A New Direction In Estate Planning: North To Alaska

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PEAK TRUST COMPANY
Elevated Trust & Wealth Management Solutions

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Alaska has legislation similar to laws in certain foreign asset protection jurisdictions. As a consequence, an American in any state can create a trust for his or her own benefit which is protected from creditors provided, among other things, it is not a transfer intended to defraud known creditors. Perhaps of greater importance, Alaska trusts open a new dimension in estate planning. One of this article's co-authors, Jonathan Blattmachr, was the principle draftsman of this Alaska legislation.

Two goals that often are sought to be achieved in estate planning are estate tax reduction and protection of assets from claims of creditors. Reducing taxes significantly may be a "sum zero" game if the assets are attached by creditors. Similarly, protecting assets from creditors' claims may not accomplish all goals sought unless taxes also are reduced. Fortunately, these two goals are not compatible, they usually are complimentary. That is, the steps to protect assets from claims of creditors may allow tax reductio to occur, as well. On the other hand, a transfer that fails to protect property from claims of the transferor's creditors is likely to fail to reduce taxes because, almost always, if a creditor of the transferor can attach he asset the transfer is regarded as incomplete for gift and estate tax purposes. The Alaska Trust Act (Chapter No. 6, SLA 1997, effective April 2, 1997) offers a new tool in the United States to accomplish the dual goals of asset protection and tax reduction. The Act also effectively repeals the rule against perpetuities for a trust created under Alaska law. This article discusses the dual goals of asset protection and estate tax reduction and how the Alaska Trust Act can be used in the context of estate planning. It also compares some aspects of Alaska trusts with certain offshore trusts.

STEPS TO REDUCE ESTATE TAXATION

It seems well accepted that an effective, if not the most effective, estate tax reduction planning step is to make lifetime transfers. Lifetime transfers can avoid gift tax (and, by removing an asset from an estate, can avoid estate tax, as well) in ways that cannot be used at death to avoid estate taxation. However, lifetime transfers are effective for these purposes only if they are "complete" under the federal estate and gift tax rules. The law appears well established that a transfer is complete for such tax purposes only if it is not (or when it no longer is) subject to the claims of the transferor's creditors. [3]

FRAUDULENT TRANSFERS, ETC.

In general, "fraudulent conveyances" with respect to creditors whose claims arise either before or after the transfer are (a) that the debtor made with actual intent to hinder, delay or defraud his or her creditors or (b) (i) for which the debtor received less than "a reasonably equivalent value" and (ii) after which the debtor had insufficient assets to meet future business needs or to pay debts. A transfer made by a debtor is fraudulent as to a creditor whose claim arose before the transfer if the debtor made the transfer without receiving "reasonably equivalent value" and the debtor was insolvent at the time of or as a result of the transfer." Proof of actual intent to defraud is not required. Most states have adopted these rules in the form of the Uniform Fraudulent Transfer Act. However, some states (including New York) sill have in effect the Uniform Fraudulent Conveyance Act. (See N.Y. Debtor and Creditor Law Secs. 273-281.) Alaska has adopted neither the Uniform Fraudulent Transfers Act nor the Uniform Fraudulent Transfers Act nor the Uniform Fraudulent Conveyance Act. [See Summers v. Hasen, 852 P. 2d 1165 n.5 (Alaska 1993).] It's fraudulent transfer rules are contained in Alaska Statuses (AS) 34.40.010 et seq.

Similar rules are contained under the Bankruptcy Code, and in the case of bankruptcy, fraudulent conveyances may be defined with reference to the Bankruptcy Code or under applicable state law. The Bankruptcy Code permits such transfers to be set aside only if made within one year before filing of the petition, but many states permit reference to a much longer period, especially in the case of transfers to family members. [See, e.g., FDIC v. Pappadio, 606 F. Supp 631, 632 (S.D.N.Y 1985) (under New York law a claim to set aside a fraudulent conveyance is governed by a six year statute of limitations).] Avoided fraudulent conveyances are "brought back" into the debtor's estate, usually for distribution to the debtor's creditors. In addition, some fraudulent conveyances are "brought back" into the debtor's estate, usually for distribution to the debtor's creditors. In addition, some fraudulent conveyances may deprive a debtor or (1) homestead or other property exemptions and (2) a bankruptcy discharge.

As a general rule, a transfer is found to have been made with an actual intent to hinder, delay or defraud creditors only if it was intended to remove assets from claims of specifically known or anticipated creditors. "If the debtor has particular creditors in mind and is trying to remove his assets from their reach, this would be grounds to deny the [bankruptcy] discharge [on the ground of a fraudulent conveyance]. If the debtor is merely looking to his future well-being, [the conveyance would not be fraudulent and as such] the discharge will be granted."

An example will help illustrate this principle. A property owner makes a gift to a family member (whether outright or in trust) which does not result in the property owner being insolvent or unable to pay her debts as they mature. She has no known or specifically identifiable creditors. Nonetheless, she realizes that a claim against her could arise on account of unforeseen circumstances, such as being involved in a car accident, occurring in the future. This gift should not be regarded as a fraudulent conveyance, despite the fact that she is making it with the general intention to protect the property from claims that could arise against her in the future.

Although the fraudulent conveyance rules apply to creditors in bankruptcy, obviously they also have a broader application. For example, in a number of states a tort claimant is permitted to attack as fraudulent a transfer made after the time of the tort but prior to any judgement."

INTERESTS IN TRUSTS

Two sets of contrasting rules must be considered to determine whether interests in trusts are subject to claims of creditors. First, as a general rule, a beneficial interest in trust that is subject to a restriction on transfer (called a "spendthrift provision") is not subject to the claims of a beneficiary's creditors. Thus, if the debtor is a beneficiary of a trust established for his or her benefit by another person (such as by a parent) which interest by its terms and/or applicable state law is not assignable, the trust assets should be protected." However, property transferred in trust for the beneficiary may be attached by the creditors of the grantor if the transfer to the trust was a fraudulent conveyance. [11]

In virtually all states, property may be placed in trust for another and thereby be protected from the claims of most creditors of the beneficiaries (and of the grantor). The degree of "creditor proofing" usually varies depending on whether the trust gives the beneficiary the right to receive all of the income, is for the "support" of the beneficiary and/or restricts alienation of the beneficiary's interests. [12] It appears the maximum protection of trust property from the claims of the beneficiary's creditors may be achieved by placing property in a trust that gives the trustee complete discretion as to whether and when to distribute income and/or principal to the beneficiary or beneficiaries of the trust, and which also imposes spendthrift restrictions. The trustee, having control over the distributions, probably should not be one of the beneficiaries, both to secure the creditor protection and to avoid inclusion of the property in the estate of a beneficiary for tax purposes (which may be viewed as an additional form of credit protection). The beneficiary, however may participate as a trustee in investment decisions and may have a non-general power of appointment over all or part of the trust corpus. [13]

Such a trust offers major advantages to the beneficiaries. First the trust assets should be entirely protected from the claims of most creditors in bankruptcy and spousal property, and in some cases, even support claims, in the event of divorce or upon death of the beneficiary. [14] In order to maximize the creditor protection, the trustee may be given broad authority not only to distribute or accumulate income and principal, but also to purchase assets for the use of trust beneficiaries. For example, the trustee may be authorized to purchase a home for the use of the beneficiary, thereby preserving that asset in the trust protected from the claims of the beneficiary's creditors. (It seems that this use by a beneficiary should not cause any income to be imputed to the beneficiary.) The purchase of assets "inside" the trust as opposed to distributions also preserves the wealth transfer tax savings that may be achieved through the use of such a trust. Thus, the property owner can confer a substantial benefit on the chosen objects of his or her bounty by transferring during lifetime or bequeathing at death assets to such a "discretionary" trust. [15]

As noted above, however, a transfer for less than fair value [16], including a gratuitous transfer in trust for the benefit of another, may be set aside if it constitutes a fraudulent conveyance. For example, a person could not defeat an outstanding liability by transferring while insolvent all of his or her assets into a trust for the benefit of his or her spouse. Thus, in the case of lifetime planning, it is best to have created trusts and make the transfers in advance of any financial difficulties in order to successfully avoid the challenge that such transfers were fraudulent conveyances. [17]

The second general rule relates to whether and to the extent of which the grantor of the trust has a beneficial interest in it. As to a trust created for one's own benefit, the "black letter" law is that a transfer in trust for the benefit of the transferor is void as against his or her creditors, whether their claims arise before or after the transfer. [18] In other words, the general rule that has prevailed throughout the United States at least until the enactment of the Alaska Trust Act [19], has been that the assets in the trust may be claimed by the creditors of the grantor to the extent the grantor is entitled or eligible to receive assets from the trust, even if the transfer to it was not in default of creditors and even though the statute of limitations for a person to make a claim that the transfer to the trust was fraudulent has expired. [20] For example, an individual creates a trust in 1970 from which the individual is eligible, but not entitled, in the exercise of discretion of a third party as trustee, to receive distributions. A judgement is rendered against the grantor in 1997 on account of a car accident that occurred in 1996. To the extent the trustee has the capacity to make a distributions of trust property to the grantor, the judgement against the grantor could be enforced according to the Restatement (2d) Trusts against the trust assets even though the grantor had no intention of defrauding that creditor, or any other creditor, when the trust was created in 1970. On the other hand, a judgement creditor of the grantor generally may not attach the assets in a trust of which the grantor is neither eligible nor entitled to receive distributions unless the transfer was in defraud of creditors.

THE TAX RULE

The treatment of self-settled domestic trusts has been explored in a series of federal tax cases that follow from the creditors' rights analysis. Specifically, if the grantor's creditors can reach the entire corpus of such a trust, the transfer to the trust is regarded as a wholly incomplete and no gift tax is due upon creation of the trust. As a corollary, however the entire trust is included in the creator's estate under Code Sec. 2036 (a)(1).

Thus in Paolozzi v. Commissioner [21], the settlor transferred property to a trust under which the trustees had discretion to pay over the income to her during her lifetime. The Tax Court determined that under Massachusetts law, the settlor's creditors could reach the maximum amount that, under the trust terms, could be paid to the settlor- that is, the entire income interest. Accordingly, the gift was incomplete to the extent of that interest. In Outwin v. Commissioner [22], also considering Massachusetts law, the Tax Court reached the same result where the trustee could distribute income and principal to the settlor in the trustee's discretion but only with the consent of the settlor's spouse. The spouse had an income interest following the settlor's death, could receive principal in the discretion of the trustee at that time, and had a limited testamentary power of appointment. However, the Tax Court concluded that the spouse's veto power was not sufficient to distinguish the situation from Paolozzi, regardless of the fact that the spouse might be an adverse party for gift-tax purposes. [23]

More recently in Paxton v. Commissioner [24], the Tax Court held that a trust was included in the settlor's estate where the trustee had discretion to apply income and principal among a class of persons including the settlor; the trustee was the settlor's son, who also had a beneficial interest in the trust. The Tax Court looked to Washington state law, but relied primarily on the Restatement rule, discussed earlier, to support its holding. [25]

OFFSHORE TRUSTS

In the past few years, there has been considerable use of trusts created in those foreign jurisdictions that provide greater protection against claims of creditors than is available under American law. A so-called "asset protection trust" allows a grantor to protect assets from his or her creditors without requiring the settlor to relinquish all interest in the assets in the trust. In general, asset protection trusts are trusts established in foreign jurisdictions that have limited the recourse of creditors to trust assets.

The selection of the foreign jurisdiction in which the asset protection trust will be established requires great care because of the existence of the English "Statute of Elizabeth" (precursor to U.S. fraudulent conveyance law, discussed above), which makes it possible to set aside a transfer that is intended to defeat future, but currently unknown, creditors. Some offshore sites have enacted "Statute of Elizabeth override" statutes to circumvent any questions concerning the applicability of the Statute of Elizabeth. Some of the offshore sites that have passed such legislation are the Bahamas, Bermuda, the Cayman Islands, the Cook Islands (which appears to offer particularly strong protection against creditors) and Gibraltar [26]. Other concerns are political stability and the availability of adequate banking and other financial services in the chosen jurisdiction.

Asset protection trusts usually are designed so that the settlor, upon creation of the trust, will experience no tax consequences. In almost all cases, an asset protection trust will be a so-called "grantor trust" for federal income tax purposes, with the result that the creator will continue to be taxed on all the trust income in the same manner as if he or she continued to own the trust property outright. [27] In addition, the settlor typically retains certain powers or interests sufficient to render the transfer to the trust an incomplete gift, thereby avoiding gift tax and keeping the trust property within the settlor's gross estate for estate tax purposes. For example, in Private Letter Ruling 9536002 (May 12, 1995) (not precedent), the IRS ruled that a transfer to an offshore trust was incomplete because the grantors retained a limited power of appointment over the trust property.

THE NEW ALASKA TRUST LAW ELIMINATION OF THE RULE AGAINST PERPETUITIES

Under the Alaska Trust Law, an interest in a trust will not fail to be valid because it is non-vested if all or part of the income or principal of the trust may be distributed in the discretion of the trustee, to a person who is living when a trust is created. [28] As a practical matter, this means a trust can be of perpetual duration provided the Trustee has discretion to distribute trust income and principal to the beneficiaries, at least one of whom is living when the trust is created. (This might be contrasted with South Dakota law, which provides that a trust may be perpetual if the trustee is authorized to sell the trust assets and with Delaware law which has abolished the rule against perpetuities in its entirety, except with respect to real estate.) Thus, a perpetual trust now can be created under the law of Alaska which imposes no income tax. And if the trust is not a grantor trust (causing the income to be attributed directly to the grantor), state (and local) income tax can be avoided to the extent trust income is not currently distributed to beneficiaries who are tax residents of states (or localities) that impose income tax.

SPENDTHRIFT PROVISIONS

Alaska law also was amended expressly to provide that a person who transfers property in trust may direct that the interest of a beneficiary of the trust may not be either voluntarily or involuntarily transferred before payment or delivery of the property to the beneficiary by the trustee. It further provides that if the trust contains such a transfer restriction, the restriction prevents a creditor existing when the trust is created, a subsequent creditor or any other person from seeking to satisfy a claim out of the beneficiary's interest in the trust, subject to four exceptions.

First, if the settlor retains the power to revoke or terminate the trust, his or her creditors may attach the trust property to the extent of the power of revocation or termination. However, a power to revoke or terminate does not include a power to veto distributions from the trust to another beneficiary, the retention of a special testamentary power of appointment, or the right to receive a distribution of income, corpus or both in the discretion of another person, including a trustee, other than the settlor of the trust. The veto power and power of appointment may be retained by the grantor to prevent the transfer to the trust from being complete for federal gift-tax purposes. [29] By the same token, retention of such powers will cause the assets to be includable in the gross estate of the grantor at death. [30]

Second, creditors of the settlor may also attach property in the trust to the extent that the trust income and principal must be distributed to the grantor.

Third, the transfer is void with respect to creditors if at the time of the transfer to the trust the settlor was in default by 30 or more days in making a payment due under a child support judgement or order. [31]

Fourth, the transfer is subject to attachment by the settlor's creditors if the transfer was intended, in whole or in part, to hinder, delay or defraud creditors under the Alaska fraudulent transfer law. (AS 34.40.010.) However, an action to claim the transfer was fraudulent may not be commenced unless (1) if the claimant was a creditor when the trust was created, the action is brought within the later of four years after the transfer to the trust was made or one year after the trust is or could have been reasonably discovered, or (2) if the claimant becomes a creditor after the transfer, the action is commenced within four years after the transfer to the trust. [32]

The foregoing means that if the settlor is not in default by 30 or more days of making a child support payment, the transfer was not intended to defraud creditors an the grantor retains no power to revoke or terminate the trust or the mandatory right to receive income or principal but only retains the right to receive a distribution in the discretion of a trustee, creditors of the grantor cannot reach the assets contained the Alaska trust. If the grantor retains the power to veto a distribution to other beneficiaries and a special testamentary power of appointment or similar right, the transfer to the trust will not be compete for gift and estate tax purposes even though it is not subject to the claims of the grantor's creditors. On the other hand, if the grantor retains no such power to veto or power of appointment or similar right, the transfer to the trust will be complete for estate and gift tax purposes. Thus, the Act offers flexibility to integrate creditor protection with the grantor's tax and other estate planning objectives.

THE RULE FOR MAKING THE TRUST ALASKAN

Although four other jurisdictions (Delaware, South Dakota, Idaho, and Wisconsin) allow trusts to last perpetually in their jurisdictions, no statutory guidance is provided by their laws as to what connection or nexus is sufficient to cause their state's law to apply to the trust. The Alaska statue, however provides an explicit rule as to what makes a trust an Alaskan trust for both the purpose of avoiding the rule against perpetuities and the purpose of creating a trust that will not be subject to claims of the settlor's creditors. First, some of the trust assets must be deposited in the state and be administered by a "qualified person." Deposited in Alaska means held in a checking account, time deposit, certificate of deposit, brokerage account, trust company fiduciary account or other similar account located in Alaska. A "qualified person" is an Alaskan domiciliary or an Alaskan trust company or bank. Second, the Alaskan trustee's duties must at least include an obligation to maintain records for the trust (on an exclusive or nonexclusive basis with other trustees) and the obligation to prepare or arrange for the preparation of income tax returns that must be filed by the trust (again on an exclusive basis or on a nonexclusive basis with other trustees). Third, part of the administration must occur in the state.

SOME CONTRASTS TO FOREIGN ASSET PROTECTION TRUSTS

Although an American now is able to create an Alaskan trust of which he or she is a discretionary beneficiary which will be protected from the claims of his or her creditors, an Alaska trust will not provide the same level of practical protection from claims of creditors which may be afforded to a trust created in one of the offshore jurisdictions, such as the Cooks Islands or the Bahamas. The laws of such offshore jurisdiction typically have extremely short statutes of limitations before the period to commence an action claiming the transfer to the trust was fraudulent runs which, as a practical matter, cannot be met by a creditor especially if the trust is created and funded sufficiently in advance of the entry of a final judgment against the debtor in an American court. [33] Second, the jurisdiction may prohibit the enforcement of American judgments. That means the action must be retried in the offshore jurisdiction. As a practical matter, that may well be impossible. Because Alaska is one of the American states, its courts will be required to give full faith and credit to any judgement of a sister state although, as indicated, a judgement against the debtor will not be enforceable against the Alaska trust unless there is a finding that the transfer to the trust was a fraudulent transfer or some other reason for voiding the trust, such as a the grantor having been in default by 30 or more days in child support payments at the time the trust was created. Third, at least some of these offshore jurisdictions explicitly exclude some claimants from contending a transfer was fraudulent. For instance, in some cases, a claim founded on a domestic right (such as an equitable distribution claim to property in the event of a divorce) cannot be brought against a trust situated in that jurisdiction.

In some ways, however a foreign asset protection trust may be less desirable than an Alaska trust. Obviously, there is greater political risk in these offshore jurisdictions than there is in the United States. In addition, new "anti-foreign trust" provisions added to the Internal Revenue Code (see, e.g., Code Sec. 6048) will not apply to an Alaska trust. Also, it may be that a court would be more prone to view the creation of a foreign asset protection trust as an attempt to remove or secrete assets than it would the creation of an Alaska trust. In a recent bankruptcy court case, the court expressed considerable hostility to the creation of an offshore trust and ultimately applied New York law to determine whether the debtor had retained a property interest in the rust (which was established under Jersey law) for purposes of determining whether he should be denied a discharge in bankruptcy. [34] It appears, however that this case may have turned on the rather extraordinary facts, which the court apparently perceived as involving a course of deception and concealment of assets by the debtor.

OPTIONS UNDER THE ALASKA TRUST ACT

A significant obstacle to the making of lifetime transfers is that the property owner is then cut off from the property. For example, some persons are willing to make a gift, and anticipate that they will be comfortable without the gifted asset and/or the income therefrom under the most likely scenarios, but are concerned about a "disaster" situation in which they might need access to the funds. They may not be at all concerned about protecting assets from creditors. In such a case, an offshore trust may be appropriate to consider. Precisely because the normal U.S. rule permitting creditors to reach the trust does not apply, the fact that the grantor is a permissible beneficiary of trust income and/or principal in the discretion of an independent trustee should not render the gift incomplete and includable in the estate under Code Sec. 2036 or 2038. Thus, the trust can be structured so that the transfer is a completed gift upon creation. [35] Gift tax would be paid (or unified credit applied). In that way, the "normal" estate planning benefits of removing gifted assets and the appreciation theron from the estate are achieved. However, the Trustee can give the settlor access to the trust assets.

These same opportunities are now available to Americans using Alaska trusts. For example, an individual could create a so-called "Crummey trust" [36] in Alaska for the benefit of himself or herself as well as members of his or her family and protect transfers to the trust from gift tax using annual exclusions with respect to the other family members. For instance, a woman who is married and has two children could transfer up to $50,000 under the protection of the annual exclusion under Code Sec. 2503(c) granting her husband and each child the right, respectively, to withdraw $10,000 and $20,000 from the trust. The transfers to such a trust created under Alaska law would be complete and should be excludable from the grantor's estate at death even though the grantor is eligible although not entitled, to receive distributions from the trust in the discretion of a trustee other than himself or herself. Of course, the beneficiaries may exercise the powers of withdrawal so that there is no property left in the trust from which the grantor could benefit. In addition, to the extent that the powers of withdrawal have not lapsed tax- free pursuant to Code Sec. 2514(e) and 2041(b)(2), the property subject to the powers of withdrawal will be includable under Code Sec. 2041(a) in the gross estates of the powerholders.

An individual also could create an Alaska trust and transfer the amount of his or her remaining gift tax exemption equivalent (which can be as great as $600,000) and remain a beneficiary eligible to receive distributions in the discretion of a trustee other than himself or herself and avoid having the property includible in his or her estate. This provides an opportunity to remove the income and appreciation earned on the property during the balance of his or her lifetime from his or her gross estate even though the grantor has retained the possibility of receiving assets back in the discretion of the trustee if appropriate circumstances arise. Similarly, an individual could make a transfer, which is complete for estate and gift tax purposes, to an Alaska trust, of which he or she is eligible to receive distributions, equal to his or her remaining GST exemption under Code Sec. 2631(a) which can be as great $1 million. This would allow the amount protected from generationskipping transfer tax to increase by post-transfer income and appreciation during the balance of the transferor's lifetime even though the grantor is an eligible beneficiary of the trust.

The entitlement to payments from a grantor retained annuity trust (GRAT) described in Code Sec. 2702(b)(1) or grantor retained unitrust (GRUT) described in Code Sec. 2702(b)(2) must terminate prior to the death of the grantor or the trust assets will be includable, in whole or in part, in the grantor's estate. [37] However, if the GRAT or GRUT is created under Alaska law, the property may continue in trust after the grantor's annuity or unitrust term ends, and the grantor thereafter could be eligible to receive distributions from the trust without causing the trust to be includable in his or her estate, provided the grantor survives the annuity or unitrust term.

CONCLUSIONS

The dual goals of asset protection and reduction in taxation are often compatible and complementary. The new Alaska Trust Act provides an opportunity for Americans in all states to create trusts in Alaska which may help achieve both goals. Although not providing all of the practical protection that may be available through similar trusts created in offshore jurisdictions, many Americans will prefer for their assets to remain in the United States. For them, Alaska trusts may be considered. Although not discussed in detail in this article, making the trust perpetual may offer additional financial tax and estate planning benefits.

ENDNOTES

1. See e.g., Paolozzi v. Commissioner, 22 T.C. 182 (1954)

2. Compare Reg. Sec. 25.2511-2(c) with Code Sec. 2038(a).

3. "If and when the grantor's dominion and control of the trust assets ceases, such as by the trustee's decision to move the situs of the trust to a state where the grantor's creditors cannot reach the trust assets, then the gift is complete for Federal gift tax purposes..." Rev.Rul 76-103, 1976-1 CM 293. See generally, Kartiganer, Rollins, & Piontnica, "Completed Gifts to Offshore Trusts and the Three-Year Rule," Journal of Asset Protection (March/April 1996).

4. See generally, P. Alces, The Law of Fraudulent Conveyance, Sec. 504 (1989) (1992 Cum. Supp. No. 2)

5. See, e.g., Tex. Prop. Code Sec. 42.004(a) (under Texas law, a debtor who acquires otherwise exempt personal property with intent to hinder, delay or defraud creditors loses the personal property exemption- however, that is not the case with the Texas homestead exemption, although a bankruptcy discharge may be denied). Anderson Mill & Lumber Co. v. Clements, 134 So. 588, 592 (Fla. 1931); (under Florida law, debtor who acquires otherwise exempt homestead property with intent to hinder, delay or defraud creditors loses homestead exemption).

6. See, e.g., Bankruptcy Code Sec. 727 (a)(2): In re Reed, 700 F. 2d 986, 988 (5th Cir. 1983) ("a debtor who converts nonexempt assets to an exempt homestead immediately before bankruptcy, with intent to defraud his creditors, must be denied a discharge in bankruptcy because of the provisions of Section 727 of the Bankruptcy Code"): In re Myerson & Kubn, 121 B.R. 145, 158-159 & n.15 (Bkrcty. S.D.N.Y. 1990)

7. Oberst v. Oberst, 91 B.R. 97, 101 (Bkrtcy, C.D. California 1988). See, also Klein v. Klein et al., 122 NYS 2nd 546 (1952) (similar)

8. See Myers v. Redmill, 266 Ala. 270. 96 So. 2d 450 (1957) Conveyance to wife two days after automobile accident), and cases cited in annot., 73 A.L.R.2d 749. See, also, annot., 38. A.L.R. 3d 597

9. Such an interest would normally be excluded from a beneficiary's bankruptcy estate as well. See Bankruptcy Code Sec. 541(c)(1) and (2). In re Remington, 15 BR 496 (Bankr. DNJ 1981) (in bankruptcy proceeding of New Jersey resident, both income and principal of trust created for his benefit by relative who resided in Pennsylvania protected under Pennsylvania law spendthrift provision was effective to provide that protection)

10. In some states, trusts are "spendthrift" only to the extent so provided in the governing instrument. In other states, they are "automatically" spendthrift unless the governing instrument provides otherwise. In still others, they may not be "spendthrift" at all (i.e they are subject to creditor claims regardless of spendthrift provisions in the instruments). See, e.g., Industrial Nat'l Bank v. Budlong, 106 RI 780, 264 A2d 18 (1970).

11. See e.g. NY Debtor and Creditor Law, Secs. 278 and 279

12. See e.g., Scott, 11A The Law of Trusts, Secs. 152, 155-157.1 (4th ed. 1987); Restatement (2d) Trusts, Secs. 155 and 157; Cal. Prob. Code Ann. Secs. 15400-15307.

13. See Code Sec. 2041

14. See Converstan v. Kellogg, 136 Mich. App. 504, 357 N.W. 2d 705 (Mich. App. 1984); Scott, supra, Sec 157.1

15. See Oshins & Blattmachr, "The Megatrust: An Ideal Family Wealth Preservation Tool", Trusts & Estates 20 (November 1991).

16. It is not always clear whether a transfer is for fair value for this purpose. The analysis will depend on applicable law and the facts of the case.

17. See Oberst v. Oberst, 91 B.R. 97 (Bkrtcy, C.D. Cal. 1988).

18 See e.g., Restatement (2d) Trusts, Sec. 156.2.

19. Although apparently not widely known a rule somewhat similar to that in Alaska is contained in Missouri Revised Statute Sec. 456.080.

20. However, it seems that not every retained interest will trigger the application of this rule. For example, a power to direct investments probably is not attachable by the grantor's creditors. A related issue is whether creditors can reach the assets of a trust over which the settlor retained a power of revocation (or a general power of appointment), and whether creditors can reach the assets of such a trust to satisfy the debts of the settlor/ decedent. It appears that the trend is to allow assets in such a trust to be used to satisfy the debts of the settlor/ decedent and toward extending the recourse of creditors (including creditors of a decedent) against such trusts in some cases by statute. See, e.g., Cal Prob Code Ann Secs 18200 and 18201; State Street Bank & Trust Co. v. Reiser 389 N.E.2d 768 (Mass. App. 1979).

ENDNOTES

21. 22 T.C. 182 (1954). See, also, Rev Rul. 77-378, 1972-2 CB 347; Rev. Rul 76-103, 1976-1 CB 394.

22. 76 T.C. 153 (1981), acq. 1981-2 C.B. 1.

23. See comm'r v. Vande Wheele, 254 D2d 895 (6th Cir. 1958), acq. 1962-1 CB 7 (same result under Michigan Law); PLR 83 50004 (same result under California law). Neither a private letter ruling (PLR) nor a national office technical advice memorandum may be cited or used as a precedent. Code Sec. 6110(j).

24. 86 T.C. 785 (1986).

25. See, however Estate of German v. United States, 85-1 TC 13,610 (Ct. Cl. 1985) and Herzog v. Comm'r, 116 F. 2d 591 (2d Cir. 1941), finding that creditors could not reach assets of a trust of which the settlor was one of several discretionary beneficiaries (or found that the Internal Revenue Service had failed to meet its burden to show that settlor's creditors could reach the asset held in the trust.) However, the conclusion reached by the Federal courts in these cases may not be the same as those reached by state courts. Compare Vanderbilt Credit Corp v. Chase Manhattan Bank, N.A., 100 AD2d 544, 473 NYS 2d 242 (2d Dep't 1984) with Herzog v. Comm'r, supra.

26. In general, it appears that asset protection trusts will be effective only against future, but currently unknown, creditors. The settlor generally, cannot be insolvent at the time the trust is created or become insolvent as a result of the creation of the trust.

27. See Code Sec. 677(a) (a trust is a grantor trust if, among other situations, the trustee, without the consent of an "adverse party" can distribute the trust assets to the grantor.) There will be no Code Sec. 1491 excise tax consequences since no tax will apply to the transfer of appreciated assets to a foreign trust so long as that trust is a "grantor trust" and the settlor is a U.S. person. Rev Rui. 87-61, 1987-1 CB 219.

28. AS 34.27.050(a)

29. Reg. Sec. 25.2511-1(c)

30. Code Sec. 2036(a)(2),2038(a).

31. An Alaska trust could not be used to avoid child support or alimony payments because neither a judgement for child support nor one for alimony is dischargeable in bankruptcy. Bankruptcy Code Sec. 523(a)(5)

32. It is possible that a court would determine that the statute of limitations of the grantor's domicile state (or another state) should be applied rather than the one provided under the new Alaska law. This could mean a shorter, longer, or "different statute of limitations. However, the determination that the trust is "spendthrift" under Alaska law should apply even if the grantor is domiciled elsewhere. See 4 Colier on Bankruptcy, 544.02 at 544-13 to 544-14 and fn. 17 (15th ed. 1989(("The tendency of the courts is to treat the law of the site of property at the commencement of the case as governing to the extent that Sec. 544(a) refers to non-bankruptcy, 70.26 at 364-365 (14th ed.) ("Whether the bankrupt's interest as a cestui que trust was, at the time of a bankruptcy, assignable or transferable, or subject to attachment, seizure or judicial sale, is a matter generally to be determined by, the law of the state where the trust has its situs." [footnote omitted]); Ferari v. Barclays Business Credit, Inc. 108 B.R. 384, 387 (D. Mass. 1989) ("The authorities.. Have shown a preference for applying the law of the site of the conveyed property); In re Remington, supra (applying Pennsylvania law). But cf. In re Portnoy, infra (alleged concealment of assets of offshore trust as grounds for denial of discharge in bankruptcy).

33. But, see 515 S. Orange Grove Owners Ass'n v. Orange Grove partners, Plaint No. 208/94 (High Ct. Raratonga, Civil Div., Nov. 6, 1995)

34. In re Larry Portnoy, 201 B.R. 685, 695 (S.D.N.Y. 1996).

35. See, e.g., PLR 9332006 (not precedent) (transfer to offshore trust of which grantor and members of grantor's family are eligible beneficiaries a completed gift and will not be in grantor's estate because under the law governing the trust creditors of the grantor cannot attach the trust assets).

36. See, generally, Blattmachr & Slade, "Building an Effective Life Insurance Trust" Trusts and Estates 29 (May 1990) explaining how to structure such a trust to hold insurance policies on the grantor's life. Crummey trusts can hold other assets as well. It seems that the life insurance proceeds should not be includable in the grantor's estate under Code Sec. 2042 if the grantor is merely an eligible beneficiary of the trust which is not subject to the claims of his or her creditors, because the incidents of ownership (which is the "touchstone" for application of Code Sec. 2042) held by a trust are not automatically attributed to the beneficiary whose life is insured. See, e.g., PLR 9434028 (not precedent).

37. The Internal Revenue Service has contended that a GRAT is includible in its entirety under Code Sec. 2039 (a) if the grantor dies during the term for which he or she is entitled to annuity payments. See PLR 9345035 (not precedent).