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Developing Trust in the Self-Settled Spendthrift Trust

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COMMENT

Developing Trust in the Self-Settled Spendthrift Trust

*Kellsie J. Nienhuser**

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*Cujus est dare, ejus est disponere.*¹

I. INTRODUCTION

Estate planning attorneys seek to help clients manage and distribute their wealth so that it can be used for personal benefit during life and passed down to their loved ones upon death.² A trust is an estate planning tool that helps accomplish these goals.³ To create a trust, a fiduciary relationship must be formed

* J.D. Candidate, University of Wyoming College of Law, 2015. Thank you to Bailey Schreiber, Kyle Hendrickson, Brianne Phillips, Professor Mark Glover, and the rest of the *Wyoming Law Review* Board for their assistance and guidance throughout the writing process. A big thank you to my fiancé, David Singleton, and my parents, Greg and Jodie. This paper would not have been possible without your encouraging words and continuous support.

¹ This maxim, meaning “whose it is to give, his it is to dispose,” has been used to justify the use of spendthrift trusts. See Gideon Rothschild & Daniel S. Rubin, *Planning with Spendthrift Trusts*, 1.4 ESTATE TAX PLANNING ADVISOR 1 (May 2002), available at <http://www.mosessinger.com/site/files/spendthrift.pdf>.

² *Id.*

³ Trusts have become increasingly popular tools for individuals to express their intentions for transferring assets to loved ones. Christopher M. Reimer, *The Undiscovered Country: Wyoming's Emergence as a Leading Trust Situs* Jurisdiction, 11 WYO. L. REV. 165, 167 (2011) (“Trusts have

requiring one person to hold property subject to an equitable obligation to keep or distribute that property for the benefit of another.⁴ Generally, a trust does not, in and of itself, prevent a beneficiary's creditors from reaching trust assets. However, a spendthrift trust contains a "spendthrift provision" prohibiting the beneficiary of a trust from voluntarily transferring an interest in the trust to a third party.⁵ The spendthrift provision also prevents creditors from reaching the trust through garnishment or attachment.⁶ Thus, a spendthrift trust is a beneficial way for a grantor to transfer assets to a beneficiary without the risk of creditor attachment.

A more recent development in estate planning is the self-settled spendthrift trust, also known as the "asset protection trust:" a trust created by an individual for his or her own benefit.⁷ Usually, spendthrift provisions are unenforceable when the trust is self-settled, meaning that the individual creating the trust is also the beneficiary.⁸ Historically, courts have found self-settled spendthrift trusts inherently fraudulent because the trusts allow debtors to insulate themselves from the claims of creditors.⁹ Therefore, courts have found self-settled spendthrift trusts to be unenforceable; once the spendthrift provision is found to be unenforceable, creditors may obtain judgments from the trust assets.¹⁰ However, in recent years, a number of states have passed statutes allowing settlors to shield assets from creditors in self-settled trusts.¹¹ Wyoming is one of these states.¹²

historically been employed by the very wealthy; however, as they have grown in popularity over the last few decades, their use as an estate planning tool has expanded among the middle and upper-middle classes."); Abigail Maurer, *Chapter 106: In Hearsay We Trust*, 42 MCGEORGE L. REV. 567, 567 (2011) ("Revocable trusts are one of the most common testamentary devices used in estate planning."); Steven Seidenberg, *Plotting Against Probate: Efforts by Estate Planners, Courts and Legislatures to Minimize Probate Haven't Killed It Yet*, 94 A.B.A. J. 57, 58 (May 2008) ("There is, for instance, a boom in revocable living trusts.").

⁴ AMY MORRIS HESS, GEORGE GLEASON BOGERT, & GEORGE TAYLOR BOGERT, *BOGERT'S TRUST AND TRUSTEES* § 1 (2014).

⁵ Richard C. Ausness, *The Offshore Asset Protection Trust: A Prudent Financial Planning Device or the Last Refuge of a Scoundrel*, 45 DUQ. L. REV. 147, 150 (2007).

⁶ *Id.*

⁷ See *infra* note 39 and accompanying text.

⁸ Timothy O. Beppler & Christopher M. Reimer, *Domestic Asset Protection Trusts: A Comparison of the Laws of Utah and Wyoming*, 23 UTAH B.J. 12, 12 (Apr. 2010); Ausness, *supra* note 5, at 150.

⁹ Ausness, *supra* note 5, at 183; Adam J. Hirsch, *Fear Not the Asset Protection Trust*, 27 CARDOZO L. REV. 2685, 2685 (2006) ("The dawn of this new species of domestic "asset protection trust" has aroused declarations—and declamations—of concern, much as its close relative and doctrinal progenitor, the spendthrift trust, once did.").

¹⁰ See *e.g.*, *Dexia Credit Local v. Rogan*, 624 F. Supp.2d 970, 976 (N.D. Ill. 2009); *In re Kuraishi*, 237 B.R. 172, 176–77 (Cal. C.D. 1999); *Security Pacific Bank Washington v. Chang*, 80 F.3d 1412, 1418 (9th Cir. 1996); *In re Brown*, 303 F.3d 1261, 1271 (11th Cir. 2002).

¹¹ Beppler & Reimer, *supra* note 8, at 12.

¹² WYO. STAT. ANN. §§ 4-10-510 to -523 (2013).

This comment argues the Wyoming self-settled spendthrift trust, known as the Qualified Spendthrift Trust, is a beneficial component to Wyoming's Uniform Trust Code. It looks at the history of asset protection trusts and the development of domestic asset protection trust statutes.¹³ Next, it discusses common criticisms of self-settled spendthrift trusts.¹⁴ Finally, this comment argues that states should follow Wyoming's lead in creating self-settled spendthrift trust statutes for three reasons.¹⁵ First, the self-settled spendthrift trust provides substantial benefits to settlors.¹⁶ Second, there are significant economic considerations for allowing self-settled spendthrift trusts.¹⁷ Third, Wyoming's statute provides sufficient limitations of the self-settled spendthrift trust to protect against abuse and defrauding of creditors.¹⁸

II. BACKGROUND

A trust is a legal arrangement in which a settlor appoints a trustee to hold property as a fiduciary for one or more beneficiaries.¹⁹ A valid trust must include a settlor and trustee, intent to create a trust, ascertainable trust res, sufficiently ascertainable beneficiaries, a legal purpose, and a legal term.²⁰ The settlor is the individual who creates the trust.²¹ Creation includes, but is not limited to, designating beneficiaries, declaring terms for distribution, designating a trustee and successor trustee, and determining what property will be transferred into the trust.²²

At the time the trust is created, the trustee takes legal title to the trust property.²³ A trustee can be either an individual or an entity.²⁴ The trustee's role is to manage

¹³ See *infra* Part II.C–E.

¹⁴ See *infra* Part II.G–H.

¹⁵ See *infra* Part III.

¹⁶ See *infra* Part III.A.

¹⁷ See *infra* Part III.B.

¹⁸ See *infra* Part III.C.

¹⁹ HESS ET AL., *supra* note 4, § 1.

²⁰ Hilbert v. Benson, 917 P.2d 1152 (Wyo. 1996). In another case, the Wyoming Supreme Court stated:

The clearly expressed intention of the settlor should be zealously guarded by the courts, particularly when the trust instrument reveals a careful and painstaking expression of the use and purposes to which the settlor's financial accumulations shall be devoted. A settlor must have assurance that his solemn arrangements and instructions will not be subject to the whim or suggested expediency of others after his death.

First Nat. Bank & Trust Co. of Wyo. v. Brimmer, 504 P.2d 1367, 1371 (Wyo. 1973).

²¹ HESS ET AL., *supra* note 4, § 41.

²² *Id.*

²³ First Nat'l Bank of Cincinnati v. Tenney, 138 N.E.2d 15, 18–19 (Ohio 1956) (“In order for a trust to be a trust, the legal title of the *res* must immediately pass to the trustee, and the beneficial or equitable interest to the beneficiaries.”).

²⁴ HESS ET AL., *supra* note 4, § 121.

the settlor's property in the best interest of the beneficiaries.²⁵ The trustee must make disbursements of income and principal to beneficiaries in accordance with the terms of the trust agreement.²⁶ Trustees often have the discretion to invest trust property with the intent of furthering the trust's purpose.²⁷ Trustees also have the responsibility of recordkeeping and accounting, as well as bringing and defending claims on behalf of the trust.²⁸

Beneficiaries have equitable title, which allows them to hold the trustee accountable for breach of the trustee's fiduciary duties.²⁹ Typically, beneficiaries are entitled to periodic distributions from the trust income and sometimes from the trust principal as well.³⁰ Trustees can distribute income of the trust to the beneficiary at intervals specified in the trust, therefore allowing the beneficiary to receive a steady stream of income, rather than one large gift.³¹ Trusts can be used for a number of purposes—everything from providing financial support for a surviving spouse and children to structuring payments in order to reduce estate taxes.³²

A. Spendthrift Trusts

While once controversial, all states now recognize spendthrift trusts in some form or another.³³ A spendthrift trust is a trust document that includes a spendthrift provision specifically prohibiting the beneficiary from alienating their interest to a third party. A beneficiary of a trust *without* a spendthrift provision generally has the freedom to transfer or assign their interest in the trust to

²⁵ RESTATEMENT (THIRD) OF TRUSTS § 2 cmt.b (2003).

²⁶ Joanne E. Hindel et al., *Discretionary, Delegating, or Directed: Duties and Responsibilities of Trustees*, 17 OHIO PROB. L.J. 187, 187 (2007).

²⁷ *Id.*

²⁸ *Id.*

²⁹ *Id.*; see Stewart E. Sterk, *Trust Protectors, Agency Costs, and Fiduciary Duty*, 27 CARDOZO L. REV. 2761, 2761 (2006) (“[A] number of familiar fiduciary duties—including the duty of impartiality, the duty to invest for total return, and the duty of care—operate to align the interests of the trustee with those of the settlor and the beneficiaries.”).

³⁰ Adam J. Hirsch, *Spendthrift Trusts and Public Policy: Economic and Cognitive Perspectives*, 73 WASH. U.L. Q. 1, 2 (1995).

³¹ *Id.*

³² AMERICAN BAR ASSOCIATION, *Trusts 1*, available at http://www.americanbar.org/content/dam/aba/migrated/publiced/practical/books/wills/chapter_4.authcheckdam.pdf (“A trust can do a number of things a will can't do, as well, including manage assets efficiently if you should die and your beneficiaries are minor children or others not up to the responsibility of handling the estate; protect your privacy (unlike a will, a trust is confidential); depending on how it is written, and on state law, a trust can protect your assets by reducing taxes; if it is a living trust, the trustee can manage property for you while you're alive, providing a way to care for you if you should become disabled. A living trust also avoids probate, lowers estate administration costs, and speeds transfer of your assets to beneficiaries after your death.”).

³³ HESS ET AL., *supra* note 4, § 222 n.64.

another.³⁴ Additionally, a creditor seeking repayment from the beneficiary could attach a lien to the assets of the trust if that trust *did not* contain a spendthrift provision. A typical spendthrift provision reads:

Except for transfers among family members, no beneficiary of a trust shall alienate, encumber or hypothecate his or her interest in the principal or income of a trust in any manner; and to the fullest extent of the law, the interests of any beneficiary shall not be subject to the claims of his or her creditors or be liable to attachment, execution or other process of law. Further, the interest of each beneficiary in the income and principal of the trust hereunder shall be free from the control or interference of any creditor of a beneficiary or any spouse of any married beneficiary and shall not be subject to attachment or susceptible of anticipation or alienation. Nothing contained in this paragraph shall be construed as restricting in any way the exercise of any powers or discretions granted hereunder.³⁵

A spendthrift trust usually contains two common provisional restrictions. First, a spendthrift provision prevents a beneficiary from voluntarily assigning his interest in the trust to another.³⁶ For example, the spendthrift provision prohibits the beneficiary from using his interest in the trust as collateral for a loan or assigning the interest over to pay off a debt to a creditor. Second, a spendthrift provision prevents a creditor from reaching the beneficiary's interest in the trust.³⁷ The creditor generally cannot attach a lien or otherwise access the trust assets.³⁸ The creditor, however, can reach the beneficiary's interest in the trust once the beneficiary actually receives the distribution.³⁹ Once the trustee makes a distribution of trust income to the beneficiary, that money and/or property becomes freely alienable.

Settlers began to include spendthrift provisions in their trusts to keep beneficiaries from squandering their interest by handing it over to creditors.⁴⁰ Often this is a concern when parents are transferring wealth to children with a

³⁴ *Id.*; Justin W. Stark, *Montana's Spendthrift Trust Doctrine: Analysis and Recommendations*, 57 MONT. L. REV. 211, 212 (1996).

³⁵ *Mason v. Mason*, 798 So.2d 895, 897 (D. Fla. 2001).

³⁶ William H. Wicker, *Spendthrift Trusts*, 10 GONZ. L. REV. 1, 1 (1974).

³⁷ *Id.*

³⁸ Hirsch, *supra* note 30, at 2.

³⁹ WYO. STAT. ANN. § 4-10-502(c) (2015). (“[A] beneficiary may not transfer an interest in a trust in violation of a spendthrift provision and, a creditor or assignee of the beneficiary may not reach the interest or attach a distribution by the trustee unless and until it is received by the beneficiary.”).

⁴⁰ Alan Newman, *The Rights of Creditors of Beneficiaries Under the Uniform Trust Code: An Examination of the Compromise*, 69 TENN. L. REV. 771, 772 (2002).

poor credit history or spending habits. Spendthrift trusts can also be used for mentally incompetent individuals who the settlor believes are unable to manage their own affairs.⁴¹ The settlor might also include a spendthrift provision when he wants to ensure that the beneficiary uses the trust assets for a specific purpose, such as education.⁴²

B. Traditional Approach to Self-Settled Spendthrift Trusts/Asset Protection Trusts

A self-settled spendthrift trust, also known as an “asset protection trust,” is a trust created by the settlor for his or her own benefit.⁴³ Historically, the general rule for self-settled spendthrift trusts is that the trust does not shield the settlor/beneficiary from claims of creditors.⁴⁴ In *Matter of Brooks*, the United States Court of Appeals for the Fifth Circuit stated this general rule was designed to prevent the settlor from accessing assets of the trust while simultaneously insulating these same assets from creditors.⁴⁵ The Fifth Circuit also held the general rule prevented debtors from withdrawing funds for their own benefit immediately after all debts were discharged.⁴⁶ In other words, “[o]ne may wish to have one’s cake and eat it, too, but the law need not bring the wish to fruition.”⁴⁷

The United States Court of Appeals for the Eleventh Circuit also held that a self-settled spendthrift trust was unenforceable against the settlor’s creditors; the court found it was immaterial whether there was an intent to defraud or whether the settlor was solvent at the time.⁴⁸ Further, a California bankruptcy court found a self-settled spendthrift trust unenforceable regardless of the fact that the primary purpose of the trust was to be used to pay the individual’s pension.⁴⁹

⁴¹ *Trusts*, *supra* note 32, at 8.

⁴² *Id.*

⁴³ Amy Lynn Wagenfeld, *Law for Sale: Alaska and Delaware Compete for the Asset Protection Trust Market and the Wealth that Follows*, 32 VAND. J. TRANSNAT’L L. 831, 839 (1999) (“To create this ideal trust a settlor transfers his assets into trust, names himself as a beneficiary, includes a provision that the trust holdings may not be voluntarily or involuntarily alienated prior to distribution, and appoints as trustee either himself or a third party over whom he retains certain powers.”).

⁴⁴ UNIF. TRUST CODE § 505 cmt. (2010) (“Subsection(a)(2) . . . follows traditional doctrine in providing that a settlor who is also a beneficiary may not use the trust as a shield against the settlor’s creditors. The drafters of the Uniform Trust Code concluded that traditional doctrine reflects sound policy. Consequently, the drafters rejected the approach taken in States like Alaska and Delaware, both of which allow a settlor to retain a beneficial interest immune from creditor claims.”); RESTATEMENT (SECOND) OF TRUSTS § 156(1) (2014) (“Where a person creates for his or her own benefit a trust with a provision restraining the voluntary or involuntary transfer of his interest, his transferee or creditors can reach his interest.”).

⁴⁵ *Matter of Brooks*, 844 F.2d 258, 261 (5th Cir. 1988).

⁴⁶ *Id.*

⁴⁷ *In re Robbins*, 826 F.2d 293, 295 (4th Cir. 1987).

⁴⁸ *In re Brown*, 303 F.3d 1261, 1268 (11th Cir. 2002).

⁴⁹ *In re Kuraishi*, 237 B.R. 172 (Cal. C.D. 1999).

C. *Offshore Asset Protection Trusts*

Due to the restrictions in the United States on self-settled spendthrift trusts (asset protection trusts), settlors began creating these trusts offshore to protect assets.⁵⁰ Offshore asset protection trusts are established in foreign jurisdictions by settlors who wish to keep assets out of reach of domestic creditors.⁵¹ The formation of an offshore asset protection trust is similar to the creation of a self-settled spendthrift trust in the United States, except these trusts are formed under laws of a foreign jurisdiction—a jurisdiction that enforces self-settled trusts.⁵² The beneficiary of an offshore protection trust is the settlor or the settlor's family members, and the trustee is generally a foreign trust company or financial institution.⁵³ These foreign trusts force creditors to bring actions in foreign jurisdictions that are generally more “debtor friendly” and find self-settled spendthrift trusts valid.⁵⁴ However, offshore asset protection trusts are not always successful.⁵⁵ For example, real property is governed by the location of the property.⁵⁶ Therefore, actions concerning United States property will be adjudicated domestically, and therefore, a foreign trust will still be subject to creditor attachment.⁵⁷

In 1994, it was estimated that more than one trillion dollars of foreign trust funds were in asset protection trusts.⁵⁸ Settlors favored these offshore trusts because foreign trusts are less accessible and, for the most part, are free from the constraints of United States law.⁵⁹ However, offshore asset protection trusts were, and still are, heavily criticized.⁶⁰ It has been argued that these offshore trusts “offend the public policy of the overwhelming majority of American states,”

⁵⁰ Ausness, *supra* note 5, at 151–52; Jonathan L. Mezrich, *It's Better in the Bahamas: Asset Protection Trusts for the Pennsylvania Lawyer*, 98 DICK. L. REV. 657, 675 (1994) (“[A]sset protection is simply a reasonable reaction to today's ‘court-happy’ society, and should be allowed until the U.S. judiciary or legal community finds a way to rein-in damaging, frivolous lawsuits and litigiousness.”).

⁵¹ Ausness, *supra* note 5, at 152.

⁵² Elena Marty-Nelson, *Offshore Asset Protection Trusts: Having Your Cake and Eating it Too*, 47 RUTGERS L. REV. 11, 13 (1994).

⁵³ *Id.*

⁵⁴ Paul M. Roder, *American Asset Protection Trusts: Alaska and Delaware Move ‘Offshore’ Trusts onto the Mainland*, 49 SYRACUSE L. REV. 1253, 1257 (1999).

⁵⁵ *Id.* at 1259–61.

⁵⁶ *Id.* at 1260.

⁵⁷ *Id.*

⁵⁸ Ritchie W. Taylor, *Domestic Asset Protection Trusts: The “Estate Planning Tool of the Decade” or a Charlatan?*, 13 BYU J. Pub. L. 163, 164 (1998).

⁵⁹ Reimer, *supra* note 19, at 168.

⁶⁰ See *infra* Part II.G.

frustrate domestic courts' jurisdiction, and disregard public policy.⁶¹ Still, others see that there are ethical and unethical ways to use such trusts.⁶²

D. Statutory Self-Settled Spendthrift Trusts

As of April 2014, sixteen states, including Wyoming, have passed legislation allowing for self-settled spendthrift trusts/asset protection trusts, similar to off-shore trusts.⁶³ While each statute attempts to achieve the goal of asset protection, they vary in formation requirements, protection exceptions, and burden of proof requirements for fraudulent transfer actions.⁶⁴ This section will look at four of these statutes, comparing some of the similarities and differences from state to state.

In 1997, Alaska and Delaware became the first two states to enact legislation allowing for self-settled spendthrift trusts.⁶⁵ For a trust to come under the protection of Alaska and Delaware's statutes, the trust must be irrevocable, must expressly state that it is governed by that state's law, and must contain a spendthrift provision.⁶⁶

However, there are exceptions to both Delaware and Alaska's statutes; these exceptions make trust assets vulnerable to certain creditor claims. Delaware does not shield trust assets from child support claims, alimony payments, or property division upon divorce.⁶⁷ Therefore, individuals in arrears of their support obligations are unable to avoid making payments by safeguarding assets within the trust.⁶⁸ Delaware's asset protection also does not apply to "any person who suffers death, personal injury or property damage . . . caused in whole or in part by the tortious act or omission of either such transferor or by another person for

⁶¹ Randall J. Gingiss, *Putting a Stop to "Asset Protection" Trusts*, 51 BAYLOR L. REV. 987, 1032 (1999); *E.T.C. v. Affordable Media*, 179 F.3d 1228, 1240 (9th Cir. 1999); *In re Lawrence*, 251 B.R. 630 (Fla. S.D. 2000) ("[S]uch a strategy contravenes the clear public policy against allowing a debtor to shield money placed in a trust for his or her own benefit from creditors, [and] defies common sense.").

⁶² *Breitenstine v. Breitenstine*, 62 P.3d 587, 593 (Wyo. 2003) ("While such trusts may have benefits in asset protection, the use of such trusts to avoid alimony, child support, and a fair division of marital property upon divorce is reprehensible to us.").

⁶³ David G. Shaftel, *Comparison of the Domestic Asset Protection Trust Statutes*, AMERICAN COLLEGE OF TRUST AND ESTATE COUNSEL (Apr. 2014). These states are Alaska, Colorado, Delaware, Hawaii, Mississippi, Missouri, New Hampshire, Nevada, Ohio, Oklahoma, Rhode Island, South Dakota, Tennessee, Utah, Virginia, and Wyoming.

⁶⁴ *Id.*

⁶⁵ ALASKA STAT. §§ 13.36.310, 34.40.110 (2015); DEL. CODE ANN. tit. 12, §§ 3570–3576 (2015); Wagenfeld, *supra* note 38, at 831.

⁶⁶ ALASKA STAT. §§ 13.36.310, 34.40.110 (2015); DEL. CODE ANN. tit. 12, §§ 3570–3576 (2015).

⁶⁷ DEL. CODE ANN. tit. 12, §§ 3573 (2015).

⁶⁸ *Id.*

whom such transferor is or was vicariously liable.⁶⁹ Thus, plaintiffs are allowed to collect judgments from trust assets on these claims. Alaska, however, has fewer exceptions to the asset protection rule. Alaska does not provide an exception for alimony payments or tort claims and only provides a limited exception for child support claims and property division upon divorce.⁷⁰

Lastly, both statutes provide exceptions for fraudulent transfers, requiring a showing of intent to defraud.⁷¹ This exception allows the creditor to reach trust assets regardless of the spendthrift provision when it is shown that the settlor intended to avoid payment.⁷²

One of the most settlor-friendly states for creating an asset protection trust is Nevada. Nevada's statute allows a self-settled spendthrift trust to shelter trust assets against child support obligations, alimony claims, tort actions, and property division upon divorce.⁷³ The state legislature does, however, apply the Uniform Fraudulent Transfer Act (UFTA) to set aside transfers made with the intent to hinder, delay, or defraud creditors.⁷⁴ The UFTA prohibits a debtor from avoiding paying a debt by transferring the money or asset to another person before the debt is collected.⁷⁵ Among other things, the UFTA looks at whether the assets were concealed, whether adequate consideration was given when the property was transferred, and whether the debtor still had possession and control of the property even after the transfer.⁷⁶

Much like the exceptions to creditor protection, formation requirements for self-settled spendthrift trusts vary from state to state. Formation requirements are the essential elements the trust must include before it is entitled to spendthrift protection, such as restrictions on revocation and an explicit spendthrift clause. For example, most asset protection trust statutes require the trust be irrevocable.⁷⁷

⁶⁹ *Id.*

⁷⁰ ALASKA STAT. §§ 34.40.1109(b)(4) & (l) (2015).

⁷¹ ALASKA STAT. §§ 34.40.110 (2015) (“[T]he transfer restriction prevents a creditor . . . from satisfying a claim out of a beneficiary’s interest in the trust, unless the creditor . . . establishes by clear and convincing evidence that the settlor’s transfer of property in trust was made with intent to defraud that creditor.”); DEL. CODE ANN. tit. 12, § 3572 (2015) (“[N]o action should be brought . . . unless the qualified disposition was made with actual intent to defraud such creditor.”).

⁷² *See* ALASKA STAT. §§ 34.40.110 (2015); DEL. CODE ANN. tit. 12, § 3572 (2015).

⁷³ NEV. REV. STAT. §§ 166.010 to -.170 (2015).

⁷⁴ *Id.* §§ 166.170, 112.180.

⁷⁵ NAT’L CONFERENCE OF COMM’RS ON UNIFORM STATE LAWS, UNIFORM FRAUDULENT TRANSFERS ACT (1984), available at https://www.stcl.edu/faculty_pages/faculty_folders/rosin/ufta84.pdf.

⁷⁶ *Id.* § 4.

⁷⁷ *See e.g.*, S.D. CODIFIED LAWS § 55-16-2 (2015); TENN. CODE ANN. § 35-16-102(7) (2015); UTAH CODE ANN. § 25-6-14 (2015); HAW. REV. STAT. § 554G-2 (2015).

However, Oklahoma allows both revocable and irrevocable trusts to safeguard assets.⁷⁸ Despite the variability from state to state, goals of self-settled spendthrift trust statutes are the same—protect the settlor from unintended alienation while providing public policy exceptions for creditors who are more vulnerable to fraudulent behavior.

E. Wyoming's Qualified Spendthrift Trust

In 2007, Wyoming passed a statute allowing “Qualified Spendthrift Trusts” (QST).⁷⁹ Wyoming allows a settlor to create a self-settled spendthrift trust if the instrument states it is a “Qualified Spendthrift Trust,” governed by Wyoming law, subject to a spendthrift provision, and is irrevocable.⁸⁰ Wyoming defines a “spendthrift provision” as “a term of a trust which restrains either a voluntary or an involuntary transfer, or both, of a beneficiary’s interest.”⁸¹ Only qualified trust property can be held in a QST. “Qualified trust property includes real property, personal property and interests in real or personal property . . . which: (i) Are the subject of a qualified transfer; and (ii) Are acquired with the proceeds of property of a qualified transfer.”⁸² A “qualified transfer” is a transfer, conveyance, or assignment of property to a qualified trustee with or without consideration.⁸³

The statute also requires a qualified transfer affidavit, written and sworn by the settlor.⁸⁴ In the affidavit, the settlor must state they have the “full right, title, and authority to transfer the property to the qualified spendthrift trust,” the property was not obtained through unlawful means, the transfer will not render the settlor insolvent, and the transfer is not intended to defraud any creditors.⁸⁵ The settlor must also assert that there is no pending litigation against him, and that he is not currently involved in any administrative proceedings.⁸⁶ The affidavit also ensures the settlor is not in default of any child support obligations or contemplating bankruptcy.⁸⁷ Finally, the settlor must maintain one million dollars in personal liability insurance or provide coverage equal to the fair market value of the trust assets, whichever is less.⁸⁸

⁷⁸ OKLA. STAT. tit. 31 § 11(5) (2015).

⁷⁹ WYO. STAT. ANN. §§ 4-10-510 to -523 (2013).

⁸⁰ *Id.* § 4-10-510; Beppler & Reimer, *supra* note 8, at 15.

⁸¹ WYO. STAT. ANN. § 4-10-103(a)(xix) (2013).

⁸² *Id.* § 4-10-511.

⁸³ *Id.* § 4-10-512.

⁸⁴ *Id.* § 4-10-523.

⁸⁵ *Id.*

⁸⁶ *Id.*

⁸⁷ *Id.*

⁸⁸ *Id.*

Creditors have limited ability to reach QST property under Wyoming statute. The property of the trust is not subject to claims of creditors unless the creditor can prove by clear and convincing evidence that it was a fraudulent transfer in violation of the Uniform Fraudulent Transfers Act.⁸⁹ *Each* creditor must produce proof of a fraudulent transfer—“proof by one creditor, assignee or agent that a transfer of property to a QST was fraudulent or wrongful does not constitute proof as to any other creditor.”⁹⁰

However, there are other circumstances, beyond fraudulent conveyances, when the QST does not shield a debtor’s assets.⁹¹ First, similar to other states’ statutes, the spendthrift provision is not enforceable against child support claims.⁹² Second, the provision is unenforceable against “[a] financial institution with which the settlor has listed qualified trust property on the financial institution’s application or financial statement used to obtain or maintain credit from the financial institution other than for the benefit of the QST.”⁹³

F. Criticisms of Self-Settled Spendthrift Trusts/Asset Protection Trusts

Self-settled spendthrift trusts receive substantial criticism. Those opposing self-settled spendthrift trusts argue these trusts “give unexampled opportunity to unscrupulous persons to shelter their property before engaging in speculative business enterprises.”⁹⁴ Opponents conclude the trusts “promote a culture in which individuals are not held accountable for their actions.”⁹⁵ It encourages people to engage in risky behavior with the assurance of knowing they are protected from losing their shielded assets.⁹⁶

Critics believe that self-settled spendthrift trusts “mislead creditors into thinking the settlor still owned the property since he appeared to be receiving its income, and thereby work a gross fraud on creditors who might place reliance on the former prosperity and financial stability of the debtor.”⁹⁷ Opponents of

⁸⁹ *Id.* § 4-10-517.

⁹⁰ *Id.*

⁹¹ *Id.* § 4-10-520.

⁹² *Id.*

⁹³ *Id.*

⁹⁴ Richard C. Ausness, *supra* note 5, at 184.

⁹⁵ Kevin R. McKinnis, *The Good, the Bad, and a New Kind of Prenup: An Analysis of the Ohio Legacy Trust Act and What Asset Protection Trusts Will Mean for Ohio*, 61 CLEV. ST. L. REV. 1105, 1125 (2013).

⁹⁶ *Id.* at 1125–26.

⁹⁷ *Id.*

the self-settled trust also fear these trusts can be deceptive—“creating a false appearance of creditworthiness[,]” thereby allowing debtors to fool creditors into loaning money while their assets sit protected and out of creditor reach.⁹⁸

A common criticism of asset protection trusts is that they are unethical and inherently fraudulent—they allow settlors to avoid paying their debts.⁹⁹ Critics argue that passing self-settled spendthrift trust statutes is “an unfortunate trend, heralding the onset of a race among the states to provide the most attractive forum for trust business.”¹⁰⁰ Some argue there is no equal protection of the law because only the wealthy have the means to fund such trusts.¹⁰¹ Additionally, critics argue creditors would have to be even more diligent in screening their borrowers before loaning money, resulting in increased administrative costs to lenders.¹⁰²

It is also argued that self-settled spendthrift trusts will make defendants judgment proof, “provid[ing] a way for doctors, lawyers, or other professionals to shield personal assets from malpractice and other tortious claims.”¹⁰³ These trusts would subsequently prevent creditors and plaintiffs from obtaining judgments awarded to them in lawsuits.¹⁰⁴

III. ANALYSIS

Despite the common criticisms and hesitations of allowing self-settled spendthrift trusts, Wyoming’s self-settled spendthrift trust is a beneficial component to Wyoming’s Uniform Trust Code, and states should follow Wyoming’s lead for three reasons. First, the self-settled spendthrift trust provides substantial benefits to settlors.¹⁰⁵ Second, there are significant economic considerations for allowing self-settled spendthrift trusts.¹⁰⁶ Finally, Wyoming’s statute provides sufficient limitations of the self-settled spendthrift trust to protect against the abuse and the defrauding of creditors.¹⁰⁷

⁹⁸ Hirsch, *supra* note 9, at 2687; Ausness, *supra* note 5, at 184.

⁹⁹ Darsi Newman Sirknen, *Domestic Asset Protection Trusts: What’s the Big Deal?*, 8 TRANSACTIONS: TENN. J. BUS. L. 133, 142 (2006)

¹⁰⁰ Hirsch, *supra* note 9, at 2686 (citations omitted).

¹⁰¹ Sirknen, *supra* note 99, at 143.

¹⁰² McKinnis, *supra* note 95, at 1125.

¹⁰³ *Id.* at 1120–22.

¹⁰⁴ *Id.* at 1125.

¹⁰⁵ See *infra* Part III.A.

¹⁰⁶ See *infra* Part III.B.

¹⁰⁷ See *infra* Part III.C.

A. *Benefits of the Self-Settled Spendthrift Trust to the Settlor*

The self-settled spendthrift trust provides substantial benefits to settlors, and state legislatures seem to agree. The Wyoming legislature and the legislatures in fifteen other states have decided that an asset protection trust is not inherently fraudulent.¹⁰⁸ While critics have argued that self-settled spendthrift trusts are inherently fraudulent, these trusts can be created for non-fraudulent purposes, such as safeguarding assets for loved ones while allowing settlors to maintain control over asset distribution. In addition to asset protection, transfer tax minimization is also a non-fraudulent purpose for establishing a self-settled spendthrift trust.¹⁰⁹

The most obvious benefit of a self-settled spendthrift trust is that trust property is shielded from involuntary creditors, such as tort claimants.¹¹⁰ Self-settled spendthrift trusts serve as “a safeguard against financial uncertainties and unanticipated litigation.”¹¹¹ The United States’ litigation system is often viewed as pro-plaintiff, giving injured plaintiffs more than their fair share when it comes to monetary judgments.¹¹² Proponents of self-settled spendthrift trusts argue such trusts protect settlors from meritless claims.¹¹³ While all people should pay their bills, “not all bills are just.”¹¹⁴ “Deep pocket defendants” frequently become targets of tort litigation.¹¹⁵ The self-settled spendthrift trust is less of a means to

¹⁰⁸ See *supra* notes 35–36 and accompanying text.

¹⁰⁹ David G. Shaftel, *Comparison of the Domestic Asset Protection Trust Statutes*, AMERICAN COLLEGE OF TRUST AND ESTATE COUNSEL (April 2014).

¹¹⁰ Sirknen, *supra* note 99, at 144–45; see Paul M. Roder, *American Asset Protection Trusts: Alaska and Delaware Move ‘Offshore’ Trusts onto the Mainland*, 49 SYRACUSE L. REV. 1253 (1999) (“Professionals exposed to malpractice suits, such as doctors, lawyers, and accountants, and business officers and directors exposed to toxic tort liability, as well as those individuals who fear hefty divorce settlements, all have sought the protection afforded in offshore asset protection trusts.”).

¹¹¹ Susanna C. Brennan, *Changes in Climate: The Movement of Asset Protection Trusts from International to Domestic Shores and its Effect on Creditor’s Rights*, 79 OR. L. REV. 755, 765 (2000) (“The growing popularity of asset protection and its supporting industry most likely occurred in response to economic and social factors including the increase in litigation and legal liability.”).

¹¹² Sirknen, *supra* note 99, at 144–45 (stating that the American judicial system permits “attorneys [to] move mass tort cases into states or jurisdictions with favorable regimes, due to plaintiff-leaning legal rules, pro-plaintiff judges, pro-plaintiff juries, and judicial ‘innovations’ such as consolidations or bouquet trials that substantially increase expected jury awards”); James R. Copland, *Administrative Compensation for Pharmaceutical and Vaccine-Related Injuries*, 8 IND. HEALTH L. REV. 275, 282–83 (2010–2011).

¹¹³ Sirknen, *supra* note 99, at 144 (“[I]n a system where persons are . . . unwilling to accept responsibility for their own actions, even if they are negligent, why should . . . anyone else wonder why there is also some number of persons unwilling to accept responsibility for their own liabilities?”); Henry J. Lischer, Jr., *Domestic Asset Protection Trusts: Pallbearers to Liability?*, 35 REAL PROP. PROB. & TR. J. 479, 526 (2000).

¹¹⁴ Sirknen, *supra* note 99, at 144.

¹¹⁵ See Judith Camile Glasscock, *Emptying the Deep Pocket in Mass Tort Litigation*, 18 ST. MARY’S L.J. 977, 979 (1987).

avoid debts and more a mechanism to protect individuals from losing everything they have spent years earning.¹¹⁶

Others see the possibility of forming the trust as a form of protecting against their own compulsion to spend.¹¹⁷ Individuals that come into wealth may have the inability to control their urge to spend; self-settled spendthrift trusts can be used as a tool to restrain excess spending.¹¹⁸ The self-settled spendthrift trust can be structured to only allow for periodic distributions; thus, these periodic distributions can limit the distribution amount to what is necessary for the individual to live on. It also prevents them from borrowing against their assets by taking the trust res out of the ownership of the settlor.¹¹⁹ Together, these benefits to individuals of allowing self-settled spendthrift trusts weigh heavily against any risk for abuse.

B. Economic Considerations for Allowing Self-Settled Spendthrift Trusts

In addition to benefitting the settlor, there are significant economic considerations for allowing self-settled spendthrift trusts. From an economic perspective, self-settled spendthrift trust statutes benefit the United States by attracting trust business to local banks and trust companies.¹²⁰ These statutes allow sizeable domestic investment and make offshore trusts inessential.¹²¹ Keeping trust business in the states will benefit the United States economy considerably.¹²² It is better to keep trust business domestic by endorsing a restricted self-settled spendthrift trust rather than invalidating these trusts and pushing settlors into foreign jurisdictions to protect their assets.

For Wyoming, allowing for self-settled spendthrift trusts means investments are made within the state, ultimately boosting the state's economy and bringing

¹¹⁶ *Id.* (“Excessive awards have resulted in economic disaster to some American business enterprises.”). “For the most part, asset protection settlors will have honest motives and should be allowed to protect the assets they have amassed through years of working and prudent investing.” Sirknen, *supra* note 99, at 159.

¹¹⁷ Hirsch, *supra* note 9, at 2711 (“Persons who recognize in themselves a compulsion to overspend and overborrow may wish to establish an asset protection trust in order to shield their assets from their own weaknesses of will, and they may be content to suffer, or even seek to contrive, their own exile from the market for credit.”).

¹¹⁸ *Id.*

¹¹⁹ *Id.*

¹²⁰ Hirsch, *supra* note 9, at 2687; Sirknen, *supra* note 99, at 150 (“Corporate trustees, estate planning lawyers, and settlors presumably all benefit financially from the use of [asset protection trusts].”).

¹²¹ Sirknen, *supra* note 99, at 79.

¹²² *Id.*

jobs to Wyoming.¹²³ Wyoming is considered a trust-friendly state.¹²⁴ Not only does Wyoming have the QST statute, but Wyoming also has no state income tax, has a 1000-year term for the rule against perpetuities for trusts, discretionary trusts, directed trusts, purpose trusts, and has unregulated private trust companies.¹²⁵ Clay D. Geittmann, a fellow of the American College of Trust and Estate Counsel, discussed the benefits of the QST. He argues that it is “one more step in making Wyoming a competitor, if not a leader, in the area of trust law.”¹²⁶ He, too, recognized the importance of the protections within Wyoming’s statute: “[T]he principal drafters strived to provide a mechanism for the creation of self-settled asset protection trusts while discouraging the abuse of these trusts by those who would use them to defraud creditors. The goal was really to keep Wyoming competitive but not to attract disreputable persons and business.”¹²⁷ The QST has become an effective mechanism for individuals to transfer wealth and has helped Wyoming remain a leading jurisdiction for trust formation. These economic considerations are just one more reason why states should follow the lead of Wyoming and pass self-settled spendthrift trust legislation similar to Wyoming’s QST.

C. *Statutory Limitations Protect Against Abuse and Fraud*

Despite the benefits to settlors and the economy, there are still risks for abuse and fraud when allowing individuals to shield their assets behind self-settled spendthrift trusts. Despite the risks, Wyoming statute provides sufficient limitations on the self-settled spendthrift trust to protect against any fraud or abuse. The statute requires the trust to be irrevocable, preventing the settlor from treating the trust as a shell for the sole purpose of defrauding creditors; it requires complete relinquishment of trust corpus. In addition to requiring the trust be irrevocable, the sworn affidavit requires the settlor to assert that they are not creating the trust with fraudulent intent, the creation of the trust will not render them insolvent, there are no pending or threatened court actions against them, they are not contemplating bankruptcy, and they are not behind on

¹²³ See *infra* notes 111–14 and accompanying text.

¹²⁴ Christopher M. Reimer & Amy M. Staehr, *Why Choose Wyoming?*, 21.5 STEP JOURNAL 55 (June 2013), available at <http://lrw-law.com/wp-content/uploads/2013/06/why-choose-wyoming.pdf>.

¹²⁵ *Id.*; Reimer, *supra* note 19, at 166–67 (“Given its strong asset protection laws, lack of income taxes, and recently revised Limited Liability Company (LLC) statutes, Wyoming is quickly outpacing other top trust situs states in terms of attracting new business. . . . Wyoming has adopted the UTC but has made over 100 substantive changes—resulting in an especially settlor-friendly code.”).

¹²⁶ Clay D. Geittmann, *Chaos to Comprehension: Estate Planning in Wyoming*, 30 WYO. LAW. 18, 20 (Dec. 2007).

¹²⁷ *Id.*

child support payments.¹²⁸ While a sworn affidavit does not *guarantee* the settlor will not defraud creditors, the document does create some reassurance that the statements were made under oath or penalty of perjury, and it serves as evidence of the statement's accuracy.¹²⁹

Wyoming statute also provides for public policy exceptions—circumstances where public policy demands that the QST does not shield a debtor's assets.¹³⁰ For example, Wyoming recognizes exceptions for child support obligations to ensure that the settlor is fulfilling his legal obligation to provide for his children.¹³¹ The exception recognizes that child support is not a typical contractual obligation but rather a societal obligation to take care of one's family. The statute also ensures that trust res listed on a financial statement or application is accessible to that creditor.¹³² This exception prevents the debtor from using the trust assets as collateral for a loan, then subsequently shielding the assets from creditor reach when it comes time to collect. Thus, this exception significantly reduces the opportunity for a secured creditor to be left with no recourse. These two exceptions further limit the chance for fraud and abuse.¹³³

Additionally, there is no need for fear of deception.¹³⁴ Trust property is shielded from creditors because it is no longer in the name of the settlor—it becomes trust property. For example, once real estate owned by a settlor named John F. Smith becomes trust property, the real estate is no longer under the name "John F. Smith," but rather is retitled as "The John F. Smith Irrevocable Trust" and "John F. Smith, Trustee." There is no deceit because the ownership of the property serves as an "alert to the world" that the property is inaccessible to creditors.¹³⁵ Therefore, a creditor who does his due diligence is not fooled.¹³⁶ Furthermore, current law requires the corpus of the trust to be segregated and earmarked in order to distinguish trust assets from settlor assets—much like business assets are separate from a business owner's personal assets.¹³⁷ Of course, it

¹²⁸ WYO. STAT. ANN. § 4-10-523 (2013).

¹²⁹ *See id.* § 4-10-523.

¹³⁰ *Id.* § 4-10-520.

¹³¹ *Id.*

¹³² *Id.*

¹³³ *Id.*

¹³⁴ *See supra* Part II.G.

¹³⁵ Hirsch, *supra* note 9, at 2688–89.

¹³⁶ "APT's could potentially benefit the public by encouraging all creditors to actually be diligent in extending credit, thereby reducing credit losses and decreasing the burden that those losses place on the public in the form of higher interest rates and fees." Sirknen, *supra* note 99, at 151.

¹³⁷ Hirsch, *supra* note 9, at 2688–89 ("None of the existing state statutes permitting the creation of asset protection trusts depart from these fundamental trust principles. Hence, asset

is possible to transfer a piece of property into the trust *after* a creditor has already loaned the money in reliance on the settlor's assets. However, Wyoming's statute addresses this concern for abuse by requiring the sworn affidavit and providing that if the trust res is listed on a financial statement or application, it is accessible to that creditor.¹³⁸

For additional protection from abuse and fraud, Wyoming's statute allows a creditor to bring a claim under the Uniform Fraudulent Transfers Act (UFTA).¹³⁹ The UFTA requires creditors to prove by clear and convincing evidence that the transfer of property to the trust was fraudulent.¹⁴⁰ A transfer is fraudulent and will be set aside if it is found that the debtor made the transfer with "actual intent to hinder, delay, or defraud any creditor" or if the transfer was made with constructive fraudulent intent.¹⁴¹ In determining intent, the court looks at a variety of factors, including whether the debtor was sued before the transfer was made, whether the debtor transferred substantially all of his assets, whether the debtor was insolvent during or shortly after the transfer was made, and whether the debtor made the transfer shortly before or after a substantial debt was incurred.¹⁴²

A less obvious protection, but one that significantly reduces the risk of fraud and abuse, the Wyoming Rules of Professional Conduct state: "A lawyer shall not counsel a client to engage, or assist a client, in conduct that the lawyer knows is criminal or fraudulent."¹⁴³ Therefore, a lawyer puts his license to practice on the line if he assists a client in forming a self-settled trust with the intent to defraud creditors.¹⁴⁴ Additionally, a lawyer could be subject to malpractice for failing to relay to clients that self-settled spendthrift trusts cannot be established for fraudulent or illegal purposes.¹⁴⁵ These limitations, together, are sufficient to discourage abuse of self-settled spendthrift trusts and limit the chance for settlors to defraud their present and future creditors.

protection trusts are not stealth-vehicles, invisible to radar. Creditors can infer their presence from their absence.").

¹³⁸ WYO. STAT. ANN. §§ 4-10-520, -523 (2013).

¹³⁹ *Id.* § 4-10-517.

¹⁴⁰ *Id.*

¹⁴¹ *Id.* § 34-14-205.

¹⁴² *Id.*

¹⁴³ WYO. RULES OF PROF'L CONDUCT R. 1.2(d).

¹⁴⁴ Brennan, *supra* note 111, at 790-91 ("Attorneys may be charged with violating the code of professional responsibility, either through their actions as co-conspirator, or by the violation of the fiduciary duty to fully disclose to clients the details and ramifications of asset protection trusts.").

¹⁴⁵ *Id.*

IV. CONCLUSION

As more states adopt statutes allowing self-settled spendthrift trusts, there appears to be no turning back.¹⁴⁶ The Qualified Spendthrift Trust is a beneficial component of Wyoming's Uniform Trust Code, and states should follow Wyoming's lead. The self-settled spendthrift trust provides substantial benefits to settlors.¹⁴⁷ Further, the self-settled spendthrift trust also provides substantial economic benefits.¹⁴⁸ Finally, Wyoming's self-settled spendthrift trust does not pose a serious risk for fraud or abuse because of the statutory limitations and requirements for establishing the trust.¹⁴⁹

Just as it took some time for scholars, lawmakers, and judges to overcome the concern, uneasiness, and uncertainty surrounding the enforceability of spendthrift trusts, it may take some time for self-settled spendthrift trusts to become more widely accepted.¹⁵⁰ Despite the concern, it looks like self-settled spendthrift trusts are here to stay.

¹⁴⁶ See *supra* note 53 and accompanying text.

¹⁴⁷ See *supra* Part III.B.

¹⁴⁸ See *supra* Part III.C.

¹⁴⁹ See *supra* Part III.A.

¹⁵⁰ See Hirsch, *supra* note 9, at 2711 ("Our political system incorporates checks and balances. Bankers and their lobbyists brought us the asset protection trust, in its various forms. Had any of these seriously threatened the national interests of the consumer credit industry, or of trial lawyers (whose livelihoods depend on victims' abilities to collect liability awards), then creditors' and trial lawyers' own lobbyists would have leapt into action, bending ears and twisting arms in the cloakroom. That no ears were deafened, nor arms sprained, as a matter of political *vérité*, is revealing in itself. It's the proverbial dog that did not bark.").