

Chicago Bar Association
Trust Law Committee
Domestic Asset Protection Trusts Subcommittee

**SUMMARY COMPARISON
OF
DOMESTIC ASSET PROTECTION TRUST LEGISLATION**

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SUMMARY COMPARISON OF DOMESTIC

ASSET PROTECTION TRUST LEGISLATION

ALASKA

- ! Assets transferred subject to a standard “spendthrift” provision to a self-settled Alaska trust, i.e., one in which the settlor retains at least some discretionary distribution interest in the income or principal (in the discretion of someone other than the settlor), are protected from the claims of creditors of the settlor even if the trust is revocable by the settlor, provided that another beneficiary who has a “substantial” interest which would be “adversely affected” by such revocation, must consent to it. Moreover, even without such required consent, the settlor may retain the right to receive discretionary distributions (in someone else’s discretion) so long as they are not required to be made to him or her. And, in the absence of such required distributions, the settlor may retain the power to veto any distributions from the trust and also retain a testamentary or similar special power of appointment effective only upon death. These retained distribution, veto and appointment rights are not deemed to make the trust revocable.
- ! The only exceptions to this sweeping asset protection for self-settled Alaska trusts are for transfers “intended” to hinder, delay or defraud creditors under Alaska’s fraudulent conveyance statute (which is different from the Uniform Act) and for transfers made at a time when the settlor is in default by 30 or more days in payments due under a court order or judgment for child support.
- ! The Alaska courts are given exclusive jurisdiction over such trusts (which must have at least one “qualified person” as a trustee and some assets in the State of Alaska subject to that trustee’s administration). Any individual resident of Alaska or any authorized trust company or bank whose principal place of business is in Alaska is a “qualified person.” And, non-qualified persons, presumably including those who are related or subordinate to the settlor, may serve as co-trustees, trust protectors or other trust advisers.
- ! Trusts not formed under Alaska law, and thus not containing an Alaska choice of law provision, may nevertheless freely change their situs to Alaska and thereby become Alaska trusts entitled to all these same creditor protections if they include a “qualified person” as a trustee, such a trustee registers the trust in Alaska, and such a trustee administers some trust assets there.
- ! The statute of limitations for any action against a claimed fraudulent transfer expires as to a creditor existing when the trust was created, within the later of four

years after the transfer or one year after it was or reasonably could have been discovered by that creditor; as to a subsequent creditor, it expires four years after the transfer.

- ! The “spendthrift” transfer restriction itself immunizes the trustee and others involved in the preparation or funding of the trust from any action for alleged conspiracy to commit a fraudulent conveyance or for aiding and abetting it. The only recourse is against the trust assets and only to the extent of the debt sought to be evaded by the fraudulent conveyance.

DELAWARE

- ! Self-settled Delaware trusts with a “spendthrift” provision are only protected from the claims of creditors of the settlor if they are irrevocable. However, in addition to the rights to veto any distributions and to exercise testamentary or similar special powers of appointment, a settlor may retain any income right, any CRUT or CRAT distribution right, any annual unitrust distribution right to five percent or less of the trust assets, any right to receive or use principal in the sole discretion of a qualified trustee or pursuant to an ascertainable standard applied by such a trustee, any use right to real property held under a QPRT, and/or the right to replace a trustee or adviser (so long as the replacement is not a related or subordinate party within the meaning of the I.R.C.) – all without making such trusts “revocable” for purposes of this statutory creditor protection. These permissible retained rights, taken together, go far beyond those permitted for the settlor of an Alaska trust subject to a similar “spendthrift” provision.

- ! However, any transfers in violation of Delaware’s fraudulent transfers statute (the Uniform Act) or adversely affecting the rights of (a) any person to whom the transferor is indebted on account of any agreement or court order for the payment of support or alimony or (b) any tort claimant with respect to an alleged tort committed prior to the transfer by the settlor or any other person for whose actions the settlor was vicariously liable, are excluded from this asset protection.

- ! As with Alaska “spendthrift” trusts, the Delaware courts are, in effect, given exclusive jurisdiction over actions affecting assets transferred to such trusts (which must, as in Alaska, have at least one “qualified trustee” located in the state with at least some assets subject to that trustee’s administration). Settlers may not be trustees or “advisers” except that they may advise as to investments.

- ! Trusts not formed under Delaware law are not automatically disqualified for the protections provided by the statute simply because they lack a Delaware choice of law provision; they are thus capable of becoming, in effect, Delaware asset protection trusts at least as to the trust assets located in Delaware.

- ! The statute of limitations for claimed fraudulent transfers is essentially the same as Alaska’s (although if an out-of-state trust is transferred to a Delaware trust in a qualified disposition, the period during which the prior trust held a transferred asset is “tacked” to the holding period of the qualified Delaware trust for this purpose, and any fraudulent transfer must be proven by “clear and convincing” evidence). However, as previously noted, transfers in derogation of family support or alimony rights or the rights of tort claimants with respect to pre-existing injuries are not protected, regardless of whether they also constitute fraudulent transfers. Thus, arguably, they may be drawn back into the settlor’s estate to

satisfy such claims against the settlor even many years later, for an indefinite period. For this reason, too, transfers to Delaware trusts may not qualify as completed gifts for transfer tax purposes.

- ! Once the statute of limitations has passed -- though not immediately as in Alaska -
- the only recourse for unauthorized dispositions not protected by the state statute is an action against the trust assets to the extent of the settlor's relevant debt, and persons involved in the preparation or funding of the trust are protected from personal liability.

RHODE ISLAND

- ! As in Delaware, after whose “qualified dispositions” statute the Rhode Island statute was modeled, self-settled Rhode Island trusts must be irrevocable and contain standard “spendthrift” restrictions on any transfers or assignments of the beneficiaries’ interests, in order to be protected from the claims of creditors of their settlors. However, unlike the array of retained beneficial interests permitted to settlors of such Delaware trusts, only veto rights over distributions, special powers of appointment exercisable at death, and distribution rights to income or principal in the sole discretion of a trustee who is neither the settlor nor a related or subordinate party are permitted to be retained by settlors of Rhode Island “qualified distributions” without jeopardizing their required irrevocability. (Apparently, even distribution rights based upon ascertainable standards applied in the discretion of such a trustee, are not permitted.)

- ! The Rhode Island statute contains the same two continuing exceptions to its protection against the claims of present or future creditors of the settlors, pertaining to support or alimony obligations or previously committed torts, as does the Delaware statute (these in addition to the general fraudulent transfer exception, which becomes time-barred after the same period(s) as Delaware’s). As just noted, these continuing exceptions may preclude any transfer to such trusts from being deemed complete for federal transfer tax purposes.

- ! Unlike the Delaware statute, however, the Rhode Island statute does not make provision for the relocation of an irrevocable out-of-state trust to Rhode Island and its subsequent subjection to the statute, is silent on the subject of non-qualifying co-trustees or any distribution or investment advisers, and does not expressly protect persons involved in the preparation or funding of the trust from personal liability even after the statute of limitations for fraudulent transfers has passed. (In Alaska, as previously noted, the only recourse at any time is against the improperly transferred assets to the extent of the particular debt sought to be avoided by the settlor, and there can be no personal liability at any time of the trustee or other persons involved in the preparation or funding of the trust.)

NEVADA

- ! The Nevada statute is distinguishable from all the others in making no exception at all to the asset protection of self-settled irrevocable spendthrift trusts other than for fraudulent transfers, for limiting actions to recover such transfers to only those transfers which were intended to hinder, delay or defraud “known creditors” of the settlor, and for imposing the following extremely short time limitations on any actions “with respect to a transfer of property to a spendthrift trust”: if the claimant was already a creditor when the transfer was made, two years after the transfer or six months after it was discovered or reasonably should have been discovered by the claimant (whichever is later); or, if the claimant became a creditor after the transfer was made, two years after the transfer.
- ! The Nevada statute also allows out-of-state banks or trust companies to act as the necessary local trustee (alone or in conjunction with others) so long as they “maintain an office in [Nevada] for the transaction of business” and administer part of the trust’s assets there.
- ! Qualified spendthrift trusts must not require that any part of the principal or income be distributed to the settlor but may allow the settlor in addition to discretionary distribution rights (determined in another’s discretion), the right to veto distributions and to exercise testamentary or similar special powers of appointment.
- ! These features, together with the lack of any requirement of specific language necessary for the creation of a spendthrift trust or a declared choice of Nevada law (thus facilitating the migration of out-of-state trusts to Nevada), would appear to make Nevada the most desirable domestic location for self-settled spendthrift trusts unless the settlor prefers fixed distribution or beneficial enjoyment rights such as are allowed by Delaware’s statute but none of the others. Of course, in the latter case, asset protection is probably not the settlor’s primary motivation in the first place.
- ! The asset protection features of a Nevada self-settled spendthrift trust, like all the other states, are enhanced to the extent that the transferred assets and the trust itself are sited in Nevada and thus entirely subject to the above-described governing law.

MISSOURI

- ! Missouri's statutory provision for spendthrift trusts could, on its face, be construed to protect self-settled spendthrift trusts where the settlor is not the sole beneficiary, retains no power to revoke or amend the trust, and retains no right to receive any specific portion of the principal or income. However, neither the state nor the federal courts have so construed this provision. Instead, it has been construed in accordance with the prevailing rule that all the assets of a trust are available to the settlor's creditors to the maximum extent that the settlor can even possibly benefit from them.

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