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MORE ON ASSET PROTECTION TRUSTS

— by Neil E. Harl*

In the April 25, 1997, issue of *Agricultural Law Digest*, we examined the asset protection trust as a device for achieving a modicum of protection from claims of creditors.¹ That concept has emerged as an off-shore trust with attention focused on a half dozen countries that have tailored their law to frustrate creditors attempting to satisfy judgments.²

A few weeks ago, The state of Alaska entered the arena with a major revision to Alaska trust law designed to lure trust assets to that state.³ Although not providing as much protection as trusts in off-shore jurisdictions, the Alaska legislation offers several notable advantages for those seeking protection from creditor action.

The Alaska statute

Under the Alaska legislation, which is effective for trusts created on or after April 1, 1997,⁴ a trust can limit transfers to creditors if the trust meets several requirements even though the grantor of the trust is also a beneficiary.⁵ Under the statute, “a person who in writing transfers property in trust may provide that the interest of a beneficiary may not be either voluntarily or involuntarily transferred before payment or delivery of the interest to the beneficiary by the trustee.”⁶ For that purpose, “property” includes real property and personal property as well as interests in real or personal property.⁷

If the trust contains a restriction on transfer, the restriction prevents a creditor existing when the trust is created, a person who subsequently becomes a creditor or another person from satisfying a claim out of the beneficiary’s interest in the trust unless— (1) the transfer was intended to hinder, delay or defraud creditors or other persons;⁸ (2) the trust specifies that the settlor of the trust may revoke or terminate all or part of the trust without the

consent of a person “who has a substantial beneficial interest in the trust and the interest would be adversely affected by the exercise of the power held by the settlor to revoke or terminate all or part of the trust;” (3) the trust requires that all or a part of the trust’s income or principal or both must be distributed to the settlor; or (4) at the time

of the transfer, the settlor is in default by 30 or more days of making a payment due under a child support judgment or order.⁹ The settlor can retain a veto power over distributions to other beneficiaries and to control disposition of the property at the settlor’s death.¹⁰ However, retention of either of those powers would cause the amount to be included in the settlor’s gross estate for federal estate tax purposes.¹¹

It is clear from the statute that the settlor could be only a discretionary beneficiary with no right to a distribution.¹²

Does Alaska law apply?

The statute itself specifies that Alaska law applies to a trust if the trust instrument states that Alaska law applies so long as— (1) some or all of the trust assets “are deposited in this state and are being administered by a ‘qualified person’;” (2) at least one trustee is a resident of Alaska or is a bank or trust company with a principal place of business in Alaska; (3) the Alaska trustee has the power to maintain the trust records, prepare income tax returns “that must be filed by the trust;” and (4) part or all of the administration of the trust occurs in Alaska, including physical maintenance of trust records in the state.¹³ The term “deposited in this state” specifically includes being held in a checking account, time deposit, certificate of deposit, brokerage account, trust company, fiduciary account, or “deposit that is located in this state.”¹⁴

Advantages of “Alaska” trust?

For those bent on frustrating attempts by creditors to reach assets in satisfaction of a judgment, a major question is whether a trust set up and maintained under the 1997 Alaska statute would have advantages over an off-shore trust.¹⁵ It would appear that Alaska trusts would offer some advantages, as noted below, but also some disadvantages as well. The advantageous aspects of “Alaska” trusts would seem to include the following—

- The 1997 Alaska statute abolishes the rule against perpetuities¹⁶ for discretionary trusts¹⁷ which adds Alaska to a list of states abolishing the ancient rule including South Dakota, Wisconsin, Delaware and Idaho.¹⁸ Specifically, the 1997 Alaska law abolishes the rule against perpetuities (which effectively limits the duration of a trust) if “the interest is in a trust and all or part of the income or principal

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of the trust may be distributed, in the discretion of the trustee, to a person who is living when the trust is created.”¹⁹ Litigation will likely be necessary to establish whether the revised Alaska rule against perpetuities applies to land located in another state. In our April 11, 1997, article,²⁰ we noted that trusts holding land are generally governed by the law of the state where the land is located.²¹

- Alaska is one of the few states with no state income tax which permits funds not distributed to accumulate free of state income tax.

- As we noted in the April 25, 1997, article on asset protection trusts,²² the cost to establish an off-shore trust can run into five figures.²³ Trusts set up under the 1997 Alaska statute should be substantially less costly to establish and administer.

Disadvantages of “Alaska” trust

Although the Alaska statute offers notable advantages, trusts established and maintained under that law fall substantially short of the off-shore trusts in protecting trust assets.

Under the new Alaska provision, the statute of limitations for a fraudulent conveyance is generally four years from the later of the date the transfer is made or one year after the transfer is or reasonably could have been discovered.²⁴ By contrast, for trusts set up in the Cook Islands, actions must be brought by the later of two years after the creditor’s cause of action accrues or one year of the transfer of the assets.²⁵

While some of the off-shore jurisdictions bidding for asset protection trusts do not recognize foreign judgments,²⁶ a judgment from another state in the United States would be enforceable in Alaska. Moreover, a bankruptcy court would be able to assert jurisdiction over an Alaska trustee.

In conclusion

The question now is whether other states will follow the lead of Alaska in establishing more of a snug harbor for

asset protection trusts than heretofore has been available in the United States.

FOOTNOTES

- ¹ Harl, “Asset Protection Trusts,” 8 *Agric. L. Dig.* 65 (1997).
- ² See generally Marty-Nelson, “Offshore Asset Protection Trusts: Having Your Cake and Eating It Too,” 47 *Rutgers L. Rev.* 11 (1994)
- ³ Alaska Stat. §§ 13.12.205, 13.36.035, 13.36.045, 13.36.34.27.050, 34.40.010, 34.40.110, added by H.B. 101, Twentieth Alaska Legislature, First Session, 1997.
- ⁴ H.B. 101, Secs. 9, 10, Twentieth Alaska Legislature, First Session, 1997.
- ⁵ Alaska Stat. § 34.40.110.
- ⁶ *Id.*
- ⁷ *Id.*
- ⁸ Alaska Stat. § 34.40.010.
- ⁹ Alaska Stat. § 34.40.110(b).
- ¹⁰ Alaska Stat. § 34.40.110(b)(2).
- ¹¹ See I.R.C. §§ 2036-2038.
- ¹² See n. 9 *supra* and accompanying text.
- ¹³ Alaska Stat. § 13.36.035(c).
- ¹⁴ Alaska Stat. § 13.36.035(c)(1).
- ¹⁵ For a discussion of the reasons for setting up an off-shore trust, see Harl, *supra* n. 1.
- ¹⁶ See Harl, “How Long for Dynasty Trusts?” 8 *Agric. L. Dig.* 57 (1997).
- ¹⁷ Alaska Stat. § 34.27.050(a)(3).
- ¹⁸ *Id.*, notes 13-17 *supra* and accompanying text.
- ¹⁹ Alaska Stat. § 34.27.050(a)(3).
- ²⁰ See n. 16 *supra*.
- ²¹ *Id.*, n. 19.
- ²² See n. 1 *supra*.
- ²³ *Id.*, ns. 17-18 *supra* and accompanying text.
- ²⁴ Alaska Stat. § 34.40.110(d)(1)(A).
- ²⁵ Harl, n. 1 *supra*, note 15.
- ²⁶ Harl, n. 1 *supra*.

CASES, REGULATIONS AND STATUTES

by Robert P. Achenbach, Jr.

ADVERSE POSSESSION

PERMISSIVE USE. The predecessors in interest to the properties owned by the parties had agreed that each could use land owned by the other that was more convenient for each to use. The disputed property in the case was used by the defendant for farming and the plaintiff used an equivalent amount of the defendant’s land for farming. The defendant sought to build a road on the disputed property and the plaintiff sought an injunction against trespass and quiet title to the disputed property. The defendant counter-claimed that the defendant owned the property either under the original agreement of the predecessors in interest or by adverse possession. The court held that the original agreement was a swap for use agreement since neither party ever claimed ownership of the exchanged properties. Therefore, the defendant’s use

of the property was permissive and no title could pass by adverse possession. **Strubberg v. Roethemeyer**, 941 S.W.2d 557 (Mo. Ct. App. 1997).

BANKRUPTCY

FEDERAL TAXATION-ALM § 13.03[7].*

AUTOMATIC STAY. The debtor had filed for Chapter 13 and included anticipated federal income tax refunds in the proposed payments of creditors. However, the IRS withheld the refund for transfer to another governmental agency in an administrative setoff. The IRS had not filed a claim in the bankruptcy case, nor had the IRS been notified about the bankruptcy case. The court held that the withholding of the refund violated the automatic stay; however, because the IRS was not aware of the bankruptcy case, the violation was not willful and