sum settlement greater than the cash surrender value of the policy, but less than the policy's death benefit. The purchaser continues to pay the policy premiums, and collects the death benefit when the policyholder dies.

In *Gladstone*, based on the expansive nature of Section 541(a), the Ninth Circuit found that a debtor's interest in unmatured term life insurance does have value to the estate, even before the death of the insured life – noting that such policies have value on the secondary market. Therefore, the transferred unmatured term life insurance polices were property of the estate under Section 541(a), and the pre-petition sales/settlements could be avoided by the trustee under Section 548.

In reaching its conclusion, the Ninth Circuit noted that the legislative history indicates that Section 541(a) was intended to "bring anything of value that the debtors have into the estate." *Id.*, quoting H.R. Rep. 95-595 (1977), at 176, reprinted in 1978 U.S.C.C.A.N. 5787, 5963, 6136, and also citing *Chappel v. Proctor (In re Chappel)*, 189 B.R. 489, 493 (9th Cir. BAP 1995) ("The legislative history of the Bankruptcy Code reveals that the concept of property of the estate is to be interpreted broadly.").

b. The 180-day "dragnet" period of Section 541(a)(5) is based on the date of a decedent's death – not the date the will is later probated or the date of distribution of assets – because the date of death is when interests arise under state inheritance law.

In regards to the creation of an interest by "bequest, devise or inheritance" or as the beneficiary of a life insurance policy or death benefit plan, the key date is generally based on the death of the subject. In other words, if the death arises within the 180-day period, then the interest is generally considered an asset of the estate – even if there is a significant delay in the initiation of a probate proceeding, the validation of the will, or the distribution of property thereunder.

The date of death is generally the determinative date under Section 541(a)(5) because state law provides that interests arise as of the date of death. As the Supreme Court has clarified, the existence and scope of a debtor's interest in a given asset is determined by state law. *Butner v. United States*, 440 U.S. 48, 54, 59 L. Ed. 2d 136, 99 S. Ct. 914 (1979); *see also In re Farmers Markets, Inc.*, 792 F.2d 1400, 1402 (9th Cir. 1986).

The Supreme Court's *Butner* opinion addresses the argument for a uniform federal approach in situations involving property rights in bankruptcy. It resolves the issue by holding that "unless some federal interest requires a different result, there is no reason why [property interests] should be analyzed differently [than under state law] simply because an interested party is involved in a bankruptcy proceeding." 440 U.S. at 55. The Supreme Court noted that "Congress has generally left the determination of property rights in the assets of a bankrupt's estate to state law." *Id.* at 54.

While there may be exceptions, it appears that probate laws throughout the United States uniformly provide that title to a decedent's property transfers at death. For example, Oregon, Washington, and California's statutes provide that title to a decedent's property passes on the decedent's death to the person to whom it is devised in the decedent's last will or, in the absence of such a devise, to the decendent's heirs as prescribed in the laws governing intestate succession. *See* ORS 114.215 ("Upon the death of a decedent, title to the property of the decedent vests…"); RCW 11.04.250 & 11.04.290; *See also Chappel v. Proctor (In re Chappel)*, 189 B.R. 489 (9th Cir. BAP 1995) (applying California law).

In *Chappel*, the Ninth Circuit BAP applied California's probate statutes to determine that title transferred as of the date of death – rather than when the will was probated (which was outside of the 180-days of Section 541(a)(5)). The BAP criticized the debtor's contention that he didn't have an interest until the will was probated:

> According to the debtor's interpretation of subsection (a)(5), a debtor legatee who wanted to keep a legacy out of the bankruptcy estate would only have to prolong probate of the will for one hundred and eighty (180) days. Clearly this result is not what Congress intended, nor is it supported by § 541.

Chappel, 189 B.R. at 494. However, the BAP concluded that, because the death actually occurred a few days before the petition date, Section 541(a)(5) was unnecessary to its conclusion that the interests were property of the Estate – instead Section 541(a)(1) applied.

In 2007, the Ninth Circuit BAP again addressed these issues in *Dardashti v. Golden (In re Dardashti)*, 2007 Bankr. LEXIS 4941 (9th Cir. BAP 2007). The debtor's Israeli father had died on November 14, 1999, which was 122 days after the debtor filed a chapter 7 bankruptcy case, and about 10 days after the "no asset" case had been closed. The death was not disclosed to the trustee. The father's will was probated in the Family Court of Israel. The will devised to the debtor some partial interests in properties located in Israel.

The father's probate estate was approved for distribution in April 2000, about 6 months after he died. Much later (over five years later), the chapter trustee learned of the debtor's interest in the Israel properties. The trustee then moved to reopen the case to administer the assets.

The BAP concluded that Israel's inheritance laws applied. Noting that the bankruptcy court had not done so (but should have), the BAP consulted English translations of the Hebrew texts on Israeli laws of inheritance to determine the nature and extent, if any, of the debtor's rights to the interest at the time of his father's death. *Id.* at *20-*21.

The BAP concluded that under Israeli inheritance law, upon a person's death, the decedent's estate passes to his heirs. *Id.* at *20-*21. The BAP determined that no rights under a will can be claimed until the probate order is entered. However, as in the United States, an heir has the right to renounce any portion of the estate after the testator's death and prior to the distribution of the estate. (Such disclaimers under Oregon and Washington law are addressed later in Parts III and IV of these materials, and they would not work post-petition.) Furthermore, an heir has the right to transfer or charge any portion of his part of the estate after the testator's death and prior to distribution of the estate. In addition, the BAP noted that creditors of the heir may attach the heir's part of the estate. *Id.*

Based on these foreign laws of inheritance, which are similar to those in the United States, the BAP in *Dardashti* concluded that the debtor had obtained his interests under Israeli inheritance law as of his father's death, 122 days after the case was filed:

> [T]he critical inquiry is whether the Debtor "acquired or became entitled to acquire" any legal or equitable interest in the Testator's estate within 180 days of commencement of the

> Debtor's bankruptcy case. We conclude that the Debtor acquired at least an equitable interest in the Testator's estate at the time of the Testator's death. That interest then automatically became a part of the Debtor's bankruptcy estate as a matter of federal bankruptcy law.

Dardashti v. Golden (In re Dardashti), 2007 Bankr. LEXIS 4941 (9th Cir. BAP 2007).

c. <u>Section 541(a)'s 180-day "dragnet" period is effectively extended for chapter 13 debtors during the pendency of the bankruptcy case, in light of Section 1306.</u>

In chapter 13, the estate is expanded under 11 U.S.C. § 1306(a) to include property acquired post-petition. Section 1306(a) of the Bankruptcy Code provides:

> Property of the [chapter 13] estate includes, in addition to the property specified in section 541 of this title — (1) all property of the kind specified in such section that the debtor acquires after the commencement of the case but before the case is closed, dismissed, or converted to a case under chapter 7, 11, or 12 of this title, whichever occurs first[.]

11 U.S.C. § 1306(a). Bankruptcy courts have evaluated how Section 1306(a) relates to Section 541(a)(5)(A) when a chapter 13 debtor receives a bequest more than 180 days after the chapter 13 petition was filed. Bankruptcy courts generally conclude that Section 1306(a) effectively extends the 180-day period, until the case is closed, dismissed, or converted. *See Dale v. Maney (In re Dale)*, 505 B.R. 8 (9th Cir. BAP 2014) (BAP opinion by the Honorable Randall L. Dunn), relying on *Carroll v. Logan (In re Carroll)*, 735 F.3d 147 (4th Cir. 2013), which provide an overview of the "great weight of authority" that inheritances outside the 180-day period are property of the chapter 13 estate.

Bankruptcy Judge Kirscher for the District of Montana applied the Ninth Circuit BAP's *Dale* opinion. *See In re Wirshing*, 2015 Bankr. LEXIS 1829, at *6 (Bankr. D. Mont., June 3, 2015). Judge Kirscher concluded that a post-180-day inheritance was property of the estate, and he granted the trustee's motion to modify the chapter 13 plan to require turnover of the inheritance (which was projected to pay all creditors in full). *Id.*

1. <u>Disclosure of the inheritance is required within 14 days under FRBP 1007(h).</u>

It is very important to disclose the inheritance promptly. Bankruptcy Rule 1007(h) requires the debtor to file a supplemental schedule regarding interests acquired or arising after the filing of the petition. This Supplemental Schedule B is to be filed <u>within 14 days</u> after the information comes to the debtor's knowledge (or within such further time as the bankruptcy court may allow). As described below, the failure to disclose promptly seems to have a significant impact in how bankruptcy courts evaluate in the impact of the inheritance on the case.

Besides filing a Supplemental Schedule B, debtors should advise their chapter 13 trustee's office. In Oregon, the local form Chapter 13 Order (LBF 1350.05) requires disclosure to the trustee:

> Except for those amounts listed in the schedules, the debtor shall report immediately to the trustee any right of the debtor or debtor's spouse to a distribution of funds (other than regular monthly income) or other property which exceeds a value of $2,500.00. This includes the right to disbursements from any source, including, but not limited to, bonuses and inheritances. Any such funds to which the debtor becomes entitled shall be held by the debtor and not used without the trustee's permission, or, if such permission is not obtained, a court order.

LBF 1350.05, ¶ 2. Therefore, debtors should be advised to report any inheritances (or other windfalls) to the chapter 13 trustee, and then hold them.

ii. An inheritance will likely justify chapter 13 plan modification as a "significant change in circumstances."

Under Section 1329(a)(1), a chapter 13 plan can be modified (at the request of the trustee or an unsecured creditor) to increase or decrease payments of disposable income. Does a post-petition inheritance require plan modification? One could argue that inheritances, like gifts, are not actually "income" – at least in the eyes of the IRS. The Internal Revenue Code provides that gross income "does not include property acquired by gift, bequest, devise, or inheritance." *See* 26 U.S.C. § 102(a). One could also argue that a post-petition inheritance would not alter the terms of a confirmed plan under Section 1327, based on *res judicata* principles.

However, at least in the Ninth Circuit, it appears that any "significant change in circumstances" warrants plan modification. *See Mattson v. Howe (In re Mattson)*, 468 B.R. 361, 369 (B.A.P. 9th Cir. 2012) (noting that the res judicata doctrine does not apply to plan modifications in the Ninth Circuit: "[W]e have held, as did the Seventh Circuit in *In re Witkowski* [16 F.3d 739 (1994)], that the bankruptcy court may consider a change in circumstances in the exercise of its discretion.").

Because the inheritance is considered property of the estate, the inheritance creates a change in value of the estate. Based on this change in circumstances, a debtor would likely be compelled to modify the chapter 13 plan (assuming the chapter 13 trustee or a creditor makes a motion). *See In re Zeitchic*, 2011 Bankr. LEXIS 4588, at *2-*3 (Bankr. E.D. N.C., Sept. 23, 2011) (requiring debtor to file modified plan, based on receipt of approximately $250,000 of inheritance); *In re Tinney*, 2012 Bankr. LEXIS 3092, at *9 (Bankr. N.D. Ala. July 9, 2012) (concluding that an inheritance was property of the estate and constituted a change in circumstances sufficient to warrant plan modification: "The benefits of chapter 13 come with a price tag... And that [ch. 13 plan] commitment is subject to modification when circumstances change the debtor's ability to pay during the life of the case."); *In re DelConte*, 2012 Bankr. LEXIS 2150 (Bankr. E.D. Va., May 15, 2012) (same).

In that *DelConte* case, a chapter 13 debtor wife received an inherited 50% interest in real estate, valued at $133,000. She did not immediately disclose the inheritance. Instead, she promptly deeded the interest to her sister for no consideration. Nearly a year later, the wife and her joint debtor husband notified the chapter 13 trustee. The chapter 13 trustee moved for modification based on the change of circumstances. Concluding that the inheritance was a substantial and unanticipated post-confirmation change of circumstances, the bankruptcy court required the wife to modify her plan to satisfy all creditors within 30 days or be dismissed without discharge. Interestingly, because there was no evidence that the husband had participated in the wife's actions, he was not impacted. The court determined that upon completion of the plan payments due under the original plan, the husband would be entitled to a discharge. *In re DelConte*, 2012 Bankr. LEXIS 2150, at *3-*9.

iii. <u>Post-inheritance, the chapter 13 plan will likely be modified based on the best-interests-of-creditors test.</u>

Generally when chapter 13 trustees learn of inheritances and seek modification, bankruptcy courts will modify the plan based on the best-interests-of-creditors test. *In re Nott*, 269 B.R. 250 (Bankr. M.D. Fla. 2000) (holding that the best-interests-of-creditors test under Section 1325(a)(4) must be applied to any modified plan, based on the amount that unsecured creditors would receive in a hypothetical chapter 7 case when the chapter 13 debtor received a nearly-$300,000 inheritance); *In re Moran*, 2012 Bankr. LEXIS 4426 (Bankr. N.D. Tex. Sept. 25, 2102) (considering plan modification based on a post-confirmation inheritance of approximately $25,000, and requiring application of the best-interests-of-creditors test as of the effective date of modified plan).

d. <u>Conversion to chapter 7 can *sometimes* protect a chapter 13 debtor's inheritance if received after 180 days of filing.</u>

In the Ninth Circuit, an inheritance received outside of the 180-day period will be treated as property of the chapter 13 estate. *Dale v. Maney (In re Dale)*, 505 B.R. 8 (9th Cir. BAP 2014). However, this conclusion has been criticized, particularly because of Section 348(f). Section 348 was amended in 1994 to make it clear that property of the estate in a case converted in good faith from chapter 13 to chapter 7 is only "property of the estate as of the date of filing of the petition, that remains in the possession of or is under the control of the debtor on the date of conversion." 11 U.S.C. § 348(f)(1)(A). The idea was that debtors should not be penalized for attempting to reorganize under chapter 13 but later failing.

The Supreme Court recently addressed Section 348(f), allowing the converting chapter 13 debtor to retain an asset acquired post-petition. *Harris v. Viegelahn*, 135 S. Ct. 182, 2015 U.S. LEXIS 3203 (May 18, 2015) (concluding that post-petition wages held by a chapter 13 trustee at the time of conversion to chapter 7 must be returned to the debtor under Section 348(f)(1)(A)). However, the Supreme Court's opinion, while unanimous, was very narrowly crafted, and it only addressed the question of a debtor's post-petition wages.

Would the Supreme Court come to the same conclusion if, instead of regular wages, the post-petition asset was windfall from an inheritance or from winning the lottery? Maybe. It would depend on the facts, and whether the "bad faith" exception of Section 348(f)(2) applied.

As with many issues, bankruptcy courts weigh the totality of the circumstances to determine whether a debtor's conversion is done in bad faith. *See, e.g., Farrar v. Sandoval (In re Sandoval)*, 2005 Bankr. LEXIS 3383, *18-*22 (9th Cir. BAP 2005) (unpublished opinion, but citing and discussing prior Ninth Circuit precedent regarding the totality of the circumstances test, and applying it to Section 348(f)(2)).

When evaluating the totality of the circumstances, the amount seems to matter. It seems that five-digit inheritances – coupled with good facts – can avoid challenge. In one case, a 28-year old widow, with four children under the age of eight, received life insurance proceeds of $64,060 when her husband died during their joint chapter 13. Their bankruptcy attorney helped her convert to chapter 7. Her counsel advised her that she could spend the life insurance proceeds because the death had occurred outside of the 180-day period in Section 541(a)(5). She promptly spent the money by paying down their mortgage, paying off a vehicle loan, and using the rest to cover the burial expenses for her husband. After learning of the situation, the chapter 7 trustee did not allege bad faith under Section 348(f)(2) – the issue was solely the interplay of Section 341(f)(1)(a) with Section 1306(a). *In re Brinkley*, 323 B.R. 685, 690 (Bankr. W.D. Ark. 2005) (concluding that the $64,060 of life insurance proceeds were not property of the chapter 7 estate, based on Section 348(f)(1)(a)); *See also In re Morrison*, 403 B.R. 895, 904 (Bankr. M.D. Fla. 2009) (same result, where no bad faith was alleged in regards to $10,000 of life insurance proceeds received by a widow after her joint debtor husband died during their chapter 13 case); *In re Stillwaggon*, 2014 Bankr. LEXIS 1085, at *7-*9 (Bankr. M.D. Fla., Mar. 19, 2014) (same result, where chapter 7 trustee alleged bad faith when chapter 13 debtor converted after she received a $57,800 inheritance; the court found no bad faith, noting that 34 of 36 plan payments had been made and as in *Sandoval*, she did not intend to "game the system").

In contrast, where the inheritance is six figures and the facts are less compelling, bad faith has been alleged by chapter 7 trustees, and bankruptcy courts have agreed. For example, a widow received $125,000.00 in life insurance proceeds when her husband died during her chapter 13 case. She promptly filed a notice of conversion, falsely stating that she could not afford the plan payments based on the loss of her husband and his income. However, the court found that her financial reporting was not accurate, and that the life insurance proceeds were sufficient to pay the unsecured debt in full. After considering the totality of the circumstances, the bankruptcy court concluded the conversion was in bad faith. *In re Smith*, 2012 Bankr. LEXIS 78, at *8 (Bankr. N.D. Ohio, Jan. 9, 2012); *See also Mullican v. Moser*, 417 B.R. 408 (E.D. Tex. 2009) (affirming bankruptcy court's finding of bad faith conversion under Section 348(f)(2), where the debtors could easily have completed their chapter 13 plan with a $162,000 IRA and other assets inherited post-petition).

Therefore, it is important to advise chapter 13 debtors to immediately disclose the receipt of inheritances, whenever they arise. Once disclosed, the debtors can consider options, including converting or modifying the plan.

III. When are interests in trusts considered property of the bankruptcy estate under either Section 541(a)(1) or Section 541(a)(5)(A)?

a. The scope of "bequest, devise, or inheritance" in the (5)(A) "dragnet"

Section 541(a) defines what interests of a debtor are included in the estate. However, the Code provides no definition of the terms bequest, devise, or inheritance in Section 541(a)(5)(A). Traditionally, a "bequest" is "a gift (transfer) by will of personal property." *Birdsell v. Coumbe (In re Coumbe)*, 304 B.R. 378, 383-84 (B.A.P. 9th Cir. 2003), quoting BLACK'S LAW DICTIONARY 160 (6th ed. 1990). A "devise" is "a testamentary disposition of land or realty; a gift of real property by the last will and testament of the donor." *Id.*, quoting BLACK'S at 452. An "inheritance" is "property which descends to heir on the intestate death of another." *Id.*, quoting BLACK'S at 782.

As already discussed, the existence and scope of a debtor's property interest is determined by state law. *State v. Farmers Mkts., Inc. (In re Farmers Mkts, Inc.)*, 792 F.2d 1400, 1402 (9th Cir. 1986), applying *Butner v. United States*, 440 U.S. 48, 54-55 (1979). Therefore, to determine what constitutes a "bequest, devise, or inheritance" under Section 541(a)(5)(A), bankruptcy courts must use state law. *See Kosmala v. Cook (In re Cook)*, 2008 Bankr. LEXIS 4728 (9th Cir. BAP, Nov. 3, 2008), citing *Magill v. Newman (Matter of Newman)*, 903 F.2d 1150, 1153 (7th Cir. 1990).

For example, proceeds from so-called "Payable On Death" bank accounts would not be a "bequest, devise, or inheritance," depending on the state's statute. *See Holter v. Resop (In re Holter)*, 401 B.R. 372 (Bankr. W.D. Wis. 2009); *In re Hall*, 394 B.R. 582 (Bankr. D. Kan. 2008).

In contrast, transfers caused by wills or testamentary trusts generally fall under this "dragnet" provision. However, non-testamentary (*inter vivos*) trusts are trickier, as discussed at length below, and should be considered under Section 541(a)(5)(A) as well as Section 541(a)(1).

b. An interest in an *inter vivos* ("between living persons") trust is probably not considered a "bequest, devise, or inheritance" under Section 541(a)(5)(A)…

1. *In re Kosmala* (9th Cir. BAP 2008) (unpublished)

In its unpublished *Kosmala* opinion, the Ninth Circuit BAP determined that a debtor's interest in a trust, as of his bankruptcy filing, was a contingent beneficial interest in a revocable *inter vivos* (*i.e.,* non-testamentary) trust. The settlor of the trust then died post-petition, within 180 days, and the debtor's interests vested. The BAP applied

Section 541(a)(5)(A) and determined the debtor's interest in the *inter vivos* trust was not property of the bankruptcy estate.

In coming to its conclusion, the BAP evaluated post-petition trust distributions to a debtor beneficiary – comparing testamentary with *inter vivos* interests. *Inter vivos* trusts are considered to be non-testamentary even when the terms of the trust may provide for the transfer of the trust's assets to its beneficiaries upon the last settlor's death. *Id.,* citing RESTATEMENT (SECOND) OF TRUSTS § 57 (1959).

The BAP explained that a disposition does not become testamentary merely because the interest of the beneficiary does not vest before the death of the settlor, or because the settlor reserves the power to revoke or modify the trust. *Id.*; *Spencer v. Zimmermann (In re Spencer)*, 306 B.R. 328, 334 (Bankr. C.D. Cal. 2004). Furthermore, there is no requirement that an *inter vivos* trust provide the beneficiary monthly income payments or be outside the control of the settlor.

In contrast, as noted by the BAP, if a trust is created after the death of the settlor by the terms of a will, then the trust – and the disposition of the trust assets – is considered to be testamentary. *Id.* at *11-12, citing RESTATEMENT (SECOND) OF TRUSTS § 56 cmt. a (1959); and *York v. Kragness (In re Kragness)*, 58 B.R. 939 (Bankr. D. Or. 1986). Distributions from such testamentary trusts received by a debtor-beneficiary within 180 days of filing are considered property of the estate. *Id.* at *12, citing *Heidkamp v. Galliher (In re Hunger)*, 272 B.R. 792, 795 (Bankr. M.D. Fla. 2002); and *In re Kragness*, 58 B.R. at 944.

Regarding the specific facts of *Kosmala*, an *inter vivos* trust existed at the time of filing. The chapter 7 debtor was a contingent beneficiary, and the trust had a spendthrift provision. His parents had set up the trust as settlors, co-trustees, and beneficiaries. The father had died previously, but the debtor's mother was still living. While the trust had some assets at the time, the debtor didn't consider himself as having an interest in it, and the trust had a spendthrift provision. Therefore, the debtor did not disclose the trust in his schedules.

The debtor's mother died within 180 days of his chapter 7 bankruptcy filing. The mother's will distributed all of her assets to the trust – a so-called "pour over" disposition. At that point (*i.e.,* within 180 days of filing), all of the parents' assets were in the trust and were "immediately" distributable to the trust's beneficiaries – including the debtor.

Even though (1) the mother's death occurred within the 180 days of Section 541(a)(5); (2) the death caused a testamentary transfer of significant assets (to the trust); and (3) the death vested the debtor's 25% interest in his parents' *inter vivos* trust within the 180-days period, the bankruptcy court and BAP both concluded that the vesting of the trust was not a "bequest, devise, or inheritance" under state law.

While the parents' will indeed caused the transfer of substantial assets upon the mother's death, that transfer was made to the trust – not to the debtor. Therefore, the BAP determined that, because the debtor's interest in the trust had vested after the petition date, it was not property of the estate under Section 541(a)(1). *Id.* at *15, citing *Schmitt v. Burton (In re Schmitt)*, 215 B.R. 417, 422 (9th Cir. BAP 1997) ("Under Oregon law, the beneficiary of a revocable trust does not have a property right."). Therefore, the trustee's contention that the trust's spendthrift provision was invalid did not matter to the bankruptcy court or BAP. The debtor's interest in the trust was not property of the estate, but Section 541(a)(1) was never considered. *See also In re Mattern*, 2006 Bankr. LEXIS 326, at *16 (Bankr. D. Kan., Mar. 9, 2006) (same holding, with similar facts including a revocable trust with "pour over" will triggered post-petition).

2. *In re Kosmala* (9th Cir. 2010) (unpublished)

The chapter 7 trustee appealed the BAP's unpublished decision to the Ninth Circuit. The Ninth Circuit issued a short unpublished opinion, quoted below in its entirety:

> Because property devised to an *inter vivos* trust from a will "is not deemed to be held under a testamentary trust of the testator but becomes a part of the trust to which it is given," Cal. Prob. Code § 6300, the real property at issue here became a part of the *inter vivos* trust to which it was devised. We have held that "'income distributions derived from an *inter vivos* trust do not fit within' the definition of § 541(a)(5)(A) and therefore escape 'the pale of the 180 day dragnet.'" *Neuton v. Danning (In re Neuton)*, 922 F.2d 1379, 1384 n.6 (9th Cir. 1990) (quoting *Newman v. Magill*, 99 B.R. 881, 884-85 (C.D. Ill. 1989)). Therefore, the Debtor's interest in the *inter vivos* trust assets is not property of the bankruptcy estate.
>
> AFFIRMED.

Kosmala v. Cook (In re Cook), 370 F. App'x 791, 791-92 (9th Cir. 2010).

This unpublished opinion of the Ninth Circuit affirmed the BAP and bankruptcy court in regards to Section 541(a)(5)(A). The Ninth Circuit opinion solely relied on its *Neuton* opinion in rendering that brief decision: *Neuton v. Danning (In re Neuton)*, 922 F.2d 1379 (9th Cir. 1990).

As described further below, *Neuton* actually appears to support the trustee's argument as to Section 541(a)(1). In other words, it appears that the contingent interest held by the debtor in *Kosmala* should have been considered property of the estate as of the petition date, applying *Neuton*.

3. *In re Crandall* (Bankr. D. Conn. 1994) (published)

When rendering its opinion in *Kosmala*, this Ninth Circuit BAP relied on the oft-cited case of *In re Crandall*, 173 B.R. 836, 838 (Bankr. D. Conn. 1994). The bankruptcy court in *Crandall* applied Washington state law and provided significant analysis of *inter vivos* trusts under Section 541(a)(5)(A). *Crandall* is important for its background regarding Section 541(a)(5), and because it also calls into question the BAP's opinion in *Kosmala* as to Section 541(a)(1).

In *Crandall*, the debtor's mother died within 180 days of his chapter 7 filing. The debtor then amended his schedules under FRPB 1007(h) to list his one-third interest in his mother's trust. The trust was revocable at any time, and the debtor was a contingent beneficiary until his interests vested upon his mother's death. The trustee contended that the trust's vesting was based on a "bequest, devise, or inheritance" and therefore made the debtor's interest property of the estate under Section 541(a)(5)(A).

As noted in *Crandall*, the 1938 revisions to the Bankruptcy Act of 1898 included inherited assets received by a debtor within six months of filing bankruptcy. Then, the Bankruptcy Reform Act of 1978 placed within the 180-day window other interests that the debtor may acquire post-petition, including as a beneficiary of a life insurance policy or of a death benefit plan. The bankruptcy court in *Crandall* noted that the Bankruptcy Reform Act of 1978 did not add to Section 541(a)(5) devices generally described as "will substitutes" – such as revocable *inter vivos* trusts. *Id.*

While *Crandall* acknowledged that revocable *inter vivos* trusts seem testamentary in nature, it determined that there were two important distinctions: First, "will substitutes are simply 'nonprobate wills' – each reserves to the owner complete lifetime dominion, including the power to name and to change beneficiaries upon death." *In re Crandall*, 173 B.R. at 838 (quoting John H. Langbein, The Nonprobate Revolution and the Future of the Law of Succession, 97 HARV. L. REV. 1108, 1109 (1984)). Second, *Crandall* emphasized that federal courts are to interpret the words of the Bankruptcy Code narrowly, and according to their plain meaning. *Id.* at 838-39 (describing the Supreme Court's "unflagging insistence" that federal courts interpret the words of the Bankruptcy Code according to their "plain meaning").

The court in *Crandall* ultimately concluded that the debtor's interest in the revocable *inter vivos* trust was not property of the estate within the meaning of Section 541(a)(5)(A). This is the conclusion reached by our BAP in *Kosmala.* However, *Crandall* did not stop there, as described below.

c. However, a contingent interest in an unvested irrevocable *inter vivos* trust likely would be considered property of the estate under Section 541**(a)(1)**.

Notwithstanding the *Kosmala* opinion, courts in the Ninth Circuit would probably conclude in a future case that a contingent interest in an unvested irrevocable *inter vivos* trust is actually property of the estate – based simply on the state of the interest as of the date of filing under Section 541(a)(1), rather than considering the Section 541(a)(5) dragnet.

1. *In re Crandall (*Bankr. D. Conn. 1994) (published)

Kosmala and other courts have relied heavily on *Crandall*'s analysis of Section 541(a)(5). However, the bankruptcy court in *Crandall* then moved on to evaluate the interest under Section 541(a)(1), as of the date of filing. Even though the argument was not raised by the parties in *Crandall*, the bankruptcy court determined that the debtor's contingent interest in the trust was in fact property of the estate under Section 541(a)(1) as of the date of filing, applying Washington state law:

> Section 541(a)(1) provides that a debtor's estate upon commencement of the case comprises, *inter alia*, "all legal or equitable interests of the debtor in property." The debtor at the commencement of his case held an interest in the Trust which he had acquired upon the execution of the Trust. *See* RESTATEMENT (SECOND) OF TRUSTS, § 56 cmt. f, illus. 8 (1959) (describing such interest as "a contingent equitable interest in remainder"); *cf.* Austin W. Scott, The Law of Trusts § 57.1 (4th ed. 1987) (stating that under such a trust, "the beneficiary at once acquires a future interest, although it is an interest subject to be divested by the exercise of the power [of the settlor to revoke or modify]"); *Burg v. Old Nat'l Bank*, 4 Wash. App. 773, 483 P.2d 1290, 1292 (Wash. App.), modified, 79 Wash. 2d 849, 490 P.2d 731 (Wash. 1971) (identifying this type of interest as "a vested remainder subject to complete defeasance").
>
> In defining property of the estate, "Congress indicated its intention to include all legally recognizable interests, although they may be contingent and not subject to possession until some future time." *In re Knight*, 164 Bankr. 372, 374 (Bankr. S.D. Fla. 1994) (citing *In re Ryerson*, 739 F.2d 1423, 1425 (9th Cir. 1984)). In the present case, the debtor's interest in the trust, regardless of nomenclature, is property of the estate.

In re Crandall, 173 B.R. 836, 839 (Bankr. D. Conn. 1994). *See also Gladys Ragsdale Tr. v. Tostige (In re Tostige)*, 537 B.R. 847, 852-53 (Bankr. E.D. Mich. 2015) (distinguishing *Kosmala* because under Michigan law, the debtor's interest in her living mother's revocable trust was considered a "vested present interest" at the time the chapter 7 petition was filed, even though such "vested interest" was contingent and subject to revocation at any time).

2. *In re Neuton* (9th Cir. 1990) (published)

It seems likely that Ninth Circuit bankruptcy courts would concur with *Crandall*'s analysis. Before *Kosmala*, the Ninth Circuit considered a debtor's contingent interest in an *inter vivos* (non-testamentary) trust, similar to the debtor's interest in *Kosmala*. *See Neuton v. B. Danning (In re Neuton)*, 922 F.2d 1379 (9th Cir. 1990). The Ninth Circuit held that the debtor's beneficial interest in an *inter vivos* trust that was revocable on the petition date constituted property of the bankruptcy estate under Section 541(a)(1), because the interest became irrevocable when the debtor's interest vested upon the death of the settlor – an occurrence which took place 46 days after the bankruptcy petition was filed:

> [C]ontingent interests of the type at issue in this case typically have been held to be property of the bankrupt estate. For example, in *In re Ryerson*, this court affirmed the *BAP's* holding that money to which the debtor became entitled eight months after filing for bankruptcy should be included in the estate, notwithstanding the fact that at the time of filing the debtor had an unvested, contingent interest. 739 F.2d 1423, 1425 (9th Cir. 1984). Similarly, in *In re Dias* the bankruptcy court found that "a beneficial interest in a trust is an equitable interest under § 541(a)(1)" despite the fact that at the time of filing it was contingent. 37 Bankr. 584, 586-87 (Bankr. D. Idaho 1984). *See also In re Bialac*, 712 F.2d 426, 431 (9th Cir. 1983) ("The courts have consistently said that options or contingent interests are property of the bankruptcy estate under section 541"); *In re Young*, 93 Bankr. 590 (Bankr. S.D. Ohio 1988) (unliquidated or contingent claims are property of the estate); *In re Turner*, 29 Bankr. 628 (Bankr. D. Me. 1983) (contingent interest in earnest money deposit in escrow account belongs to the estate). *Cf.* RESTATEMENT (2D) OF TRUSTS § 162 ("The mere fact that the interest of the beneficiary is contingent and not vested does not preclude creditors of the beneficiary from reaching it").

Neuton, 922 F.2d at 1382-83. After so concluding, the Ninth Circuit then evaluated the spendthrift provisions of the trust under California law and determined that a portion of the future payments under the trust were unprotected and subject to the chapter 7 trustee's administration. *Id.* at 1384-85.

3. *In re Schmitt* (9th Cir. BAP 1997) (published)

It should be noted that the Ninth Circuit BAP has published an opinion after *Neuton* saying that, under either Oregon and California law, a "beneficiary of a revocable trust does not have a property right." *Burton v. Ulrich (In re Schmitt)*, 215 B.R. 417, 422 (9th Cir. BAP 1997). While this appears contradictory to the analysis above, the analysis was sparse and conditional, and the facts were distinguishable.

In this pre-*Kosmala* opinion, the Ninth Circuit BAP in *Schmitt* addressed a chapter 7 trustee's settlement of the debtor's contingent interest in a revocable trust. The BAP had to determine whether the trustee's $2,000 settlement of an interest in a trust was reasonable, when the debtor contended the value was approximately $4,500 and when – as the scathing dissent pointed out – the trust documents had not been produced.

In *Schmitt*, the BAP only briefly evaluated Oregon and California law. The BAP then explained that, even if the debtor had an interest in the revocable trust, the debtor's contingent interest was so speculative to make the attachment and sale of the debtor's interest in the revocable trust unreasonable. *Id.* at 423. The BAP therefore affirmed the bankruptcy court's approval of the trustee's $2,000 settlement, despite the trustee's lack of complete information about the trust. Because of these particular circumstances, *Schmitt* would likely not impact a bankruptcy court's future application of *Neuton*.

4. *In re Jones* (9th Cir. BAP 2014) (unpublished)

Neuton is still good law. In fact, our 9th Circuit BAP recently relied on *Neuton* in a similar case. *See Jones v. Mullen (In re Jones)*, 2014 Bankr. LEXIS 488, at *13 (9th Cir. BAP, Feb. 5, 2014). In the unpublished *Jones* opinion, the BAP panel (which included Judge Dunn) concluded that, at the time of filing, the chapter 7 debtor held a contingent, revocable future interest in his mother's real property.

In *Jones*, the debtor's interest was based on a Beneficiary Deed that would transfer the mother's real property to her son upon the mother's death. The mother died post-petition (within 180 days), and the bankruptcy court authorized the trustee to sell the property.

On appeal, the BAP panel explained that it did not need to determine whether the transfer by deed constituted a "bequest, devise or inheritance" under Section 541(a)(5), because Section 541(a)(1) definitely applied to make the contingent interest property of the estate. *Id.* at *15; compare with *Burton v. Ulrich (In re Schmitt)*, 215 B.R. 417, 422 (9th Cir. BAP 1997).

Therefore, to be safe, debtors should be advised to disclose on Schedule B even unvested and contingent/potential interests in trusts of family members who have not died, as such interests would probably be considered property of the bankruptcy estate.

IV. Are Spendthrift Provisions in a Trust Agreement Effective?: How to distinguish corpus from income under Section 541(a)(1) and (5)(A).

The Restatement (Second) of Trusts defines a spendthrift trust as a "trust in which by the terms of the trust or by statute a valid restraint on the voluntary and involuntary transfer of the interest of the beneficiary is imposed." RESTATEMENT (SECOND) OF TRUSTS, § 152(2).

A true spendthrift trust "prevents the beneficiary from transferring his right to future payments of income or capital; the creditors … are also prevented from attacking the beneficiary's interest to satisfy their claims." *Birdsell v. Coumbe (In re Coumbe)*, 304 B.R. 378, 382 (9th Cir. BAP 2003), quoting *Togut v. Hecht (In re Hecht)*, 54 B.R. 379, 383 (Bankr. S.D. N.Y. 1985).

The Bankruptcy Code excludes from the estate any property that contains "[a] restriction on the transfer of a beneficial interest of the debtor in a trust that is enforceable under applicable nonbankruptcy law." 11 U.S.C. § 541(c)(2). Under Section 541(c)(2), an anti-alienation provision in a valid spendthrift trust created under state law is an enforceable "restriction on the transfer of a beneficial interest of the debtor," thereby excluding the trust assets from the bankruptcy estate. *See Patterson v. Shumate*, 504 U.S. 753, 757-58 (1992).

a. Corpus of valid spendthrift trust = no estate interest

Therefore, based on Section 541(c)(2), "a bankruptcy trustee can assert no claim to the corpus of a spendthrift trust because it is not property of estate." *Birdsell v. Coumbe (In re Coumbe)*, 304 B.R. at 384. *See also Magill v. Newman (In re Newman)*, 903 F.2d 1150, 1152 (7th Cir. 1990) (holding that the debtor's interest in the distribution of the corpus of the spendthrift trusts was not property of estate); *Mitchell v. West (In re West),* 81 B.R. 22, 25-26 (9th Cir. BAP 1987) ("The debtor's interest in property excluded under section 541(c)(2) is not listed in section 541(a)(5)…. By this omission, Congress intended that such property not come into the estate.").

This law applies to valid spendthrift provisions. Sometimes spendthrift provisions are deemed invalid or unenforceable, as discussed further.

b. Income from spendthrift trust if testamentary = property of the estate

In contrast to corpus distributions, a majority of bankruptcy courts have held that an income distribution from a testamentary spendthrift trust constitutes a "bequest" within the meaning of § 541(a)(5)(A) and therefore is property of the estate. *See, e.g., Gordon C. York, Inc. v. Kragness (In re Kragness)*, 58 B.R. 939 (Bankr. D. Or. 1986) (holding that, despite spendthrift language protecting the corpus, the distributions from the testamentary trust within the 180-day period were "bequests") In *Kragness*, Judge Radcliffe concluded the bequests were not protected because "once trust income is paid to [the beneficiary] the income so paid is no longer subject to the protection of the spendthrift provisions contained in the trust." *Id.*

Therefore, a post-petition distribution from a testamentary trust must be evaluated, to determine what is corpus versus income. The corpus portion of the distribution would not be property of the estate under Section 541(c)(2). To the extent the distribution includes income, that portion would likely be deemed a "bequest" and therefore property of the estate pursuant to Section 541(a)(5)(A). *See, e.g., Birdsell v. Coumbe (In re Coumbe)*, 304 B.R. 378, 386 (B.A.P. 9th Cir. 2003) (providing a detailed discussion on the subject).

c. Income from spendthrift trust if *inter vivos* (non-testamentary) and vesting post-petition = probably not property of the estate

If the spendthrift trust is *inter vivos* (*i.e.,* not testamentary) and the vesting by settlor's death occurs within the 180 days after filing, then a bankruptcy court will likely look to the date of filing. If the spendthrift provision was valid as of the petition date, then the interest, and any income therefrom, would not be property of the estate under Section 541(c)(2). *Zimmermann v. Spencer (In re Spencer)*, 306 B.R. 328, 332 (Bankr. C.D. Cal. 2004) ("An asset is determined to be estate property by examining the nature of the asset **on the date the bankruptcy petition was filed**.") (emphasis in original). According to *Kosmala* and *Spencer*, the fact that the vesting occurred within the 180-day period of Section 541(a)(5)(A) would not matter, because the vesting of an inter vivos trust is not a "bequest, devise, or inheritance."

V. When are IRAs (like Social Security Benefits) Protected from Creditors Under an Exemption?

Although a beneficial interest in an individual retirement account ("IRA") is considered property of a bankruptcy estate, most IRAs are considered fully exempt – except if they were inherited.

Under Oregon Revised Statutes (ORS) section 18.358, most IRAs are fully exempt and protected. If an IRA is an ERISA-qualified plan – such as 401(k)'s and 403(b)'s – then the IRA should qualify as being exempt under Oregon law. *See* ORS 18.358. This statute also protects social security benefits. *Hobson v. Hobson*, 136 Or. App. 516, 901 P2d 914 (1995).

Separate from state exemption law, the Bankruptcy Code provides unlimited exemptions for many retirement plans (with a few exceptions and limitations) – so the entire amount of the retirement account would be protected. *See* 11 U.S.C. § 522. However, the Supreme Court has ruled that an inherited IRA are not "retirement funds" within the meaning of §522(b)(3)(C) and thus not exempt. *Clark v. Rameker*, 134 S. Ct 2242, 189 L. Ed.2d 157 (2014). An inherited IRA is considered to be any IRA inherited pre-petition and which the debtor did not establish or fund. Previously, bankruptcy courts generally had held that an inherited IRA was protected under Section 522(b)(3)(C). The Supreme Court noted that inherited IRAs are unique and not a retirement asset. Inheritors cannot put additional funds into the account, and recipients of inherited IRAs may withdraw the entire balance of the account at any time and use it for any purpose without penalty. Therefore, they do not get protection under bankruptcy law.

VI. Can an Inheritance be Avoided Strategically?: The Risks and Benefits of Using Disclaimers under Oregon Law

a. <u>What is a Disclaimer and how does it work?</u>

A "disclaimer" has been defined as "the refusal to accept an interest in or power over property." UNIFORM DISCLAIMER OF PROPERTY INTERESTS ACT, § 2(3) (1999). Disclaimers are a creature of state law and are generally statutory.

A properly-executed disclaimer can be powerful, effectively shielding the disclaimed inheritance or other interest from the disclaimant's creditors. The disclaimer does this by "relating back" to the date of the decedent's death. This relation-back provision is a legal fiction that "retroactively eliminates" any property interest that a disclaimant had previously held in the disclaimed property. *Gaughan v. Edward Dittlof Revocable Trust (In re Costas)*, 555 F.3d 790 (9th Cir. 2009).

The Supreme Court addressed disclaimers in *U.S. v. Irvine*, 511 U.S. 224 (1994). The Court explained that "an effective disclaimer . . . relate[s] back to the moment of the original transfer of the interest being disclaimed, having the effect of canceling the transfer to the disclaimant *ab initio* and substituting a single transfer from the original donor to the beneficiary of the disclaimer." *Id.* at 239. "An important consequence of treating a disclaimer as an *ab initio* defeasance is that the disclaimant's creditors are barred from reaching the disclaimed property." *Id.* at 239-240.

b. Disclaimer law in Oregon, under the Uniform Disclaimer of Property Interest Act (UDPIA)

Oregon has adopted the Uniform Disclaimer of Property Interest Act ("**UDPIA**"), which has also been enacted in Alaska, Arizona, Arkansas, Colorado, Delaware, District of Columbia, Florida, Hawaii, Indiana, Iowa, Maryland, Minnesota, Nevada, New Mexico, North Dakota, Texas, U.S. Virgin Islands, Virginia, West Virginia. Oregon's UDPIA is codified at ORS 105.623–105.649.

Oregon's version of the UDPIA is attached as **Appendix A**.

i. Requirements for an effective disclaimer under the UDPIA

Oregon's most-relevant statutes regarding disclaimers are ORS 105.629 and 105.630. The elements for an effective disclaimer are provided in 105.629(3), as follows:

> (3) To be effective, a disclaimer must:
>
> (a) Be in writing or otherwise recorded by inscription on a tangible medium or by storage in an electronic or other medium in a manner that allows the disclaimer to be retrieved in perceivable form;
>
> (b) Declare that the person disclaims the interest in the property or in the power;
>
> (c) Describe the interest in property or power over property that is disclaimed;
>
> (d) Be signed by the person making the disclaimer; and
>
> (e) Be delivered or filed in the manner provided in ORS 105.642 (Delivery or filing).

To ensure a disclaimer is valid and enforceable, be sure to follow the detailed conditions for proper delivery/filing as set forth in ORS 105.642.

ii. Acceptance renders a disclaimer void.

Another important condition is that the disclaimant not first accept the interest. ORS 105.643 states that a disclaimer of interest is barred if "The disclaimant accepts the interest sought to be disclaimed." *See In re Kolb*, 326 F.3d 1030 (9th Cir. 2003) (describing the acceptance analysis as a "fact sensitive inquiry that centers on the conduct of the beneficiary, and the result of such conduct").

The Ninth Circuit summarized a number of examples of "acceptance" that invalidated disclaimers throughout the country. The Circuit determined that California's disclaimer law was intended to "prohibit the disclaimer of an interest accepted through conduct by a beneficiary implying an intent to direct or control the property in a manner that conveys more than a *de minimis* benefit to the beneficiary or a third party." *Id.* at 1039.

Because avoiding "acceptance" of any benefit is important, one might consider filing the disclaimer prior to death. However, disclaiming too early can also render a disclaimer invalid. *See Matter of Estate of Baird*, 131 Wash.2d 514, 933 P.2d 1031 (Wash. 1997) (invalidating a disclaimer that was filed before the decedent died).

c. Effective disclaimers are not "transfers" and therefore are not avoidable as fraudulent transfers.

ORS 105.633 addresses the timing of a disclaimer, and it creates the legal fiction that "the disclaimed interest passes as if the disclaimant had died immediately before the time of distribution." ORS 105.633(3)(a)(A). In addition, ORS 105.629(6) provides that "[a] disclaimer made under ORS 105.623 to 105.649 is not a transfer, assignment or release." Through these UDPIA sections, effective disclaimers are powerful because they cannot be avoided as a fraudulent transfer, in or out of bankruptcy.

i. Ninth Circuit law regarding pre-bankruptcy disclaimers.

Generally, disclaimers properly executed under state law are not fraudulent transfers under Section 548. Our Oregon Bankruptcy Court was one of the first courts to address the question after the Supreme Court's decision in *Drye v. U.S.*, 528 U.S. 49 (1999). *Drye* was a non-bankruptcy case, in which the Supreme Court concluded that a federal tax lien attached to a tax debtor's disclaimed property, despite state law relation-back rules. In 2000, chapter 7 trustee Michael Grassmueck used *Drye* (and the one post-*Drye* bankruptcy court opinion, from Iowa) to argue that a pre-petition disclaimer should be considered an avoidable transfer under Section 548.

In a 2011 opinion, now-Chief Judge Brown ruled against the trustee, noting that Congress has given the IRS superior rights compared to other creditors. *In re Nistler*, 259 B.R. 723, 726-27 (2001), appling the pre-*Drye* precedent of the Ninth Circuit BAP: *In re Bright*, 241 B.R. 664 (9th Cir. BAP 1999). The issue was then disputed in other bankruptcy courts around the country.

The Ninth Circuit was the first Circuit to address the issue, in *Gaughan v. Edward Dittlof Revocable Tr. (In re Costas)*, 555 F.3d 790, 794-95 (9th Cir. 2009). The Ninth Circuit affirmed the opinions of the BAP and the bankruptcy court. The Ninth Circuit applied a similar analysis to Chief Judge Brown's *Nistler* opinion, concluding that *Drye*, as a tax lien case, was distinguishable. *Id.* at 797 (holding that a disclaimer, properly executed under state law, does not qualify as the "transfer . . . of an interest of the debtor in property" for purposes of Section 548).

The concept behind these rulings – both pre- and post-*Drye* – is that a beneficiary never possesses the disclaimed property. Based on the legal fiction of "relation back" created by state statute, a disclaimer is not considered a fraudulent transfer because it's not actually a "transfer." *See also Laughlin v. Nouveau Body and Tan, L.L.C. (In re Laughlin)*, 602 F.3d 417, 428 (5th Cir. 2010) (following the Ninth Circuit's analysis in

Costas to similarly determine that a valid disclaimer under state law not a transfer after *Drye v. U.S.*, 528 U.S. 49, 120 S. Ct. 474, 145 L. Ed. 2d 466 (1999).

ii. EXCEPTION: Post-petition disclaimers during the bankruptcy case are generally ineffective and avoidable.

In contrast to pre-petition disclaimers, a disclaimer executed after the bankruptcy case is commenced will likely be deemed ineffective. *See, e.g., In re Stambaugh*, 2010 Bankr. LEXIS 3141, *8-*9 (Bankr. N.D. Iowa, Sept. 17, 2010) (finding disclaimer invalid because the death, and the disclaimer, arose within the 180 days after the petition date). The *Stambaugh* opinion provides an overview of the case law on the subject – including the Ninth Circuit's *Costas* opinion.

d. Disclaimers require care; attorneys advising debtors regarding disclaimers of inheritance may want to write their own disclaimers (in their engagement agreement).

Disclaimers can be powerful tools. However, if challenged, they can often be rendered invalid and ineffective. If the disclaimer is part of a debtor's pre-bankruptcy planning, then expect that the disclaimer will be challenged by the trustee. Disclaimers are not common. However, the disclaimers the author has seen in his representation of chapter 7 bankruptcy trustees have all been successfully challenged and settled, and the Professional Liability Fund (the Oregon State Bar's malpractice insurer) was involved in at least one of the cases. This is primarily because (1) the disclaimer requirements are quite specific, and (2) the equities seem to often weigh against them.

Courts who have addressed challenges to disclaimers seem to disfavor them and apply the requirements strictly, presumably because they can lead to inequitable results. Not every disclaiming party will be doing so in bad faith, and the circumstances will matter.

While the concept remains generally unspoken and is not discussed in opinions, it is possible for other beneficiaries (who are generally family members) to later return the disclaimed assets to the debtor who disclaimed, once the trustee or the active creditor is no longer watching. Such a transfer back to the disclaiming party could be treated as a post-petition gift, and it might not be recoverable by the trustee or by the discharged creditors. Regardless of whether this concept is a factor, it seems that when a disclaimer's effectiveness is challenged, courts are generally willing to scrutinize the validity of disclaimers and apply strict standards on debtors who attempt to disclaim.

If you are representing a debtor who wants to disclaim a pre-petition inheritance, be very careful to read the state disclaimer statutes that would be applicable (generally based on the decedent's state) and engage a lawyer from that state to assist your client. If the decedent is in your state of practice, be sure to communicate your own "disclaimer" to your client regarding the scope of your representation and what you can and can't promise, to protect yourself from later claims of malpractice if the disclaimer is determined to be ineffective.

If you are representing a trustee or creditor and the debtor disclaimed, obtain and then review the disclaimer and the supporting evidence carefully (including communications among the disclaiming party, the personal representative, and the other beneficiaries). Review the state's disclaimer laws carefully and determine whether it was properly crafted, filed, and served. In particular, evaluate whether the disclaiming party already accepted some form of benefit from the inheritance.

Oregon Revised Statutes (ORS) Chapter 105 — Property Rights (2017 Edition)

UNIFORM DISCLAIMER OF PROPERTY INTERESTS ACT

105.623 Short title. ORS 105.623 to 105.649 may be cited as the Uniform Disclaimer of Property Interests Act. [2001 c.245 §1]

105.624 Definitions for ORS 105.623 to 105.649. As used in ORS 105.623 to 105.649:

(1) "Disclaimant" means the person to whom a disclaimed interest or power would have passed had the disclaimer not been made.

(2) "Disclaimed interest" means the interest that would have passed to the disclaimant had the disclaimer not been made.

(3) "Disclaimer" means the refusal to accept an interest in property or a power over property.

(4) "Fiduciary" means a personal representative, trustee, agent acting under a power of attorney or other person authorized to act as a fiduciary with respect to the property of another person.

(5) "Jointly held property" means property held in the name of two or more persons under an arrangement pursuant to which:

(a) All holders have concurrent interests; and

(b) The last surviving holder is entitled to the whole of the property.

(6) "Person" means an individual, corporation, business trust, partnership, limited liability company, association, joint venture, government, governmental subdivision, agency, public corporation or any other legal or commercial entity.

(7) "State" means a state of the United States, the District of Columbia, Puerto Rico, the United States Virgin Islands or any territory or insular possession subject to the jurisdiction of the United States. The term includes an Indian tribe or band, or Alaskan native village, recognized by federal law or formally acknowledged by another state.

(8) "Trust" means:

(a) A charitable or noncharitable express trust, including any additions made to the trust, whenever and however created; and

(b) A trust created pursuant to a statute or judgment that requires the trust to be administered in the same manner as an express trust. [2001 c.245 §2; 2003 c.576 §369; 2009 c.294 §15]

105.626 Scope. ORS 105.623 to 105.649 apply to disclaimers of any interest in or power over property without regard to when the interest or power that is disclaimed was created. [2001 c.245 §3]

105.628 Effect on other law. (1) Unless displaced by a provision of ORS 105.623 to 105.649, the principles of law and equity supplement ORS 105.623 to 105.649.

(2) ORS 105.623 to 105.649 do not limit any right of a person to waive, release, disclaim or renounce an interest in property, or power over property, under a law other than ORS 105.623 to 105.649. [2001 c.245 §4]

105.629 Power to disclaim; general requirements; when irrevocable. (1) A person may disclaim, in whole or part, any interest in property or any power over property, including a power of appointment. A person may disclaim the interest or power even if the person who created the interest or power imposed a spendthrift provision or similar restriction on transfer or imposed a restriction or limitation on the right to disclaim.

(2) Except to the extent that a fiduciary's right to disclaim is expressly restricted or limited by another statute of this state or by the instrument creating the fiduciary relationship, a fiduciary may disclaim, in whole or part, any interest in property or power over property, including a power of appointment, without regard to whether the fiduciary is acting in a personal or representative capacity. A fiduciary may disclaim the interest or power even if the creator of the interest or power imposed a spendthrift provision or similar restriction on transfer or a restriction or limitation on the right to disclaim, or an instrument other than the instrument that created the fiduciary relationship imposed a restriction or limitation on the right to disclaim.

(3) To be effective, a disclaimer must:

(a) Be in writing or otherwise recorded by inscription on a tangible medium or by storage in an electronic or other medium in a manner that allows the disclaimer to be retrieved in perceivable form;

(b) Declare that the person disclaims the interest in the property or in the power;

(c) Describe the interest in property or power over property that is disclaimed;

(d) Be signed by the person making the disclaimer; and

(e) Be delivered or filed in the manner provided in ORS 105.642.

(4) A partial disclaimer may be expressed as a fraction, percentage, monetary amount, term of years, limitation of a power or as any other interest or estate in the property.

(5) A disclaimer is irrevocable when the disclaimer is delivered or filed pursuant to ORS 105.642 or when the disclaimer becomes effective as provided in ORS 105.633 to 105.641, whichever occurs later.

(6) A disclaimer made under ORS 105.623 to 105.649 is not a transfer, assignment or release. [2001 c.245 §5]

105.633 Disclaimer of interest in property. (1) For the purposes of this section:

(a) "Time of distribution" means the time when a disclaimed interest would have taken effect through possession or enjoyment.

(b) "Future interest" means an interest that takes effect through possession or enjoyment, if at all, at a time later than the time that the interest is created.

(2) Except for a disclaimer governed by ORS 105.634 or 105.636, the following rules apply to a disclaimer of an interest in property:

(a) The disclaimer takes effect when the instrument creating the interest becomes irrevocable or, if the interest arises under the law of intestate succession, when the decedent dies.

(b) The disclaimed interest passes according to any provision in the instrument creating the interest providing for the disposition of the specific interest in the event the interest is disclaimed, or according to any provision in the instrument creating the interest providing for the disposition of interests in general in the event the interests created by the instrument are disclaimed.

(3) If the instrument creating the interest does not contain a provision described in subsection (2)(b) of this section, or if the interest arises under the law of intestate succession, the following rules apply:

(a) (A) If the disclaimant is an individual, except as otherwise provided in subparagraphs (B) and (C) of this paragraph, the disclaimed interest passes as if the disclaimant had died immediately before the time of distribution.

(B) If by law or under the instrument the descendants of the disclaimant would share in the disclaimed interest by any method of representation had the disclaimant died before the time of distribution, the disclaimed interest passes only to the descendants of the disclaimant who survive the time of distribution.

(C) If the disclaimed interest would pass to the disclaimant's estate had the disclaimant died before the time of distribution, the disclaimed interest instead passes by representation to the descendants of the disclaimant who survive the time of distribution. If no descendant of the disclaimant survives the time of distribution, the disclaimed interest passes to those persons, including the state, but excluding the disclaimant, and in such shares, as would succeed to the transferor's intestate estate under the intestate succession law of the transferor's domicile had the transferor died at the time of distribution. However, if the transferor's surviving spouse is living but is remarried at the time of distribution, the transferor is deemed to have died unmarried at the time of distribution.

(b) If the disclaimant is not an individual, the disclaimed interest passes as if the disclaimant did not exist.

(4) Upon the disclaimer of a preceding interest, a future interest held by a person other than the disclaimant takes effect as if the disclaimant had died or ceased to exist immediately before the time of distribution, but a future interest held by the disclaimant is not accelerated in possession or enjoyment. [2001 c.245 §6; 2009 c.17 §1]

105.634 Disclaimer of rights of survivorship in jointly held property. (1) Upon the death of a holder of jointly held property, a surviving holder may disclaim, in whole or part, the greater of:

(a) A fractional share of the property determined by dividing the number one by the number of joint holders alive immediately before the death of the holder to whose death the disclaimer relates; or

(b) All of the property except that part of the value of the entire interest attributable to the contribution furnished by the disclaimant.

(2) A disclaimer under subsection (1) of this section takes effect upon the death of the holder of jointly held property to whose death the disclaimer relates.

(3) An interest in jointly held property disclaimed by a surviving holder of the property passes as if the disclaimant predeceased the holder to whose death the disclaimer relates. [2001 c.245 §7]

105.636 Disclaimer of interest by trustee. If a trustee disclaims an interest in property that otherwise would have become trust property, the interest does not become trust property. [2001 c.245 §8]

105.638 Disclaimer of power of appointment or other power not held in fiduciary capacity. If a holder disclaims a power of appointment or other power not held in a fiduciary capacity, the following rules apply:

(1) If the holder has not exercised the power, the disclaimer takes effect as of the time the instrument creating the power becomes irrevocable.

(2) If the holder has exercised the power and the disclaimer is of a power other than a presently exercisable general power of appointment, the disclaimer takes effect immediately after the last exercise of the power.

(3) The instrument creating the power is construed as if the power expired when the disclaimer became effective. [2001 c.245 §9]

105.639 Disclaimer by appointee, object or taker in default of exercise of power of appointment. (1) A disclaimer of an interest in property by an appointee of a power of appointment takes effect as of the time the instrument by which the holder exercises the power becomes irrevocable.

(2) A disclaimer of an interest in property by a person who is an object of an exercise of a power of appointment, or by a person who is a taker in default of an exercise of a power of appointment, takes effect as of the time the instrument creating the power becomes irrevocable. [2001 c.245 §10]

105.641 Disclaimer of power held in fiduciary capacity. (1) If a fiduciary disclaims a power held in a fiduciary capacity that has not been exercised, the disclaimer takes effect as of the time the instrument creating the power becomes irrevocable.

(2) If a fiduciary disclaims a power held in a fiduciary capacity that has been exercised, the disclaimer takes effect immediately after the last exercise of the power.

(3) A disclaimer under this section applies to another fiduciary if the disclaimer so provides and the fiduciary disclaiming has the authority to bind the estate, trust or other person for whom the fiduciary is acting. [2001 c.245 §11]

105.642 Delivery or filing. (1) As used in this section, "beneficiary designation" means an instrument, other than an instrument creating a trust, naming the beneficiary of:

(a) An annuity or insurance policy;

(b) An account with a designation for payment on death;

(c) A security registered in beneficiary form;

(d) A pension, profit-sharing, retirement or other employment-related benefit plan; or

(e) Any other nonprobate transfer at death.

(2) Subject to subsections (3) to (12) of this section, delivery of a disclaimer may be made by personal delivery, first class mail or any other method likely to result in receipt of the disclaimer.

(3) If the interest to be disclaimed is created under the law of intestate succession or an interest created by will, other than an interest in a testamentary trust:

(a) A disclaimer must be delivered to the personal representative of the decedent's estate; or

(b) If a personal representative is not serving at the time the disclaimer is made, the disclaimer must be filed with a court having authority to appoint the personal representative.

(4) In the case of an interest in a testamentary trust:

(a) A disclaimer must be delivered to the trustee;

(b) If a trustee is not serving at the time the disclaimer is made but a personal representative for the decedent's estate is serving, the disclaimer must be delivered to the personal representative; or

(c) If neither a trustee nor a personal representative is serving at the time the disclaimer is made, the disclaimer must be filed with a court having authority to enforce the trust.

(5) In the case of an interest in an inter vivos trust:

(a) A disclaimer must be delivered to the trustee serving at the time the disclaimer is made;

(b) If a trustee is not serving at the time the disclaimer is made, the disclaimer must be filed with a court having authority to enforce the trust; or

(c) If the disclaimer is made before the time the instrument creating the trust becomes irrevocable, the disclaimer must be delivered to the settlor of a revocable trust or the transferor of the interest.

(6) In the case of an interest created by a beneficiary designation made before the time the designation becomes irrevocable, a disclaimer must be delivered to the person making the beneficiary designation.

(7) In the case of an interest created by a beneficiary designation made after the time the designation becomes irrevocable, a disclaimer must be delivered to the person obligated to distribute the interest.

(8) In the case of a disclaimer by a surviving holder of jointly held property, the disclaimer must be delivered to the person to whom the disclaimed interest passes.

(9) In the case of a disclaimer by a person who is an object of an exercise of a power of appointment or a taker in default of an exercise of a power of appointment at any time after the power was created:

(a) The disclaimer must be delivered to the holder of the power or to the fiduciary acting under the instrument that created the power; or

(b) If a fiduciary is not serving at the time the disclaimer is made, the disclaimer must be filed with a court having authority to appoint the fiduciary.

(10) In the case of a disclaimer by an appointee of a nonfiduciary power of appointment:

(a) The disclaimer must be delivered to the holder of the power, the personal representative of the holder's estate or to the fiduciary under the instrument that created the power; or

(b) If a fiduciary is not serving at the time the disclaimer is made, the disclaimer must be filed with a court having authority to appoint the fiduciary.

(11) In the case of a disclaimer by a fiduciary of a power over a trust or estate, the disclaimer must be delivered as provided in subsection (3), (4) or (5) of this section as if the power disclaimed were an interest in property.

(12) In the case of a disclaimer of a power by an agent, the disclaimer must be delivered to the principal or the principal's representative. [2001 c.245 §12]

105.643 When disclaimer barred or limited. (1) A disclaimer is barred by a written waiver of the right to disclaim.

(2) A disclaimer of an interest in property is barred if any of the following events occurs before the disclaimer becomes effective:

(a) The disclaimant accepts the interest sought to be disclaimed;

(b) The disclaimant voluntarily assigns, conveys, encumbers, pledges or transfers the interest sought to be disclaimed or contracts to do so; or

(c) The interest sought to be disclaimed is sold pursuant to a judicial sale.

(3) A disclaimer, in whole or part, of the future exercise of a power held in a fiduciary capacity is not barred by the previous exercise of the power.

(4) A disclaimer, in whole or part, of the future exercise of a power not held in a fiduciary capacity is not barred by its previous exercise unless the power is exercisable in favor of the disclaimant.

(5) A disclaimer is barred or limited if so provided by a law other than ORS 105.623 to 105.649.

(6) A disclaimer is barred if the purpose or effect of the disclaimer is to prevent recovery of money or property to be applied against a judgment for restitution under ORS 137.101 to 137.109.

(7) A disclaimer of a power over property that is barred under this section is ineffective. A disclaimer of an interest in property that is barred under this section takes effect as a transfer of the interest disclaimed to the persons who would have taken the interest under ORS 105.623 to 105.649 had the disclaimer not been barred. [2001 c.245 §13; 2007 c.483 §1]

105.645 Tax qualified disclaimer. Notwithstanding any other provision of ORS 105.623 to 105.649, if as a result of a disclaimer or transfer the disclaimed or transferred interest is treated pursuant to the provisions of the Internal Revenue Code and the regulations promulgated under that code, as in effect on December 31, 2010, as never having been transferred to the disclaimant, then the disclaimer or transfer is effective as a disclaimer under ORS 105.623 to 105.649. [2001 c.245 §14; 2011 c.526 §16]

105.646 Recording of disclaimer. If an instrument transferring an interest in property or a power over property that is subject to a disclaimer is required or permitted by law to be filed, recorded or registered, the disclaimer may be so filed, recorded or registered. Failure to file, record or register the disclaimer does not affect the validity of the disclaimer as between the disclaimant and persons to whom the property interest or power passes by reason of the disclaimer. [2001 c.245 §15]

105.647 Application to existing relationships. Except as otherwise provided in ORS 105.643, an interest in property or power over property existing on January 1, 2002, may be disclaimed in the manner provided by ORS 105.623 to 105.649 after January 1, 2002, unless the time for delivering or filing a disclaimer had expired under law in effect immediately before January 1, 2002. [2001 c.245 §16]

105.648 Effect on recovery of money or property under ORS 411.620. ORS 105.623 to 105.649 do not allow any person to disclaim an interest in property, including any jointly held property, if the purpose or effect of the disclaimer is to prevent recovery of money or property under ORS 411.620. [2001 c.245 §17]

105.649 Uniformity of application and construction. In applying and construing ORS 105.623 to 105.649, consideration must be given to the need to promote uniformity of the law with respect to disclaimers among states that enact versions of the Uniform Disclaimer of Property Interests Act. [2001 c.245 §18]