

**ALASKA STATE LEGISLATURE
SENATE JUDICIARY STANDING COMMITTEE**

April 4, 2013

2:37 p.m.

MEMBERS PRESENT

Senator John Coghill, Chair
Senator Lesil McGuire, Vice Chair
Senator Fred Dyson
Senator Donald Olson
Senator Bill Wielechowski

MEMBERS ABSENT

All members present

COMMITTEE CALENDAR

SENATE BILL NO. 65

"An Act relating to property exemptions for retirement plans, individual retirement amending Rule 64, Alaska Rules of Civil Procedure, and Rule 301(a), Alaska Rules of accounts, and Roth IRAs; relating to transfers of individual retirement plans; relating to Evidence." the rights of judgment creditors of members of limited liability companies and partners of limited liability partnerships; relating to the Uniform Probate Code, including pleadings, orders, liability, and notices under the Uniform Probate Code and the Alaska Principal and Income Act, the appointment of trust property, the Alaska Uniform Prudent Investor Act, co-trustees, trust protectors, and trust advisors; relating to the Alaska Principal and Income Act; relating to the Alaska Uniform Transfers to Minors Act; relating to the disposition of human remains; relating to the tax on insurers for life insurance policies; relating to insurable interests for certain insurance policies; relating to restrictions on transfers of trust interests; relating to discretionary interests in irrevocable trusts; relating to the community property of married persons; and

- HEARD & HELD

PREVIOUS COMMITTEE ACTION

BILL: SB 65

SHORT TITLE: RETIREMENT PLANS; ROTH IRAS; PROBATE

SPONSOR(S): SENATOR(S) COGHILL

02/27/13 (S) READ THE FIRST TIME - REFERRALS
02/27/13 (S) L&C, JUD
03/21/13 (S) L&C AT 1:30 PM BELTZ 105 (TSBldg)
03/21/13 (S) Heard & Held
03/21/13 (S) MINUTE(L&C)
03/26/13 (S) L&C AT 1:30 PM BELTZ 105 (TSBldg)
03/26/13 (S) Moved CSSB 65(L&C) Out of Committee
03/26/13 (S) MINUTE(L&C)
03/27/13 (S) L&C RPT CS 2DP 2NR SAME TITLE
03/27/13 (S) DP: DUNLEAVY, ELLIS
03/27/13 (S) NR: OLSON, MICCICHE
04/01/13 (S) JUD AT 1:30 PM BELTZ 105 (TSBldg)
04/01/13 (S) Heard & Held
04/01/13 (S) MINUTE(JUD)
04/03/13 (S) JUD AT 1:30 PM BELTZ 105 (TSBldg)
04/03/13 (S) Heard & Held
04/03/13 (S) MINUTE(JUD)
04/04/13 (S) JUD AT 2:30 PM BELTZ 105 (TSBldg)

WITNESS REGISTER

BETH CHAPMAN, Attorney
Juneau, AK

POSITION STATEMENT: Provided a sectional analysis of SB 65.

DAVID SHAFTEL, Attorney
Anchorage, AK

POSITION STATEMENT: Provided a sectional analysis of SB 65.

ACTION NARRATIVE

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CHAIR JOHN COGHILL called the Senate Judiciary Standing Committee meeting to order at 2:37 p.m. Present at the call to order were Senators McGuire, Dyson, Wielechowski, and Chair Coghill.

SB 65-RETIREMENT PLANS; ROTH IRAS; PROBATE

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CHAIR COGHILL announced the consideration of SB 65. [Version 0 was before the committee.]

SENATOR OLSON joined the committee.

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BETH CHAPMAN, Attorney, stated that she practices in the area of estate planning and has an office in Juneau. She explained that she would discuss the bill sections according to subject matter.

CHAIR COGHILL noted that David Shaftel and Douglas Blattmachr were available on-line to add to the discussion.

MS. CHAPMAN provided the following sectional analysis:

Sections 6 and 7, relate to representation for settlement agreements. Section 6 amends AS 13.06.120. It is the provision that is used for giving notice in probates and estate matters. It removes the reference to judicially supervised settlements in any non-judicial proceedings. This was done to clarify what notice proceedings this applies to. Section 7 adds a new subsection (b) to provide definitions. Paragraph (1) defines "order" to mean a judicial order or nonjudicial order. Paragraph (2) adds to the definition of "proceeding" to include nonjudicial proceedings, and the settlement of accounts under any procedure authorized under the probate code. This was done to ensure that all nonjudicial proceedings are covered under the notice provision.

Section 8 relates to the duties of trustees and co-trustees. This clarifies current practice, which is that duties can be granted to different trustees to oversee distributions of a trust and to manage the investments of a trust.

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SENATOR WIELECHOWSKI referenced page 8, lines 3-4. He asked if this completely exonerates excluded trustees from any obligation to review, inquire, investigate, or make recommendations.

MS. CHAPMAN said that's correct, and that is consistent with current statute. A co-trustee that has been delegated one power is not responsible for the actions of another co-trustee because they have no authority.

SENATOR WIELECHOWSKI asked if an excluded trustee would have any responsibilities.

MS. CHAPMAN replied that they have the responsibilities that were delegated to them. They would not be exonerated for any action that falls within their powers.

SENATOR WIELECHOWSKI asked if a co-trustee would be excluded from any obligation if he/she knew of fraud that was occurring.

MS. CHAPMAN offered her belief that the co-trustee would be held liable because not disclosing the fraud would be a breach of their overall fiduciary duty to the beneficiaries.

SENATOR WIELECHOWSKI observed that the language is extremely broad and appears to completely exonerate an excluded trustee.

CHAIR COGHILL said his understanding is that it's directly related to an authority that is assigned to the trustee.

MS. CHAPMAN agreed; it is intended to say that if one trustee has the sole discretion to invest trust assets and one trustee has the sole discretion to make distributions, the distributions trustee does not have an obligation to review what the investment trustee is doing.

CHAIR COGHILL asked Mr. Shaftel if he had anything to add.

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DAVID SHAFTEL, Attorney, Anchorage, Alaska, agreed with Ms. Chapman's analysis. These types of statutes have been enacted in a variety of states and are designed to protect one trustee from another trustee's negligence, not fraud.

MS. CHAPMAN continued the sectional analysis.

Sections 9 through 11 relate to decanting, which is the ability of a trustee to make changes to the terms of a trust that are in the best interests of the beneficiary. Alaska was the second state in the country to adopt this type of provision, but the statute lacks guidance to trustees on how to use this power. These changes are based on the revisions to the New York statute, which Alaska modeled initially. The purpose of the decanting statute is to allow a trustee to modify a trust to correct errors and to adjust to changed circumstances and laws. A trustee can make modifications based on the authority he/she has and in the best interest of the beneficiary. For example, a trustee with unlimited authority to make distributions could put the funds into a new trust and continue the terms of the trust. This is useful for minors or individuals who have special needs. A trustee who has a limited power to distribute also has limited authority to make changes. A beneficiary may object to the exercise for a certain period of time. Restrictions also exist to protect mandatory distribution rights, tax benefits, and to prohibit the trustee from increasing their compensation or decreasing their liability.

Section 14 relates to the appointment of individuals who will help oversee a trust. Current statute allows the appointment of a trust protector and requires that person to be a disinterested non-family member. Appointing a disinterested third party is no longer consistent with trust practices and that provision was removed. Allowing family members to be appointed further protects the beneficiary.

Section 15 adds a new provision regarding trust advisors. If the terms of a trust designate the trustee to follow the direction of a non-trustee advisor, the advisor may be held financially liable to the beneficiary for the actions the advisor directs the trustee to take. This change further protects the beneficiary as well as the directed trustee.

Sections 33 through 35 amend the Uniform Transfers to Minors Act. The Act allows the transfer of assets to an account for the benefit of a minor. The account custodian may make distributions for the benefit of the minor. Under the current statutes, the custodianship ends when the minor reaches age 18 and the minor is entitled to the assets. The amendment provides an opportunity for the custodian to extend the time in which the custodianship account will stay in place. The minor must be given notice of the extension and they have the right to object. If the minor does not object, the custodianship will continue and be managed for their sole benefit.

SENATOR WIELECHOWSKI asked if the minor must be notified six months before their 18th birthday.

MS. CHAPMAN agreed it is a six month notice period.

Section 36 relates to the adoption of the Disposition of Human Remains Act. The purpose is to allow decedents to leave legally binding directions regarding the disposition of their remains, and to designate an agent to see that their wishes are followed. If a person has not provided directions, then a priority list is provided of the persons who may control the disposition of the decedent's remains. A statutory form is provided so the assistance of an attorney is not necessary.

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SENATOR WIELECHOWSKI asked if this would change the legislation he introduced and that passed several years ago regarding disposition of remains for military members.

MS. CHAPMAN said no. The disposition of the remains of members of the organized militia under AS 26.05.262, the armed forces under AS 26.10.065(a), and the United States Coast Guard under AS 26.10.065(b) are exempt from the provisions in AS 13.75.

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MR. SHAFTEL continued the sectional analysis.

Sections 1 through 3 provide asset protection for inherited interests in retirement plans. These amendments conform Alaska law to the majority case rule that has been developed in bankruptcy courts in a number of states. Arizona, Florida, and Texas have enacted similar provisions.

Sections 4 and 5 clarify that a creditor's exclusive remedy against an interest in a limited liability company is a charging order against the interest, and other legal or equitable remedies are not available. These protections apply for multiple member entities and single member entities.

Sections 12 and 13 relate to placing an insurance policy in a trust. When a settlor selects an insurance policy and names a friend as a trustee, they generally don't want to burden the friend with the obligation of monitoring the insurance company for solvency and appropriate investment practices. This amendment insulates the trustee from liability associated with those insurance policies.

Sections 16 through 32 contain amendments to the 2003 Uniform Principal and Income Act that reflect the final regulations that the Internal Revenue Service issued regarding unitrusts. A trustee is allowed to choose a unitrust rate of three to five percent rather than be limited to the four percent amount in current law. There is also an explicit definition of "income" for a trust drafted as a unitrust. It provides for the ordering of distributions among types of income and principle. A smoothing period of up to five years is allowed to determine what assets will be used when applying the unitrust percentage.

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SENATOR WIELECHOWSKI asked for a definition of unitrust.

MR. SHAFTEL explained that a unitrust is a trust that distributes a fixed percentage of the value of the trust assets on an annual or more frequent basis.

Section 37 amends the insurable interest statute for life insurance contracts. This clarifies that a trustee of a life insurance trust who is holding the policy for the benefit of members of the person who set up the trust is an insurable interest.

Section 38 is a companion provision to the LLC provision discussed in Sections 4 and 5.

SENATOR WIELECHOWSKI inquired if employers in Alaska are prohibited from buying insurance policies on their employees and naming themselves as beneficiaries.

MR. SHAFTEL said his understanding is that Alaska law does not allow that.

Section 39 eliminates deadwood provisions.

Section 40 shortens the statute of limitation on creditor claims from four years to two years. This is consistent with a nationwide trend.

SENATOR WIELECHOWSKI questioned the public policy rationale for limiting the statute of limitations.

MR. SHAFTEL said it's a policy call, but it's consistent with what appears to be the modern trend.

CHAIR COGHILL asked if the four year limitation had been challenged.

MR. SHAFTEL said no, although actions have been brought for fraudulent transfers.

SENATOR WIELECHOWSKI asked if he would have six months to file a cause of action or claim for relief if he discovered a fraudulent transfer three years after it occurred.

MR. SHAFTEL agreed.

SENATOR WIELECHOWSKI asked if a judge or a jury would make the decision that the person could have reasonably known.

MR. SHAFTEL explained that questions of fact are jury decisions, otherwise it's a judge decision.

Section 41 codifies the common law protection that a creditor of the beneficiary cannot compel distributions from the trust. This section also allows the transfer of an IRS interest to a trust.

SENATOR WIELECHOWSKI asked if this new section of law was Sec. 34.40.118 on page 39, lines 21-30.

MR. SHAFTEL agreed.

SENATOR WIELECHOWSKI observed that this provision essentially allows people to skirt the inheritance tax.

MR. SHAFTEL disagreed. He pointed out that the law now allows an individual to transfer up to \$5 million to a trust, and transferring the IRA interest would use up a portion of that exempt amount, depending on the value of the IRA. Current law doesn't affirmatively allow an individual to transfer an IRA interest to a trust and estate planners have been cautious and haven't done it. This isn't a matter of federal law, and this just clarifies that there is the option in state law.

SENATOR WIELECHOWSKI asked if a 20 year old beneficiary would incur tax consequences if he/she took a distribution from the IRA that was put in the trust.

MR. SHAFTEL stated that this does not change the income tax consequences with respect to that IRA. The advantage of placing an IRA into a grantor trust is that the growth of the asset would not be subject to estate tax. This is already allowed with other assets.

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Sections 42 through 46 amend Alaska's the optional community property provision that was enacted in 1998. This provision provides an attractive income tax benefit when the first spouse dies, because there's an adjustment to the fair market value of the basis of the assets of both halves of the estate. The amendment clarifies that a community property trust is one way to opt into Alaska's community property system. It eliminates confusing language about statute of limitations. It clarifies that property that spouses agree is community property is owned as such regardless of the way that it is titled. It also enacts remedies for improper transfers and limitation periods within which those remedies must be pursued.

Sections 47 through 50 are technical provisions regarding repealed sections, indirect rule change, applicability and the requirement for two-thirds majority vote of each house.

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SENATOR WIELECHOWSKI expressed appreciation for the time spent on the explanation.

CHAIR COGHILL stated he would hold SB 65 in committee and take action at the next meeting.

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There being no further business to come before the committee, Chair Coghill adjourned the Senate Judiciary Standing Committee meeting at 3:25 p.m.