

ALASKA STATE LEGISLATURE
SENATE JUDICIARY STANDING COMMITTEE

February 28, 2020

1:32 p.m.

MEMBERS PRESENT

Senator John Coghill, Chair
Senator Peter Micciche, Vice Chair
Senator Shelley Hughes
Senator Jesse Kiehl

MEMBERS ABSENT

Senator Lora Reinbold

COMMITTEE CALENDAR

SENATE BILL NO. 191

"An Act relating to trusts and trustees, including trust division, the powers of trustees, delayed gifts to trusts, and community property trusts; and providing for an effective date."

- HEARD & HELD

SENATE BILL NO. 192

"An Act relating to fiduciary discretion and the allocation of capital gains to income under the Alaska Principal and Income Act."

- SCHEDULED BUT NOT HEARD

PREVIOUS COMMITTEE ACTION

BILL: SB 191

SHORT TITLE: TRUSTS, TRUSTEES, COMMUNITY PROPERTY

SPONSOR(s): SENATOR(s) COGHILL

02/14/20	(S)	READ THE FIRST TIME - REFERRALS
02/14/20	(S)	JUD
02/26/20	(S)	JUD AT 1:30 PM BELTZ 105 (TSBldg)
02/26/20	(S)	Heard & Held
02/26/20	(S)	MINUTE(JUD)
02/28/20	(S)	JUD AT 1:30 PM BELTZ 105 (TSBldg)

WITNESS REGISTER

MATTHEW BLATTMACHR, President & CEO
Peak Trust Company; President
Alaska Trust & Estate Professionals
Anchorage, Alaska

POSITION STATEMENT: Answered questions during the hearing on SB 191.

AIMEE BUSHNELL, Staff
Senator John Coghill
Alaska State Legislature
Juneau, Alaska

POSITION STATEMENT: Presented a white paper and answered questions during the hearing on SB 191.

ABIGAIL O'CONNOR, Attorney
O'Connor Law, LLC; Vice President
Alaska Trust & Estate Professionals
Anchorage, Alaska

POSITION STATEMENT: Answered questions during the hearing on SB 191.

JAMIE DELMAN, Attorney
Shaftel Delman LLC
Anchorage, Alaska

POSITION STATEMENT: Answered questions during the hearing on SB 191.

ACTION NARRATIVE

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CHAIR JOHN COGHILL called the Senate Judiciary Standing Committee meeting to order at 1:32 p.m. Present at the call to order were Senators Hughes, Micciche, Kiehl and Chair Coghill.

SB 191-TRUSTS, TRUSTEES, COMMUNITY PROPERTY

[1:33:37 PM](#)

CHAIR COGHILL announced the consideration of SENATE BILL NO. 191, "An Act relating to trusts and trustees, including trust division, the powers of trustees, delayed gifts to trusts, and community property trusts; and providing for an effective date."

CHAIR COGHILL said the agenda for this hearing is to respond to the questions that arose at the last hearing, starting with Ms. Bushnell who will review a white paper.

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AIMEE BUSHNELL, Staff, Senator John Coghill, Alaska State Legislature, Juneau, Alaska, explained that the white paper the Chair mentioned relates to Alaska Gift Trusts. It was prepared by the Alaska Trust and Estate Professionals (ATEP), a nonprofit organization that works to present a unified voice for many trust and estate professionals in Alaska. The white paper starts with an explanation that the transfer tax system is completely separate from income taxes since these gifts happen after the money has been earned and taxed.

The gift and estate tax exemptions are unified. Currently, the exemption is \$11,580,000 per individual, and the tax rate on gifts or inheritances that exceed \$11,580,000 is 40 percent. This is historically high. In 1995, the exemption limit was at \$600,000 and anything that exceeded that figure was taxed at 55 percent. In 1976, the allowable estate tax exemption was \$60,000 and everything beyond that was taxed at 77 percent. On January 1, 2026, the estate tax exemption will be reduced to \$5,000,000, indexed for inflation. Federal legislation has been introduced to reduce the exemption further to \$3,500,000 or less. The exemptions on estate taxes could also be reduced by a new administration in Washington, D.C.

MS. BUSHNELL said that under SB 191, families who expect to be affected by the estate tax can take advantage of this exemption now, to save their children and grandchildren estate taxes in the future. Saving estate tax can help preserve family owned businesses and ensure that one generation's wealth can be preserved for the benefit of future generations. The paper provides several scenarios to better explain how this can help families with their estate planning and caring for their descendants.

The concept of the Alaska Gift Trust is that someone makes a written promise to gift money. That promise is enforceable and irrevocable, although plenty of safeguards are built into the statute to make sure a person does not inadvertently make such an irrevocable promise. The promise must be satisfied within nine months of the promisor's death, but it may also be filled while the person is still alive.

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MS. BUSHNELL said the white paper reiterates the requirements in the bill that a number of specific steps need to be followed to use these provisions in statute. First, a person would need to create an Alaska Gift Trust, which must be a written document stating that the trust is a gift trust created under the statute. The trust must deposit at least \$10,000 in an Alaska bank account, and at least one trustee must be an Alaskan resident, bank, or trust company with its primary place of business in Alaska. Second, the person must sign the written promise, include an express reference to the statute, and include a statement that the trustee intends to be legally bound by the promise, both of which are safeguards against inadvertent usage of the statute. The promise is for a certain amount of money, and the terms of the promise require that the money be delivered to the trust within nine months of the person's death or sooner. Third, the person must deliver the written promise to the trustee of the trust. Once the promise is delivered to the trustee and has passed 180 days it becomes a promissory note or negotiable instrument.

She said [Section 4] of SB 191 is a new concept that makes the promise of a gift "a negotiable instrument." This will give trustors, trustees, attorneys, and courts existing statutes to reference for its application. The white paper lists scenarios and examples to illustrate how the Alaska Gift Trust would work.

MS. BUSHNELL said the white paper goes on to discuss the impact on a promisor's estate after death as well as potential risks and resolutions.

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CHAIR COGHILL said the promise of a gift is not necessarily a contract, but a promise to give.

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MATTHEW BLATTMACHR, President & Chief Executive Officer, Peak Trust Company; President, Alaska Trust & Estate Professionals, Anchorage, Alaska, stated that in its initial form, the gift provision is an enforceable promise that is executed via a contract.

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CHAIR COGHILL asked what national discussion has occurred on this new gift trust concept.

MR. M. BLATTMACHR replied there hasn't been much talk about it at the state or national level. While there is express law allowing it, no law expressly disallows it.

CHAIR COGHILL summarized that this structure would take advantage of the high tax limit on estate taxes. There has been a lot of push back on inheritance taxes because the money being gifted has already been earned and taxed. He described the concept of gifting money to the next generation as reasonable.

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SENATOR HUGHES asked if the concept of a gift trust started in Alaska because it didn't sound as though other states were doing this.

MR. M. BLATTMACHR agreed that the promise of a gift provision is not being done elsewhere. The concept was created via the Alaska Trust and Estates Professionals, so it is an Alaskan concept. If this bill passes, Alaska will be the only state to expressly allow this type of estate planning.

SENATOR HUGHES commented that she was pleased to hear Alaska is innovative. She asked if this provides an advantage to the state, such that people will want to set up their trusts in Alaska. She further asked if SB 191 will help the state economically.

MR. M. BLATTMACHR said he wished Alaska could trademark some of the estate and trust concepts that the legislature has pioneered. Alaska is viewed as an innovative state, particularly in the trust and estate industry. Competitor states watch Alaska closely to see what estate laws are introduced and passed. He offered his belief that other states will copy Alaska's laws. In further response, he agreed there is definitely an advantage in passing SB 191 since it will encourage Alaskans and non-Alaskans to implement this type of estate planning in Alaska.

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SENATOR KIEHL asked how the IRS treats income and appreciation of community property.

MR. M. BLATTMACHR replied the general rule for community property is that not only the principal, but any income and interest is community property, which was the intent of the original community statute passed in Alaska. It is also the default regime [by the IRS] and all other states. The clarification in SB 191 to community property is the result of a

court decision that the Alaska Trust & Estate Professionals believes misinterprets the intent at the state and federal level because it separates the principal from the income and appreciation. SB 191 would clarify that the principal, income, and appreciation are all considered community property. The bill would give people the choice to divide principal from income and appreciation, although doing so is not common. Several practitioners in the Alaska Trust & Estate Professionals group have questioned whether allowing that flexibility might violate the community property regime. The ultimate intent in the bill is to expressly clarify that unless a person specifically declares that income and appreciation is not community property, the default rule is that it will be.

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SENATOR KIEHL asked if the IRS would allow a person to make the declaration that income and appreciation is not community property.

MR. M. BLATTMACHR said he was unsure if the IRS is "okay" with that, so a person would want to discuss community property decisions with his or her legal or tax counsel. However, the bill currently provides an option to do so.

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SENATOR KIEHL said the first paragraph of the white paper indicates the transfer tax system is completely separate from income tax. He asked if this creates any implications for personal or corporate income taxes.

MR. M. BLATTMACHR answered no; the gift provision allows people to take advantage of the gift or estate tax exemption, but it does not provide any particular personal income tax benefit.

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SENATOR KIEHL said the statute provides that the surviving spouse is entitled to an elective share of the estate, which is about one-third of the augmented estate. The augmented estate appears to include the value of property transferred through an irrevocable transfer. He read [a portion of AS 13.12.205(a)(2)(A)], "an irrevocable transfer in which the decedent retained the right to the possession or enjoyment of, or to the income from, the property,...". This would seem to include "the promise of a gift." He asked if the augmented estate includes the value of a person's "promise of a gift" to include the augmented estate to which the surviving spouse is

entitled. If so, he asked if the surviving spouse would receive this before or after the trust is paid.

MR. M. BLATTMACHR agreed that surviving spouses receive special protection under Alaska law related to the estate of the deceased spouse. He deferred further comment to Ms. O'Connor.

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ABIGAIL O'CONNOR, Attorney, O'Connor Law, LLC; Vice President, Alaska Trust & Estate Professionals (ATEP), Anchorage, Alaska, related a scenario to illustrate how she and Mr. Delman envisioned the elective share would work once the person dies and the promise of a gift becomes a claim against the estate. If a person has assets of \$10 million in cash in his or her estate, that cash is still part of the augmented estate because it is an asset of the estate. However, the net probate estate that goes into the augmented estate is reduced by debts, so it's almost a wash. However, the white paper cites another section of law that says if the transfer is made during the marriage and within two years preceding death, [then the spouse would be entitled to a portion of the promised money if he or she claimed the elective share].

CHAIR COGHILL asked her to cite the section.

MS. O'CONNOR replied it is AS 13.12.205(a)(3)(C). She stated that the assets that the decedent had would be part of the probate estate but would be reduced by the promise to arrive at the net probate estate amount. She said it is essentially a gift, but it is also a debt. The ATEP does not think that the spouse would be any worse off than if the decedent had made an actual transfer of the cash asset prior to death. Instead of making the promise of a gift, if the decedent gave the \$10 million to the trust during his/her lifetime, it would not be included in the net probate estate. If it was made within two years before death it would come into the estate under the surviving spouse provision. In response to whether the decedent enjoys the rights of property, the answer is yes; the assets in the decedent's estate are ones the decedent enjoys. In terms of the actual promise of a gift, the decedent does not retain any benefit since it is a debt, she said.

SENATOR KIEHL commented that the surviving spouse provision did not make him feel any more comfortable.

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CHAIR COGHILL remarked that a husband and wife using the Alaska Gift Trust should be cautious.

MR. M. BLATTMACHR agreed. He added that if one spouse owns a separate asset, they have the ability to gift it by promise. Under current law, they can gift the asset in actuality since the surviving spouse has no right or claim.

CHAIR COGHILL remarked that it would make for interesting relationships.

SENATOR KIEHL added that if the gift was made while both spouses were living, it might lead to interesting conversations.

CHAIR COGHILL asked how a surviving spouse would currently assert a claim if the spouse was excluded from a large portion of the estate or how the law would exclude the claim.

MS. O'CONNOR answered that it would depend on whether the decedent retained any interest. She related a scenario in which the decedent made a gift to a trust for children from his first marriage and the decedent retained no interest. If it is within two years prior to his death, the gift would become part of the augmented estate. She didn't believe the gift would go back into the estate if the decedent created the gift prior to the marriage or five years prior to his or her death. That's why they're saying the spouse would not be in any worse position under the bill, she said.

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MS. O'CONNOR advised that estate planners always look at the effect on the surviving spouse when gifting strategies are part of the estate plan. If counsel represents one party and that spouse gives away assets to his or her children, but does not tell the other spouse, it will be a red flag regardless of the mechanism used in the estate planning. She said the bill does not create any more dangerous situation than under current law. If counsel is trying to protect assets from a spouse, it is usually done via a post-nuptial agreement and each spouse is represented by counsel.

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CHAIR COGHILL said the committee members are not practitioners so they want to be sure that community property is managed such that surviving spouses are not left high and dry by potentially unscrupulous tactics.

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MS. O'CONNOR clarified two points. In response to the question about whether the Gift Trust is a contract, she said it is because it is fully enforceable, but it is different because in a contract each party has usually given something up. This is different; this trust does not give anything in exchange for the promise of a gift, but the person making the gift is held to that contract.

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CHAIR COGHILL said his understanding is that the promise of a gift turns into a debt to the estate once the person dies.

MS. O'CONNOR replied the promise of a gift will become a debt immediately. After 180 days, it is treated like a promissory note. She suggested members think of the promise of a gift to a trust as an atypical contract.

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MS. O'CONNOR turned to the national discussion and whether the Alaska Gift Trust is unique. She said she was not aware of any other state using this concept. The theoretical concept of the promise of a trust was first raised in an article several years ago by Austin Bramwell [an adjunct professor of law at New York University School of Law, attorney at Law, Milbank, Tweed, Hadley & McCloy LLP]. She related her understanding that Pennsylvania may have common law that such a promise could be enforceable, but she did not have any details. That state does not have a gift trust provision in law, she said. Further, the idea of a promise of a gift can also be found in charitable giving pledges. Mr. Delman can elaborate on this further, she said.

She said the Alaska Gift Trust provision is unique, but some of the underlying theories have been discussed nationally. She offered her belief that this will gain national recognition since the buzz in the national estate planning community is how to use exemptions. She anticipated that the Alaska Gift Trust in SB 191 would be very helpful and that Alaska would be a trailblazer.

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CHAIR COGHILL asked for the reason for using 180 days.

MS. O'CONNOR deferred to Mr. Delman to respond.

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JAMIE DELMAN, Attorney, Shaftel Delman LLC, Anchorage, Alaska, answered that the intent of the 180 day period was to encourage a continuing nexus with the State of Alaska. This would allow people to form a trust and contribute the promise of a gift, which has to stay with the trustee for a period of time. He said 180 days was selected, but it could be shorter.

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CHAIR COGHILL asked what has to happen during that 180-day period of time.

MR. DELMAN responded that the typical process before the 180-day point would be that someone would create, draft and sign the trust, the trustee would sign the trust document, and the promisor would create the written promise and deliver it to the trustee. He envisioned the 180 days as "a holding period," with no expectation that the written promise would change hands. If the trustee needed to make a distribution to a beneficiary, he or she might need to sell property, which could include the obligation.

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CHAIR COGHILL asked what the "notwithstanding the provisions of AS 45.03,..." language related to the 180 days means.

MR. DELMAN responded that this provision relates to a promissory note typically being issued for value.

CHAIR COGHILL asked Mr. M. Blattmachr to weigh in.

MR. M. BLATTMACHR said that was his understanding; no consideration is given to the provisions of AS 45.03.

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SENATOR KIEHL said it would be helpful to understand the benefit to having the promise of a gift be a negotiable instrument.

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MR. DELMAN responded that there are two reasons to do so. First, in order for the person creating this written promise to use the exemption, that person must file a gift tax return reporting the value of the written promise. If the written promise is so restrictive that it cannot be sold by the trustee or transferred in any way, the value of the written promise would be much lower than a standard promissory note. He highlighted the importance that the type of asset that this bill would create is like other assets and is saleable and transferable.

He said a second and more compelling reason is to think about the written promise as a whole rather than thinking about it in a vacuum. He related a scenario in which a trustee owns a written promise and they also own a commercial building that is subsequently damaged in an earthquake. The estate consists of a \$1 million written promise and a \$500,000 building that incurs \$200,000 in damages. The trustee should always be able to sell trust property in order to meet his or her fiduciary duties. To repair the earthquake-damaged building, the trustee may need to sell its other asset. Certainly, sitting on an unsalable asset is not a good position for a trustee.

MR. DELMAN explained that if a trust only owns a \$1 million promise to pay and the trustee has the fiduciary duty to make a distribution to a beneficiary in need, the trustee might need to sell the note.

CHAIR COGHILL commented that he better understands this since he has been an executor of two different estates.

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SENATOR KIEHL expressed concern that this would be a negotiable instrument that does not need to have any value attached. He said a person who is less than honorable and is at death's door could write 1,100 \$10,000 promises and proceed to sell those \$10,000 notes without any funds to support the promises.

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SENATOR MICCICHE said the \$10,000 notes would be worth a fraction of the value to someone who is willing to negotiate on that debt. He offered his view that this type of opportunity is available in any law that pertains to debt and he did not see this as an issue in SB 191.

MR. DELMAN agreed that the value of the note is based on the person who is making the promise. He said a dishonest person could also sell his or her own promissory note under current law. If a person has an estate worth \$1 million and the individual tries to sell a \$2 million debt, it would be a case of buyer beware. The person's ability to pay would determine the value of the note.

MR. BLATTMACHER said nothing stops a "bad actor" and in any investment it is buyer beware. He added that while it would not be common to sell the note outside of an inter-family situation, it could happen.

CHAIR COGHILL related three benefits: a person gets to decide how their assets are distributed, the intended beneficiaries would obtain the real value of the asset, and the IRS does not tax the gift. He asked if his understanding was correct.

MR. M. BLATTMACHR answered yes.

CHAIR COGHILL asked for an explanation of how tax lawyers will view this given that the rules may change.

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MR. M. BLATTMACHR answered that typically if laws change there is not a claw back or retroactivity. However, if a person takes action today and tomorrow's rules are less favorable, it is to that person's advantage.

CHAIR COGHILL asked if the full value of the asset would flow to the beneficiaries if the value were to increase.

MR. M. BLATTMACHR answered yes.

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SENATOR HUGHES asked if any laws would protect a senior who got scammed by a bad actor.

MR. M. BLATTMACHR answered that if the seller made a gross misrepresentation, that person could potentially be convicted of fraud. If there was no misrepresentation, he said he hoped the seller would realize the buyer was unknowing and would not sell the asset for more than it was worth.

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MR. DELMAN reminded members that under the Alaska Gift Trust, the party selling the instrument is the person who creates the trust and transfers the written promise. After 180 days lapses, if the trustee determines a need for cash, the trustee can sell the instrument. An entire body of trust law guides the trustee. The person who creates the promise "quite literally" trusts the trustee, he said. The trustee has a fiduciary duty to the trust beneficiaries, and the likelihood of a trustee trying to scam a third party would be less than a random person on the street trying to sell something to an unsuspecting party.

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SENATOR HUGHES asked whether something in the body of trust law would allow the trustee to be sued if they did something fraudulent or acted in bad faith.

MR. DELMAN answered absolutely.

SENATOR HUGHES asked whether any advertising will be done to bring in investment business to the state or if any active word of mouth efforts will be made.

MR. DELMAN said estate planners throughout the country are very connected in terms of developing law, but he was not aware of any campaigns to advertise this innovative law.

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MS. O'CONNOR said it is unlikely any direct advertising would occur since it typically is not done in the industry, but the Alaska Trust & Estate Professionals were likely to actively promote it through the existing national network. She anticipated that the Alaska Gift Trust would gain momentum because people are eager to find ways to use the federal gift tax exemption.

CHAIR COGHILL commented that businesses in Alaska would be more excited than everyone else.

[2:25:47 PM](#)

SENATOR MICCICHE related his understanding of the overall effect of SB 191. Currently, the promise of a gift to a trust allows a \$11.5 million gift tax exemption. If the person waits and the actual gift is given after January 1, 2026, the exemption would be reduced to \$5 million. But because the \$6.5 million is subject to a 40 percent tax rate, the trust will receive \$4 million.

He offered his view that the only potential for abuse is already covered in the bill. He related a scenario in which someone would offer to "give the trust 'x' amount someday if the person pays him or her 'x' amount today." That scenario would be covered in SB 191 because the Alaska Gift Trust provision is created for promises without consideration. That scenario would result in something in return, which is not allowed.

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SENATOR KIEHL said his concern was that despite the discussion about fraud or misrepresentation, this bill, as currently written, does not require any fraud or misrepresentation to sell

something with no value behind it. That is why the "notwithstanding language" is required. He said it seems that there are protections for things that people want to buy and sell, but only for sophisticated buyers. He wondered if limiting who could trade in the negotiable promissory notes would provide some safeguards without opening up an opportunity for abuse.

CHAIR COGHILL said he represented two families as executor for the estates because the parties trusted him to handle it appropriately. People use estate and trust companies to have their estates properly managed. He asked Mr. M. Blattmachr to address potential mismanagement.

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MR. M. BLATTMACHR responded that while nothing is given up front, the asset has value. He related a scenario in which during dinner his grandfather promises to give him \$5 million upon his death. However, that is not an enforceable promise. This Alaska Gift Trust provision in SB 191 changes that such that the promise of a gift is enforceable and thus has value.

SENATOR KIEHL suggested that a chronic inebriate could be sobered up and sign a promise, but there would not be any value.

CHAIR COGHILL pointed out that the person must be able to make a minimum \$10,000 deposit to an account in the state.

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SENATOR MICCICHE applauded the creativity of delayed gifts to trusts. He recommended that people read the Alaska Trust & Estate Professionals' white paper "Alaska Gift Trusts" [dated February 27, 2020]. He noted that it answered his questions. It explains the statutory hierarchy when the trust cannot satisfy its obligations. For example, a person may promise a gift of \$2 million in Tupperware stock worth \$74 per share, but it is now worth \$7 per share.

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CHAIR COGHILL expressed appreciation for the white paper.

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CHAIR COGHILL stated that SB 191 will be held in committee.

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SENATOR HUGHES complimented the sponsor's staff.

SENATOR MICCICHE reiterated that the white paper explained a lot. He did not think amendments were necessary, but further explaining the risks of trust law and the assets included in trusts could help members feel more comfortable with the current structure in the bill.

CHAIR COGHILL said the bill has been thoroughly vetted by [the Alaska Trust & Estate Professionals group]. He commented on the value of examining what could go wrong for the benefit of Alaskans and for those who manage trusts, who are subject to legal requirements. He suggested that the new concept in Section 4, related to Alaska Gift Trusts is something members are still contemplating to obtain a full understanding.

[SB 191 was held in committee.]

[2:37:27 PM](#)

There being no further business to come before the committee, Chair Coghill adjourned the Senate Judiciary Standing Committee meeting at 2:37 p.m.