Steve Leimberg's Asset Protection Planning Email Newsletter - Archive Message #328

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From: Steve Leimberg's Asset Protection Planning Newsletter
Subject: Tom Greene: "Well-Crafted" Self-Settled Trusts Formed by Nonresident Settlors Will Withstand Legal Challenge

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"Notwithstanding widely different state public policy views, a nonresident settlor can expect that [for a properly drafted trust] either: jurisdictional limitations; the creditor's lack of full faith and credit enforcement arguments; the SSDS Trust's 'substantial relationship' to the state of trust formation for validity purposes; or the designation of the trust state to govern will thwart the creditor's suit, allowing the trust to survive intact.

Let's be clear on this notion of duty. Even if some estate planning attorneys resist the idea, you can be assured the plaintiffs' bar will not. The next wave of creative malpractice actions could well be against estate planning attorneys who fail to advise clients about asset protection alternatives, filed by clients who have suffered financial reverses which could have been avoided with such planning."

Tom Greene provides members with extensive commentary that reviews whether self-settled trusts formed by nonresident settlors will withstand legal challenge.

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Here is Tom Greene's commentary.

EXECUTIVE SUMMARY:

This treatment hypothesizes a scenario where a nonresident settlor, with no existing or foreseeable creditor obligations, establishes a self-settled discretionary spendthrift trust in a state with statutes authorizing the creation of such trusts. The settlor's spouse and two children, all living together, are the absolutely discretionary beneficiaries. The trust authorizes the trustee to name the settlor as a beneficiary in the future. Years later, a claim arises against the settlor from unforeseen, but conceivable events.

The question presented is: "Will the trust survive a court challenge?"

It can be presumed that the plaintiff believes his prospects for success are greater in the settlor's home state, which *arguendo* prohibits self-settled trusts than the trust state, so he is likely to sue in the settlor's home jurisdiction; however, it is posited that neither a court in the settlor's state of residence, or a sitting federal district court will have jurisdiction over the trust, as distinguished from the plaintiff personally, because the trustee only has incidental contact with the settlor's resident state and does not purposely avail itself of the benefits of doing business in the state. If the local court were to bootstrap jurisdiction, it is unlikely that the trust state's courts will enforce a full faith and credit challenge to the trust due to the local court's lack of jurisdiction, the minimal relationship of the settlor's home state to the trust and the trust state's public policy favoring SSDS Trusts. Consequently, the sole venue for original jurisdiction likely will be a federal bankruptcy court sitting in the settlor's state of residence, which generally will require an involuntary bankruptcy petition.

Since the facts do not involve a fraudulent transfer of assets into the trust, the duty of the bankruptcy court will be to make a choice of law determination based on which state - the trust state or the settlor's resident state - has the most substantial

relationship to the trust. Under the facts presented in the hypothetical Model Trust, a preponderance of the nexus factors favors the trust state; therefore, it can be presumed that the law of the trust state will prevail and the trust will be validated.

Although self-settled trusts historically were not favored by the states, they are now authorized in 16 states. Notwithstanding widely different state public policy views, a nonresident settlor can expect that either: (1) jurisdictional limitations, (2) the plaintiff's lack of full faith and credit enforcement arguments, (3) the designation in the trust instrument of the trust state law to govern; or (4) the trust state's "substantial relationship" to the trust will thwart the creditor's suit, allowing the trust to survive intact. This may come as a surprise to planners and attorneys not familiar with the nuances of this type of trust.

COMMENT:

Faced with financial stress, some planners and their clients have launched desperation SSDS Trusts that were bound to fail. Typically, there is a "Hail Mary" fraudulent transfer attempt, with the trustee domiciled in the SSDS Trust state, but little else existing to connect the trust to the trust state. In response, the courts have often searched for ways to render equitable relief, muddying the waters for well-designed plans.[1] A primary goal of this Commentary is to differentiate the good from the bad, thereby, providing a fact-based guideline for practitioners seeking legitimate benefits for their clients who don't live in a SSDS Trust-enabled state.

To date, no court has adjudicated whether a creditor may reach the assets of a properly designed and implemented domestic SSDS Trust. However, quoting an article by Fogel, "the long and short of this discussion is… the only means of enforcing a judgment against such a domestic asset protection trust may be to attack the creation of the trust as a fraudulent transfer. Whether or not the post transfer creditor will be successful will likely depend on whether the particular creditor was a contemplated creditor at the time of the transfer."[2]

There are five (5) paths leading to the survival of a SSDS Trust based on the Model Trust, as outlined in the Commentary. Likely, only one path need succeed for the trust to prevail:

(1) A court in the settlor's state of residence denies jurisdiction to the plaintiff after determining that the trust state has legal jurisdiction over the matter due to the location of the trust and trust assets in the trust state and the trustee's "minimum contacts" with the state court.

(2) *Arguendo*, the local court bootstraps jurisdiction and renders a judgment invalidating the trust. Under the Full Faith and Credit Clause, the trust state's strong public policy in favor of such trusts likely will cause its courts to deny enforcement of the nonresident settlor court's judgment if the trust is found invalid on the sole ground the settlor can be added in the future as a beneficiary. Such a prospect may even encourage the plaintiff to withdraw the suit.

(3) The settlor is able to avoid involuntary bankruptcy, leaving the plaintiff without a jurisdictional venue in which to complain.

(4) A federal bankruptcy court validates the trust by applying the law of the trust state due to that state's more substantial relationship to the trust than the local court, based on Restatement (Second) § 270.

(5) A federal bankruptcy court determines the trust's terms are enforceable against a creditor, based on Restatement (Second) § 273

There are compelling reasons for a nonresident settlor engaged in trust planning to consider a self-settled discretionary spendthrift trust – privacy, fear of a future financial reversal, potential tax benefits, fear of an unfounded claim, flexibility to modify the trust if circumstances change, avoidance of intra-family quarrels and a host of others. While the legal sustainability of a properly structured and implemented SSDS Trust with a nonresident settlor remains untested in court, a preponderance of the evidence and scholarly comment points toward the trust's survival. From a practical viewpoint, it can be said that a trust structured like the Model Trust will have proven its worth if it provides real benefits to the settlor and either: (1) is sustained or (2) if a dispute arises, leads to an attractive settlement.[3]

Opportunities in Self-Settled Trust States for Nonresident Settlors

Introduction

If a nonresident settlor creates a self-settled discretionary spendthrift trust ("SSDS Trust" or "trust"), in a state with authorizing statutes, will the trust survive a court challenge? The answer to the question is "it depends," but this seemingly inconclusive answer is significant, because it implies accurately that there is a reasonable set of circumstances from which to conclude that a nonresident settlor may transfer assets to a self-settled trust formed in a state authorizing such trusts and, upon court challenge, the trust will survive.

SSDS Trusts are irrevocable trusts in which the settlor is allowed to designate himself a discretionary beneficiary or be so-named later by the trustee. The result is that the settlor may achieve a range of benefits, including the potential to access the trust's assets, while certain creditors may have greater difficulty seizing the assets in the trust.

The purpose of this Commentary is to: (1) provide a cursory history of SSDS Trusts and their uses (2) outline the elements of a well-constructed SSDS Trust; and (3) examine the survivability of a SSDS Trust, if challenged in court.

Background of SSDS Trusts

For years, in response to a growing number of lawsuits and the size of jury verdicts, estate, financial, and business planners relied on a variety of client protection strategies, such as: limited liability companies ("LLC"), annuities, IRAs, life insurance, property gifts, and family limited partnerships. As the demand for asset protection strategies increased, it was inevitable that planners and their clients would look to SSDS Trusts as a possible solution. However, because no state allowed self-settled trusts prior to the creation of the first SSDS Trust in Alaska in 1997,[4] advisors turned to foreign jurisdictions. This led to the creation of off-shore SSDS Trusts in the 1980's in places like the Cook Islands and Nevis. Although these trusts became moderately popular, there were abuses[5] and U.S. estate planning practitioners generally were reluctant to involve their clients.[6] As an alternative to off-shore SSDS Trusts, states began enacting new trust laws providing creditor protection and other benefits for trusts in which the settlor retained a discretionary interest. There are now 16 states that allow SSDS Trusts.[7]

The list of states looking into the advantage of SSDS Trusts is growing. For example, in 2016, a limited statute became law in West Virginia and, in Georgia's most recent legislative session, H. B. 456, authorizing the creation of self-settled

trusts, was introduced for the first time. It cannot be known when or whether other states will adopt similar legislation, but this Commentary seeks to demonstrate to nonresident settlors and their planners that settlors domiciled in states without SSDS Trust statutes may achieve a wide range of useful benefits by creating an SSDS Trust in one of the leading SSDS Trust jurisdictions.

SSDS Trust statutes vary by state, sometimes considerably, as do the trust laws of the states in which a nonresident settlor may be domiciled. The lack of uniform standards poses a challenge in attempting to provide actionable information to practitioners; therefore, this Commentary sets forth a Model Trust drawn from the law of leading SSDS Trust jurisdictions ("trust states"), as those states' laws and policies relate to nonresident settlors.[8]

Asset Protection No Longer the Sole Driving Force

By the early 2000's, SSDS Trust planners began to recognize that SSDS Trusts offered significant trust benefits in addition to pure asset protection, which heretofore had been their sole focus.[9] For example, South Dakota has empaneled a standing trust task force with representatives from state government and the private sector to monitor new trends in creative trust legislation throughout the country.

The following is a listing of situations in which SSDS Trusts might be beneficial,[10] although all of these benefits are not available in every state. Below the list is a short review of SSDS Trust advantages, generally offered in the leading SSDS Trust states.

1. A client might be more willing to create other types of irrevocable trusts if the funds can be accessed in an emergency. Examples include: an irrevocable life insurance trust, a charitable lead trust, a charitable remainder trust, a grantor retained annuity trust, a qualified personal residence trust or a spendthrift trust for a young adult or disabled person. Further, some of these vehicles are vulnerable to creditor claims that could be insulated.

2. A client might desire a trust that exhausts her gift tax exemption or GST exemption.

3. In some states, the trust can be used to receive a taxable gift to reduce federal and state estate taxes.

4. Under Rev. Rul. 2004-64, favorable tax treatment for grantor trusts can be assured.

5. In certain states, SSDS Trusts allow the option of federal estate tax inclusion or exclusion.

6. The trust can be used to protect officers and directors.

7. The trust can be used for pre-marital planning.

8. In certain states, the trust can be used to avoid state income tax.

9. The trust can be used by foreign persons who wish to own U.S. sitused assets held by a U.S. trustee.

10. Before immigrating, nonresident aliens may engage in transfer tax planning.

11. Trusts moved from offshore or other domestic jurisdictions can be protected.

The leading SSDS Trust states offer a trust solution with a range of potential advantages to settlors who designate their law to govern their trusts. Although all the solutions are not applicable in every state, these include:

1. The elimination of state income tax. Also, trusts may not be required to file state income tax returns or qualify for exemption from such taxes;

2. No state capital gains, dividend, interest or intangible taxes;

3. Low insurance premium taxes.[11]

4. Unlimited duration “rule against perpetuities” statutes;[12]

5. If a trust's provisions need to change due to evolving tax laws or changes in the settlor's family or business, the trustee can decant a trust into a new trust with different provisions,[13] and reform or make trust modifications;[14]

6. Two-year fraudulent conveyance statute;[15]

7. Automatic total seal privacy for all court matters involving trusts, including litigation, reformation and modification and court blessed decants;[16]

8. Sole and exclusive remedy charging order protection for LLCs.[17]

9. Special provisions encouraging the trend of international families looking for the safety of a U.S trust situs and trustee;[18]

10. Permitting the use of special purpose LLCs[19] to function as: trust protectors (to watch over the trust and change the trustee in the event of misconduct); [20] and trust investment and distribution advisors;[21]

11. If settlors have concern about the motivation of their heirs to become self-sufficient, they may decide what notice, if any, is given to beneficiaries about the trust's value and provisions;[22]

12. Allows for the creation of "purposeful trusts" [23] and dynasty trusts;[24]

13. In an action against the trust, the prevailing party may be awarded attorney's fees;[25]

14. Provides protection for trust advisors in the counseling, drafting, preparation, execution, and funding of a trust.[26]

Model Trust

Since the validity of a SSDS Trust will be based on its unique provisions and situational factors, this Commentary will reference a hypothetical SSDS Trust, with these accompanying facts and provisions ("Model Trust"):

- The trust designates the trust state of formation as the governing jurisdiction;

- The trust document cites estate planning, taxation and other advantages as reasons for creating the trust;

- Trust administration, such as filing tax returns, is performed by a corporate trustee with substantial SSDS Trust experience domiciled in the trust state and no substantive contacts with the nonresident settlor's home state;

- The trust is irrevocable;

- The settlor has no present or foreseeable creditor or judgment claims;

- The settlor's spouse and two children are primary trust beneficiaries, with the trustee having absolute spendthrift discretion to make distributions to them or payments on behalf of them, subject to the direction of the trust distribution advisor;

- At trust formation, the settlor names a trust protector with power to replace the trustee and trust advisors and add or remove trust beneficiaries who are descendants of the settlor's grandparents, which includes the settlor.

- Neither the trust protector nor any of the trust advisors are controlled by the settlor and there are no pre-arrangements. Beneficiary interests are non-transferable and meet standard spendthrift trust requirements.

- The trust generally prohibits payments to the settlor's creditors.

- The trust LLC is funded by transfers of securities and cash from various settlor accounts. (Author comment: The Commentary will discuss specific techniques available to planners for the transfer into the trust of real property and LLCs (e.g., business assets), as well as cash and financial assets).

- A portion of the trust's assets are held in cash in an independent bank in the trust state;
- Only a minority portion of the settlor's estate assets are transferred into the trust;
- The trust advisors are LLCs organized in the trust state; and
- Trust legal work is performed by special trust counsel in the trust state and the settlor's personal counsel.

Legal Challenge Issues

Jurisdiction: Overview

A creditor may obtain jurisdiction and a binding judgment over the person of a nonresident settlor, who has formed a SSDS Trust, but that judgment will not allow him to attach the Model Trust trustee or trust assets because the assets are no longer "owned" by the settlor. In order to grant a binding judgment, the forum court must have jurisdiction over the out-of-state trustee and assets.[27] This is the essence of the Due Process Clause of the U.S. Constitution, which limits the exercise of a state court's jurisdiction over nonresident defendants to those who "have certain minimum contacts" with the forum state.[28] The interpretation of "minimum contacts" has been addressed and refined by case law and is treated below. Regardless, the Model Trust contemplates a trustee with no contact with the settlor's home jurisdiction. Thus the state court in the settlor's state of residence should be barred from obtaining "original jurisdiction"[29] over the trust or its assets. By default, in most situations, the case will be adjudicated in bankruptcy court, or not at all.[30]

Defining "Minimum Contact" Requirement for Forum Court Jurisdiction

Prior to the Fourteenth Amendment, the idea of a state court exercising jurisdiction over persons or property outside its borders was considered to be an absolute nullity[31] over which the federal courts exercised no authority. With the adoption of the Amendment, judgments purporting to bind the person of a defendant over whom the court had not acquired *in personam* jurisdiction were void. But,

questions regarding the sufficiency of nexus required for jurisdiction inevitably arose, as state interests competed for jurisdiction.

The first modern case of relevance attempting to articulate the contact required to establish jurisdictional reach was *International Shoe Co. v. Washington*.[32] There, the Supreme Court opined that: to establish that the forum court possesses personal jurisdiction over a nonresident defendant, a plaintiff must allege and prove that the defendants have "minimum contacts" with the forum state that are "continuous, purposeful, and systematic." Thirteen years later, the United States Supreme Court, in *Hanson v. Denckla,*[33] considered *International Shoe* and went on to elucidate the jurisdictional principles that have become the foundation for factually distinguishing cases with different degrees of contact and for cases where forum courts seek to obtain jurisdiction over nonresident trustees.

In *Hanson,* the United States Supreme Court held that the Florida court lacked personal jurisdiction over the Delaware trustees. Quoting *Hanson,* "It is essential in each case that there be some act (Emphasis added) by which the defendant purposefully (Emphasis added) avails itself of the privilege of conducting activities within the forum state, thus invoking the benefits and protections of its laws."
In *Hanson,* the court held the trustee's acts in sending trust payments and documents into the jurisdiction where the settlor had taken up residence were insufficient as a matter of law to constitute the requisite minimum contacts.

In 2003, Hanson was the foundational precedent in *Rose v. FirStar Bank*,[34] also involving the issue of forum court jurisdiction over a nonresident trustee. In *Rose*, the Rhode Island Supreme Court found the Ohio trustee's contacts with the Rhode Island beneficiaries were: (1) its communications with and its distribution of money to them for over 27 years; (2) sending trust statements; (3) mailing trust-related checks, and (4) making occasional trust-related telephone calls to the beneficiaries. Based on these facts, the Court concluded the trustee did not purposely avail itself of the privilege of doing business.

The *Rose* court's decision rejected the plaintiff's argument that the case should turn on the adequacy of the trustee contacts, as set forth in *McGee v. International Life Insurance Co.,*[35] which had recently concluded that the trustee contacts were sufficient to satisfy due-process considerations. *McGee* involved an insurance contract between a Texas insurer and a California policyholder, where the policyholder accepted the offer from the Texas insurer to renew its insurance

contract and mailed the required premiums from California to the Texas insurer. The United States Supreme Court held that, based on the Texas insurer's purposeful solicitation of this reinsurance business from the California policyholder and the policyholder's acceptance of the offer in California, a California court could exercise jurisdiction over the Texas defendant because "[i]t is sufficient for purposes of due process that the suit was based on a contract which has a substantial connection with [the forum]."

The *McGee* facts were also rejected by the Montana Supreme Court in *In the Matter of Estate of Ducey*.[36] In that case, the Montana court faced a similar jurisdictional question and concluded that, for Montana to assume personal jurisdiction over the nonresident trustee, would exceed the limits of due process. The Court distinguished *McGee,* reasoning that the Nevada bank's payments of trust income to the settlor in Montana, and "several bits of trust administration that may be compared to the mailing of premiums in *McGee,*" did not constitute acts in Montana that bear the same relationship to the trust agreement as the solicitation of reinsurance in *McGee.* In summary, the critical elements distinguishing *McGee* can be reduced to "solicitation" and "contract." In subsequent cases,[37] these elements have been logically expanded, but not changed.

Jurisdiction and full faith and credit issues are often intertwined. In 1998, the United States Supreme Court decided *Baker v. General Motors Corp*.[38] Quoting the Court, "With respect to judgments…" A State is not required…to afford full faith and credit to a judgment rendered by a court that "did not have jurisdiction over the subject matter or the <u>relevant parties</u> (Emphasis added*)." Underwriters Nat. Assurance Co. v. North Carolina Life & Accident & Health Ins. Guaranty Assn*., 455U. S. 691, 705 (1982). Consequently, before a court is bound by [a] judgment rendered in another State, it may <u>inquire into the jurisdictional basis of the foreign court's decree.</u>" (Emphasis added)

Looking to future courts' views of minimum contacts in jurisdictional cases, it is reasonable to anticipate that courts will evaluate the nature and number of the acts and contacts and how close the relationship is between the contacts and the forum state – particularly as to whether or not there is solicitation, contract or the performance of services. Media advertising, attendance at professional conferences, articles in national press and journals and providing promotional material and website materials do not appear to satisfy the case law due process

requirements for jurisdiction. Similarly, with respect to websites, passive internet sites, merely providing information, may not meet the *Baker* jurisdictional test; but, interactive sites conducting business transactions begin to resemble *McGee.*

In Rem Jurisdiction

In rem jurisdiction describes the power a court may exercise over both real and personal property. In some cases, the forum state may have its only colorable claim for jurisdiction over SSDS Trust assets that are located in its jurisdiction;[39] however, David G. Shaftel suggests that, if real estate is contributed to an LLC formed in the trust state, the interest might be considered intangible property with a situs in the [trust] state.[40] Citing Gideon Rothschild,[41] Shaftel also suggests the possibility of an added layer of protection by having the settlor sell the real property to another grantor trust in exchange for an installment note secured by the real property. The mortgage note could then be contributed to the trust LLC, thereby becoming intangible personal property in the trust state. Using this structure, if the court were to obtain *in rem* jurisdiction over the property, it can be argued that the rights of the prior secured interest holder are paramount to the ability of the unsecured debtor to obtain possession of the property.[42]

Limited Liability Companies

In the hypothetical Model Trust scenario, for simplicity, cash and financial assets are held by the trustee inside an LLC formed in the trust state for such purpose. No law or Commentary can be found arguing that these LLC member interests or similar intangible property interests should not be held safely by the trustee; but options exist for planners interested in "belt and suspenders" measures to further assure that future courts won't be able to overreach their bounds. As discussed earlier, the Model Trust is drafted so that, after its creation, the trustee (not the settlor) forms an LLC in the trust state to be the vehicle holding the trust's financial assets upon transfer. A few other precautions, which may be considered by planners, regarding the location, nature, transfer and management of the financial assets, follow.

Given the unpredictability of judicial decisions, it is imaginable that an aggressive future court might devise a theory to pierce the trust-held LLC in an effort to assert direct jurisdiction over the individual assets. If this were to occur, the nature of the assets themselves, separate from their trust ownership, could become

determinative. In *In re Huber,*[43] Mr. Huber created an Alaska LLC into which he placed Washington real property and business assets. He then transferred his LLC member interests and other assets into an Alaska trust just prior to filing for bankruptcy. Given Mr. Huber's imminent bankruptcy, it is likely the court would have invalidated the transfer of any of his assets due to fraudulent transfer rules. However, if the court in a future case somehow were to pierce the trust LLC, a more balanced fact pattern can be conjured, where the type and location of the trust assets becomes the determining factor in deciding which state has the most significant relationship to the trust.

Cash and Financial Assets

In determining the jurisdictional location of property in the form of cash and financial assets, neither the Uniform Commercial Code[44] nor the Restatements offer useful guidance; therefore, the best source of authority has been found to be The Hague Convention. Although The Hague's rules are non-binding, the process of identifying the legal location of property, among so many nations, has been considered thoroughly. Due to the sheer volume and diversity of the international transactions before The Hague, its rules on this matter are powerful authority.

Over time, The Hague has explored many methodologies for identifying the location of financial assets, but ultimately its work concentrated on an approach that came to be known as the "agreement plus reality test." Paraphrased, Article 4(1)(a) states that the applicable law is the state law of the jurisdiction agreed on by the intermediary (e.g., bank or brokerage firm) and the settlor, provided that the intermediary has an office in the state selected and that office (i) effects or monitors entries to securities accounts; (ii) administers payments or corporate actions relating to securities held with the intermediary; or (iii) is otherwise engaged in a business or other regular activity of maintaining securities accounts.[45]

Relating The Hague test to the Model Trust, a clear designation in the trust naming the trust state to be the governing law for the location of the trust's property should be effective if the trust state bears a sufficient relationship to the activities of the bank and/or brokerage firm holding the trust's assets. Thus, there should be no doubt that cash and securities assets, as held in the Model Trust, will be deemed to be located in the trust state. These additional financial assets protections can be arranged in such a manner that the settlor may continue working with her existing financial advisor to direct strategy, allocate assets and select securities.

Privately-Held Business Interests

The settlor also may wish to transfer into the trust LLC the member interests of an LLC holding a privately-held business located in the settlor's state of residence. It has been argued herein that these business interests, now in the trust LLC, have become intangible property under the jurisdiction of the trust state.[46] There does not appear to be contra law on this matter; however, in one federal bankruptcy case, the court looked to the origins of the transferred property, as one factor, among many, in determining which state had the "most substantial relationship" to the trust.[47] For this reason, planners looking to maximize safety may choose between two options: (1) fund the trust only with cash and financial assets, or (2) if the business transfer is essential to the estate plan, take extra steps to establish the trust state as the state with the most substantial relationship to the trust.

The potential for local courts' exercising *in rem* jurisdiction over assets located in their jurisdictions is a reality. Therefore, real property, LLCs, and financial assets may require added layers of protection. For each separate asset class transferred into the trust, a plan should be developed, balancing the costs and effort required for the added protection versus the level of exposure to the settlor.

Federal Jurisdiction

Faced with the Model Trust facts, a federal district court sitting in the settlor's resident state also will not have jurisdiction, derived from either diversity jurisdiction or federal question jurisdiction, because a federal court only has the same personal jurisdiction as a state court in the state where the federal court sits.[48] Again, the long-arm jurisdictional question will be whether the trustee has "purposefully availed itself of the benefits of doing business in the settlor's state of residence,"[49] which the Model Trust trustee does not, and most SSDS Trust trustees avoid.

By elimination, the bankruptcy court, with national jurisdiction, sitting in a federal district in the settlor's resident state, may be the only venue with original jurisdiction over the Model Trust assets.[50] Further, the plaintiff's access to bankruptcy court fulfills the mandate of the Constitution's Supremacy Clause, Article VI., § 2, stating that conflicts between federal and state law are required to be resolved in favor of the federal law. As will be seen, the bankruptcy courts' precedent is to determine "choice of law" based on which state has the "most

substantial relationship to the trust;" thus, these courts should be viewed as favorable forums for the Model Trust concept. An interesting practical result of this jurisdictional limitation is that, if the settlor avoids filing for bankruptcy and is able to avoid involuntary bankruptcy, the challenge may not reach court, allowing the trust to survive.[51]

Model Trust Jurisdictional Implications

The Model Trust facts state somewhat simplistically that there are no substantive contacts between the trustee and the settlor in her resident state; however, it is realistic to presume that, over time, the trustee will engage in a certain amount of incidental activity with the settlor and the beneficiaries, such as the mailing of statements, issuing checks, periodic telephone calls, and back and forth emails. Since it is presumed that the current law in the nonresident settlor's domicile *arguendo* prohibits self-settled trusts,[52] the precedent of *Hanson* and subsequent cases should give comfort to planners, considering the use of a trust designed similar to the Model Trust, that a nonresident settlor's forum court will be unable to justifiably obtain jurisdiction over the trust's assets. Just as important, (1) it will be demonstrated that, even if the plaintiff obtains a judgment in the settlor's local jurisdiction, likely he will be unable to enforce it and, (2) as will be examined, if in the court proceedings, the bankruptcy court is forced to choose one law over the other, it will choose the trust state law over the nonresident settlor's home state law.[53]

Full Faith and Credit Clause

Article IV of the United States Constitution begins with the command, "Full Faith and Credit shall be given in each State to the Public Acts, Records, and Judicial Proceedings of every other State."[54]

Defining the Question

This Commentary earlier concluded that, neither the state court nor a federal district court will be able to obtain original jurisdiction over the Model Trust's trustee or assets, leaving bankruptcy court as the most likely venue for jurisdiction in most cases. Assuming *arguendo* that the local state court does determine to

exercise jurisdiction over the trustee and the trust assets, how will the trust be affected?

If the plaintiff wins a judgment invalidating the trust, the plaintiff's problem is that, because the trust assets are located in the trust state, under the control of the trustee, the plaintiff's attorney must ask a court in the trust state to enforce the judgment under the mandate of the Full Faith and Credit Clause of the U.S. Constitution ("FF&C Clause").[55] Afterwards, if that decision is appealed by either party, a federal appeals court may be asked to examine whether the FF&C Clause applies, but the applicable law will remain the same.

Barriers to FF&C Clause Enforcement

The plaintiff will be presented with significant barriers in seeking to enforce its judgment.

The State Court of the Nonresident Settlor Will Not Have Jurisdiction Over the Trustee

Before the trust state court "may or can" enforce the judgment, it must find that the local court's judgment is valid, which, in turn, requires the forum state to possess jurisdiction over the trust and its assets. The court in the settlor's resident state does not. *Hanson* is again precedent, as well as the other law previously cited, confirming that a judgment-rendering forum court must have jurisdiction over the trust or the trust assets for its judgment to receive full faith and credit in another state. Based on these precedents, the Model trustee does not have the minimum contacts with the settlor's residence that would require submitting to the jurisdiction of its courts.

It has been suggested that the *Hanson* "minimum contacts" doctrine may be trending toward a "center of gravity" approach,[56] e.g., that, for the settlor's resident state to possess jurisdiction over the Model Trust, the trust arrangement must have a more substantial relationship to the settlor's home state than to the trust state. Although no precedent for this approach could be found, the concept would favor the Model Trust due its trust state having a considerably more substantial relationship to the trust than the settlor's home state. Based on precedent and trends, it can be expected that the local court will not have the jurisdiction required

to support its judgment, thereby mandating the trust state to refuse to enforce the judgment against the settlor.

Trustee Not Required to Enforce Statutes of Another State Contrary to Its Own Public Policy

The next major legal barrier is set forth in Restatement (Second) of Conflict of Laws § 270 stating the doctrine that: An inter vivos trust in movables is valid if valid under the law of the state designated by the settlor to govern the validity of the trust, provided that the application of its law does not violate a strong public policy of the state with which, as to the matter at issue, the trust has its most significant relationship.

The public policy exception was examined by the Supreme Court in *Baker v. Gen. Motors Corp*. for public acts (e.g., statutes).[57] *Baker* is authority for the principle that a state will not be forced to enforce another state's public policy at the expense of its own public policy. Quoting *Baker*, "The Full Faith and Credit Clause does not compel 'a state to substitute the statutes of other states for its own statutes dealing with a subject matter concerning which it is competent to legislate' (quoting *Pac. Emp'rs Ins. Co. v. Indus. Accident Comm'n*, 306 U.S. 493, 501 (1939)."

An article by Elizabeth Redpath commented:

> The idea that one state, by the imposition of contrary public policy, can undercut the privileges conferred by another state is admittedly discomforting, but it is the lesser of two evils. Without the public policy exception, full faith and credit could mandate outcomes that are unfathomable to the majority of Americans…In other words, although the public policy exception can delay the spread of popular public policy, it can also forestall the spread of unpopular public policy. More critically, if states are going to continue to serve as laboratories for new social and economic experiments, then every state—the "trial" states and the "control" states—must remain sovereign…Horizontal federalism is based on the assumption that separate sovereigns achieve great economic and social progress. And separate sovereigns are neither separate nor sovereign without the

> power to make and enforce their own domestic policies. The Full Faith and Credit Clause should fit within this context.[58]

Model Trust FF&C Clause Implications

As shown, the Model Trust designates the trust state's law to govern. And, the trustee, not only does not have the requisite "minimum contacts" with the settlor's home state which would require submitting to its jurisdiction, the trust state, in fact, has the most substantial relationship to the trust. Leading SSDS Trust statutes, which are continually supported and amended by the states' legislatures, and the trust state's private business and governmental economic interests are strong evidence these trust states have a public policy favoring SDFS Trusts.[59] Therefore, it is reasonable to expect that the trust state court will refuse to enforce a forum court's judgment issued solely on the arbitrary policy ground the settlor may be added later as a beneficiary of the trust. Notably, these arguments also refute the claim by proponents of "foreign" asset protection trusts that "domestic" SSDS Trusts are ineffective due to the existence of the FF&C Clause.

Fraudulent Transfers

Overview

The right of creditors to invalidate fraudulent conveyances can be traced back to the Statute of 13 Elizabeth, Chapter 5 (1571). As developed through the centuries, transfers are fraudulent if made with the intent to hinder, delay or defraud a creditor.[60] Fraudulent transfers are civil, not criminal, actions; therefore, if a transfer violates the fraudulent transfer statute of the Federal Bankruptcy Code, the settlor's domicile state or the SSDS Trust state, the court's historically granted "right" will be to set aside such a transfer and allow the creditor to satisfy the debt from the transferred property.[61]

As will be seen, it is important to understand the distinction between fraudulent transfer law and the Self-Settled Trust Rule, which entered the common law under the reign of Henry VIII's father, Henry VII, in the century prior to enactment of the Statute of Elizabeth.[62] Over time, the Self-Settled Trust Rule, has been incorporated into the trust law of many states utilizing differing methods to void past and future transfers to a trust in which the settlor retains a beneficial interest. In 2012, the Illinois Supreme Court[63] clarified the litigating parties' confusion over

the difference between the common law Rule and fraudulent transfer law. Quoting the Court: “the common law focuses on…the interest retained by the settlor, not simply the fraudulent transfer…the [fraudulent transfer] Act and the common law each operate in some circumstances where the other does not, thus negating any inference that the common law rule would render the Act superfluous…The Act is effective, but the common law rule is not, in a much larger sphere, which includes both situations that do not involve trusts and in connection with transfers into trusts that are not for the settlor’s benefit because they permit distributions only to other persons.’’[64]

The Crux - Claims by “Unforeseen but Conceivable” Future Creditors[65]

In the example of a straight forward fraudulent transfer claim, a debtor or person contemplating a risky endeavor will have moved assets to a “captive” third party with the intent of: (1) shielding the assets from the debtor’s forced repayment to a creditor or (2) making the assets unavailable to cover the settlor’s financial exposure if the endeavor fails or creates settlor losses. These claims speak to true fraudulent transfers and are outside the purview of SSDS Trust law. Instead, proper SSDS Trusts are concerned with interpreting the law of future creditors, which involves unanticipated events and obligations to unknown future creditors.

Cases and Commentary

In its 1890 *Schreyer v. Scott* opinion,[66] the United States Supreme Court enshrined the twofold theory underpinning claims by future creditors. First, a person fully contemplating entering into a risky transaction or incurring debt shall not be allowed to remove owned attachable assets from the reach of creditors. Second, that person cannot obtain credit by the sleight of hand of “showing” assets, which, in fact, are now “nominee owned” by a third party for the benefit of the transferor.

The Court’s decision was rooted in five distinguishing elements: (1) a deceptive conveyance; (2) the transferor seeming to remain in possession and ownership of the assets; (3) the transferor obtaining credit or avoiding financially risky endeavors; (4) actions so near in time to the transfer that an inference of fraud is necessary; and (5) there is some specific future creditor in mind. In short, the law of future creditors exists to protect persons who may not hold a claim today, but who are highly likely to hold a claim in the near future.

Quoting *Schreyer,*

> Reverses came unexpectedly, while in the pursuit of his ordinary business, without any intention on his part to defraud his creditors, and it may be said that, without any fault on his part, except a want of human foresight, he became embarrassed and insolvent. It is not apparent that [the transferor] had in view, at the time of the execution of the deed to his wife, any such result, or that he in any way contributed to produce the result which followed, for the purpose of defrauding his creditors and enjoying the advantages to be derived from the provisions made for his wife. Under such circumstances, the presumption of any fraudulent intent is rebutted, and it is manifest that he had done no more than any businessman has a right to do, to provide against future misfortune when he is abundantly able to do so.

Since *Schreyer*, there have been many court cases and rulings interpreting statutes and cases on the subject of future creditors. Some of these cases involve SSDS Trusts, but most don't; however, this is a distinction without a difference because the key determinative words - "with actual intent to hinder, delay or defraud any creditor" – apply whenever the claim is made, without regard to the personage of the transferor or debtor, or the nature and form of the transferee. A sampling of relevant cases over time is cited in Endnote no.,[67] and citations to scholarly commentary on the subject are cited in Endnote no.[68]

Uniform Voidable Transactions Act

An interesting development in the area of fraudulent transfers occurred in 2014 when the Uniform Law Commission ("ULC") adopted revisions to the Uniform Fraudulent Transfers Act "(UFTA"). The most noticeable of these amendments was the renaming of the UFTA to the Uniform Voidable Transactions Act ("UVTA"); however, the most "mentionable" aspect of the revisions is buried in the last paragraph of Comment 8 under Section 4 of the Act, which can only be described as a stealth attempt to rewrite the history of fraudulent conveyance law and make transfers to a self-settled spendthrift trust voidable *per se*, with consequences even for lifetime QTIP trusts, lifetime credit-shelter trusts, CRTs, GRATs, and QPRTs.

According to Richard W. Nenno (who attended the UVTA conference as an observer) and Daniel S. Rubin,[69] Comment 8 "seem[s] to reflect [the reporter's] individual disapproval of these vehicles and, perhaps, on that basis, seriously misstate[s] the law." Nenno and Rubin's commentary explains why Comment 8 does not accurately interpret existing law, should not have been adopted by the ULC and should not be adopted by states enacting the UVTA. The essence of Nenno and Rubin's correction of the erroneous Comment 8 is that: (1) "the transfer must still be proven to have been made either with an intent to hinder, delay, or defraud creditors or in connection with the debtor's insolvency," and (2) the applicable legal precedent falls under Chapter 10 (§§ 267-282) of the Second Restatement of Conflict of Laws, and NOT fraudulent transfer law (including the UFTA and the UVTA). Quoting Nenno and Rubin:

> One looks in vain for a section of the UFTA, or of the UVTA, providing that a transfer to a self-settled trust is voidable *per se* – it's simply not there. To be clear, the reporter is unable to direct us (and neither are we aware) of a single state statute that declares a transfer to a self-settled spendthrift trust to be a voidable transfer *per se*. Instead, creditor's rights vis-à-vis self-settled spendthrift trusts are governed by trust law – not voidable transfer law.

Although nine states have adopted parts of the UVTA revisions, there has been push-back on Comment 8 in the adopting states.[70] Commentators, legislators and attorneys can only wonder when and why the ULC determined that its announced mission to bring clarity and stability to state and statutory law became an "unannounced" mission to change precedent and write new law where it previously did not exist. It should be a concern to all attorneys that the laudable respect the ULC has garnered in bringing "objective uniformity" to the law, in areas such as the Uniform Commercial Code, has been tainted by its writing of commentary based on personal opinion, not law.

A final matter of small note, relating to the UVTA, pertains to the addition of a new Section 10 addressing instances where more than one state is involved in the transfer (e.g., SSDS Trust by a nonresident settlor). Section 10 provides that the UVTA will be governed by the law of the state where the individual resides. This

language represents a clarification of existing thought, and does not amount to a change in law.

Ultimately, the future of the UVTA will play out in ULC committees and state legislatures; nevertheless, the viability of the Model Trust will be unaffected. Suppose a state were to enact the UVTA in its most extreme form, it is still "merely" a state law. That state's claim for long-arm jurisdiction over the out-of-state trust will not be enhanced a twit; nor would the UVTA revisions overcome the plaintiff's potentially fatal problems in attempting to enforce a state court's bootstrap judgment under the FF&C Clause. And, the federal bankruptcy courts' Restatement (Second) choice of law precedent also will be unaffected. Depending on the facts of the case, the "applicable" state law in bankruptcy court will be the law of the state with the most substantial relationship to the trust (Restatement (Second) § 270) or the law of the state designated in the trust instrument to govern the trust (Restatement (Second) § 273), which will usually be the same.

Special Note Regarding Physicians

General acceptance of SSDS Trusts by physicians would do much to further trust usage. Individually, and as a group, physicians practice in most markets where attorneys and planners practice. All physicians have an inherent fear of 'unforeseeable but conceivable" malpractice suits, but they may have been steered away from self-settled trusts by a generalist planner concerned that a plaintiff patient might be able to set aside a transfer as fraudulent. A common misconception is that SSDS Trusts are fraudulent if asset protection is a primary purpose. However, this Commentary demonstrates that, unless the physician has more than a theoretical basis to contemplate the future occurrence of a lawsuit(s), he should not be excluded from enjoying the benefits of SSDS Trusts. Fogel specifically addressed the physician issue:[71]

> For example, suppose a doctor creates an asset protection trust because [she] fears being sued for malpractice at some point in the future. If the doctor later commits malpractice, may the injured patient set aside the transfer as fraudulent with respect to that injured patient? Generally, such a patient may not set aside the transfer because the patient was not a contemplated creditor at the time of the transfer.

Model Trust Fraudulent Transfer Implications

The violation of fraudulent transfer statutes is by far the most common defect of SSDS Trusts that are invalidated.[72] The legal and moral imperative to prevent actual fraudulent transfers is unchallenged; however, neither the spirit nor the letter of the law is compromised if the Model Trust is created and the transfers are made at a time when the settlor has no current or foreseeable creditor or judgments problems. For practitioners, up-front due diligence is essential to avoiding a fraudulent transfer trap.[73]

SSDS Trust Validity is a Choice of Law Question

Overview

If the validity of the Model Trust is challenged in court and, *arguendo,* the case survives jurisdictional, full faith and credit and other procedural barriers, the sitting court, be it federal or state, will be mandated to choose the law of one of the two conflicting jurisdictions. Generally speaking, in conflicts of law matters, the states defer to the stated intention of the settlor of a trust,[74] except, of course, when they don't. This is where the historical Self-Settled Trust Rule concept enters the picture. Suppose the trust code of a non-SSDS Trust state is modeled after the Uniform Trust Code, providing that, as to non-real property, the validity of a trust is determined by the law of the jurisdiction designated in the trust, unless the effect is contrary to a public policy of the jurisdiction having the most significant relationship to the matter.[75]

Using the Model Trust as a factual platform, at first blush it would appear that this state statutory language will lead to governance by the trust state: the trust designates the trust state law to govern; the trust state has the "most significant relationship" to the matter; and, the trust is not contrary to the trust state's public policy. Nonetheless, in non-SSDS Trust states, usually this will not be the state law due to either: (1) the existence of an overriding spendthrift trust creditors' claims statutory provision providing that a self-settled trust settlor's creditors may reach the maximum amount that can be distributed to the settlor, or (2) the existence of common law case precedent for either: (a) the Self-Settled Trust Rule or (b) a similar - but only very technically different - public policy prohibition against self-settled trusts. Thus, the local law and the trust state law will be in direct conflict as to the sustainability of the SSDS Trust. The result is that each case's unique facts

and each states' laws must be evaluated, as well as federal procedures, to determine which state law will prevail for cases that have not been sidelined earlier on jurisdictional or full faith and credit grounds.

Also, there are "one-off" matters that have effected conflicts of law cases, including: courts ignoring "most significant relationship" factors; courts overruling statute and precedent in a well-intended, but misguided, effort to administer equitable relief; courts not understanding the distinction between Restatement § 270 and § 273; and, at least one court, ignoring clear precedent to invalidate an SSDS Trust on the "unsupported" ground that the nonresident's state had a "strong public policy" against the trust. A specific treatment of choice of law issues in the relevant courts follows:

Bankruptcy and Bankruptcy Court

It is incumbent upon attorneys intending to present SSDS Trusts to their clients as a planning option to understand the potential effects of bankruptcy on their clients' planning goals; however, it must be reemphasized that, if bankruptcy is foreseeable when the trust is created, it should be assumed that transfers into the trust are voidable as fraudulent conveyances. In general, there are four areas for planners to take cognizance: (1) Will the SSDS Trust assets be included in the bankruptcy estate and available for distribution to creditors? (2) What is the impact of voluntary versus involuntary bankruptcy? (3) As to the validity of the trust, will the bankruptcy court apply the law of the trust state or the law of the settlor's residence state? (4) What effect, if any, will the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 ("BAPCPA")[76] "10-years clawback rule" have on the trust?

Bankruptcy Estate Trust Exclusion

Bankruptcy estates include "all legal or equitable interests of the debtor in property as of the commencement of the case;[77] however, certain assets or interests are excluded[78] or exempted[79] from the debtor's estate. For trust settlors, the most important exclusion is Bankruptcy Code §541(c)(2), which states: "A restriction (Emphasis added) on the transfer of a beneficial interest of the debtor in a trust that is enforceable under applicable nonbankruptcy law is enforceable in a case under this title."[80] The result is that the settlor's equitable interest in a valid spendthrift trust should not be included in her bankruptcy estate.[81] Consequently, the practical

effect of the trust exclusion is that a bankruptcy court's ruling should be limited to whether or not there has been a fraudulent transfer and which state's spendthrift law will apply.

Voluntary Versus Involuntary Bankruptcy

Earlier, it was concluded that a bankruptcy court with national jurisdiction, sitting in the settlor's state of residence, likely will be the venue for original jurisdiction over the Model Trust assets.[82] Further, if the settlor can avoid filing for bankruptcy or is able to avoid involuntary bankruptcy, the challenge may not reach court, allowing the trust to survive.[83] One writer has commented that "it is extremely unlikely that a…settlor will file for bankruptcy," adding that, of the hundreds of SSDS Trusts he has prepared, not one client has gone through bankruptcy.[84]

Although involuntary bankruptcy is a threat, debtors are provided with potential defenses. (1) Generally, involuntary bankruptcy will not be granted if such debts are subject to a bona fide dispute as to liability or amount. Consequently, a debtor may be able to avoid involuntary bankruptcy if: (a) he is generally not in default (b) he contests the amount of such debt in good faith or (c) he contests his liability for such debts in good faith. (2) A debtor may have a remedy against creditors who file an involuntary petition in bad faith and (3) An amendment to the 2005 Bankruptcy Act suggests a technical defense simple by refusing to undergo credit counseling.[85]

Will the Bankruptcy Court Apply the Law of the Trust State or the Nonresident Settlor's State of Residence?

In the instance of a well-structured SSDS Trust, like the Model Trust, where no fraudulent transfer exists, the bankruptcy courts can be expected to look at precedent from the Restatement (Second) Conflicts of Law to make a determination as to which state's law will apply. A 2013 bankruptcy case, *In Re Huber*[86] was the first to invalidate a SSDS Trust created under the law of a state different from the residence of the settlor.[87] In *Huber,* the settlor was a Washington State resident who created an Alaska SSDS Trust administered by an Alaska trustee. Facts cited by the Court included:

1. Huber was a Washington real estate developer who, in the 2008 downturn, was threatened with financial disaster on multiple fronts;

2. To avoid his creditors, Huber created an SSDS Trust in Alaska. Shortly before filing for bankruptcy, he funded the trust with the transfer of Washington real property and business assets he had recently placed into an Alaska LLC and a small amount of cash.

3. Huber's son was a co-trustee;

4. Huber transferred 78% of his assets to the trust;

5. Huber began to receive substantial trust distributions immediately;

6. The trustee did little active administration;

7. The trust stated that it was created for creditor protection;

8. The trust was executed in Washington; and

9. All the settlor's legal work was performed in Washington.

The Bankruptcy Court for the Western District of Washington correctly held that the bankruptcy had established that five badges of fraud existed in the case, which supported an inference of actual fraudulent intent to hinder, delay, or defraud Mr. Huber's creditors, to wit: (1) the debtor was threatened with litigation when the transfers occurred; (2) the transfers were of substantially all of the debtor's assets; (3) the debtor retained control of the transferred property; (4) the transfer from the debtor to the trust was to an insider; and (5) the debtor was attempting to remove the assets from the reach of the creditors.

Having properly struck down the transfers as fraudulent transfers, under both federal and state law, the court turned to the more far reaching choice of law issue, to wit: Should the validity of the trust be determined by the law of Alaska (for) or the law of Washington (against) and what factors should be considered? In reaching its decision, the Court first acknowledged that it would apply federal choice of law rules, which rely on the Restatement (Second) § 270(a).

> An inter vivos trust of interests in movables is valid if valid (a) under the local law of the state designated by the settlor to govern the validity of the trust, provided that this state has a substantial relation to the trust and that the application of its law does not violate a strong public policy of the state with which, as to the matter at issue, the trust has its most significant relationship… (Emphasis added)

Applying § 270(a), the Court made a factual finding that Washington state had the most substantial relationship to the trust by looking at four controlling (but not exclusive) factors for guidance. The stated controlling factors were:

1. place of business or domicile of the trustee;
2. location of trust assets;
3. domicile of settlors; and
4. domicile of beneficiaries

The Court also took note of the state of origin of the transferred assets, and the location of the creditors and the attorney who prepared the trust. Finally, the Court found that Washington State had a strong public policy against self-settled trusts. Following these facts, the Court chose the law of Washington, not Alaska, the state designated in the trust, and rooted its finding of trust invalidity on the ground that all of the relationship factors favored the settlor's home state of Washington. In baseball this would be called batting 0 for 4. Notwithstanding the "bad facts," the case's relevant precedent is not the end ruling; rather the case is significant because the Court considered the unique facts of the case to be the determinant of which state had the most substantial relationship to the trust for choice of law purposes.

Huber has been seen by casual observers as a blow to self-settled trusts, but they have misunderstood. It is the opposite. By basing choice of law "validity" on the named "significant relationship" factors, the court de facto has provided a virtual safe harbor for structuring a SSDS Trust sustainable in bankruptcy. By comparison, the Model Trust is not a fraudulent transfer, does not involve real estate, and meets all the *Huber* "substantial relationship" factors, except for the impossible: the residence of the settlor and her family beneficiaries. And this latter

issue was specifically addressed in *Hanson,* where the Court labeled the urging of the plaintiff "that, because the settlor and most of the appointees and beneficiaries were domiciled in Florida, the [forum] court of that State should be able to exercise personal jurisdiction over the nonresident trustees…a non sequitur."

In its ruling, the *Huber* Court noted that Washington "has a strong public policy" against self-settled trusts, essentially following the Rule. However, this factor is of no import with regard to the Model Trust, as demonstrated by reading the above excerpt from Restatement (Second) § 270(a), setting forth the Court's justification in giving consideration to Washington public policy, but only because it had the most substantial relationship to the trust matter. The Model Trust scenario is easily distinguished: the trust state has the most substantial relationship to the trust and does not have a "strong public policy" against SSDS Trusts.

BAPCPA and Bankruptcy Code §548(e) 10-Year Claw-Back Rule

In April 2005, Congress rushed through, and the President signed, the Bankruptcy Abuse Prevention and Consumer Protection Act, referred to as BAPCPA.[88] Thusly, Bankruptcy Code § 548(e) of the Act, addressing the bankruptcy treatment of self-settled trusts, was born. For analysis purposes, the relevant § 548(e) language provides that trustees may sue to avoid a transfer to a self-settled trust or similar device made on or within 10 years before the date of the filing of a bankruptcy petition if, the transfer was made "with actual intent to hinder, delay, or defraud" any creditor to which the debtor was or became indebted on or after the date that such transfer was made.

Multiple questions are raised by the Act and particularly the language in § 548(e); however, taking the most cautious road to interpretation, § 548(e) does not alter the requirement that there must be a fraudulent transfer before the court can void a transfer; therefore, the ten-year claw-back rule does not negatively impact the legal landscape for SSDS Trusts. In fact, it has been argued by Bankruptcy Judge, Honorable William Houston Brown that § 548(e) only applies to specific actual creditors,[89] a view which would strengthen SSDS Trusts.

In his commentary regarding § 548(e), Steve Oshins observed that if the settlor of an SSDS Trust is not named as a beneficiary at trust creation, but can be named later (e.g. the Model Trust), the trust will not fit the definition required by § 548(e)

that the debtor be a "beneficiary of such trust or similar device."[90] Oshins also points out that the section language further requires the transfer be made "to a self-settled trust or similar device," another unmet condition, because, at the time of execution, the trust is not self-settled.[91] While these interpretations are not assured, they also cannot be dismissed lightly.

Nonresident Settlor State Courts

A great deal of confusion about the sustainability of SSDS Trusts has been caused by commentators mistakenly focused almost entirely on the law of the settlor's home state, as if these states' laws were the gravamen of the matter. In fact, due to jurisdictional issues, FF&C issues, and the choice of law balancing that must take place in federal bankruptcy court, the number of trust challenges that can be expected to be resolved in local courts is relatively small; of course, these trusts are no less important to the planners and their clients. Thus far, it has helped advance the syllogistic logic of this Commentary to presume *arguendo* that the courts and statutes of non-SSDS Trust states prohibit such trusts; but, this has been merely a scrivener's device. The claim that "SSDS Trust terms are not enforceable in a settlors' home state courts" is simply inaccurate, as the issue is often contestable.

The plaintiff's strongest claim will be in a state with case precedent for the common law Self-Settled Trust Rule. In such states, absent a superseding statute, transfers into a self-settled trust, irrespective of location, will be against state law, unless the court can be convinced that the Rule has been compromised by changing times or if, perhaps, the court conducts a deeper examination of the public policy issues. Nonetheless, as discussed, having a favorable state law will do little to aid the plaintiff, if the SSDS Trust is located in a favorable trust state and properly established.

Plaintiffs in state court also may attack SSDS Trusts on one or both of two other fronts. Some non-SSDS Trust states will have language in their model trust code speaking to trust conflicts of law issues similar to the now familiar Restatement (Second) § 270 "substantial relationship" concept, setting forth which competing state's choice of law statutes will govern the "validity" of a trust and the meaning of its provisions.[92] Looking at separate case facts where the settlor states have the most substantial relationship to the trust, superficial analysis has generally argued

that these provisions give the state courts reasonable grounds to "invalidate" the trust. But, as wise lawyers often say, "Not so fast."

In an insightful commentary,[93] Barry S. Engel offers a compelling argument regarding the court's dicta in *Huber*.[94] Engel contends that the Court misapplied Restatement § 270 and, instead, should have relied on Restatement § 273. His argument is that the court resolved the wrong question. Restatement § 270 speaks to the "validity" of the trust, but validity is not the issue, as trusts are inherently valid contracts (e.g., revocable trusts and IRA trusts are also self-settled trusts). Rather, the relevant question is "whether the [valid] trust will be enforceable as against the creditors of that person."

The title of Restatement (Second) § 273 "Restraints on Alienation of Beneficiaries' Interests," is prima facie evidence of the incisiveness of Engel's argument. Paraphrased, § 273 states that whether the creditor may be assigned a beneficiaries' interest is determined by the governing law designated in the trust, "and otherwise," by the law of the state to which the administration of the trust is most substantially related. The words "and otherwise" are crucial, because, in this context, they can only be interpreted to mean the state law designated to govern the trust will prevail in enforcement cases and, only if there is no designation, will substantial relationship factors even come into play. Taking Engel's argument to its natural conclusion, the terms of a trust instrument designating the trust state's law to govern, when combined with the trust state's law enforcing the trust's provisions against creditors, present a difficult to refute argument demanding that the state court enforce the trust's terms.

Nenno & Sullivan fully support Engel's view, also using *Huber* to distinguish the uniquely different purposes of § 270 and § 273:

> …[I]t is clear that the court misapplied the Restatement, under which issues are divided into matters of validity, governed by § 270 and construction, administration, and creditor rights, governed by other sections of the Restatement. Under this framework, matters of "validity' are confined to issues such as whether the trust violates the rule against perpetuities or the rule against accumulations. In contrast, § 273 of the Restatement deals specifically with the question of a

> creditor's ability to reach trust assets, and provides that the law designated by the settlor governs – without stated exception.

Thus, § 273 broadens the protection of SSDS Trusts by narrowing the relevant choice of law issues to the terms of the trust and a knowledgeable interpretation of the Restatement provisions.[95]

The plaintiff's remaining claim likely will be that the settlor's state of residence has an overriding "public policy" against irrevocable trusts that benefit the settlor, and thereby, the trust should be deemed "invalid, *per se*."[96] This claim is similar in effect to the Self-Settled Trust Rule claim, but, in practice, may be more difficult to support with evidence and logic. Contra public policy positions were common prior to the adoption of SSDS Trusts, but with the passage of time, deeper examination has shown that these views, some aged, tend to be superficial and clearly do not contemplate the evolution of the intents and purposes of modern SSDS Trusts. More recent thinking on a few of these issues follows. Later, the Commentary will discuss public policy issues in greater depth.

Many states' public policies protect an individual's equity build-up in IRAs, life insurance policies and annuities. These and similar vehicles are no less self-settled trusts than SSDS Trusts. Consequently, it would seem disingenuous for a court in one of these states to claim that the state has a "strong public policy" against SSDS Trusts.

Another incongruity is rooted in tax law. A number of states without SSDS Trust statutes or, with limited statutes, have enacted laws protecting the assets of an irrevocable grantor trust from creditor claims where the trustee, in its discretion, may reimburse the settlor for income tax resulting from assets in the trust. The existence of these 15 enacted statutes impales the argument that these states have a "strong public policy against SSDS Trusts.[97]

"For reasons of policy" is not a reason."[98] Dated model codes have withheld their approval of SSDS Trusts or advanced the notion that they are against public policy without explaining just how they are against public policy.[99] And, unless <u>model</u> lawmakers can spell out their rationales, how can <u>actual</u> lawmakers assess these rules?[100] Consider a bank operating in a competitive credit environment. As a matter of policy, shouldn't this voluntary creditor be free to reach any agreement it

desires without interference from lawmakers and courts? "Those creditors who desire more protection can get it by demanding a security interest or additional contractual restrictions on debtors' behavior as a condition of the loan."[101] If a transfer to an SSDS Trust downgrades a sound borrower into a poor credit risk, then the bank simply can deny the credit. Should not legal regulation be restricted to situations where market imperfections create inefficiencies, or where market participants are prone to make systematic errors of judgment?[102] Why should the legislature or the courts intervene to protect the more sophisticated party to the contract?

SSDS Trusts are evolving. An example of a SSDS Trust provision not yet even contemplated by the non-SSDS Trust courts and legislatures, as restated from the Model Trust summary above, follows:

> …the trust protector has absolute discretionary power to add trust beneficiaries who are descendants of the grantor's grandparents.

Thus, additional questions are raised, leaving the law unsettled in forum states, at least as to whether those states' laws will apply to a trust following the tenets of the Model Trust: (1) What if the settlor is not a beneficiary under the trust, but can be added later by the trustee or a trust advisor. (Author comment: there can be no "implied agreement")? and (2) Is there a cogent argument that the nonresident settlor's home state has a "public policy" so strong that a court will arbitrarily "strike down" a trust and, with it the settlor's wishes, solely on the ground that the settlor can be added as a beneficiary? Relevant actions of nonresident settlor legislatures in this and other matters indicate the answer may be "no."[103]

Even Professor Scott states that "differences in spendthrift trust law are not enough to establish a "strong public policy' which would justify disregarding the law of the state of administration chosen by the settlor."[104] And, what logic is there for a policy favoring alienation of property through outright gifts, while casting aspersion on irrevocable trust gifts that have a few strings attached in case of an emergency? None.

Trust State Court Jurisdiction

It was concluded earlier that the law of the state where the self-settled trust is created will govern a properly established and implemented SSDS Trust with a

nonresident settlor, if the settlor's home court (and in some cases, the trust state court) finds that the trust state has jurisdiction due to the location of the trustee, the trust assets and other relationship factors in the trust state and the trustee's minimal contact with the settlor's state of residence.[105] In such an instance, the trust state's code[106] will typically provide that the meaning and legal effect of a governing instrument will be determined by the trust state's trust validity law, unless the application of that law is contrary to public policy of the trust state, which, by definition, it is not.

Recent Utah State Court Decision

Perhaps more interesting than *Huber* is the relatively recent Utah Supreme Court's decision in *Dahl v. Dahl,* 2015 UT 79. *Dahl* involved a Utah divorcing spouse who sought her share of marital property from a Nevada-formed self-settled trust controlled by her husband, but which was jointly funded by the husband and wife years before. The State's High Court construed the trust "revocable" under Utah law on the ground that Mr. Dahl, the executing settlor, retained an unrestricted power to amend the trust. Although Mrs. Dahl was largely unknowing of the particulars of the funding, the court ruled that both spouses were original settlors and, because the trust was revocable she was entitled to a return of her contribution to the trust. If the Court had ruled solely on the issue of "revocability," its reasoning, however odd, generally could have been supported. Instead, the case has been roundly criticized by commentators.[107]

The controversy is over the Court's second finding, which refused to enforce the trust's Nevada choice of law provision, concluding instead that Utah had a "strong public policy interest in the equitable division of marital assets." To support its claim of "strong public policy," the Court cites, (1) *Waddoups v. Amalgamated Sugar Co*, 2002 UT 69, 54 P. 3d 1054 (2002); (2) Utah Code § 75-7-107 & cmt. and (3) *Jacobsen Constr. Co. v. Teton Builders*, 2005 UT 4, ¶ 19, 106, 106 P.3d 719, Inexplicably, the Court's "strong public policy" position is not supported by any of its opinion sources: *Waddoups*, UTAH CODE § 75-7-107 OR *Jacobsen*, (See Endnote no.[108] for a critical analysis of the court citations). Further, the court failed to even discuss what should have been the case's central issue - the substantial relationship factors.

Summarizing, for purposes of clarity and precedent, the *Dahl* opinion is extremely limited, applying only in Utah, solely for the purpose of providing support for equitable relief in marital dissolution.

Implementation

Each SSDS state has specific requirements for a SSDS Trust to qualify for its jurisdictional venue. In the leading trust states, there are generally four requirements: (1) the trust instrument must be irrevocable, (2) it must contain a spendthrift provision, (3) it must incorporate the trust state law to govern its validity, construction and administration and (4) the trustee must be domiciled in the trust state.[109] A poorly drafted or improperly implemented SSDS Trust can fail for many reasons; therefore, a court asked to uphold an SSDS Trust can be expected to take a close look at the particulars of the trust arrangement to insure that "it is what it appears to be" and that all statutory requirements have been followed. Examples of potentially failed implementations would be an "implied agreement" or "sham" between the settlor and the trustee;[110] or if the trustee's activities exceeded minimal contacts with the settlor's home state.[111] Planners should take care to meet all requirements and, in particular, to avoid a fraudulent transfer by insuring that proper due diligence procedures are followed as to existing and foreseeable liabilities.[112]

Contract Clause

It has been argued that a creditor seeking to attack a SSDS Trust can claim it is a violation of the Contract Clause of the U.S. Constitution on the ground that the trust state's statute violates the Contract Clause by eliminating the creditor's ability to seize assets to which he would otherwise have had access before the enactment of such statute.[113] Irrespective of the merits of this argument, in the Model Trust, the Contract Clause claim practically will not affect the trust because the Clause would only apply to contract creditors who existed on or prior to the effective date of the enactment of the trust state's statutes, generally over a decade ago.

More on Public Policy

Although most SSDS trusts are not challenged,[114] there has been a troubling pattern in some of the ones that have gone to court. Of course, these cases are in

court for the very reason that they are troubling; but a more interesting analytic is at work. In practice, different creditors' claims raise different sorts of policy concerns. In a complex commercial environment, this may not be a matter about which we are capable of generalizing.[115] In his thoughtful article on the subject, Adam J. Hirsch, wades through these issues and concludes "that the fundamental principles of asset protection doctrine are…compatible with public policy."[116]

Below is a discussion of some of the more relevant public policy issues.

Clients' Right to Asset Protection Planning

In an article, the Osbornes well-assess the critical environment for SSDS Trusts:[117]

> While proclamations from the ivory tower have occasional value for the practitioner, it is far too easy for a legal purist peering down from high aloft to focus on a few instances of flagrant abuse…, stake out a position of moral outrage, and then universally condemn anyone who dares to engage in asset protection planning. (Author comment: "What is an LLC, after all?") Although perhaps satisfying their sensibilities and finely-honed sense of moral rectitude…such a reaction is simplistic, unhelpful and unsupportable after even a cursory look at the asset planning abuse protections already well-established in the law…
>
> Almost all estate planning lawyers, almost all of the time, represent honorable, law abiding clients, men and women who daily contribute to society by their productivity and with their generosity, who pay their bills and their taxes, and who are not deadbeats, cheats, frauds, or criminals. These same good people, some of whom have acquired significant wealth by their own hard work or that of their forebears, are legitimately concerned about the excesses of an American litigation system which sometimes more resembles a lottery-like payoff game than it does a reliable forum for the settlement of genuine claims.

TOM HANKS SLAPPED WITH LAWSUIT OVER SON CHET'S CAR CRASH

Entertainment, The Wrap, Tim Kenneally, Mar 29th 2016 10:09 AM.

> "Chester Hanks was driving his vehicle in an unreasonable and unsafe manner and was under the influence of alcohol and/or drugs at the time his vehicle struck Mr. Moogan's vehicle," the suit claims. According to the complaint, Tom Hanks and his wife, Rita Wilson own the vehicle that Chet was driving. "Despite knowing that Chester Hanks was a careless and reckless driver they negligently handed him the keys," said Moogan.

> Let's be clear on this notion of duty. Even if some estate planning attorneys resist the idea, you can be assured the plaintiffs' bar will not. The next wave of creative malpractice actions could well be against estate planning attorneys who fail to advise clients about asset protection alternatives, filed by clients who have suffered financial reverses which could have been avoided with such planning.

Cases Can Be Distinguished

Each trust is different and the same brush should not tar all cases. The hypothetical Model Trust illustrates facts so dissimilar to cases like *Huber*, in both intent and fact, that it demonstrates that individual cases can and should be distinguished and justice served to all parties.

The Non-Asset Protection Benefits to Settlors Are Substantial

The statutory benefits in trust states are real and substantial, so much so that it seems fair to ask: "If SSDS Trusts are sustainable in the face of legal challenge, do local estate attorneys have an <u>obligation</u> to discuss with their clients the pros and cons of designating a strong SSDS Trust state, as their trust jurisdiction?" Reframed, the proper question may be: "Why not, particularly if creditor protection is of no consequence to the settlor?"

Fraudulent Conveyance Protections Already Exist

To what rights should pre-existing <u>voluntary</u> creditors be entitled? Should debtors be able to make risky loans and then render themselves judgment-proof? The answer is no, but the question is a red herring. Fraudulent conveyance law affords the basic protections that every unsecured creditor presumably would insist on to make any loan agreement viable. And under all of the leading domestic statutes, fraudulent conveyance law applies to the creation of an SSDS Trust.[118]

Further, protection for creditors from fraudulent conveyances has been strengthened by the passage of the BAPCPA, where, the legitimacy of SSDS Trusts was acknowledged by Congress when it chose to: (1) defer the authorization and regulation of such trusts to the individual states' legislatures,[119] and (2) specifically approved the right of bankruptcy estates to "claw back" assets fraudulently transferred into self-settled trusts.[120]

Legislatures' "Motives"

Hirsch states: "The driving force behind these legislative initiatives is clear enough. States are vying for trust business."[121] "We cannot, however, condemn these "marketing statutes merely because their motives are impure. Policy developments and time may yet vindicate the vehicles they authorize,"[122] "much as its close relative and doctrinal progenitor, the spendthrift trust, once did."[123] Another keen example is the history of states competing for industry by offering tax-exempt bonds and other monetary incentives to companies bringing a substantial number of employees into their states.

SSDS Trusts Are Not Deceptive

If SSDS Trusts were deceptive, creating a false appearance of creditworthiness, the markets would be effected. Fortunately, no risk of deception arises, because there is no appearance of the debtor continuing to own any of the assets in the trust. Trustees must segregate and earmark the assets in order to distinguish them from the settlor's assets. None of the leading trust state statutes depart from this fundamental trust principle. "Hence, SSDS Trusts are not stealth vehicles, invisible to radar."[124] Their existence will be clear from a cursory review of a modern lender's credit application; and a failure to disclose will constitute a definitive badge of fraud under the fraudulent conveyance statutes and run afoul of federal banking laws.

Special Exceptions Creditors

Trust states vary considerably in the degree to which they allow SSDS Trusts to protect persons with claims for alimony, child support and property in marital dissolution. Generally, these obligations fall under what are called 'special creditor exceptions" and must be evaluated on state-by-state basis.

Involuntary Creditors

The most thought-provoking public policy issue facing the asset protection doctrine is presented by the following hypothetical scenario: An SSDS Trust is created, "when the waters are calm," for tax advantages, trust flexibility and to guard against unforeseen, but conceivable, involuntary creditors' claims. Later, there is a car accident. Certainly, the settlor cannot be accused of fraud since no claim or expectation of a claim had arisen when the trust was executed. Therefore, if an SSDS Trust follows the Model Trust and is properly established and otherwise sustainable, the trust should be a barrier to the claim.[125]

Should this prospect sound alarm bells? Already, most states consider many techniques, which provide some degree of creditor protection, to be sound public policy. Examples include: IRAs, life insurance, annuities, homesteads, tenancies by the entirety and Section 529 plans. Some of these already are, technically or de facto, self-settled trusts. Should SSDS Trusts be treated differently? Philosophically, does the settlor's potential right to protection encourage dangerous acts? It seems doubtful, as dangerous behavior also poses risks to the settlor and others; but unfortunately this question does not lend itself to a double-blind study. Generally, public policy favors the free alienation of property. Is this a logical situation to restrict alienation?[126] A more in-depth discussion of these questions is beyond the scope of this Commentary; but, hopefully, these questions will provide seeds for readers' thought.

All Roads Lead to "Most Significant Relationship"- a Question of Fact

In the illustrative Model Trust, all possible significant relationship factors lead to the trust state, so why should its law not apply? For a practitioner, it is essential to carefully establish and document the all-important relationship of the trust to the trust state, as the issues of jurisdiction, enforcement under the FF&C Clause and choice of law may all turn on variations of this singular point.

Professor Danforth on Professor Scott

As cited in an Osborne article,[127] Robert T. Danforth of Washington and Lee University School of Law published a balanced, provocative, and insightful article on creditors' rights and trust law in the Hastings Law Journal.

> Professor Danforth's most provocative and significant conclusion stems from his examination of the tautological maxim of American law that one cannot create a self-settled spendthrift trust. Professor Danforth points out that while the rule is essentially set forth in both Professor Austin Wakeman Scott's treatise and the Restatement (Second) of Trusts (for which Professor Scott was the reporter and principal author), neither source offers a solid, independent rationale or theoretical basis for the rule. Moreover, and most interesting, the cases cited by Professor Scott do not, in fact, support the rule as he lays it out. As Professor Danforth gently remarks about these cases, it seems that "[Professor Scott] read them somewhat generously in support of his position."
>
> Professor Danforth further argues that the rule against self-settled spendthrift trusts, as espoused by Professor Scott, is not based on sound legal theory for a number of reasons. First, the rule ignores the rights of non-settlor beneficiaries, since the creditor can defeat the interests of those beneficiaries as well as the interests of the settlor. Second, it assumes a collusion between the settlor and the trustee, in which the trustee will blindly comply with the settlor's bidding, ignoring the legal obligations of fiduciaries. Third, it grants creditors greater rights than the settlor, since the creditor can compel distributions and the settlor cannot. Finally, the rule fails to distinguish situations in which the creditor retains a power of disposition from those in which the settlor does not.

Incongruous Results

Theories for local courts exercising expanded long-arm jurisdiction can meet with unexpected public policy results. Consider two scenarios proposed by Professor Whitten:[128] (1) If State X were to issue a license to carry a concealed weapon to someone in State X, all other states would have to allow the licensee to carry a concealed weapon within their borders also, as a matter of full faith and credit. (2) Similarly, if State Y decided to issue driver’s licenses to ten-year olds, all other states also would have to allow State Y ten-year olds licenses to drive within their borders as a matter of full faith and credit. Although these scenarios (at least the

second) may seem extreme, it is easy to imagine real world cases where court procedure and a particular courts' notion of public policy collide.

Other Policy Support

Limitations prevent this from being an exhaustive discussion of relevant public policy issues. A short list of other policy matters, not discussed herein, includes: (1) Much of the world already allows self-settled trusts. (2) Trillions of dollars have/are moving to these jurisdictions. (3) SSDS Trusts create economic incentives and encourage entrepreneurship. (4) SSDS Trusts preserve U.S. business. (5) SSDS Trusts allow for U.S. oversight, and (6) It is illogical that outright gifts are allowed, but not SSDS Trusts.[129]

Policy Issues Conclusion

Notwithstanding the unconcluded debate over these matters of public policy theory and substance, for the purpose of sustaining the Model Trust, it should be enough that the trust state is designated to govern and/or has a more substantial relationship to the trust, the trustee, trust assets, administration and ancillary trust matters than the settlor's home court.

SSDS Trust Taxation

Estate and Gift Taxes: Overview

The typical domestic SSDS Trust is structured to be an incomplete gift for federal gift tax purposes and includible in the settlor's gross estate for federal estate tax purposes.[130] However, if the trust is properly-drafted, it is also possible for it to be a completed gift for federal gift tax purposes and have the trust assets excluded from the settlor's estate for federal estate tax purposes.[131] This opportunity arises from a 2010 private letter ruling[132] finding that, for self-settled trusts where the settlor is a resident of the state with trust jurisdiction, the gift can be both complete and excluded from the settlor's gross estate if: (1) there is no pre-existing agreement between the participants; (2) the grantor does not retain power to remove the trustee and name the grantor; and (3) there is no local law subjecting the assets to claims of creditors. As the trust is the taxpayer, the referenced local law is the law of the trust state.[133]

For SSDS trusts with a nonresident settlor, there has been no specific revenue ruling; however, Rothschild, Blattmachr, et al., stake out the position that the settlor's residence in another state would not alter the result.[134] Quoting the authors, "In both Ltr. Ruls. 9837007 and 2009944002, the grantor was an Alaskan. However, it does not seem that the conclusions reached would be different if the grantor were domiciled in another state." The authors found *Estate of German,*[135] where Mrs. German, the grantor, was a Floridian, but the trust was created and administered under the laws of Maryland, to be on point. "The Court makes it clear that the question of whether the trust would be included in Mrs. German's estate turned on "the extent of the defendant's rights with respect to the trust income and assets under Maryland law," not Florida law" … Ltr. Rul. 2009944002 seems completely consistent with the official position of the IRS."

Comparing Traditional Irrevocable Trusts and SSDS Trusts

If the planner's goal is to prevent the settlor from making a completed gift, she should have the settlor retain a testamentary power, such as a power of appointment over the trust and a lifetime power, such as a power to veto distributions.[136] Conversely, if the settlor does not keep these or similar powers, the gift will be treated as completed upon the settlor parting with dominion and control over the property placed in the trust.[137] However, a unique problem is presented with SSDS Trusts because, in order not to create a nexus that could jeopardize the trust's carefully crafted asset protection,, it is unwise to allow the settlor to retain the standard trust powers that would ensure an incomplete gift. Under I.R.C. §2038(a)(1) or §2036(a)(2), whether the creation of a SSDS Trust will be a completed gift or subject to estate tax at the settlor's death will turn on the somewhat narrow question of whether creditors are able to attach the trust assets. All pertinent cases and rulings indicate that the settlor will not make a completed gift, nor obtain estate tax exclusion, if she retains the power to enable the creditors "backdoor" access to the gift by incurring debt and thereby "relegating" creditors to trust assets.[138] Established SSDS Trust states have eliminated this problem by enacting statutory language specifically preventing creditors from reaching trust assets to satisfy the settlor's debts.

GST Tax

The settlor's allocation of her §2631 GST exemption from the federal generation-skipping transfer tax ("GST tax") to transfers to a domestic SSDS Trust will not be

effective as long as the trust is subject to an estate tax inclusion period, i.e., as long as the trust is includible in her gross estate.[139] That issue may not be resolved conclusively until after the settlor's death (when the IRS, with hindsight as to patterns of distribution and claims of creditors, may establish estate tax inclusion). Consequently, the settlor might want to fund a trust to which GST exemption is to be allocated with assets that she will not need and in which she reserves no interest. She might then place the balance of the assets to be protected in a domestic SSDS Trust that is not structured to be a completed gift or excludible from the gross estate.[140]

Model Trust Taxation Implications

Federal Transfer Taxes

In many cases, in order for the Model Trust to be advantageous for large estate tax exclusion purposes, planners want the trust gift to be a completed gift and the value of the gift excluded from the transferor’s gross estate. Generally, the trust state statutes will allow SSDS Trust drafters the option of including or excluding the gift from the estate of the settlor.[141] The viability of both options is supported by learned authorities, even in the absence of a formal IRS determination.[142] For planners wishing to take a “wait and see” view, there are other approaches to accomplish large estate tax planning, such as taking advantage of various grantor trust techniques, e.g., intentionally defective grantor trusts. Notably, for a couple transferring less than $10 million, the gross estate inclusion limitation should not lead to exposure to incremental taxation if the couple’s gift tax exclusion remains adequate to cover the transfer.

Trust Income Tax in the Nonresident Settlor’s Residence Jurisdiction

If the trustee and trust assets are located in a low or zero tax rate trust income state and the settlor resides in a high trust income tax state, for some high rate states, it is possible to establish the SSDS Trust as a nongrantor trust, effectively shifting the trust income tax liability into the “no/low tax” state. In other states, trust income tax shifting may not be viable for a nonresident settlor, e.g., the state may tax the trust if only a single beneficiary is a state resident. This may be true even if the Model Trust has scant nexus to the nonresident settlor (e.g., trustee, property, et. al. are located in the trust state), as states’ trust income taxation policy can be

far reaching. Therefore, each applicable state's trust income tax law must be evaluated independently.

Attorney Ethical Considerations

It has been seen that SSDS Trusts offer numerous benefits to estate planning clients, only one of which is to reduce the risk of future and unforeseen creditors accessing transferred assets. For example, the trust state law may protect attorneys and others who assist in establishing SSDS Trusts in the state. As for the settlor's home state, although generally there is no precedent, the majority view is that a SSDS Trust attorney providing similar assistance does not create the risk of ethical discipline.[143] Under the right circumstances, estate planning, using an SSDS Trust, should be as ethical as it is valuable. A full review of attorney ethics requirements under state bar codes and independent law is beyond the scope of this Commentary. Instead, a brief check-list of some of the points that should be of greatest interest to planners is provided below under the two topics: (1) actions to definitely avoid and (2) actions to be sure and undertake.[144] This topic does not address the ethics code of any specific state bar association, but speaks in terms of the most likely treatment of the ethical issues. Attorneys must research their own states' laws.

Avoid

1. Moral ambiguity. For qualified trust candidates, the tangible opportunities (e.g., modification flexibility, favorable notice provisions, and potential tax benefits) should make the more abstract potential for asset protection benefits seem incidental. An attorney considering SSDS Trusts should not have a moral quandary if he or she is persuaded that such trusts are an attractive tool for a client engaged in estate planning who has assets above and beyond what is needed for estimated liabilities.

2. Assisting in a fraudulent transfer.

3. Joint representation conflicts. In addition to the requirement of full disclosure and consent, an attorney must have a reasonable belief that representation, in light of the conflict of interest, will not adversely affect any of the parties. If not, resignation from one or both of the parties is likely required.

4. Omitting to discuss SSDS Trusts with clients. As part of estate planning, attorneys are ethically bound to provide competent representation to the client. As SSDS Trusts become more ubiquitous, and client awareness increases, an obligation to inform clients may be forced on attorneys.

Pro-Active Steps

1. Identify realistic candidates. A potential candidate will: (a) have significant assets, (b) have unforeseen, but conceivable risks (e.g., be engaged in a regulated industry), (3) be financially solvent after the transfer, and (4) have no fraudulent or criminal intent.

2. Counsel clients regarding the benefits of SSDS Trusts.

3. Due diligence: The first step in due diligence will be a thorough intake interview. Particular attention should be paid to situations involving judgment, bankruptcy, divorce or recent movements of assets.

4. If not expert on the unique provisions of SSDS Trusts and the applicable out-of-state law, retain advice.

5. Engagement letter.

HOPE THIS HELPS YOU HELP OTHERS MAKE A *POSITIVE* DIFFERENCE!

Thomas E. Greene III

TECHNICAL EDITOR: DUNCAN OSBORNE

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CITATIONS:

[1] Author comment: It has been argued that the greatest threat to SSDS trusts may lie in renderings by courts with a limited knowledge of trust law and a crowded calendar. Both plaintiffs and defendants will be wise to anticipate the appellate court process. In all cases, the plaintiff's legal team will need to weigh this prospect against the potential benefits.

[2] Fogel, *Scylla and Charybdis Attack: Using Trusts for Medicaid Planning and Non-Medicaid Asset Protection*, 35 ACTEC J. 45, 47 (Summer 2009).

[3] Steven J. Oshins, *The Hybrid Domestic Asset Protection Trust: A Third Party Trust That Can Turn into a Self-Settled Trust: Does a DAPT Work?* www.oshins.com (2013).

[4] Author's comment: Prior to 1997, the states generally held that self-settled trusts were invalid *per se* either because they were against public policy (usually for unstated reasons) or the state followed the common law Self-Settled Trust Rule. The Rule has been rolled forward and incorporated in the Restatement (Second) of Trusts § 156 (1959) and the Restatement (Third) of Trusts § 58(2) (2003), which simply states: "A restraint on the voluntary and involuntary alienation of a beneficial interest retained by the settlor of a trust is invalid." As will be discussed, neither of these reasons pertains to the law of fraudulent transfers. See e.g., Alaska enabling statute §§ 34.40.010 to 34.40.13 (first U.S. state self-settled trust statute, post amendments).

[5] See e.g., *SEC v. Brennan*, 230 F. 3d 65 (2nd Cir. 2000) (Debtor convicted of bankruptcy fraud.); *In re Lawrence*, 279 F. 3d 1294 (11th Cir. 2002) (Debtor retained control powers over trust and was cited for contempt and incarcerated.); *Bank of America v. Weese,* 277 B.R. 241 (D.Md. 2002) (asset transfer just prior to bankruptcy); *In re Portnoy*, 201 B.R. 685 (Bankr. S.D.N.Y. 1996) (The only trust connections to the Jersey Channel Islands law were that the trust was settled and administered in Jersey and the trustee was a Jersey resident).

[6] Author comment: Although some commentators argue that foreign asset protection trusts are preferred over their domestic cousins due to the full faith and credit protections afforded to domestic creditors, this is now a minority view. This Commentary demonstrates that plaintiffs pursuing assets held in domestic SSDS

Trusts have underlying jurisdictional problems, which also impact their FF&C claims. Further, foreign trusts are associated with greater foreign financial risk, higher costs, a greater risk of fine or imprisonment and a generally unspoken belief that they tend to involve fraudulent conveyances and other abuses.

[7] See Steven J. Oshins, 7th *Annual Domestic Asset Protection Trust State Rankings Chart* (April 2016) (States by rank: Nevada, South Dakota, Tennessee, Ohio, Delaware, Missouri, Alaska, Wyoming, Rhode Island, New Hampshire, Hawaii, Utah, Virginia, Oklahoma, Mississippi, West Virginia) (Author comment: Colorado has limited elements of an SSDS Trust (Colo. Rev. Stat. §§ 38-10-111), but does not meet ranking qualifications).

[8] Author comment: Commentary references to "trust state" or "SSDS Trust" law generally apply to the states of Alaska, Delaware, Nevada and South Dakota. The use of these states trust laws for purposes of the Model Trust is not intended to recommend these states solely or imply that they are the only preferred states. They are referenced because they are certainly among the top states and because of the author's prior trust experience. For practitioners selecting a trust state for their clients, the author does recommend considering only states which have fully-rounded SSDS Trust laws and scholarly commentators regularly updating the legal community on trust developments in the state. A few of the most prolific commentators are: for Alaska, David G. Shaftel, law firm of Shaftel Law Offices, Anchorage, Alaska; for Delaware, Richard W. Nenno, Managing Director and Trust Counsel, Wilmington Trust Company, Wilmington Delaware and John E. Sullivan, III, law firm of Sullivan & Sullivan, Ltd, Cleveland, Ohio; for Nevada, Steven J. Oshins, law firm of Oshins & Associates, Las Vegas, Nevada. For a thorough comparison of the states' laws, see ACTEC Comparison of the Domestic Asset Protection Trusts Statutes, updated through September 2015, edited by David G. Shaftel, available online under its Title.

[9] See David G. Shaftel, *Alaska's Five-Year Experience with Self-Settled Discretionary Spendthrift Trusts,* Estate Planning, October 2002.

[10] See Nenno & Sullivan, 868 T.M., *Domestic Asset Protection Trusts* (for a discussion of SSDS Trusts generally).

[11] See e.g., S.D. Codified Laws § 10-44-2.

[12] See e.g., S.D. Codified Laws §§ 43-5-1 – 9 & 55-1-20.

[13] See e.g., S.D. Codified Laws §§ 55-2-15 – 21. See Steven J. Oshins, *3rd Annual Trust Decanting State Rankings Chart* (January 2016).

[14] See e.g., S.D. Codified Laws § 55-3-24.

[15] See e.g., S.D. Codified Laws § 55-16-10.

[16] See e.g., Al W. King III, *Planning with South Dakota Domestic Asset Protection Trusts*, American Bar Association, Section of Real Property, Trust and Estate Law, Chicago, IL (June 2015).

[17] See e.g., S.D. Codified Laws §§ 47-34A-504, 48-7-703 & 47-34A-504(g) (LLC sole member protection).

[18] See King, *supra,* at n. 16.

[19] See e.g., S.D. Codified Laws § 51A-6A-66.

[20] See e.g., S.D. Codified Laws § 55-1B-6.

[21] See e.g., S.D. Codified Laws §§ 55-1B-9,10.

[22] See e.g., S.D. Codified Laws § 55-2-13.

[23] Author comment: In response to settlors' desires not to raise "trust-fund terrors," some trust state legislatures have enacted statutes, like S.D. Codified Laws § 55-1-20, 22, authorizing settlors to create trusts with designated goals and purposes, rather than defined beneficiaries. "Purpose" examples would be to permit the trustee to fund a loan to a grandchild's well-planned business endeavor or pay the costs of travel, lodging and expenses to a family gathering and planning retreat.

[24] See e.g., S.D. Codified Laws §§ 43-5-1 to 43-5-20 & §55-1-20.

[25] See e.g., S.D. Codified Laws § 55-16-13.

[26] *Id.*

[27] See *Hanson v. Denckla*, 357 U.S. 235 (S. Ct., 1958); *Rose v. FirStar Bank*, 819 A.2d 1247 (R.I., 2003); *In the Matter of Estate of Ducey*, 241 Montana 419, 787 P.2d 749 (1990); See Restatement (Second) of Conflict of Laws §104 cmt. a. See 218 *Wilkes v. Phoenix Home Life Mut. Ins. Co.*, 902 A.2d 366, 382 (Pa. 2006); *Estate of Waitzman*, 507 So. 2d 24, 25 (Miss. 1987); *Underwriters Nat. Assurance Co. v. North Carolina Life & Accident & Health Ins. Guaranty Assn*. 455 U. S. 691, 705 (1982).

[28] *International Shoe Co. v. Washington*, 326 U.S. 310, 66 S. Ct. 154, 90 L. Ed. 95 (1945).

[29] See *Hanson, supra,* at n. 27; *Int'l Shoe, id.* See *Dahl v. Dahl,* 2015 UT 79 (Cited here solely to demonstrate an instance where the state court gained jurisdiction, but only because multiple cases were later joined at the appellate court).

[30] See David G. Shaftel & David H. Bundy, *Part I. Domestic Asset Protection Trusts Created by Nonresident Settlors*, Estate Planning (April 2005).

[31] *Pennoyer v. Neff*, 95 U. S. 714.

[32] *Int'l Shoe, supra,* at n. 28.

[33] *Hanson, supra,* at n. 27.

[34] *Rose*, *supra,* at n. 27.

[35] *McGee v. International Life Insurance Co.,* 355 U.S. 220, 78 S. Ct. 199, 2 L. Ed. 2d 223 (1957).

[36] *Ducey*, *supra,* at n. 27.

[37] See *World-Wide Volkswagen Corp. v. Woodson*, 444 U.S. 286 (1980) (detailing additional actions that could constitute "minimum contacts," to wit: directly or indirectly performing or delivering services or products into the state, closing sales and benefitting from the state's laws); *Helicopteros Nacionales de Columbia v. Hall,* 466 U.S. 408, 414 (1984) (Without other actions, occasional trips into the state will not meet the requirement). But see cases with unique circumstances, where jurisdiction over the trustee was granted: *Seijo v. Miller*, 425 F. Supp. 2d

194 (D.P.R. 2006) (The Federal District Court for the District of Puerto Rico found that Puerto Rico had a "manifest interest" in providing a convenient forum for its residents.); *Cummings v. Pitman*, 239 S.W.3d 77 (Ky. 2007) (The trustee was an attorney practicing law in the forum state.); *Sloan v. Segal*, 2008 Del. Ch. LEXIS 3 (Del. Ch. 2008) (The local Court asserted jurisdiction based on its interest in determining whether a long-time resident had exercised her right of appointment in an uncoerced and knowing manner). See cites at Nenno & Sullivan, *supra*, at n. 10.

[38] *Baker v. Gen. Motors Corp*., 522 U. S. 222, 233 (1998).

[39] See Restatement (Second) of Conflicts of Laws § 276 (providing that "[t]he administration of a trust of an interest in land is supervised by the courts of the situs as long as the land remains subject to the trust"); See *Hanson, supra*, n. 27. But see, *Walker v. W. Mich. Nat'l Bank & Trust*, 324 F. Supp. 2d 529, 534 n. 3 (D. Del. 2004), aff'd., 145 Fed. Appx. 718 (3d Cir. 2005).

[40] See Shaftel, *supra,* at n. 30 (But, if the property is commercial income property, planners should investigate whether the property already may be registered in the state and required to submit to its jurisdiction).

[41] Gideon Rothschild at the panel discussion entitled "*Everything You Always Wanted to Know About Domestic Asset Protection Trusts but Could Never Find Out*," at 38 U. Miami Heckerling Inst. on Est. Plan. (2004).

[42] Author comment: In the absence of favorable court decisions, the transfer of local real estate and businesses into SSDS Trust LLCs should be approached with caution; nonetheless, a weighing of risk and reward may well lead planners to recommend the transfers utilizing the techniques described in the Commentary.

[43] *In re Huber*, *201 B.R. 685 (*Bankr. W.D. WA May 17, 2013*).*

[44] See e.g., Ga. Code Ann. Title 11, a state statute adapted from the UCC, applies to "attachments" in commercial transactions, not jurisdiction. Also, see UCC § 11-8-502 (a claim cannot be asserted against an intermediary under the facts of the Model Trust).

[45] James Steven Rogers, *Conflicts of Law for Transactions in Securities Held through Intermediaries*: *Determining the Intermediary's Jurisdiction – The Hard Part,* p. 310, Cornell International Law Journal: Vol.39: Iss. 2, art. 3 (2006).

[46] Shaftel, *supra,* at n. 30.

[47] *Huber*, supra, at n. 43.

[48] Rule 4(k)(1) & (2) of the Federal Rules of Civil Procedure (Serving a summons establishes personal jurisdiction only over a defendant who is subject to general jurisdiction in the court where the district court is located, unless the claim arises under federal law (e.g., bankruptcy).

[49] *Hanson, supra,* at n. 27.

[50] Fed. R. Bankr. P. 7004(d) & 9016; See *Shaftel, supra*, at n. 30.

[51] Shaftel, *supra,* at n. 30.

[52] See e.g., Ga. Code Ann. § 53-12-82(2) (stating that, with respect to an irrevocable spendthrift trust, creditors or assignees of the settlor may reach the maximum amount that can be distributed to or for the settlor's benefit. Author's comment: Modern SSDS Trusts and pertinent law cast challenge the practical effectiveness of these types of statutes).

[53] Quoting this Commentary: "The Model Trust scenario is easily distinguished: the trust state has the most substantial relationship to the trust and does not have a "strong public policy" against SSDS Trusts."

[54] U.S. Const. art. IV, § 1.

[55] *Id.;* See *Shaftel, supra,* at n. 30.

[56] See Duncan E. & Mark E. Osborne, *Asset Protection Trust Planning,* The American Law Institute Continuing Legal Education with CLEW (June 2005) (Osbornes caution about principles and facts that could alter the result such as: (1) where the trustee is "doing business" (2) Should a "center of gravity" approach be used in choice of law determinations? (3) Will there be long-arm jurisdiction if the trustee has sufficient contacts with the forum state? (4) the effects of *in rem*

jurisdiction (5) Is the trust a sham? (6) Is the trust against public policy? (7) enforcement under the Full faith & Credit Clause; and (8) Supremacy Clause concerns. Author comment: All these issues are discussed and resolved in this Commentary).

[57] See *Baker*, *supra* at n. 38 (Author comment: The case law distinguishes "public acts," (e.g. statutes) from monetary judgments to which the public policy exception does not apply).

[58] See e.g., Elizabeth Redpath, *Between Judgment and Law: Full Faith and Credit, Public Policy and State Records*, Emory Law Journal; Vol. 62, Issue 3, p. 639 (January 2013), discussing Adar *v. Smith* (*Adar I*), 597 F.3d 697, 701 (5th Cir. 2010), *rev'd*, 639 F.3d 146 (5th Cir. 2011) (en banc), *cert. denied*, 132 S. Ct. 400 (2011) (Author comment: Although *Adar* involved the problems of a gay couple attempting to correct the birth certificate record of their adopted child after moving to a different state with a public policy opposing gay adoptions, the full faith and credit principals should be equally applicable).

[59] Author anecdotal evidence based on discussions with knowledgeable professionals. Due to the paucity of challenges, there are no court cases confirming this assertion.

[60] See a thorough treatment of fraudulent conveyances, including a discussion of badges of fraud, by Michael L. Cook, Adam L. Hirsch, et al., *Fraudulent Conveyances* (January 2008), Schulte Roth & Zabel LLP & Skadden, Arps, Slate, Meagher & Flom LLP, attorneys, New York City, available online. But see S.D. Codified Laws § 55-16-10 (requiring that the creditor show "clear and convincing evidence" to hinder, delay or defraud).

[61] See 11 U.S.C. §§ 548,544(b). See e.g., Ga. Code Ann. §§18-2-7 to 10; S.D. Codified Laws §§ 54-8A-1 to 54-8A-12.

[62] See *Richard W. Nenno and Daniel S. Rubin on the Uniform Voidable Transactions Act – Are Transfers to Self-Settled Spendthrift Trusts by Settlors to Non-APT States Voidable Transfers Per Se?* Asset Protection Planning Newsletter #327.

[63] *Rush Univ. Med. Ctr. v. Sessions*, 980 N.E.2d 45 (Ill. 2012).

[64] See Nenno & Rubin, *supra* at n. 62.

[65] Special credit for the identification of cases and commentary cited in the immediately following sections is given to Nenno & Sullivan, *supra,* at n. 10.

[66] *Schreyer v. Scott*, 134 U.S. 405, 409 (1890).

[67] See *Stratton v. Edwards*, 54 N.E. 886, 887 (Mass. 1899) ("grantor …had an actual intent to contract debts, and a purpose to avoid the payment of them by the conveyance."); *Fleet Nat'l Bank v. Booth*, 2001 Mass. Super. LEXIS 94 (Super. Ct. 2001) (generally quoting *Stratton)*; *Innis v. Robertson*, 2001 Mass. Super. LEXIS 234 (Super. Ct. 2001) (similar), *aff'd*, 854 N.E.2d 105 (Mass. App. Ct. 2006), *review denied*, 856 N.E.2d 182 (Mass. 2006); *Martin v. Bajgar*, 1996 Mass. Super. LEXIS 466 (Super. Ct. 1996), *aff'd,* 701 N.E.2d 972 (Mass. App. Ct. 1998); *Shamrock, Inc. v. FDIC*, 629 N.E.2d 344, 349 (Mass. App. Ct. 1994) ("It is a perfectly usual employment of the trust device to place property in a safe harbor against the possibility of future rough financial seas."); *Coleman v. Tepel,* 230 F. 63 (3d Cir. 1916) (supports the theory that for there to be a fraud against future creditors it must be proven that the transferor corporation rendered itself insolvent to injure those creditors. Even so, retaining a reasonable degree of post-transfer solvency will avoid fraud if there is a track record over time after the transfer and prior debts were paid); *Wantulok v. Wantulok,* 214 P.2d 477 (Wyo. 1950) ("There must be definite proof that the creditors existed who were able to be defrauded"); *Klein v. Klein,* 112 N.Y.S.2d 546 (Sup. Ct. 1952) (The grantor's "hands were as clean as anyone who ever came into equity. What he did amounted to no more than insurance against a possible disaster.") See more recent cases: e.g.: *In re Mortensen*, 444 B.R. 225 (Bankr. E.D.N.Y. 2011) (Self-settled spendthrift trust set aside because grantor's expenses were more than five times his income, inferring an intent to place the property out of the reach of creditors.); *Riechers v. Riechers,* 679 N.Y.S.2d 233 (Sup. Ct. 1998) (In allocating marital assets the court noted in dictum regarding the self-settled foreign trust that, "a cause of action would not lie to set aside the trust since the trust was established for the legitimate purpose of protecting family assets for the benefit of the Riechers family members."); *Case v. Fargnoli,* 702 N.Y.S.2d 764 (Sup. Ct. 1999) (The fraudulent transfer law "requires proof that defendant had some good indication of oncoming insolvency"); *In re Earle*, 307 Bankr. 276 (Bankr. S.D. Ala. 2002) ("There was no evidence indicating that at the time the trust was created Mrs. Earle knew that she was about to incur

debt beyond her ability to pay."); *Danis v. Great American Insurance Co.,* 823 N.E.2d 59 (Ohio Ct. App. 2004), *appeal not accepted*, 824 N.E.2d 541 (Ohio 2005) (The court stated in dictum that fraud on future creditors will prevail only if settlor is seeking to evade anticipated claims.); *In re Bergman*, 293 Bankr. 580 (Bankr. W.D.N.Y. 2003) (Transfer not fraudulent because it was disclosed and business reverses were unexpected). But see, *United States v. Tingey*, 716 F.3d 1295 (10th Cir. 2013), *aff'g sub nom. United States v. Brown*, 2011 BL 261591 (D. Utah 2011) (Although omitting to issue a formal finding of fraudulent transfer, based on the facts that the taxpayer failed to pay income taxes for many years, had other financial difficulties and was indicted for financial misdealing, the court found that his motivation for transferring a vacation cabin to his brother-in-law was avoiding IRS debt, not "familial affection"). See cites at Nenno & Sullivan, *supra*, at n. 10.

[68] See Sullivan, "*Future Creditors and Fraudulent Transfers*," 22 Del. J. Corp. L. 955, 1049 (1997); Danforth, "*Rethinking the Law of Creditors' Rights in Trusts*," 53 Hastings L.J. 287, 330 (Jan. 2002); Alces, *The Law of Fraudulent Transactions* §5:85 at 5172 (2006); Fogel, "*Scylla and Charybdis Attack: Using Trusts for Medicaid Planning and Non-Medicaid Asset Protection,*" 35 ACTEC J. 45, 47 (Summer 2009). For a contrary, but dated, view, see Sterk, "*Asset Protection Trusts: Trust Law's Race to the Bottom?"* 85 Cornell L. Rev. 1035, 1045 n. 62 (May 2000). See cites at Nenno & Sullivan, *supra*, at n. 10.

[69] See Nenno & Rubin, *supra* at n. 62.

[70] See e.g., Chapter 2 of Title 18 of the Official Code of Georgia Annotated, as amended by revisions to Article 4, relating to the Uniform Voidable Transactions Act (formerly the Uniform Fraudulent Transfers Act), which adopts portions of the UVT, but rejects, in whole, Comment 8.

[71] See Fogel*, supra,* at n. 68.

[72] Author's anecdotal experience.

[73] See Michael A. Spielman & Kahn Kleinman, *Understanding Asset Protection Planning; Knowing and Qualifying Your Client,* p. 5, American Bar Association, Section of Real Property, Probate & Trust Law, 18th Annual Estate Planning Symposium, Young Lawyers Institute, Washington, D.C. (2007); David G. Shaftel,

IRS Letter Ruling Approves Estate Tax Planning Using Domestic Asset Protection Trusts: Fraudulent Transfers, The Journal of Taxation, Estates, Trusts, & Gifts, p. 7, at n. 21 (April 2010).

[74] Restatement (Second) Conflict of Laws: Introductory Note to Chapter 10, excerpted. In some states, the relevant Restatement provisions may be found in the states' trust code.

[75] See Eugene F. Scoles, *Choice of Law in Trusts*: Uniform Trust Code, Sections 107 and 403, 67 Mo. L. Rev. (2002), available at http://scholarship.law.missouri.edu/mir/vol67/iss2/3, *see* art. n. 2 & Unif. Trust Code § 107 (2000).

[76] Pub.L. 109–8, 119 Stat. 23, enacted April 20, 2005, is a legislative act that made several significant changes to the United States Bankruptcy Code.

[77] 11 USC § 541(a)(1).

[78] *Id.* § 541(b), (c)(2).

[79] *Id.* § 522.

[80] 11 USC §541(c)(2).

[81] 2 Cowans, *Bankruptcy Law and Practice* §5.9 at 86 (1998) ("Under the Code's concept of property, the inclusion definition … for practical purposes includes as an estate asset everything other than a spendthrift trust").

[82] Shaftel, *supra,* at n. 30.

[83] Shaftel, *supra,* at n. 30.

[84] Steven J. Oshins, *Steve Oshins & the Hybrid Domestic Asset Protection Trust,* LISI Asset Protection Newsletter #200 (May 10, 2012) at http://www.leimbergservices.com.

[85] Duncan E. Osborne & Mark E. Osborne, *Asset Protection Trust Planning,* The American Law Institute Continuing Legal Education with CLEW (June 2005).

[86] *Huber*, *supra,* at n. 43.

[87] Howard M. Zaritsky, *Bankruptcy Court Rejects Out-of-State Domestic Asset Protection Trusts: Trust Fails Under Two Sections of Bankruptcy Code,* Probate Practice Reporter, Vol. 25, No. 7 (July 2013).

[88] P.L. 109-8, *supra*, at n. 76.

[89] See Brown & Ahern, *2005 Bankruptcy Reform Legislation with Analysis 77* (2005).

[90] Oshins, *supra*, at n. 84.

[91] Oshins, *supra*, at n. 84.

[92] See e. g., Ga. Code Ann. §§ 53-12-4,5.

[93] Barry S. Engle, Engel Law pc, Denver, CO., http://www.barryengel.com/asset-protection-developments/is-in-re-huber-important-to-anyone-other-than-mr-huber.

[94] Huber, *supra,* at n. 43.

[95] Engel expresses concern that many courts are not experienced in trust law, which has contributed to the misapplication of § 270.

[96] In some states, de facto, the public policy claim and the Self-Settled Trust Rule merge to become the same claim.

[97] The referenced states are: Arizona, Florida, Kentucky, Maryland, Michigan, New Jersey, North Carolina, Oregon, New York, and Texas. Arizona and New Hampshire protect the assets in a supplemental needs trust from the settlor's claim. Arizona, Florida, Kentucky, Michigan and Maryland have enacted statutes clarifying that the assets of an inter vivos QTIP trust cannot be breached by the creditors of a donor spouse after the death of the donee spouse.

[98] See Adam J. Hirsch, *Fear Not the Asset Protection Trust: I. Variations on a Theme,* Cardozo Law Review, vol. 27:6, p. 2699 (January 2006).

[99] *Id*., p. 2697.

[100] *Id.*, p. 2697, 98.

[101] *Id.*, p. 2688.

[102] *Id.*

[103] See Commentary.

[104] Scott and Fratcher, *The Law of Trusts* §573, at 190 (4th ed. 1989).

[105] *Hanson, supra,* at n. 27; *Int'l Shoe, supra,* at n. 28.

[106] See e.g., S.D. Codified Laws § 29A-2-703.

[107] See e.g., Zaritsky, *supra,* at n. 87.

[108] Author comment: The Court began its *Dahl* reasoning by citing from *Waddoups* stating: "Because Utah is the forum state, Utah choice of law rules apply." The Court then stopped in place, ignoring that the *Waddoups* citation is merely a lead-in to the case's next sentence, which is the gravamen of the *Waddoups* Court's assertion: "In Utah we apply the "most significant relationship" approach, as described in the Restatement (Second) of Conflict of Laws, in determining which state's law should apply to a given circumstance." As demonstrated in the discussion of *Huber*, the application of Restatement (Second) § 270 easily could have led to a different result; however, this cannot be known because the Court's opinion did not bother to set forth the Utah versus Nevada significant relationship factors.

Citing UTAH CODE § 75-7-107 and *Jacobsen,* the Court further states: "Under Utah's choice-of-law rules, we will generally enforce a choice of law provision contained in a trust document, unless doing so would undermine a strong public policy of the State of Utah," adding the parenthetical: ("This section does not attempt to specify the strong public policies sufficient to invalidate a settlor's choice of governing law.") A reading of UTAH CODE § 75-7-107 finds no language supporting the court's assertion. To the contrary, CODE § 75-7-107 provides the legislative authority for CODE § 25-6-14, *Asset Protection Trust*, which authorizes the creation of self-settled trusts in Utah. While not directly on point, the policy intent of the Utah legislature on such trusts seems to be set forth

in subsection (3)(a) of § 25-6-14, which prohibits a trust creditor from satisfying a claim against the settlor out of transfers to the trust – hardly a strong public policy prohibition.

The utility of *Jacobsen,* cited as precedent in *Dahl,* is also questioned. In *Jacobsen*, another Utah Supreme Court case, the Court's principal finding was that the location of the plaintiff's primary place of business in Utah, by itself, created a sufficiently rational nexus for the Utah court to justify exercising local jurisdiction over the Wyoming defendants. To summarize: The Court cited *Jacobsen,* which made "nexus" issues the gravamen of its findings; then the same justices chose to ignore nexus in its *Dahl* decision just a few years later. Query why the Supreme Court cited Jacobsen, then ignored it? Apparently, the Court cited *Jacobsen* to justify its finding because Jacobsen had cited *Bremen v. Zapata Off-Shore Co,* 407 U.S.1 (1972*),* a federal case, which previously held that "a contractual (emphasis added) choice of forum clause should be held unenforceable "if enforcement would contravene a strong public policy in the forum in which suit is brought…" The *Jacobsen/Bremen* opinions appear to be nothing more than eye-wash, as there is no justification for why the same court applied "nexus" in *Jacobsen*, but not *Dahl;* and then went down a rabbit hole, ignoring the profundity of Utah law altogether and applied Federal contract law to the *Dahl* case, which involved trust law, especially since the Court was well-aware that Utah had binding conflicts of law precedent which deferred to *Restatement (Second)* § 270 on nexus matters. Moreover, the *Dahl* Court's opinion made clear it understood the important practical and legal rationales underlying the separation of contract law and trust law. Speculation about these arbitrary findings leads one to pose the question "Did the ragged history of Utah in the area of marital matters lead the Court to deliver its interpretation of equitable justice, rather than appellate law?" If so, the decision can be explained, but that does not make it precedent.

[109] See e.g., S.D. Codified Laws § 55-16-2(1) - (3).

[110] Shaftel, *supra,* at n. 30 ("For safety practitioners should adhere to a rule of thumb that no more than one-third to one-half of the client's net worth should be transferred into the trust". Author comment: There is no court precedent for this rule).

[111] *Hanson, supra,* at n. 27; *Int'l Shoe, supra,* at n. 28.

[112] See Spielman, *supra* at n. 73.

[113] See Osbornes, *supra*, at n. 85.

[114] Author's anecdotal experience.

[115] See Hirsch, *supra,* at n. 98, p. 2688.

[116] See Hirsch, *supra,* at n. 98, p. 2686.

[117] See Osbornes, *supra*, at n. 85.

[118] See, "*Delaware Asset Protection Trusts: Avoiding Fraudulent Transfers and Attorney Liability,*" 32 Estate Planning 22 (Jan. 2005); Fox & Huft, "*Asset Protection and Dynasty Trusts,"* 37 Real Prop., Prob. & Tr. J. 287, 303–07 (Summer 2002); Danforth, "*Rethinking the Law of Creditors' Rights in Trusts,"* 53 Hastings L.J. 287, 326–33 (Jan. 2002). See cites at Nenno & Sullivan, *supra,* at n 10.

[119] See Hirsch, *supra*, at n. 98, p. 2702-05.

[120] 11 USC § 548(e)(1) (allows a bankruptcy trustee to reach a self-settled trust or similar device that the settlor created within 10 years of the filing of a bankruptcy petition with actual intent to hinder, delay or defraud an existing or future creditor). See Commentary for a more detailed discussion of § 548(e)(1).

[121] See Hirsch, *supra,* at n. 98, p. 2687.

[122] See Hirsch*, supra*, at n. 98, p. 2688.

[123] Austin A. Scott, *The Law of Trusts* § 156, William F. Fratcher ed. 1987 & Supp., art. n. 2, 2A Mark L. Ascher & Margit T. Rigney eds. 2005.

[124] See Hirsch, *supra,* at n. 98, p. 2688,89.

[125] Because the Model Trust is hypothetical and there has been no case law on point, the assertion is the author's, based on legal and factual deduction; See generally, Nenno & Sullivan, *supra*, at n. 10; Shaftel, *supra,* at n. 31; Hirsch, *supra*, at n. 99.

[126] See Hirsch, *supra,* at n. 98, p. 2693.

[127] See Osbornes, *supra*, at n. 85.

[128] Ralph U. Whitten, *Full Faith and Credit for Dummies*, 38 Creighton L. Rev. at 477 (2005). See cites at Redpath, *supra* at n. 58.

[129] See Nenno & Sullivan, *supra*, at n. 10 for a discussion of public policy issues.

[130] See Gideon Rothschild, Douglas J. Blattmachr, Mitchell M. Gans, and Jonathan G. Blattmachr, *IRS Rules Self-Settled Alaska Trust Will Not be in Grantor's Estate,* Estate Planning vol.37/no.1 (Jan. 2010).

[131] See Shaftel, *IRS Letter Ruling Approves Estate Tax Planning Using Domestic Asset Protection Trusts*, 112 J. Tax'n 213 (Apr. 2010); Covey & Hastings, *"IRC Sec. 2036(a)(1); Grantor as Beneficiary of Discretionary or Ascertainable Standard Trust,"* Prac. Drafting 9953–58 (Jan. 2010); Rothschild, et al., *id*.; Blattmachr, Slade & Crawford*, Estate Planning for Persons with Less Than $5 Million*, 34 Estate Planning 18, 23 (Mar. 2007); Smith, *Careful Pre-Immigration Planning Can Save Significant Taxes,* 34 Estate Planning 30, 34–38 (Feb. 2007); Danforth, *The Role of Federalism in Administering a National System of Taxation*, 57 Tax Law. 625, 636–38, 657–58 (Spring 2004); Fox & Huft*, Asset Protection and Dynasty Trusts,* 37 Real Prop., Prob. & Tr. J. 287, 329–36 (Summer 2002). See cites at Nenno & Sullivan, *supra*, at n. 10.

[132] PLR 200944002 (July 2009); Shaftel, *id.*

[133] See Rothschild, et. al., *supra* at n. 130.

[134] See Rothschild, et. al., *supra* at n. 130.

[135] *German Est. v. U.S.*, 85-1 USTC ¶ 13,610 (Cl. Ct. 1985).

[136] See PLR 201208026 (testamentary appointment not sufficient to make gift incomplete, adding the requirement that a lifetime interest must also be retained. For more recent rulings in support, see PLR 201430003 – PLR 20143007, which allow incomplete gifts to non-grantor trusts). But see changes in New York income

and estate tax laws, effective January 2014, treating ING trusts as grantor trusts for state income tax purposes.

[137] I.R.C. § 25.2511-2(b).

[138] *Paxton Est.v. Comr.*, 86 T.C. 785 (1986); *Outwin v. Comr.*, 76 T.C. 153 (1981); *Vander Weele v. Comr.*, 27 T.C. 340 (1956), *aff'd*, 254 F.2d 895 (6th Cir. 1958); *Paolozzi v. Comr.*, 23 T.C. 182 (1954); *German Est. v. U.S.*, 85-1 USTC ¶13,610 (Cl. Ct. 1985); Rev. Rul. 2004-64, 2004-27 I.R.B. 7; Rev. Rul. 77-378, 1977-2 C.B. 347; Rev. Rul. 76-103, 1976-1 C.B. 293; PLR 200944002; TAM 199917001; PLRs 9837007, 9332006, 8037116; GCM 35112 (11/13/72). For summaries of most of these cases and rulings, see Fox & Huft, *Asset Protection and Dynasty Trusts,*" 37 Real Prop., Prob. & Tr. J. 287, 331–35 (Summer 2002). See cites at Nenno & Sullivan, *supra*, at n. 10.

[139] I.R.C. §2642(f) & §26.2632-1(c).

[140] *Id.*

[141] See King, *supra,* at n. 16.

[142] See Rothschild, et. al., *supra,* n. 130.

[143] Richard W. Nenno, *Planning with Domestic Asset Protection Trusts: Part I,* 40 Real Prop. Prob. & Tr, J. 263 at 348.

[144] Jeffrey C. O'Brien, *Ethical Considerations in Asset Protection Planning*, prepared and presented by: Mansfield, Tanick & Cohen, PA; available online (2006).