# HB

# 459

9-LS1335\M
Bannister
2/9/96

CS FOR HOUSE BILL NO. 459( )

IN THE LEGISLATURE OF THE STATE OF ALASKA

NINETEENTH LEGISLATURE - SECOND SESSION

BY

Offered:
Referred:

Sponsor(s): REPRESENTATIVE VEZEY

A BILL

FOR AN ACT ENTITLED

**"An Act relating to the jurisdiction governing a trust, to challenges to trusts or property transfers in trust, to the validity of trust interests, and to transfers of certain trust interests."**

BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF ALASKA:

* Section 1. AS 13.36.035(a) is amended to read:

(a) The court has exclusive jurisdiction of proceedings initiated by interested parties concerning the internal affairs of trusts, **including trusts covered by (c) of this section. Except as provided in (c) - (d) of this section, proceedings that** [. PROCEEDINGS WHICH] may be maintained under this section are those concerning the administration and distribution of trusts, the declaration of rights and the determination of other matters involving trustees and beneficiaries of trusts. These include [, BUT ARE NOT LIMITED TO,] proceedings to

(1) appoint or remove a trustee;

(2) review trustees' fees and to review and settle interim or final

accounts;

(3) ascertain beneficiaries, determine any question arising in the administration or distribution of any trust including questions of construction of trust instruments, instruct trustees, and determine the existence or nonexistence of any immunity, power, privilege, duty or right; and

(4) release registration of a trust.

*** Sec. 2.** AS 13.36.035 is amended by adding new subsections to read:

(c) A provision that the laws of this state govern the validity, construction, and administration of the trust and that the trust is subject to the jurisdiction of this state is valid, effective, and conclusive for the trust if

(1) some or all of the trust assets are deposited in this state or are being managed by a qualified person;

(2) the trustee is a qualified person; and

(3) the principal place of administration is located in this state.

(d) The validity, construction, and administration of a trust with a state jurisdiction provision are determined by the laws of this state, including the

(1) capacity of the settlor;

(2) powers, obligations, liabilities, and rights of the trustees and the appointment and removal of the trustee; and

(3) existence and extent of powers, conferred or retained, including a trustee's discretionary powers, the powers retained by a beneficiary of the trust, and the validity of the exercise of a power.

*** Sec. 3.** AS 13.36.045(a) is amended to read:

(a) The court will not, over the objection of a party, entertain proceedings under AS 13.36.035 involving a trust registered or having its principal place of administration in another state, unless

(1) all appropriate parties could not be bound by litigation in the courts of the state where the trust is registered or has its principal place of administration; [OR]

(2) the interests of justice otherwise would seriously be impaired**; or**

**(3) the trust contains a state jurisdiction provision; and**

**(A) some or all of the trust assets are deposited in this state or are being managed by a qualified person; or**

**(B) the trustee is a qualified person.**

*** Sec. 4.** AS 13.36 is amended by adding new sections to read:

Sec. 13.36.310. CHALLENGES TO TRUST. Except as provided in AS 34.40.110, a trust that is covered by AS 13.36.035(c) or that is otherwise governed by the laws of this state, or a property transfer in trust that is covered by AS 13.36.035(c) or that is otherwise governed by the laws of this state, is not void, voidable, liable to be set aside, defective in any fashion, or questionable as to the settlor's capacity, on the grounds that the trust or transfer avoids or defeats a right, claim, or interest, or contravenes a law or a judicial or administrative order or action that recognizes, protects, enforces, or gives effect to the right, claim, or interest. In this subsection, "right, claim, or interest" means a right, claim, or interest conferred by law on a person by reason of a personal or business relationship with the settlor or by way of a marital or similar right.

Sec. 13.36.390. DEFINITIONS. In AS 13.36,

(1) "qualified person" means

(A) an individual who, except for brief intervals, military service, attendance at an educational or training institution, or for absences for good cause shown, resides in this state, whose true and permanent home is in this state, who does not have a present intention of moving from this state, and who has the intention of returning to this state when away;

(B) a trust company that is organized under AS 06.25 and that has its principal place of business in this state; or

(C) a bank that is organized under AS 06.05, or a national banking association that is organized under 12 U.S.C. 21 - 216d, if the bank or national banking association possesses and exercises trust powers and has its principal place of business in this state;

(2) "settlor" means a person who transfers property in trust; "settlor" includes a person who furnishes the property transferred to a trust even if the trust is created by another person;

(3) "state jurisdiction provision" means a provision that the laws of this state govern the validity, construction, and administration of a trust and that the trust is subject to the jurisdiction of this state.

* **Sec. 5.** AS 34.27.050(a) is amended to read:

(a) A nonvested property interest is invalid unless

(1) when the interest is created, it is certain to vest or terminate no later than 21 years after the death of an individual then alive; [OR]

(2) the interest either vests or terminates within 90 years after its creation; **or**

**(3) the interest is in a trust and 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 the trust is created**.

* **Sec. 6.** AS 34.27.060 is amended to read:

Sec. 34.27.060. REFORMATION. Upon the petition of an interested person, a court shall reform a disposition in the manner that most closely approximates the transferor's manifested plan of distribution and is within the 90 years allowed by AS 34.27.050(a)(2), (b)(2), or (c)(2) if

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(2) a class gift is not but might become invalid under AS 34.27.050 and the time has arrived when the share of any class member is to take effect in possession or enjoyment; or

(3) a nonvested property interest that is not validated by AS 34.27.050(a)(1) **or (3)** can vest but not within 90 years after its creation.

* **Sec. 7.** AS 34.40.010 is amended to read:

Sec. 34.40.010. INVALIDITY GENERALLY. **Except as provided in AS 34.40.110, a** [A] conveyance or assignment, in writing or otherwise, of an estate or interest in land, or in goods, or things in action, or of rents or profits issuing from them or a charge upon land, goods, or things in action, or upon the rents or profits from them, made with the intent to hinder, delay, or defraud creditors or other persons of their lawful suits, damages, forfeitures, debts, or demands, or a bond or other

evidence of debt given, action commenced, decree or judgment suffered, with the like intent, as against the persons so hindered, delayed, or defrauded is void.

* **Sec. 8.** AS 34.40.110 is repealed and reenacted to read:

Sec. 34.40.110. RESTRICTING TRANSFERS OF TRUST INTERESTS. (a) A person who in writing transfers property in trust may provide that the interest of a beneficiary of the trust may not be either voluntarily or involuntarily transferred before payment or delivery of the interest to the beneficiary by the trustee. In this subsection,

(1) "property" includes real property, personal property, and interests in real or personal property;

(2) "transfer" means any form of transfer, including deed, conveyance, or assignment.

(b) If a trust contains a transfer restriction allowed under (a) of this section, the transfer 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 the

(1) transfer was intended in whole or in part to hinder, delay, or defraud creditors or other persons under AS 34.40.010;

(2) trust provides that the settlor 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; in this paragraph, "revoke or terminate" does not include a power to veto a distribution from the trust or a similar power; or

(3) trust requires that all or a part of the trust's income or principal, or both, must be distributed to the settlor.

(c) The satisfaction of a claim under (b)(1) - (3) of this section is limited to that part of the trust to which (b)(1) - (3) of this section applies.

(d) In this section, "settlor" means a person who transfers real property, personal property, or an interest in real or personal property, in trust.

* **Sec. 9.** This Act does not apply to a trust unless the trust is created on or after the effective date of this Act.

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(c) A provision that the laws of this state govern the validity, construction, and administration of the trust and that the trust is subject to the jurisdiction of this state is valid, effective, and conclusive for the trust if

(1) some or all of the trust assets are deposited in this state or are being managed by a qualified person;

(2) the trustee is a qualified person; and

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(d) The validity, construction, and administration of a trust with a state jurisdiction provision are determined by the laws of this state, including the

(1) capacity of the settlor;

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(B) a trust company that is organized under AS 06.25 and that has its principal place of business in this state; or

(C) a bank that is organized under AS 06.05, or a national banking association that is organized under 12 U.S.C. 21 - 216d, if the bank or national banking association possesses and exercises trust powers and has its principal place of business in this state;

(2) "settlor" means a person who transfers property in trust; "settlor" includes a person who furnishes the property transferred to a trust even if the trust is created by another person;

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*New Text Underlined* [DELETED TEXT BRACKETED]

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(B) a trust company that is organized under AS 06.25 or a bank that is organized under AS 06.05, if the trust company or bank has its principal place of business in this state;

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(1) "property" includes real property, personal property, and interests in real or personal property;

(2) "transfer" means any form of transfer, including deed, conveyance, or assignment.

(b) If a trust contains a transfer restriction allowed under (a) of this section, the transfer 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 the

(1) transfer was intended in whole or in part to hinder, delay, or defraud creditors or other persons under AS 34.40.010;

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(3) trust requires that all or a part of the trust's income or principal, or both, must be distributed to the settlor.

(c) The satisfaction of a claim under (b)(1) - (3) of this section is limited to that part of the trust to which (b)(1) - (3) of this section applies.

(d) In this section, "settlor" means a person who transfers real property, personal property, or an interest in real or personal property, in trust.

* Sec. 9. This Act does not apply to a trust unless the trust is created on or after the effective date of this Act.

# LEGAL SERVICES

DIVISION OF LEGAL AND RESEARCH SERVICES
LEGISLATIVE AFFAIRS AGENCY
STATE OF ALASKA

(907) 465-3867 or 465-2450
FAX (907) 465-2029
Mail Stop 3101

130 Seward Street, Suite 409
Juneau, Alaska 99801-2105

**MEMORANDUM** December 26, 1995

**SUBJECT:** Sectional Summary of bill draft relating to trusts (Work Order No. 9-LS1335\F)

**TO:** Representative Al Vezey
Attn: Joe Ryan

**FROM:** Theresa Bannister
Legislative Counsel

You have requested a sectional summary of the above-described bill.

As a preliminary matter, note that a sectional summary of a bill should not be considered an authoritative interpretation of the bill and the bill itself is the best statement of its contents.

Section 1. Modifies the statute that gives the superior court exclusive jurisdiction of certain trust proceedings. Includes trusts described in sec. 2 of the bill and coordinates the provisions of the statute with sec. 2. Makes a technical change by deleting "but are not limited to."

Section 2. Subsection (c ) states that a provision in a trust that this state's laws govern the trust and that the trust is subject to this state's jurisdiction is valid, effective, and conclusive if either of two listed conditions is met. These co nditions relate to the location of trust assets and the relationship of the trust asset manager or trustee to this state.

Subsection (d) states that a trust's validity, construction, and administration are determined by this state's laws, if the trust has a state jurisdiction provision. Identifies some of the matters covered by this provision.

Section 3. States that this state's superior court will not, if a party objects, handle a trust's proceedings under AS 13.36.035 if the trust is registered or has its principal place of administration in another state, unless certain conditions are met. Among these conditions is if the trust has a state jurisdiction provision and either (1) trust assets are deposited in this state or managed by a qualified person, or (2) the trustee is a qualified person.

Section 4. AS 13.36.310 states that, except as provided in AS 34.40.110, a trust, or a property transfer in trust, that is governed by this state's laws isn't void, voidable, liable to

be set aside, defective, or questionable as to the settlor's capacity, on the grounds described in the section.

AS 13.36.390 defines "qualified person," "settlor," and "state jurisdiction provision" for AS 13.36.

Section 5. States that a nonvested property interest is invalid unless, among the other listed reasons, the interest is in a trust and income or principal of the trust is subject to discretionary distribution by the trustee to a person living when the trust is created.

Section 6. Conforms this section to the amendment made in sec. 5 of the bill.

Section 7. Coordinates this section with the new provisions in sec. 8 of the bill.

Section 8. Subsection (a) allows a person who transfers property in trust and in writing to provide that a trust beneficiary's interest may not be transferred before payment or delivery of the interest to the beneficiary.

Subsection (b) states provides that the above transfer restriction prevents a creditor or other person from using the beneficiary's trust interest to satisfy a claim unless certain listed conditions are met.

Subsection (c ) limits the part of a trust that may be used to satisfy a claim otherwise allowed under (b).

Subsection (d) defines "settlor" for the section.

Section 9. Indicates that the bill's provisions only apply to trusts created on or after the effective date of bill.

If I may be of further assistance, please advise.

TLB:glc
95-474.glc

# Alaska State Legislature

## House of Representatives

Official Business

State Capitol
Juneau, Alaska 99801-1182
(907) 465-3718

### House Majority Leader

# *SPONSOR STATEMENT*

Alaska is in the unique position of having neither a state income tax nor a state sales tax. This fact has made Alaska a very favorable venue for managers of large investment portfolios, administrators of trusts and other investors who want the security and protection of the United States Government and the American banking system for their investments.

To attract these investments, certain changes have been suggested to the statutes governing trusts in Alaska. These changes when enacted, will open the door to Alaska management of billions of dollars that are now fleeing to offshore jurisdictions. According to the latest figures reported by Congress' Joint Committee on Taxation, American families transferred over $460 billion off-shore last year alone.

It is becoming increasingly obvious to policy-makers that this out-flow of U.S. capital comes at a steep cost. U.S. citizens who transfer assets in trust off-shore do not gain any tax advantages -- indeed unless structured carefully, there can be extortionate tax costs. Thus, there is no tax loss to U.S. jurisdictions. But the out-flow results in much more. It reduces the capital base available for other investment in the U.S., it increases the costs of capital and it reduces the increased banking and legal work in the U.S. associated with creating and administering Family Trusts. And there is no indication that Americans of good intention will stop seeking to use this very traditional method of preserving their family's wealth and protecting it from adversity. Currently, only one American state -- Missouri -- has enacted a statute to offset the tremendous capital out-flow, but it suffers from defects and ambiguities that make many practitioners uncomfortable recommending it as a viable option. Therefore, it could be a great asset to Alaska, and the U.S. generally, to enact legislation that would make it possible for Americans to create Family Trusts in the U.S.

Passage of HB-459 will be the key to opening this great opportunity for Alaska.

# Alaska State Legislature

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# *SPONSOR STATEMENT*

## THE FAMILY TRUST ACT

## Proposed Amendments to Titles 13 and 34 of the Alaska Statutes

### I. Purpose of the Bill

Among the many traditional reasons for establishing trusts, one is the preservation of assets for one's family. This very ancient and common form of "asset protection" is not usually undertaken by one who is or who is about to become insolvent. If so, traditional rules will protect creditors who are harmed by the creation of the trust. Quite the contrary, trusts such as these are more typically created by individuals who are seeking to shelter a "nest egg" from the attendant risks of modern economic life and provide a source of support for the future. Such a trust is usually irrevocable and gives the trustee full discretion to accumulate income or to "sprinkle" income and principal among a class of beneficiaries that can include the grantor (a "Family Trust"). The key element for Family Trusts is that no person, not even a family member, can invade the trust.

However, under the laws of many states a Family Trust is not an effective shield against improvidence. This is so because of relatively modern innovations in trust law. For example, traditionally a Family Trust would be safe from the claims of the grantor's creditors. Under the laws of many states today,

however, it is possible for the creditors of the grantor (and in some cases, even creditors of the beneficiaries) to reach the assets of a Family Trust even though neither the grantor nor any beneficiary could do so. This result is often predicated on the public policy that a person should not be able to put assets beyond the reach of his creditors and yet retain their use. But in practice, the rule operates contrariwise. It actually makes it possible for the grantor to do indirectly what he otherwise cannot do directly. By racking up debts that he cannot repay, for example, the grantor is indirectly able to withdraw assets from the trust, to the detriment of the family. In the typical Family Trust, however, the grantor would not be able to withdraw the trust assets unilaterally.

It is clear that the rule in most jurisdictions makes sense when a trust is in fraud of creditors, a sham or created solely for the benefit of the grantor with the understanding that the grantor alone would continue to benefit from a trust. In those cases, the rule operates to enforce the public policy mentioned above. However, in respect to a traditional Family Trust, the rule operates a hardship on families and makes perfectly respectable--and many times important--family planning impossible.

In the face of this problem, and testament to their bona fides in creating Family Trusts, many American families have turned to off-shore jurisdictions such as the Cook Islands, Cayman Islands, Jersey, Bermuda and many others for their trust needs. These jurisdictions have enacted statutes that clarify the law and make it possible to create a Family Trust without the risk that the grantor's creditors will attach trust assets, unless the transfer in trust was in fraud of the transferor's creditors. According to the latest figures reported by Congress' Joint Committee on Taxation, American families transferred over $460 billion off-shore last year alone.

It is becoming increasingly obvious to policy-makers that this out-flow of U.S. capital comes at a steep cost. U.S. citizens who transfer assets in trust off-shore do not gain any tax advantages -- indeed unless structured carefully, there can be extortionate tax costs. Thus, there is no tax loss to U.S. jurisdictions. But the out-flow results in much more. It reduces the capital base available for other investment in the U.S., it increases the costs of capital and it reduces the increased banking and legal work in the U.S. associated with creating and administering Family Trusts. And there is no indication that Americans of good intention will stop seeking to use this very traditional method of preserving their family's wealth and protecting it from adversity. Currently, only one American state -- Missouri -- has enacted a statute to offset the tremendous capital out-flow, but it suffers from defects and ambiguities that make many practitioners uncomfortable recommending it as a viable option. Therefore, it could be a great asset to Alaska, and the U.S. generally, to enact legislation that would make it possible for Americans to create Family Trusts in the U.S.. This could be accomplished with little substantive change in the substantive law of trusts in Alaska and without working to the detriment of creditors. The proposed Bill therefore clarifies current law in Alaska by saying that irrevocable transfers to a fully discretionary trust -- even when one of the potential beneficiaries is the transferor -- are not liable to the claims of creditors unless the transfer is otherwise in fraud of creditors under Alaska law.

# Alaska State Legislature

## HISTORICAL BACKGROUND

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The practice of placing property in trust in order to preserve it for the use of one's family is as old as the concept of the trust itself. In the 15th century, the trust developed under the common law of England as a means, among other things, to protect the property of the landed gentry as they did battle in Europe, thus preserving their property for family members. The trust assured the gentleman that rival nobles, the Church or others, could not rob his family of their fortune while their protector was absent. Over the centuries, the use of trusts has varied. Sometimes a trust was used to protect a family from the claims of the Church, at others to protect a family from the claims of the Crown. In more modern times, trusts have been used to protect the assets of Jews from seizure by the Nazis. Over its long history, the trust has consistently been a means of securing a family's wealth to its "natural" objects with minimal risks from the claims of others. In its origin, a trust was very much a Family Trust.

As old as the Family Trust is, so too is the notion that an irrevocable fully discretionary trust created solely for the benefit of the Settlor is void. The rule is grounded in the very good reason that such a "self-settled" trust is particularly prone to abuse and, more important, it violates a common sense of fairness. An individual should not be able to put his assets beyond the reach of his rightful creditors when the assets nevertheless remain available for his use.

For example, statutes dating back to the 16th Century in England have rendered void a trust created by a person primarily for his benefit. American jurisdictions have continued this type of rule in effect. For example, in New York, the Estates, Powers and Trusts Low provides:

> A disposition in trust for the use of the creator is void as against the existing or subsequent creditors of the creator.

And for well near 100 years, these statutes have been interpreted to mean that a "self-settled" trust, whether discretionary or not, is void only if the Settlor is the sole beneficiary. For example, cases in New York (until very recently) have consistently held that an irrevocable discretionary trust created for the benefit of a class that includes the grantor is not subject to the claims of the grantor's creditors.

In recent times, however, many American jurisdictions have expanded the basic "self-settled" trust rule and thus made it very difficult for a person to create a Family trust. In large part, this development has been the result of abusive (sometimes real, sometimes perceived) transactions. But in reacting to these abuses, state legislatures and courts have gone too far and effectively restricted the traditions and reasonable uses of Family Trusts.

In particular, state courts have begun to construe the "self-settled" trust rule to mean that an irrevocable trust which includes the Settlor as a permissible beneficiary, even if the Settlor has retained no powers over the trust or the trustee, will be void as against the Settlor's creditors. In a recent New York case, for example, the court found that such a trust (even though there was no evidence to suggest that the trustee exercised his discretion in favor of the Settlor alone) was void against the Settlor's creditors on public policy grounds because it put the Settlor's assets beyond the reach of her creditors while remaining available for her use. Vanderbilt.

Despite the intuitive appeal of this argument, the extension of the "self-settled" trust rule is unwarranted. Consider, for instance, that an irrevocable discretionary trust, by its nature, puts assets beyond the reach of a beneficiary's creditors. Indeed, that's the difference between an outright gift and a gift in trust.

Where a trust includes the Settlor as a permissible beneficiary and where there is nothing to suggest that the trust is primarily for the benefit of the Settlor or is a sham, there is no policy reason to alter the basic rule. Under these circumstances, the Settlor has no assurance that he will receive any of the assets of the trust. They are beyond his reach, unless the trustee determines to make a distribution. It does not offend notions of fairness, therefore, that the assets also be beyond the reach of the Settlor's creditors.

Indeed, fairness would require that the Settlor's creditors in such a case not be able to reach the assets of the trust. For example, if a family wishes to safeguard its wealth against disaster and therefore, the matriarch irrevocably creates a fully discretionary trust for the benefit of every member of the family, naming a bank as trustee, the family rightly would assume that no one of them (not even the Settlor) would be able to reach the assets of the trust. By allowing the Settlor's creditors to reach the assets in a case such as this, state courts make it possible for the Settlor to do indirectly what he is prohibited from doing directly. It makes it possible for the Settlor to amass debt that he cannot repay, knowing that the trust assets will be available to satisfy his creditors' claims. This is the equivalent of allowing the Settlor to make mandatory withdrawals from the trust.

Some jurisdictions have resisted the temptation of overreaching. In places such as Cayman, Bermuda and other off-shore jurisdictions, for example, statutes have been passed which adopt a rule that an irrevocable discretionary trust for the benefit of a class that includes the Settlor, is immune from the claims of the Settlor (or his creditors) unless the transfer was in fraud of his creditors, under local law. And in Missouri, the legislature recently enacted a similar statute. It provides:

> A provision restraining the voluntary or involuntary transfer of beneficial interests in a trust will prevent the Settlor's creditors from satisfying claims from the trust assets except:
>
> > (1) Where the conveyance of assets to the trust was intended to hinder, delay or defraud creditors or purchasers, pursuant to section 428.020, RSMo; or
> >
> > (2) To the extent of the Settlor's beneficial interest in the trust assets, if at the time the trust was established or amended:
> >
> > > (a) The Settlor was the sole beneficiary of either the income or principal of the trust or retained the power to revoke or amend the trust; or
> > >
> > > (b) The Settlor was one of a class of beneficiaries or retained a right to receive a specific portion of the income or principal of the trust that was determinable solely from the provisions of the trust instrument.

Thus, as in the off-shore jurisdictions, it would appear that an irrevocable discretionary trust established in Missouri for the benefit of the Settlor and his family would appear not to be subject to the claims of the Settlor's creditors if the trust so provides. Unfortunately, Section (2)(b) of the Missouri statute is ambiguous and the conclusion is not as obvious as it could be. As a result, few practitioners have sought to establish Family Trusts in Missouri.

These jurisdictions are not "asset protection" jurisdictions where creditors can expect an unfriendly reception or whether unscrupulous Settlors can defraud their creditors. Instead, these jurisdictions have returned to the traditional notion that, except where the Settlor has retained dominion and control over the assets in a trust or where the Settlor is the sole beneficiary or

where the transfer was in fraud of the Settlor's creditors, an irrevocable discretionary trust truly puts the trust assets beyond the reach of the Settlor and therefore should also be protected from the reach of the Settlor's creditors.

This notion of the use of Family Trusts is not only consistent with the tradition of the law of trusts but still rings true with property owners. Evidence the fact that last year alone, over $460 billion dollars was transferred to off-shore trusts such as the type described above. While it is possible, in some cases, that these trusts are abusive, it is likely that most of them are not. And for the likely majority that are not, American states with their over-reaching rules are forcing people to transfer their assets off-shore in order to obtain reasonable protection of their family's assets. This has the effect of transferring out of the US. the earning power, capital base and local banking and legal work that might otherwise be used here to promote local economies. And because foreign jurisdictions might in some cases have animosity toward foreign creditors, the result of the over-reaching rule is one that works to the collective detriment of creditors, property owners and the U.S. economy.

The conditions are therefore ripe for Alaska to fill the breach and provide a friendly jurisdiction to those who wish to establish Family Trusts. By the terms of the proposed legislation, only those trusts established with bona fides will successfully bar creditors' claims. So, for example, an irrevocable discretionary trust created for the benefit of the Settlor and his family, where the trustee is independent of the Settlor, makes distributions in response to the needs of the family and not the direction of the Settlor, and where their transfer does not leave the Settlor insolvent and is not motivated by a desire to avoid specific creditors, will be immune from the claims of the Settlor's creditors. Everything about such a trust suggests that the Settlor has parted with dominion and control over the trust assets. He could not compel the trustee to distribute

any of the assets nor could he exercise any other control over the assets. In such a case, it seems fair and reasonable to prohibit the Settlor from forcing a distribution to himself by racking up debt he cannot afford to repay.

If, however, a trust is created primarily for the benefit of the Settlor or if the Settlor retains powers over the trust or over the trustee (either explicit or implicit), the proposed bill would not protect the trust from the claims of the Settlor's creditors. For example, a trust over which the Settlor retains a power to revoke will remain liable to the claims of the Settlor's creditors. Or a trust which is created with the understanding that the trustee would make distributions to the Settlor any time he requested them, then that trust, too, would remain liable to the claims of the Settlor's creditors. In both circumstances, the Settlor has, either explicitly or implicitly, retained ownership of the trust assets and may force their distribution to him. Fairness therefore dictates that the Settlor's creditors have the same access to the trust assets as the Settlor.

The proposed Bill would provide generous flexibility for Family Trusts that fall in between those two extremes. For example, if the Settlor could not compel distribution but he could veto a proposed distribution by the trustee, the proposed Bill would nevertheless protect the trust assets from the claims of the Settlor's creditors. Likewise, if a Family Trust required that the Settlor receive the income of the trust quarterly, under the proposed Bill, only the income of the trust would be vulnerable to the claims of the Settlor's creditors. The integrity of the trust would nevertheless remain secure. In the first case, the power retained by the grantor enables him to preserve assets, not acquire them for his use. Thus, it is equitable that his creditors not be able to convert such a power into a power to distribute to the Settlor. In the second case, the creditors would not be able to undo the security of the family in the trust simply because

the Settlor retained a partial interest. Equity would require that the Settlor's creditors be able to recover exactly what the Settlor could demand, and no more.

By adopting the proposed Bill, Alaska will be returning to a more conservative position on trusts. It will be doing no more than making it possible for traditional Family Trusts to exist free from the over-reaching claims of creditors, where those claims against the trust would fail if made by the Settlor. It would not be expanding the ability of Settlors to evade creditors nor would it be restricting creditors fair access to a debtor's assets. Instead, Alaska would return itself to the more balanced and substantive view of Family Trusts that existed before the recent over-reaching.

And, collaterally, Alaska could bring to its economy a business boom unprecedented in the State since the oil boom. Even if only one-tenth of the trust business that goes off-shore were to come to Alaska, it would see $4 billion of assets move into the state. That, in turn, will increase the capital base in Alaska, and stimulate capital growth. This would give rise to banking and legal business, and serve as a catalyst to the economic "mushrooming" that has occurred in the off-shore jurisdictions that adopted such legislation.

It is notable that these off-shore jurisdictions, like Alaska, do not have an income tax. It is true that a tax-friendly regime creates an added incentive for property owners who wish to create Family Trusts. But it is often not the motivating reason. For example, Settlors will typically have to pay federal income tax on all income of the trust because it will be a grantor trust for federal income tax purposes. There is a temptation for states to reap a short-run gain by levying income tax on Family Trusts located in its jurisdiction. But Alaska would be well advised to avoid that temptation. For most families, an income tax would make Alaska a less desirable jurisdiction that Cayman or the Cook Islands. And in those jurisdictions that do not have an income tax, the

exponential effects of the trust business more than compensate for the loss of potential income tax revenue.

It should be stressed again that the proposed Bill is not a "device" for unscrupulous debtors and, therefore, should not create animosity among sister states. It does not make Alaska a "tax haven" or a jurisdiction unfriendly to creditors' claims. Indeed, the proposed Bill affords creditors broad protection when assets are transferred in fraud of their interests or when the Settlor retains powers over the trust assets. Quite the contrary of being anti-creditor, the proposed Bill is both creditor and family friendly. It rebalances the legal equities between individuals and creditors so that when an individual permanently and irrevocably parts with his property for the benefit of his family, he cannot squander the family's wealth through the inadvisable accumulation of debts.

## V. Budgetary Implications

There are no costs associated with this legislation. Instead, it is projected that there will be a dramatic increase in state revenue as banks, lawyers and other businesses benefit from the increased economic activity in Alaska.