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Trent Maxwell

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Domestic Asset Protection Trusts: A Threat to Child Support?

INTRODUCTION

In 1997, Alaska became the first state to pass a usable statute allowing the creation of domestic asset protection trusts (DAPTs). Delaware was quick to follow, passing asset-protection legislation of its own later that year. Since then, a total of fourteen states have passed legislation allowing the creation of DAPTs. The impetus behind this legislation has been the respective states’ hope for an increase in trust business and the revenue that it would generate. In order to achieve this result, the DAPT statutes are structured so that settlors must utilize services within the DAPT state—such as


2. DEL. CODE ANN. tit. 12, § 3570 (2012). A desire to not be “outdone” by Alaska’s new statute appears to have been a driving force behind the adoption of Delaware’s statute. See Qualified Dispositions in Trust Act, Synopsis, H.R. 356, 139th Gen. Assemb., 71 Del. Laws 159 (1997) (explaining that the Act is “intended to maintain Delaware’s role as the most favored domestic jurisdiction for the establishment of trusts”).

3. See COMPARISON OF THE VARIOUS STATE DOMESTIC ASSET PROTECTION TRUST STATUTES (David G. Shaftel ed. 2012), [hereinafter COMPARISON] available at http://shaftellaw.com/docs/DAPTStatutes_June2012update_Final.pdf (counting thirteen states with DAPT legislation, but noting uncertainty whether Colorado has truly passed a DAPT statute and also noting pending DAPT legislation in Ohio, which, if both states were included, would bring the total to fifteen states). Ohio has since passed the DAPT legislation. Ohio Rev. Code Ann. § 5816 (West 2013).

4. See, e.g., Lee, supra note 1, at 156–62 (discussing the legislative history behind the passage of the Alaskan statute allowing DAPTs, including various statements by Alaskan representatives). Lee concludes that “a primary motivation for [the] . . . ultimate passage of the bill was the economic growth of Alaska.” Id. at 162; see also Act 182, 2010 Haw. Sess. Laws 592, § 1 (“The intent of this Act is to offer incentives to high net-worth individuals throughout the United States and throughout the world to transfer a portion of their liquid net worth into this State for asset and trust management. This Act is designed to increase the assets under management by Hawaii’s private financial sector, [and] increase state tax revenues . . . .”).

5. See John K. Eason, Home from the Islands: Domestic Asset Protection Trust Alternatives Impact Traditional Estate and Gift Tax Planning Considerations, 52 FLA. L. REV. 41, 56 (2000) (“Both Alaska and Delaware have designed their statutes to increase trust business within the respective states, by imposing certain trustee and administration requirements upon the creditor-protected trust.”).
requiring trust assets to be deposited within the state and requiring trust administration to be done by a state resident or company. In also a bid to attract trust business, many states have chosen to severely limit or entirely abolish the Rule Against Perpetuities. By eliminating the effect of the Rule Against Perpetuities, so-called dynasty trusts can be created, which are exempt from the generation-skipping transfer tax.

While it is unclear whether these states have achieved their goal of increasing revenue, it is clear that the recent DAPT legislation has had a significant impact on creditors’ rights. As states vie to become the top trust situs, states are incentivized to pass progressively more debtor-friendly legislation in order to draw trust business into their state. Because of the perverse incentives it creates, this competition has been dubbed a “race to the bottom.”

One question that states have been confronted with in passing DAPT legislation has been how to treat child support—whether this “creditor” claim would be treated the same as other claims, or whether an exception would be made so DAPTs could not be used to avoid child support claims.


8. Sitkoff & Schanzenbach, supra note 7, at 419.


10. For a discussion of whether these states have achieved their goal of increasing revenue, see infra Part III.


14. See, e.g., Lee, supra note 1, at 157–59 (describing the legislative discussions on how child support would be treated under the proposed statute). “[I]t appears that with regards to creditors’ rights, the legislators focused primarily on the potential claims of children . . . .” Id.
While much has been written about the passage of DAPT statutes in general, this Comment adds to the discussion by specifically examining how states have tackled this question of how to treat child-support creditors. The majority of states that have passed DAPT legislation have included an exception for child support; however, disparity exists among the states on the strength of the exceptions and under what circumstances the exceptions apply. Furthermore, at least one state did not include any exception for child support at all, in effect treating child-support claimants the same as any other creditor-debtor relationship. Such legislation is troubling not only for its immediate effect on child-support dependents of settlors in DAPT states, but for how this legislation might pressure other states to eliminate child-support exceptions from their own statutes in order to compete for trust business. This Comment argues that states should include strong exceptions for child-support dependents because the creditor-debtor relationship is unique in this context, shielding of child support debts is immoral, and the economic cost to society of not having an exception for child-support claimants likely outweighs the economic benefits to the states.

Part I of this Comment examines the history behind self-settled trusts, including the traditional view of these trusts, the rise in the use of off-shore trusts, and finally the creation of domestic asset protection trusts. Part II summarizes the DAPT statutes that have been passed, particularly focusing on how the respective statutes treat child support, and also discusses why tax considerations are likely the motivation behind some states choosing to provide little or no protection to child support in their DAPT statutes. Part III explores policy considerations for including child support exemptions in DAPT statutes; such as the unique nature of the creditor-debtor relationship, and examines why tax considerations may be driving states that have passed DAPT statues to eliminate all exemption creditors (including child support “creditors”). Lastly, Part IV concludes that DAPT statutes that provide no exception, or

15. For a summary of how the various DAPT states have treated child support, see infra Part III.
17. See infra Part II.
18. See infra Part III.
only a weak exception, for child support are a threat to child support and should be disallowed for public policy reasons.19

I. HISTORY OF DOMESTIC ASSET PROTECTION TRUSTS

In order to gain a better understanding of how DAPTs function, it is useful to explore the background that gave rise to this type of trust. This Part examines how spendthrift and self-settled spendthrift trusts have traditionally been viewed by the courts. Next, the rise of offshore self-settled spendthrift trusts is explored, and the advantages and disadvantages of offshore trusts are discussed. Lastly, this Part describes how offshore trusts provided the inspiration for DAPTs and highlights the pros and cons of DAPTs as contrasted with offshore trusts.

A. Traditional Principles Regarding Spendthrift Trusts

1. Spendthrift trusts

Historically, English law did not permit trusts to shield the trust assets from attachment by creditors.20 This law was carried forward into America, whose laws were predominantly based upon English laws.21 However, in the 1875 landmark case of Nichols v. Eaton,22 the United States departed from English law to allow so-called “spendthrift trusts,” which permitted settlors to create trusts for others that prevent creditors from attaching the beneficiary’s interest in the trust.23 While hotly contested at the time,24 spendthrift trusts are now readily accepted as a standard vehicle of trust law.25

19. See infra Part IV.
22. 91 U.S. 716 (1875).
23. Boxx, supra note 20, at 1201–02. The rationale behind allowing such spendthrift trusts is explained in Sterk, supra note 12, at 1042 (“The rationale for enforcing spendthrift trusts has been that the trust property belongs not to the trust beneficiary, but to the trust settlor. Because the settlor has no obligation to transfer the property to the beneficiary, the settlor is entitled to transfer it to the beneficiary subject to conditions, including the condition that the property be shielded from the beneficiary’s creditors.”).
24. For a detailed history of the debate surrounding the decision allowing spendthrift trusts, see Anne S. Emanuel, Spendthrift Trusts: It’s Time to Codify the Compromise, 72 Neb.
2. Self-settled spendthrift trusts

Despite widespread recognition of spendthrift trusts after Nichols v. Eaton, this recognition did not extend to spendthrift trusts created for the benefit of the settlor.26 The general principle prohibiting asset protection for self-settled spendthrift trusts is illustrated by an English rule from the fifteenth century: “all deeds of gift of goods and chattels made or to be made [in] trust, to the use of that person or persons that made the same deed or gift, be void and of none effect.”27 A more current formulation of this rule is encapsulated in the Restatement (Second) of Trusts, which states:

(1) Where a person creates for his own benefit a trust with a provision restraining the voluntary or involuntary transfer of his interest, his transferee or creditors can reach his interest.

(2) Where a person creates for his own benefit a trust for support or a discretionary trust, his transferee or creditors can reach the maximum amount which the trustee under the terms of the trust could pay to him or apply for his benefit.28

Thus, traditional trust law provides that if the settlor can still receive assets from the trust, such as in a self-settled trust, then any spendthrift provision is of no effect, and creditors can attach the settlor-beneficiary’s interest in the trust.29 Until recently, this has


25. See Boxx, supra note 20, at 1202 (“Currently, all states give spendthrift provisions some degree of recognition, although some states set limitations on enforcement of such provisions.”); see also Sterk, supra note 12, at 1042 (“Courts and legislatures have responded to this device with constraints of varying severity, but spendthrift trusts have nevertheless become widely accepted.”).

26. Boxx, supra note 20, at 1202–03; see also Sterk, supra note 12, at 1043 (“[E]ven more entrenched than spendthrift trust doctrine itself is the rule that a spendthrift provision for the settlor’s own benefit is unenforceable.”).


28. Restatement (Second) of Trusts § 156 (1959); see Darsi Newman Sirknen, Domestic Asset Protection Trusts: What’s the Big Deal?, 8 TRANSACTIONS: TENN. J. BUS. L. 133, 133–34 n.4 (2006) for a list of cases that have adopted the Restatement’s view. The rule set forth in the Restatement (Second) of Trusts has been carried forth in the Restatement (Third) of Trusts. See Restatement (Third) of Trust § 58(2) (2003) (“A restraint on the voluntary and involuntary alienation of a beneficial interest retained by the settlor of a trust is invalid.”).

29. JESSE DUKEMINIER ET AL., WILLS, TRUSTS, AND ESTATES 624 (8th ed. 2009) (“Under traditional law, the settlor cannot shield assets from creditors by placing them in a trust for the settlor’s own benefit. Even if the trust is discretionary, spendthrift, or both, the
been the law of the land in the United States. However, with several foreign jurisdictions and now a number of U.S. States abrogating this rule, settlors have many locations to choose from that allow them to create a trust that is both self-settled and protected against creditors.30

B. Offshore Trusts

In the mid-1980s several foreign jurisdictions, many of them small islands, designed a business scheme intended to drive trust business to their countries.31 The focus of these jurisdictions was to create trust laws that would allow wealthy individuals to protect their assets from creditors.32 The most significant change to traditional trust laws initiated by these offshore locations permitted a settlor of a trust to have creditor protection despite being a beneficiary of the trust.33 Hence, under these foreign trust laws, “creditors may neither compel a trust distribution nor attach the settlor’s trust interest in satisfaction of the settlor’s debts.”34

The efforts of these foreign jurisdictions have proved to be extremely lucrative, as estimates indicate that between $1 and $5 trillion are located in offshore asset protection trusts35 (OAPTs).36 Currently, there are over sixty foreign jurisdictions from which to choose, with some of the more popular offshore locations including “the Bahamas, Belize, Cayman Islands, Cook Islands, Cyprus, Gibraltar, and the Turks and Caicos Islands.”37

settlor’s creditors can reach the maximum amount that under any circumstances the trustee could pay to the settlor or apply for the settlor’s benefit.”).

30. See infra Part III.B–C.
32. Id. Similar to the competition among U.S. states to become the top trust situs, the competition among foreign jurisdictions to become the top international trust situs by passing debtor-friendly laws has also been called a “race-to-the-bottom.” See Jeffrey A. Schoenblum, Preface, The Rise of the International Trust, 32 Vand. J. Transnat’l L. 519, 524 (1999).
33. Eason, supra note 5, at 50.
34. Id.
35. Thomas M. Brinker Jr. et al., Demystifying Offshore Trusts: Capitalizing on a Valuable Asset Protection Tool, 15 J. Int’l Tax’n 30, 32 (2004). The actual amount of assets held in these accounts may be even higher, as others have estimated that as much as $6 trillion exist in offshore trusts. See Danforth, supra note 27, at 310 (citing David Leigh, Billions Hidden Offshore: Jersey Faces Clampdown, Guardian (London), Sept. 26, 1998, at 1).
37. Id. at 62; see also Denise C. Brown, Caribbean Asset Protection Trust: Here Comes the
1. Advantages of offshore trusts

There are several reasons why OAPT's quickly gained popularity. First, several factors make it harder for creditors to access funds held in an offshore trust. One reason is that foreign jurisdictions are not under “constraints imposed by the U.S. Constitution,” such as the Full Faith and Credit Clause. Thus, if a creditor obtains a judgment against a settlor in a U.S. jurisdiction, the foreign jurisdiction is not required to, nor perhaps likely to, recognize this judgment. While it may be possible for the creditor to sue the settlor in the foreign jurisdiction and obtain a judgment against the settlor there, this process is burdensome and expensive. Not only will the creditor have to bring suit in that jurisdiction under foreign laws but also the creditor will find it harder to obtain a judgment because the standard of proof is often higher than it would be in the United States. Additionally, the creditor must usually retain local counsel instead of keeping his or her U.S. counsel, which can present problems of its own.
Another reason it is harder to obtain a judgment in these offshore locations is that the foreign jurisdictions often have a shorter statute of limitations for claims than in the United States, thus making it harder for the creditor to bring suit before the claim is barred.\textsuperscript{44} To further complicate matters, a cause of action that exists in the United States may not even exist in these foreign jurisdictions.\textsuperscript{45} Even those creditors who can overcome these barriers to successfully file suit in the foreign jurisdictions might find out that their efforts are for naught, as “flight” clauses allow trustees to simply move the trust assets to another jurisdiction before judgment can be obtained, so that process begins all over again in another jurisdiction.\textsuperscript{46} Collectively, these barriers act as a great deterrent to creditors, gradually wearing them down until they decide to stop pursuing a fruitless claim.\textsuperscript{47}

A second advantage to OAPTs is that self-settled spendthrift trusts have been allowed in foreign jurisdictions for several years now, allowing some peace of mind to the settlor as to how foreign and U.S. laws will be applied to these funds, while U.S. states offering these types of trusts are a new development.\textsuperscript{48} A third benefit is that OAPTs offer a great deal of privacy for settlors due to confidentiality laws in the foreign jurisdictions.\textsuperscript{49} Lastly, having assets in off-shore trusts can provide tax-saving benefits to the settlor.\textsuperscript{50}

\textsuperscript{44} Brinker et al., supra note 35, at 60 (contrasting the one-year statute of limitations found in some foreign jurisdictions with the typical three- to five-year period found in the United States); see also Marty-Nelson, supra note 36, at 61 (noting one attorney’s remarks that the “practical effect” of these significantly reduced statute of limitations periods is that “by the time you find out where the money is and file your action, the statute of limitations bars the suit”).

\textsuperscript{45} Brinker et al., supra note 35, at 60 (“[M]ost foreign jurisdictions do not recognize a [surviving] spouse’s right to an elective share against the estate.”).

\textsuperscript{46} Marty-Nelson, supra note 36, at 66.

\textsuperscript{47} Brinker et al., supra note 35, at 60 (“After one or two attempts to bring suit, a rational creditor will conclude that the costs of pursuing the claim outweigh any potential benefit.”); see also Sirknen, supra note 28, at 135 (“[T]he trust instrument may provide for a change of trust situs if the assets are put in danger. Many creditors are not willing to follow a trust as it flees from one jurisdiction to another, perhaps making several situs changes before the creditor finally throws its proverbial towel into the ring.”).

\textsuperscript{48} See Reimer, supra note 7, at 168. Reimer notes that “for many years, the general rule in U.S. jurisdictions was that trusts in which the settlor is also a beneficiary were against the tenets of conscionability.” Id.

\textsuperscript{49} Beazer, supra note 40, at 21; see also Mario A. Mata, Frequently Asked Questions Regarding Offshore Wealth Preservation, PRAC. TAX L., Spring 2004, at 27, 29 (“[O]ffshore secrecy laws . . . provide clients, particularly very wealthy families, the ability to protect the
2. Disadvantages of offshore trusts

Despite the popularity of offshore asset protection trusts, they come with several disadvantages. First, OAPTs are very expensive, with initial start-up costs around $18,500 and maintenance costs running to several thousand dollars each year.51 Second, a stigma is often associated with the use of offshore accounts,52 which may dissuade some potential settlors from taking advantage of these asset protection tools.53 However, the general perception towards the use of OAPTs may be positively increasing.54 Third, political instability is a risk in these foreign jurisdictions.55

50. Reimer, supra note 7, at 168 (“[T]he U.S. Internal Revenue Code has been structured so that settlors were allowed to take advantage of a number of estate and income tax minimization techniques, further guarding the corpus of a trust and allowing unencumbered growth in foreign jurisdictions.”).

51. Eric Henzy, Offshore and “Other” Shore Asset Protection Trusts, 32 VAND. J. TRANSNAT’L L. 739, 740 (1999); see also Brennan, supra note 11, at 765–66 (“Asset protection is an expensive venture; anyone considering the creation of an offshore trust should have a net worth of at least $500,000 and be prepared to incur start-up costs of at least $15,000 for a $1 million account along with a one percent yearly administration fee.”).

52. See Brown, supra note 37, at 142–43. A current example of the stigma associated with offshore accounts was witnessed in the recent election, with some critics accusing Governor Mitt Romney of “hiding” illegal activity in his offshore accounts. See Leon & Marlene Schmidt, Letter to the Editor, Romney’s Offshore Accounts Raise Suspicion, THE GAZETTE, Aug. 23, 2012, available at http://thegazette.com/2012/08/23/romneys-offshore-accounts-raise-suspicion/ (raising the possibility that Governor Romney had used offshore accounts to avoid paying taxes).


54. See Beazer, supra note 40, at 19 (“OFCs are no longer just sunny places for shady people.”); see also Brown, supra note 37, at 137 (“Although the Caribbean APT has received bad press in the past, it remains a legitimate asset protection and estate planning tool.”); see also 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, 149 (2007) (advocating that “offshore asset protection trusts serve a legitimate purpose”). But cf. id. at 149 n.6 (noting that “legal commentators disagree about the legitimacy of [OAPTs],” and comparing several of these comments). Many of these favorable viewpoints of OAPTs are advocated either by practitioners involved in the business of setting up these trusts or by legal commentators whose knowledge of these asset protection tools presumably far surpasses that of a normal lay person. Hence, the unfavorable perception of OAPTs among the general population may likely remain unchanged. See, e.g., Stephanie Mencimer, The Real Problem with Romney’s Offshore Investments, MOTHERJONES.COM, http://www.motherjones.com/politics/2012/09/mitt-romney-offshore-investments-cayman-islands (Sept. 25, 2012, 2:00 AM) (“Offshore tax havens are better known for facilitating money laundering and tax evasion than legitimate business.”).

55. Reimer, supra note 7, at 169 (Reimer also notes the risk of potentially
Fourth, in recent years the United States has passed laws that have substantially increased the reporting requirements for offshore accounts and that have increased the civil and criminal penalties for non-compliance with these requirements. Additionally, some U.S. courts have held settlors in contempt of court for failing to comply with a court order to repatriate trust assets to the United States, rejecting the settlors’ arguments (likely for good reason) that it is impossible for the settlors to direct the disposition of the trust assets under the terms of the trust instrument. Because of the foregoing reasons, some settlors may be hesitant to put funds in an OAPT, particularly in light of the emergence of a new, viable asset protection tool, the DAPT, which is discussed below.

C. The Emergence of Domestic Asset Protection Trusts

In 1997 Alaska became the first state to pass a statute allowing for the creation of a DAPT. This legislation was inspired by the “offshore” countries’ success in attracting trust business. While on a fishing trip together in Alaska, an attorney and his brother came up with the idea of passing a DAPT statute that could compete with the unenforceable trust terms and unaccountable trustees.); see also Marty-Nelson, supra note 56, at 66 (“When investigating OAPTs . . . a settler need consider . . . the potential of a military coup in the situs nation, and the subsequent consequences to the trust assets.”). 56. Christopher M. Reimer, International Trust Domestication: Migrating an Offshore Trust to a U.S. Jurisdiction, 25 QUINNIPIAC PROB. L.J. 170, 183 (2012); see also Danforth, supra note 27, at 310 (noting the “onerous reporting requirements imposed on foreign trusts by the Internal Revenue Code”).

57. See, e.g., F.T.C. v. Affordable Media, 179 F.3d 1228 (9th Cir. 1999). The court in Affordable Media stated:

[W]e are not certain that the Andersons’ inability to comply in this case would be a defense to a finding of contempt. It is readily apparent that the Andersons’ inability to comply with the district court’s repatriation order is the intended result of their own conduct[—]their inability to comply and the foreign trustee’s refusal to comply appears to be the precise goal of the Andersons’ trust.

Id. at 1241. For a detailed analysis of this case, see Randall J. Gingiss, Putting a Stop to “Asset Protection” Trusts, 51 BAYLOR L. REV. 987, 996–1000 (1999); see also In re Lawrence, 279 F.3d 1294, 1299–1300 (11th Cir. 2002) (“The sole purpose of this [duress] provision appears to be an aid to the settlor to evade contempt while merely feigning compliance with the court’s order . . . . [W]here the person charged with contempt is responsible for the inability to comply, impossibility is not a defense to the contempt proceedings.”), reviewed in DUKEMINIER ET AL., supra note 29, at 634.

58. See Lee, supra note 1. Apparently the idea to create a trust state that would compete with OAPTs was conceived by a New York trust lawyer, his brother, and an Alaskan lawyer while together on a fishing trip in Alaska. See id. at 156–57; DUKEMINIER ET AL., supra note 29, at 625–26.
offshore trust business. Since Alaska’s passage of its DAPT statute, several more states have followed suit, bringing the number of states that have passed DAPT legislation to fourteen.\(^{59}\) The fundamentals of DAPTs are discussed below, along with the advantages and disadvantages of these asset protection tools.

1. **Structure of DAPTs**

   Conceptually, DAPTs are very similar to OAPTs. Like an OAPT, a DAPT allows a settlor to create a self-settled spendthrift trust that provides asset protection against the settlor’s creditors.\(^{60}\) DAPTs are generally irrevocable trusts,\(^{61}\) although one state has allowed a DAPT to be revocable.\(^{62}\) As noted above, the creation of revenue through the passage of DAPT statutes was a driving force behind their passage.\(^{63}\) Thus, DAPT statutes were designed in such a way as to increase trust business within the state.\(^{64}\) Alaska’s statute is illustrative because it requires that “some or all of [the] asset[s] be deposited in Alaska” and that the trust be “administered by a ‘qualified person’ who is either an individual who is an Alaska resident, or an Alaska trust company or bank.”\(^{65}\)

2. **Advantages of DAPTs**

   Commentators have noted several advantages of settlors placing assets in a DAPT instead of an OAPT. First, the danger of political

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59. See supra note 3.

60. Adam J. Hirsch, *Fear Not the Asset Protection Trust*, 27 CARDOZO L. REV. 2685 (2006); See also COMPARISON, supra note 3, at 2 (noting that the “primary goals of DAPTs are asset protection and, if so designed, transfer tax minimization”).

61. COMPARISON, supra note 3, at 2.

62. OKLA. STAT. tit. 31, § 13 (2012) (“A preservation trust may be established as a revocable and amendable trust . . . .”). Oklahoma’s departure from other DAPT states in this regard is described in Hirsch, supra note 60, at 2687 (“Upon joining the bandwagon in 2004, Oklahoma added its own, intriguing wrinkle: Uniquely among the states, Oklahoma allows asset protection trusts to be made revocable, in whole or in part, and explicitly bars creditors from using judicial process to force settlors to exercise the retained right of revocation. Hence, in effect, settlors can impress a self-settled trust in Oklahoma with a restraint on involuntary alienation without simultaneously restraining voluntary alienation. By exercising a reserved right of revocation, wholly personal to themselves, settlors can recover the corpus at will, but creditors cannot touch it.”).

63. See supra note 4 and accompanying text.

64. See Eason, supra note 5.

65. Shaftel, supra note 6.
instability associated with some foreign jurisdictions is greatly reduced, along with the potential problem of unaccountable trustees.

Second, while DAPTs do not necessarily have a “sterling” reputation, their use may be held in a higher regard than the use of OAPTs. Third, a DAPT is not as expensive as an OAPT, making DAPTS more accessible to a greater number of people.

3. Disadvantages of DAPTs

Although DAPTs offer some advantages over offshore trusts, DAPTs also have potential drawbacks that may make them not as attractive as OAPTs. One significant limitation is uncertainty concerning how conflict of laws principles and the Full Faith and Credit Clause of the U.S. Constitution will affect the application of DAPTs. This uncertainty may arise when a creditor brings suit

66. Sterk, supra note 12, at 1051.
67. See Brinker et al., supra note 35, at 55 (“[P]erpetual trusts created in the U.S. offer some significant advantages to the grantor… [including] a greater degree of certainty concerning the administration of the trust . . . .”).
68. Henzy, supra note 51, at 741. See also id. at 741 n.10 (quoting Lynn M. LoPucki, Virtual Judgment Proofing: A Rejoinder, 107 YALE L.J. 1413, 1415 (1998)) (“Americans can now judgment proof-themselves without transferring their money and the titles to their properties to strangers offshore.”).
69. One commentator has noted that a state’s effort to increase the favorable perception of DAPTs within its state can be seen by how the state has named its DAPT statute. See Dan Holbrook, The TIST Test: Tennessee Competes for Trust Dollars, 43 TENN. B.J. 21, 21 (“Because ‘asset protection’ may hint at something shady, with visions of widows and orphans eating dog food, or bankrupt businessmen leaving creditors holding the bag while they retire for life at their villa in the Caymans, Tennessee’s law refers to our version of DAPTs euphemistically as ‘Tennessee Investment Services Trusts,’ or TISTs.”).
70. See Brennan, supra note 11, at 779; See Henzy, supra note 51, at 740–41 (noting that the cost to create a DAPT is between $6,000 and $12,000 in contrast with cost of $18,500 that can be required to create an OAPT).
71. One commentator has gone so far to suggest that DAPTs simply cannot compete with the asset protection offered by OAPTs. See Eason, supra note 5, at 63 (“It is impossible for any state in the U.S. to offer the same degree of protection as offshore jurisdictions that have high burdens of proof, virtually no recognition of foreign judgments, the English rule for taxing attorney’s fees as costs, and extremely short limitations periods in which to seek avoidance of a transfer claimed to be fraudulent.”); Cf. Sterk, supra note 12, at 1051 (opining that despite DAPTs offering less asset protection than OAPTs, the former may still be able to compete for trust business with the latter due to DAPTs’ advantages over OAPTs).
72. U.S. CONST. art. IV, § 1.
73. See Paul, supra note 13, at 365.
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against a debtor in a non-DAPT state and then seeks to enforce the judgment from the debtor’s assets held in a trust set up in a DAPT state. While the trust assets may be protected under the DAPT state’s law, this may not be the case under the non-DAPT state’s laws. Despite the conflict of laws between the two forums, the Full Faith and Credit Clause would usually require that a judgment rendered against the debtor in a non-DAPT state be honored in a DAPT state. Hence, it is very important to know which state law (DAPT or non-DAPT) will be applied.

a. Determining which state law governs. Several factors must be considered to determine which state law governs. It is extremely common for the settlor of an asset protection trust to insert a choice of law provision in the trust instrument, designating the laws of the jurisdiction that allow the asset protection trust to govern the trust. Normally, courts will honor a choice of law provision in a trust instrument when deciding general questions about how the trust is to be administered. Hence, if the dispute is brought in a DAPT state, the Full Faith and Credit Clause would compel the non-DAPT states to "recognize the judgment upholding the validity of the domestic asset protection trust, even though the trust's provisions strongly conflict with the laws of those other [non-DAPT] states." Conversely, if the judgment were rendered in a DAPT state, the Full Faith and Credit Clause would compel the non-DAPT states to "recognize the judgment upholding the validity of the domestic asset protection trust, even though the trust's provisions strongly conflict with the laws of those other [non-DAPT] states."
state and the DAPT was set up within the state, then the governing law is easy to determine—the DAPT state will simply apply its own law. But, when suit is brought in a non-DAPT state, the answer is not as clear.

Many commentators have argued that non-DAPT states may choose not to apply the DAPT state’s law, despite the settlor’s choice of law provision, if doing so would violate a “strong public policy” of the non-DAPT state. Two particular instances when a non-DAPT state may determine that enforcing the law of the DAPT state would violate a “strong public policy” of the non-DAPT state are (1) claims regarding fraudulent conveyances and (2) disputes determining whether a spendthrift provision in self-settled trusts should be enforced to protect the settlor from claims brought by creditors. Many DAPT states have tried to overcome this potential...
obstacle by including legislation with their DAPT statute that grants them exclusive jurisdiction over any matters concerning trusts within their state. 83 However, such legislation is likely to have little to no effect on a non-DAPT state’s decision to apply its own law if the DAPT state’s laws would offend its state’s public policy. 84

b. Full Faith and Credit Clause. As noted above, if a judgment is obtained in a non-DAPT state against a DAPT, the Full Faith and Credit Clause of the Constitution requires that the DAPT state honor this judgment. While there is a chance that the DAPT state may choose not to honor the judgment of the non-DAPT state because it violates its own public policy, 85 this possibility is extremely slight. 86 Therefore, a big disadvantage of choosing a DAPT over an


84 See Veit, supra note 83, at 287 (“An out-of-state court is likely to hear a fraudulent conveyance action regarding an Alaska Trust in spite of the Act’s purported grant of exclusive jurisdiction to the Alaska courts over ‘proceedings initiated by interested parties concerning the internal affairs of trusts.’”).

85 See Reimer, supra note 56, at 181 (“[T]here is an argument that a Wyoming court should not enforce such judgments [of a non-DAPT state] because they conflict with the strong public policy of the forum state.”).

86 See Veit, supra note 83, at 287 (quoting RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 103 (1971) (amended 1989)) (“Finally, the full faith and credit clause of the United States Constitution would require that Alaska give full effect to the judgment of an out-of-state court that a transfer to an Alaska Trust was a fraudulent conveyance. The only possibly applicable exception recognized by the Restatement is likely irrelevant. Section 103 declares that a state need not recognize or enforce the judgment of another state if such recognition or enforcement would ‘involve an improper interference with important interests’ of the state being asked to enforce the judgment. The comment to the Restatement provision describes the application of this exception as ‘extremely narrow.’ A state’s ‘strong public policy’ against enforcement of the claim will not suffice to constitute interference with important interests.”); See Henzy, supra note 51, at 754 (citing Baker v. Gen. Motors Corp., 522 U.S. 222, 233 (1998)) (“While ‘a court may be guided by the forum State’s “public policy” in determining the law applicable to a controversy . . . [the Supreme Court’s] decisions support no roving “public policy exception” to the full faith and credit clause.’ Thus, absent fraud or lack of personal or subject matter jurisdiction, the courts of a state must recognize a judgment from a state or federal court in another state, even if such judgment is not consistent with local policy or law.”). Some commentators have noted that the Full Faith and Credit Clause treats legislative acts and judgments unequally since a forum state may disregard the non-forum state’s statutory law more easily than a non-forum state may disregard judgments from the forum state. See Bryan Nichols, “I See the Sword of Damocles Is
OAPT is the possibility that a non-DAPT state may apply its own law, resulting in the DAPT state being required to enforce the judgment.\textsuperscript{87}

However, as the number of states that allow DAPTs has increased and will likely continue to increase in the future, the odds steadily decrease that a court in a non-DAPT state will find that these trusts violate the public policy of that state because these trusts are then less of an anomaly.\textsuperscript{88}

c. Personal jurisdiction issues. In addition, the non-DAPT state must have either personal jurisdiction over the trustee or \textit{in rem} jurisdiction over the trust assets, since the trust assets are no longer held by the settlor.\textsuperscript{89}

\textit{Hanging Above Your Head!"} Domestic Venue Asset Protection Trusts, Credit Due Judgments, and Conflict of Law Disputes, 22 REV. LITIG. 473, 484 (2003) ("[The Full Faith and Credit Clause], by its language alone, creates a firm principle of judicial and legislative comity between states: both the laws and judicial pronouncements of sister states must be accepted by the state in question. That the full faith and credit clause requires parallel treatment of judgments and legislative acts is self-evident. However, the disparity between what appears to be obvious and what has actually occurred is quite prevalent."); See Henzy, supra note 51, at 754 ("[T]he full faith and credit obligation is more exacting in the case of judgments.").

\textsuperscript{87} Veit, supra note 83, at 287–88 ("The full faith and credit clause distinguishes the protection of the offshore trusts from the protection of an Alaska Trust. . . . A transfer to an offshore trust would be far more impervious to attachment by creditors because of the judgment’s unenforceability.").

\textsuperscript{88} See COMPARISON, supra note 3 ("The fact that fourteen states now have DAPT statutes moves this approach from the eccentric anomaly category to an accepted asset protection and transfer tax minimization planning technique. As more and more states enact DAPT statutes, the conclusion that a non-DAPT state has a ‘strong public policy’ against a DAPT trust seems less likely."); See Danforth, supra note 27, at 325 ("As more states adopt [D]APT and other debtor-friendly legislation, courts in those jurisdictions will become less inclined to find that the foreign state’s [D]APT law violates their public policy. Moreover, even in states without [D]APT legislation, courts in those states may recognize the myriad ways in which their own state laws allow non-[D]APT devices (such as limited partnerships and tenancies by the entirety) for protecting against creditors’ claims and thus be disinclined to find that the foreign [D]APT legislation violates its public policy. In these two significant respects, we can anticipate that recovering from [D]APTs will become increasingly more difficult."); See Brennan, supra note 11, at 787 ([A] creditor may also bring an action attacking the validity of a domestic asset protection trust based on its self-settled nature. [Some cases] indicate courts’ willingness to use this rule, either directly or indirectly, to strike down an offshore asset protection trust. However, if other states follow Alaska and Delaware’s lead in repealing the rule against self-settled trusts, a breakdown in the respect for and use of this rule may result.").

\textsuperscript{89} See Sterk, supra note 12, at 1089 ("Once the settlor transfers property to the asset protection trust, a personal judgment against the settlor is of limited value, because the settlor no longer claims any legal interest in the property. The trustee, not the settlor, becomes the creditor’s adversary in the dispute over legal ownership of the trust property."); Eason, supra note 5, at 68 (citations omitted) ("The prior judgment would not affect directly interests in
If the non-DAPT forum state does not have personal jurisdiction over the trustee, the DAPT state has no obligation to enforce the judgment against the settlor. While a creditor could bring an action in the DAPT state having personal jurisdiction over the trustee, this would add considerably to the cost of litigation, and is likely to deter most creditors from pursuing their claim. Likewise, while in rem jurisdiction may be easy to obtain for real property located in the non-DAPT state, a creditor may have difficulty establishing in rem jurisdiction over other property because the location of the property is not as easily ascertained. Accordingly, as long as DAPT trustees are careful to minimize their contact with non-DAPT states and trust assets are held within the DAPT state, a creditor’s ability to obtain judgment is greatly reduced.

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90. Eason, supra note 5, at 68 n.97 (construing Hanson v. Denckla, 357 U.S. 235, 254–56 (1958)) (noting Hanson v. Denckla, in which the Supreme Court held “that state of trustee domicile was not bound to give full faith and credit to judgment rendered by state of settlor’s and most beneficiaries’ domicile, where second state lacked personal jurisdiction over trustee”).

91. See Danforth, supra note 27, at 325 (“[T]he creditor must obtain a judgment from a court having personal jurisdiction over the trustee.”).

92. See Keith Adam Halpern, Domestic Asset Protection Trusts: What Is Your State of Asset Protection?, 7 FLA. ST. U. BUS. REV. 139, 149–50 (2008) (“[O]ne may have a losing battle enforcing a DAPT court’s judgment upon a [DAPT] trustee. Unless the [DAPT] trustee has the required minimum contacts with the judgment debtor’s state, the judgment creditor will likely be required to obtain . . . counsel [within the DAPT state], domesticate the judgment to [the DAPT state], and re-initiate portions of the litigation all over again. This double expense (probably closer to triple) is a practical dissuading mechanism to a creditor pursuing a judgment. . . . Geography is, of course, a completely unsophisticated reason to stop a valuable claim, but it has prevented unaccounted scores of claimants due to the legal fees necessary to access trust assets.”).

93. See Sterk, supra note 12, at 1097 (“When tangible property, particularly real property, is involved, establishing the location of that property will generally be straightforward. However, when intangible property—partnership interests and corporate shares—is at stake, the creditor faces serious difficulties.”).

94. See Danforth, supra note 27, at 325 (“Savvy trustees, seeking to protect the assets of their [D]APT clients, will undoubtedly structure their affairs to minimize the risk of subjecting themselves to personal jurisdiction in states that do not recognize [D]APTs.”); Sterk, supra note 12, at 1090 (“The creditor, however, has no apparent basis for obtaining personal jurisdiction over a [DAPT] trustee, so long as the trustee has taken care not to solicit business outside the trustee’s home jurisdiction.”); Eason, supra note 5, at 69 (“The trustee’s contacts with the non-DAPT state and the location of trust property are . . . crucial considerations in the establishment and administration of any [DAPT], as the wrong decision here could


d. Contracts clause challenges. Another potential challenge to DAPTs may come from a creditor claiming that the DAPT statutes authorizing the creation of DAPTs are void since these statutes violate the Contracts Clause of the U.S. Constitution. The Contracts Clause prohibits states from passing laws that “substantially impair the obligations of parties to existing contracts or make them unreasonably difficult to enforce.” By allowing settlors to protect their assets mitigate strongly in favor of the judgment creditor. Thus, a primary consideration for both the asset protection attorney and the transfer tax planning attorney is the selection of a trustee with a policy of minimizing personal jurisdiction contacts with states other than the DAPT jurisdiction, the laws of which are intended to govern trust affairs.”; Sirknen, supra note 28, at 153 (suggesting that “[t]o prevent a non-[D]APT court from having jurisdiction, the trustee should be a resident of the [D]APT state or a corporation doing business only in the [D]APT state (so that it does not have ‘minimum contacts’ with the forum state), and the trustee should hold all trust assets within the [D]APT state (so that a non-[D]APT court cannot have in rem jurisdiction over trust assets”).

Conversely, if such precautions are not taken, the creditor may more easily reach the assets held in the DAPT. Eason, supra note 5, at 69 (“If the forum state has jurisdiction over the trustee and/or trust property, then the DAPT is clearly vulnerable. . . . If such personal jurisdiction is found to exist and due process requirements are otherwise complied with, the asset protection sought could easily be lost as a result of litigation in the non-DAPT jurisdiction.”).

One commentator has suggested that instead of waiting for the trust to be attacked, the trustee should bring a declaratory judgment action in the DAPT state so that the trust’s validity will be decided by the DAPT state. See Sirknen, supra note 28, at 155–56 (“The trustee[ ] has the option . . . to take an offensive posture and bring a declaratory judgment action in the [D]APT state. Obviously, the [D]APT state will use its own law to uphold the trust, and the Full Faith and Credit Clause will require other states to uphold that judgment. Although the [D]APT state courts may not have personal jurisdiction over the creditor, they will most likely have jurisdiction over the trust assets, since all [D]APT statutes require at least some of the assets to be held within the [D]APT state. If the trustee sends notice of the proceeding to the creditor and gives him an opportunity to come defend his position, the creditor can still be bound by the judgment of the [D]APT state. Thus, creditors existing at the time of the declaratory action will be estopped from bringing later challenges to the trust.”). But cf. Jay Adkisson, Will Declaratory Judgments Be the Savior of Domestic Asset Protection Trusts? Probably Not, FORBES.COM, (Apr. 27, 2013, 1:08 PM), http://www.forbes.com/sites/jayadkisson/2013/04/27/will-declaratory-judgment-actions-be-the-savior-of-domestic-asset-protection-trusts-probably-not/.

95. Lee, supra note 1, at 171; Boxx, supra note 20, at 1230; Eason, supra note 5, at 67 (“One author considers this avenue of attack as ‘probably the only viable Constitutional claim that could potentially obliterate the new [domestic] asset protection trust laws.”) (citing Leslie C. Giordani, Asset Protection: Domestic and Foreign Planning Alternatives, 33 S. FED. TAX. INST., Oct. 1998, app. B at W-70 ). The Contracts Clause can be found at U.S. CONST. art. I, § 10, cl. 1.

behind the shield of DAPTs, creditors may argue that this has impaired their contractual rights to reach the assets that would have been available to them before the passage of the DAPT statutes. However, the Contracts Clause does not apply to future creditors, and there is a strong counter argument that the contractual rights of existing creditors have not been impaired; rather, merely the remedies available to these creditors to enforce these rights have been affected. Thus, most commentators feel that such a challenge would not present a real threat to the success of DAPTs.

II. DAPTS AND CHILD SUPPORT

As noted previously, a chief consideration among states that have passed DAPT legislation is how each respective state would treat child support claims. Some legislators were concerned that settlors could utilize DAPTs to avoid alimony or child support payments. Accordingly, most states included some sort of exception for child support. However, not all states included such an exception, and


99. See Giordani & Osborne, supra note 97, at 8 (“[O]ne defense would be an argument that fraudulent transfer laws offset the impairment of creditor/debtor contracts inherent in Alaska’s new law, providing present and foreseeable creditors with a viable remedy when faced with a debtor who has transferred assets to avoid his or her repayment obligation.”). Even if a creditor can successfully argue that the DAPT statute has “substantially impair[ed]” an “existing contractual obligation,” the creditor will still be out of luck if a court determines that the “state [had] a justifiable purpose for passing the law and . . . the legislature narrowly drafted the statute to achieve that purpose.” Boxx, supra note 20, at 1231.

100. See, e.g., Eason, supra note 5, at 67 (“[I]t would seem that such an argument is tenuous, at best . . . .”); Sirknen, supra note 28, at 153 (“[DAPTs], however, should not be vulnerable under [the Contracts Clause] because the clause prohibits impairment of existing contracts, and most [D]APTs have an exception that allows creditors existing at the time the trust is created to bring claims within a certain number of years.”).


102. See, e.g., Wagenfeld, supra note 101, at 860–61.

103. See COMPARISON, supra note 3. In including an exception for child support, these states followed the general principle that spendthrift clauses do not prevent child support “creditors” from being able to reach the beneficiary’s interest in the trust. See Wagenfeld, supra note 101, at 844 (“United States courts will generally enforce spendthrift trusts that are created by the settlor for the benefit of a third party. However, there are several exceptions to this
even for those states that did include an exception in their DAPT statutes, the exceptions often vary in the language that is used and in the conditions necessary to be applicable.

Hence, in order to determine whether DAPT statutes are a threat to child support, it is necessary to examine the language of these child support exceptions when included in the statute. The DAPT statutes can be grouped into three categories, depending on whether the DAPT statute included a strong exception, a weak exception, or no exception at all.

A. States with a Strong Child Support Exception

The majority of states have included exceptions in their respective DAPT statutes that appear to offer a significant amount of protection for child support. States that fall into this category are Delaware, Missouri, New Hampshire, Oklahoma, Rhode Island, South Dakota, Tennessee, Ohio, Virginia, and Wyoming.

Some of these exceptions explicitly state that child support creditors can obtain a court judgment allowing attachment of trust assets. For instance, Missouri’s DAPT statute states, “a beneficiary’s child . . . who has a judgment against the beneficiary for support or maintenance . . . may obtain from a court an order
attaching present or future trust income.” Other exceptions simply state that the protections afforded in the DAPT statute do not apply to child support creditors.

B. States with a Weak Child Support Exception

Some states included an exception for child support in their respective DAPT statutes that provide only weak protection for child support. The three states that fit into this category are Alaska, Hawaii, and Utah. For example, Alaska’s DAPT statute provides that creditors of the settlor (including child support “creditors”) may attach the funds that the settlor transfers into the trust, but only if the settlor is in default thirty days or more of a court order judgment or order for child support. Similarly, Hawaii’s statute states that the restrictions placed on creditors “to avoid permitted transfers” by the settlor to the trust do not apply to child support claimants, but only apply if the settlor is in default “thirty days or more of making a payment due under the agreement or order.”

Under such a statutory scheme, it is easy to imagine possibilities where a settlor could avoid child support. For example, so long as a settlor made sure to be up-to-date with child support, or a settlor ensured that he or she was not in default for not paying child support more than thirty days, the settlor could fund the trust, which could then not be reached. As such, these child support exceptions prevent settlors from creating a DAPT trust only if child support creditors exist at the time of the transfer to fund the trust and offer no protection to child support after the trust is created. For instance, this situation may arise if a settlor’s

119. MO. ANN. STAT. §§ 456.5–503.2 (West 2013).
121. See ALASKA STAT. § 34.40.110 (b)(4) (2012).
123. See UTAH CODE ANN. § 25-6-14 (2013).
124. ALASKA STAT. § 34.40.110 (b)(4) (2012).
126. See Wagenfeld, supra note 101, at 860–61.
127. Id.
128. See Lee, supra note 1, at 163.
child is born after the creation of the trust, in which case the trust assets would be out of reach for any child support judgment.\textsuperscript{129}

\textit{C. States with No Child Support Exception}

At the extreme of the DAPT spectrum is Nevada, which did not provide any exception for child support creditors. Nevada’s DAPT statute reads as follows:

[T]he interest of the beneficiary [shall not] be subject to any process of attachment issued against the beneficiary, or to be taken in execution under any form of legal process directed against the beneficiary or against the trustee, or the trust estate, or any part of the income thereof, but the whole of the trust estate and the income of the trust estate shall go to and be applied by the trustee solely for the benefit of the beneficiary, free, clear, and discharged of and from any and all obligations of the beneficiary whatsoever and of all responsibility therefor.\textsuperscript{130}

Because Nevada’s DAPT statute does not include any exception for child support claimants, it presents the greatest threat to child support. Nevada’s decision not to include an exception for child support is alarming because in a “race to the bottom”\textsuperscript{131} to become the top trust situs, Nevada’s law has become the new standard for other states.\textsuperscript{132}

\textit{D. Tax Considerations Drive the Race to the Bottom}

At first glance, the states that included little or no protection for child support in their DAPT statutes might appear to have done so

\begin{itemize}
  \item \textsuperscript{129} Wagenfeld, \textit{supra} note 101, at 861.
  \item \textsuperscript{130} Nev. Rev. Stat. §166.120 (2012) (emphasis added).
  \item \textsuperscript{131} See \textit{supra} note 13 and accompanying text.
  \item \textsuperscript{132} For instance, Utah, which once provided a strong exception for child support, recently amended its statute to severely weaken this protection. Somewhat similar to Alaska’s and Hawaii’s statutes, Utah’s statute requires that settlors must sign an affidavit, swearing that they are not in default of paying child support at the time assets are transferred into the fund. Utah Code Ann. § 25-6-14 (5)(h) (2013). Before distributions can be made to the settlor-beneficiary, the trustee must give thirty days advance notice to any child support dependent of the settlor, letting them know of the impending distribution. However, the statute does not provide a way for the child support dependent to attach the distribution before it happens. Assumedly, the child support dependent must go to court each time a distribution is to be made to have a chance at getting the assets, by which time the assets may have already been depleted. Consequently, the exception (if it can be called one) has little teeth in protecting child support dependents.
\end{itemize}
in an attempt to be the “best” asset protection situs—i.e., the state could then market DAPTs set-up in its state as being completely creditor proof, even from child support claimants. While this factor may be part of the equation, a different factor, specifically estate tax, more likely explains why certain states, such as Nevada and Alaska, did not include an exception for child support.

Internal Revenue Code (I.R.C.) § 2036 states that a person’s property will be included in that person’s estate for estate tax purposes if the person retains “the possession or enjoyment of . . . the property.”[133] In other words, if creditors can reach trust assets, the question arises whether the settlor still retains possession or enjoyment of the property. If the answer is yes, then trust assets are included in the settlor’s estate when the settlor dies.

Applied in the DAPT context, I.R.C. § 2036 means that trust assets can potentially be included in the settlor’s estate and increase the amount of estate taxes that must be paid if child support claimants can reach the trust assets. In analyzing whether a settlor still wields power over trust assets under I.R.C. § 2036, it is irrelevant that a settlor would likely object to and attempt to prevent the transfer of trust assets to a child support claimant; rather, the mere possibility of such a transfer may be indicative of the settlor retaining “possession or enjoyment of” trust assets. Because estate tax reduction is a key feature that makes DAPTs attractive to potential settlors, whether a state’s DAPT statute allows for estate tax reduction under I.R.C. § 2036 is an extremely important consideration, and possibly the deciding factor, in which state a settlor chooses to set up a DAPT.

When states considered the best structure for their DAPT statutes, they were keenly aware of this issue.[134] The solution for some states was simple—make DAPTs in their state impervious to all creditors. Alaska’s statute, for example, was “clearly intended to completely shield these trusts from any claims of creditors.”[135] Other states, such as Delaware, also intended their DAPT statute to provide settlors with estate tax benefits,[136] but also included an exception for child support. However, because Delaware’s statute includes this

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134. See, e.g., Wagenfeld, supra note 101, at 861–62.
135. Id. at 862.
136. Id. at 865.
exception for child support, its statute is less likely to provide this
estate tax benefit.137

For several years after the creation of DAPTs, the IRS declined to
rule on whether these trusts would be included in the settlor’s
estate.138 In 2009, the IRS ruled favorably for assets held in an
Alaskan DAPT, stating that they would not be included in the
settlor’s estate for estate tax purposes.139 However, a recent ruling
potentially establishes that only DAPTs that do not allow any
creditors (including child support creditors) to reach trust assets are
the only type of DAPT that provides these tax benefits for settlors.140
Although the current IRS stance is unclear, if such protection from all
creditors is necessary to provide estate tax benefits, states now have a
strong incentive to structure their DAPT statutes to prevent all
creditors from reaching trust assets, thus making the threat of people
using DAPTs to avoid paying child support even greater.

III. PUBLIC POLICY CONSIDERATIONS

DAPT statutes that do not include strong exceptions for child
support violate important public policy considerations. These
considerations mainly revolve around the immorality of allowing
settlers to hide assets from child support claimants, but potentially
include economic considerations as well.

In evaluating how DAPTs without strong exceptions for child
support have already affected or are likely to affect child support, there
is currently a lack of data to analyze. A purview of the relevant case law
did not turn up any cases involving DAPTs and child support; the case
law on DAPTs in general appears to be very sparse.141 Some

137. See Veit, supra note 83, at 293–94.
138. See id. at 293.
139. David G. Shaftel, IRS Letter Ruling Approves Estate Tax Planning Using Domestic
Asset Protection Trusts, 112 J. TAX’N 213, 216 (2010), available at
2009)).
141. See Paul, supra note 13, at 365 (“[T]he author is unaware of any domestic appellate
court that has enforced a judgment against a qualified disposition in a DAPT. . . .DAPTs are
new devices that have yet to be tested.”); Sirknen, supra note 28, at 158 (“Despite hundreds
of trusts being created, however, the author has been unable to find any case in which a
creditor has brought a challenge to a domestic APT.”); Wagenfeld, supra note 101, at 875
(“[W]hether the recent legislation will accomplish this unique combination of benefits to
settlers and the potential detriment to creditors has yet to be tested by a court.”); see also
commentators may view this dearth of case law as evidence that DAPTs are not a threat to child support. Admittedly, there are compelling reasons why case law may be lacking in this area; settlors who have enough assets to set up a DAPT are likely not the type of people who are going to shirk paying child support, and they are also more likely motivated to create a DAPT to obtain estate tax and general asset protection benefits then to stiff child support dependents. Additionally, even if it was the intention of a settlor to avoid paying child support, some commenters have suggested that in DAPT states lacking a strong child support exception, the courts would prevent settlors from doing so by creating a judicial exception for child support, regardless of the statutory language. Lastly, because the total number of DAPTs appears to be very small,
DAPTs are not likely to affect “more than a handful of people each year.”

Regardless of whether DAPTs have been used to avoid paying child support, DAPTs pose a real and potent threat to child support because the plain language of these statutes clearly permits settlors to shield their assets from child support claimants. Moreover, it seems unlikely that a court would create a judicial exception for child support when the language in the DAPT statute is unambiguously clear concerning protection for trust assets against all creditors.

This threat is made even more real by the fact that as DAPTs become more popular and well known, it is likely that the difficulty and cost of creating a DAPT will be reduced, making them available to a greater number of people, who can potentially abuse the system. Hence, what may now be an innocuous threat to child support in the hands of good-intentioned settlors (at least concerning paying child support) could turn into a vicious tool against child support as ill-intentioned deadbeats learn of and utilize these trusts. While there is certainly uncertainty regarding how these trusts will be used going forward, that very uncertainty justifies greater statutory protection for child support, whose importance should be valued higher than a state’s desire to increase trust revenue within the state. DAPT states without a strong exception for child support should not recklessly keep such a readily available option that allows deadbeat settlors to victimize child support dependents.

The following two sections further develop the public policy considerations mentioned above. The first section discusses the immorality of allowing such deadbeat settlors to avoid paying child support. The second section attempts to provide a purely economic analysis of whether allowing such action is desirable, and tentatively concludes that allowing such action is unwise from an economic standpoint.

A. Child Support—A Moral Duty

There are several ways to analyze the issue of whether DAPT legislation that does not contain a strong exception for child support

146. See id. at 157–58 (quoting Elizabeth Warren, Reducing Bankruptcy Protection for Consumers: A Response, 72 GEO. L.J. 1333, 1335 n.17 (1984)).

147. For instance, websites such as Legalzoom.com may in the future offer a lower-cost alternative to setting up a DAPT.
should be disfavored due to public policy considerations. Some legal scholars may fervently argue that the issue should be addressed solely under an economic analysis, and such an analysis is included below; however, this issue begs the question: should money even matter when deciding? For some, the answer is resoundingly no.

Some duties are of such importance that states should not create incentives for persons to disregard them. One such responsibility is the moral duty for one to pay one’s debts. While directed at spendthrift trusts in general, one commentator has argued that paying one’s debts is not only the “right thing to do,” but “there is something disturbing about a country that would allow debtors to leave their debts unpaid and still enjoy an extravagant lifestyle.”

Although many states permit this principle to be routinely disregarded through spendthrift trusts created for the benefit of others, alimony and child support claimants are almost universally granted “special” status, thereby preventing the debtor from avoiding the payment of such claims.

Such exceptions for child support and alimony appear to be grounded in the reasoning that these duties are “sacrosanct” and, as such, are worthy of legislative protection. In other words, the unique and special relationship between family members, in particular the relationship between parents and children, comes with attendant responsibilities and duties that trump basic duties owed to other third parties. To allow settlors to use DAPTs to avoid these duties would be “reprehensible.” Or as one commentator has declared, if courts truly “care about family, this [result] shouldn’t be allowed.”

148. See Danforth, supra note 27, at 364.
149. Id. (citing Professor Boxx).
152. Breitenstine v. Breitenstine, 62 P.3d 587, 593 n.1 (Wyo. 2003); see DUKEMINIER, supra note 29, at 636; Wagenfeld, supra note 101, at 874 (“The problem with this means of raising state revenue [through passing DAPT legislation] is that well-settled concepts of fairness in creditors’ rights issues are being sacrificed. This has the potential to cause offensive outcomes where spouses and children of settlors are denied support payments.”).
153. Baker, supra note 39, at 55 (noting the use of DAPTs to defraud spouses).
Moreover, child support claimants may have an even stronger case than alimony claimants. Unlike former spouses, who at least presumably had a choice whether to “contract” with the settlor through marriage, children of these settlors had no choice whether they would “contract” with their settlor-parent. Rather, their relationship with the settlor arises from the settlor’s actions. Because the blame for the “creditor-debtor” relationship rests in total or at least in part on the settlor-parent and not at all with the child, then it should be against public policy for settlors to be able to avoid paying the child-support dependent.

B. Economic Analysis

Whether DAPT statutes should include a strong exception for child support can also be analyzed under a purely economic basis. In other words, do the costs of not having a strong exception for child support exceed the benefits that these DAPTs derive from not having such an exception? Because of a lack of data in this field, an answer to this question is not readily available. But some factors may indicate that the costs to these DAPTs states could exceed any benefit to these states, in which case not including a strong exception for child support in DAPT statutes is not economical. A further discussion of this analysis follows.

1. Economic benefit

As previously noted, revenue creation has been the main impetus behind states passing DAPT legislation. While there is “tentative evidence” that DAPT statutes in general have increased trust business in the states that have passed these statutes, the magnitude of their effect is vague. Furthermore, it is even more unclear to what extent, if any, DAPT statutes that do not contain a strong exception for child support increase trust business within their respective states in comparison to DAPT statutes that do contain strong exceptions.

154. See Lee supra note 1, at 162.
155. Sitkoff & Schanzenbach, supra note 7, at 411–12. While it is unclear to what extent the passage of DAPT statutes has affected states’ trust business, states that have abolished the Rule Against Perpetuities have seen on average an increase of twenty percent of trust business within their respective state. Id., at 410–11.
It is important to note, however, that any increase in trust business from not including a strong exception for child support would not directly benefit the state as a whole; rather, any direct benefit would go to only a select group of financial institutions or professionals (e.g., trust lawyers) involved in the creation and administration of these trusts.\textsuperscript{156} Regulatory capture by those involved in the trust business can possibly explain the successful passage of DAPT statutes despite such lopsided distribution of benefits.\textsuperscript{157} However, these states and the population as a whole may indirectly benefit through the increased generation of taxes from these institutions and individuals or through the influx of additional money in the state’s economy.\textsuperscript{158}

2. Economic cost

Similar to researching any benefits from DAPTs that lack a strong child support exception, there is also a lack of data concerning the potential costs caused by these statutes. Throughout the nation in general “[o]ver $100 billion is owed in unpaid child support,“ with “nearly half of that to taxpayers supporting children on public assistance.”\textsuperscript{159} However, it is unknown to what extent any of this amount is owed by DAPT settlors, and in particular, by DAPT settlors in states that do not have a strong child support exception.

Importantly, unlike potential benefits of DAPTs lacking a strong child support exception, which would directly benefit only a small group with the DAPT state, the economic costs of these statutes would more likely be borne by all taxpayers of the state if settlors avoided paying child support. Moreover, the cost for the settlor’s

\textsuperscript{156} See Sterk, \textit{supra} note 12, at 1060 (“The competition for trust business . . . differs from the competition for corporate charters in one significant respect: Filling the state government’s coffers does not appear to be a major factor motivating trust-friendly jurisdictions . . . . Jurisdictions seeking to become trust havens . . . . appear content to draw business to local financial institutions and lawyers, even without direct benefit to the public fisc.”). Regulatory capture by those involved in the trust business can possibly explain the successful passage of DAPT statutes despite such lopsided distribution of benefits.

\textsuperscript{157} See \textit{id.} at 1060 n.126 (“Organized interest groups, including the bar and trust companies, seek legislation that will enable them to generate more business, even at the expense of other local residents (particularly creditors).”).

\textsuperscript{158} See Wagenfeld, \textit{supra} note 101, at 859.


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child support avoidance could not only include the state’s current financial assistance to the child, but also other potential harm associated with children growing up in poverty. 160

Also, it is significant that the potential economic costs of these DAPTS do not necessarily have to fall to the DAPT state. A DAPT set up in a DAPT state without a strong exception for child support, such as Nevada, could potentially allow a settlor to hide assets from a child support claim arising in another state, such as California, which does not allow DAPTs at all. 161 In this regard, a state that has a DAPT without a strong exception for child support can cause a negative externality on other states.

Moreover, DAPT states with smaller populations may have to internalize even less economic costs as they likely have a lower number of local settlors in comparison to foreign settlors. 162 Since settlors and child support claimants are likely to reside in the same state, these states are able to externalize the majority of any potential costs to other states. 163 As more states likely join the DAPT competition, however, trust business will be drawn away from these smaller states, in part, and be dispersed among these new DAPT states. 164 If this occurs, it is even more likely that the potential economic costs caused by not having a strong exception for child support will outweigh any benefit to these states. 165 However, in such a scenario it is unlikely for any one state to change its DAPT statute to support child support because it would then receive no benefit but would still bear the costs associated with these statutes. 166 Hence, unless all states contract with each other to eliminate the externalizing effect of these trusts, or Congress acts to prohibit these types of trusts, 167 states with a DAPT statute lacking strong protection for child support will have an incentive to keep their statutes intact.

160. For example, such harm could include “poor heath” and the increased cost of “health care and incarceration.” See Understanding Poverty, Urban Institute, http://www.urban.org/poverty/consequencesofpoverty.cfm (last visited Sept. 24, 2013).

161. The cost could also be borne by other DAPT states, both those with or without a strong exception for child support.

162. See Sterk, supra note 12, at 1069.

163. See id.

164. Id.

165. See id. at 1069–70.

166. See Sterk, supra note 12, at 1070.

167. See Danforth, supra note 27, at 366.
IV. CONCLUSION

DAPT statutes that do not include a strong exception for child support present a real threat to child support. While most DAPT states included strong exceptions for child support in their DAPT statutes, three states—Alaska, Hawai, and Utah—included only weak exceptions for child support, and one state—Nevada—did not include an exception for child support at all. Because of estate tax considerations and in order to compete with other DAPT states, more states are likely to eliminate or weaken any exception for child support in their DAPT statutes.

Despite a lack of evidence that DAPTs in these latter states are currently being used to avoid paying child support, these states’ DAPT statutes and the likely trend that other states will pass similar statutes are troubling because the plain language of these statutes would permit settlors to avoid paying child support. Such avoidance of child support through the use of DAPTs is immoral because of the “sacrosanct” duties parents owe to support their children and the unique nature of the creditor-debtor relationship. Moreover, while somewhat unclear, an economic analysis also supports the conclusion that DAPTs without strong exceptions for child support are unjustified because revenue from such trusts would directly benefit only a small, select group of people within the DAPT states, yet the potential cost of such statutes is borne by everyone in the state where the child resides. Accordingly, for these public policy concerns, DAPT statutes that do not contain a strong exception for child support should be disallowed, stopping trust law’s “race to the bottom” in this area.

Trent Maxwell*

* J.D. Candidate, April 2014, J. Reuben Clark Law School, Brigham Young University. The Author would like to thank Professor Robert S. (Rust) Tippett for suggesting the topic for this Comment and for his guidance throughout the writing process.