Asset Protection & Estate Planning
Why Not Have Both?

By Barry A. Nelson

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Asset Protection & Estate Planning – Why Not Have Both?

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This article addresses the importance of situs selection for partnerships, LLCs, trusts, and to obtain tenants by the entirety protection. As laws change and certain states provide greater asset protection, professionals who structure businesses, investment entities and trusts should consider whether creating trusts and business investment entities outside of their home states should be suggested to clients for greater asset protection, especially if the tax treatment and costs are not materially different. This article also addresses how estate planning and asset protection should be integrated, taking into account applicable state laws in the following situations:

1. *To maximize use of the $5 million estate and gift tax exemption of both husband and wife while simultaneously enhancing asset protection using an inter vivos QTIP trust and/or credit shelter trust.*
2. *To protect the future inheritance of a child or grandchild who is subject to a judgment in the form of alimony or support.*
3. *To maximize protection of members of LLCs or partners of partnerships.*
4. *To invest in real estate as husband and wife as tenants by the entirety that would be protected against a judgment against only one spouse.*

Also addressed are lessons to be learned from experiences of those who have come before us where asset protection techniques have been tested, the benefits of planning ahead, and the consequences of overly aggressive asset protection planning including the incarceration of debtors.

I. Introduction

Recently, much has been written about the benefits of using the laws of states such as Alaska,[1] Delaware,[2] Florida,[3] Nevada,[4] South Dakota,[5] Wyoming[6] and

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[1] ALASKA STAT. §§ 32.11.340; 10.50.380; 34.40.110 (LP, LLC and domestic asset protection legislation).

[2] DEL CODE ANN. TIT 6 § 18-703, TIT. 12 §§ 3536(c)(2), 3570(10)(c), 3574(a) (LLC, inter vivos qualified terminable interest property ("QTIP") trust and domestic asset protection trust legislation).

[3] FLA. STAT. §§ 620.1703, 736.0505 (LP and inter vivos QTIP trust legislation).

[4] NEVADA REV. STAT. §§ 78.746; 86.401; 88.535; 166.040 (corporate, LP, LLC and domestic asset protection trust legislation).

many others, to take advantage of favorable asset protection laws for partnerships, limited liability companies ("LLCs"), trusts, homestead and assets titled by a husband and wife as tenants by the entirety. Asset protection and estate planning should be considered together when advisors suggest the appropriate entities to conduct business and the jurisdictions to form businesses and trusts. For years, advisors have suggested Delaware for business operations.[7] State legislatures, business groups and bar associations have struggled to balance protection of beneficiaries of trusts and owners of businesses against the interests of banks, other lenders, creditors and judgment holders. Many states, such as Florida, are inconsistent with the level of asset protection provided in its trust and business laws as compared to other states. For example, Florida is among the most protective for homestead,[8] limited partnership interests,[9] tenants by the entirety property,[10] life insurance,[11] annuities,[12] retirement planning[13] and inter vivos QTIP trusts.[14] However, the Executive Committee of the Real Property Probate and Trust Law Section of the Florida Bar voted against a 2010 proposal for Florida to enact self-settled asset protection trust legislation. In 2011, Florida enacted a "Patch" that provides protection to members of most multimember LLCs, but not to single-member LLCs. States such as Wyoming and Nevada provide protection to members of multimember, as well as single-member, LLCs.[15] After long debate, Florida became the first state to differentiate between

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[5] S.D. CODIFIED LAWS §§ 48-7-703; 47-34A-504; 55-1-36 (LP, LLC and domestic asset protection trust legislation).

[6] WYO. STAT. ANN. §§ 4-10-506(e); 4-10-510; 17-29-503 (inter vivos QTIP trust, LLC and domestic asset protection trust legislation).

[7] *See* Mohsen Manesh, *Delaware and the Market for LLC Law: A Theory of Contractibility and Legal Indeterminacy*, 52 B.C. L. REV. 189, 210-20 (Jan. 2011); Jill E. Fisch, *Thirteenth Annual Corporation Law Symposium: Contemporary Issues in the Law of Business Organizations: The Peculiar Role of the Delaware Courts in the Competition for Corporate Charters*, 68 U. CIN. L. REV 1061, 1061-71 (Summer 2000).

[8] *See* Barry A. Nelson, *Homestead: Creditor Issues*, *in* ASSET PROTECTION IN FLORIDA (The Fla. Bar & LexisNexis, 2d ed., 2011); Barry A. Nelson, *Florida Surprise*, 147 TRUSTS & EST. 44 (May 2008).

[9] *See* Barry A. Nelson, *Olmstead: Right Result, Wrong Reason*, 35 EST. GIFT & TRUSTS J. 233 (Sept. 2010); Thomas O. Wells & Jordi Guso, *Asset Protection Proofing Your Limited Partnership or LLC for the Bankruptcy of a Partner or Member*, 81 FLA. BAR J. 34 (Jan. 2007).

[10] *See* FLA. STAT. § 689.11; Anne Buzby-Walt, *Are Florida Laws on Tenancy by the Entireties in Personalty as Clear as We Think?*, 85 FLA. BAR J. 52 (Sept./Oct. 2011).

[11] *See* Jonathan E. Gopman et al., *Unraveling the Mysteries of the Florida Exemptions for Life Insurance and Annuity Contracts, Part 1*, 82 FLA. BAR J. 52 (Dec. 2008).

[12] *See id.*; Alan S. Gassman et al., *Creditor's Rights Under Private Annuities and Grantor-retained Annuity Trusts in Florida*, 83 FLA. BAR. J. 49 (July/Aug. 2009).

[13] *See* Kristin M. Lynch, *Death by IRA Beneficiary Designation*, 150 TRUSTS & EST. 56 (Sept. 2011); David Pratt & Lisa M. Stern, *Tax and Asset Protection Benefits Afforded Florida Domiciliaries*, 84 FLA. BAR. J. 32 (Feb. 2010).

[14] *See* Barry A. Nelson & Richard R. Gans, *New §736.0505(3) Assures Tax/Asset Protection of Inter Vivos QTIP Trusts*, 84 FLA. BAR J. 50 (Dec. 2010).

[15] NEVADA REV. STAT. § 86.401(2)(a) ("This section: Provides the exclusive remedy by which a judgment creditor of a member or an assignee of a member may satisfy a judgment out of the member's interest of the judgment debtor whether the limited-liability company has one member or more than one member"); WYO. STAT. ANN. § 17-29-503(g) ("This section provides the exclusive remedy by which a person seeking to enforce a judgment against a judgment debtor, including any judgment debtor who may be the sole member").

single-member and multimember LLCs.[16] As states consider how to attract business and trust formation, they may need to reexamine the consequences of maintaining existing laws that are less protective of beneficiaries, partners, members and shareholders and that may discourage informed attorneys, accountants and financial advisers from forming new businesses or trusts therein.

The issues are controversial and bankers and lawyers have disagreed on the policy and economic benefits of generous asset protection laws.[17] Members of the Florida Bar Real Property, Probate and Trust Law Section debated whether inter vivos QTIP legislation that helps to assure favorable tax treatment and asset protection should be proposed to the Florida legislature.[18] QTIP legislation was ultimately supported by the Executive Counsel of the Florida Bar Real Property Probate and Trust Law Section and was enacted, effective July 1, 2010.

Certain states such as Alaska,[19] Wyoming,[20] South Dakota [21]and Nevada[22] appear to have less difficulty enacting liberal asset protection legislation. In Florida, trust bankers appear more open minded to the benefits of liberal asset protection provisions, such as enactment of self-settled asset protection trust legislation, but regional banks have lobbied against any new laws that protect potential borrowers.

In June of 2010, the Florida Supreme Court, in the case of *Olmstead v. FTC*,[23] considered the rights of a creditor against a debtor who was the sole member of a Florida LLC.[24] The Florida Supreme Court held that a court may order a judgment debtor to surrender the debtor's interest in the single-member LLC to satisfy the judgment. Although the decision of the Florida Supreme Court in *Olmstead* was

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[16] FLA. STAT. § 608.433(6) ("a charging order is not the sole and exclusive remedy by which the judgment creditor may satisfy the judgment against a judgment debtor who is the sole member of a limited liability company or the assignee of the sole member").

[17] The Florida Bankers Association lobbied against laws providing greater asset protection, such as the recent amendment to Florida's LLC Statutes Section 608.433. *Compare* Florida Senate Meeting Minutes (Podcast), Apr. 25, 2011, *available at* http://www.flsenate.gov/committees/show/bi (remarks of Senator David Simmons, "This bill is a compromise between the Florida Bar members and the Florida Bankers Association...The Florida Bankers Association is looking to protect banks who lend to individuals and who might borrow money and then transfer an interest into an LLC to hide from creditors"), *with* Master List of Legislative Positions 2010-12, FLA. BAR. Aug. 2, 2011, *available at* http://www.floridabar.org/tfb/TFBLegNW.nsf/dc7ee304c562ed5b85256709006a26ee/e9db5ca1c9671a0385256b2f006cd0ce?OpenDocument#Tax%20Section(explaining that both the Business Law Section and Real Property, Probate and Trust Law Section supported amendment of section 608.433).

[18] *See* FLA. STAT. § 736.0505 (update enacted July 2010).

[19] ALASKA STAT. §§ 32.11.340; 10.50.380; 34.40.110 (favorable LP, LLC and self-settled trust legislation).

[20] WYO. STAT. ANN. §§ 4-10-506(e); 4-10-510; 17-29-503 (favorable inter vivos QTIP, LLC and self-settled trust legislation).

[21] S.D. CODIFIED LAWS §§ 47-34A-504; 48-7-703; 55-1-36 (favorable LP, LLC and self-settled trust legislation).

[22] NEVADA REV. STAT. §§ 86.401; 88.535;166.040 (favorable LP, LLC and self-settled trust legislation).

[23] 44 So. 3d 76 (Fla. 2010).

[24] *Id.* at 76-77. *See* Section III., *infra*. The issue was whether the sole owner of a Florida LLC (i.e., commonly referred to as a single-member LLC) could benefit from charging order protection. If not the creditor could gain full control of the LLC.

not surprising to those who understood that the purpose of the charging order was to protect other members or partners of LLCs/partnerships, the reasoning of the Florida Supreme Court should serve as a wakeup call for all states to examine the consistency, or lack thereof, of remedies of creditors of a partner of a partnership or member of an LLC. *Olmstead*, discussed in Section III., below, serves as an example of how a court could compare a state's LLC and Limited Partnership Act provisions to distinguish remedies available to creditors against partners and members. Slight distinctions in LLC and partnership charging order statutes could result in a divergence in protection should a partner/member find him or herself subject to a judgment.[25] States having laws similar to Florida at the time *Olmstead* was decided should consider whether they want to provide charging order protection for single-member LLCs (such as in Nevada and Wyoming) or provide charging order protection only for multimember LLCs (such as in Florida).

While asset protection techniques are frequently discussed at educational seminars, in articles and treatises (e.g., thirteen states have adopted some form of self-settled asset protection trust legislation),[26] some techniques are less well known. For example, currently four states[27] have enacted legislation to make it clear that inter vivos QTIP trust assets remain protected in a spendthrift trust as to the initial donor, even if the donor's spouse predeceases the initial QTIP trust donor and the inter vivos QTIP trust assets revert to a credit shelter trust for the initial donor spouse (see discussion in Section II., below). The time to consider the jurisdictional issues is when trusts, partnerships, LLCs and other businesses are created.

II. Inter Vivos QTIP Trusts and Credit Shelter Trusts to Take Advantage of $5 Million Exemptions

A. Introduction, Planning Under the 2010 Tax Relief Act

Since January 1, 2011, the Tax Relief Unemployment Insurance Reauthorization, and Job Creation Act of 2010 (the "2010 Tax Relief Act")[28] increased the applicable exclusion amount to $5 million (until

[25] *See* Olmstead, 44 So. 3d 76.

[26] Alaska, Colorado, Delaware, Hawaii, Missouri, Nevada, New Hampshire, Oklahoma, Rhode Island, South Dakota, Tennessee, Utah and Wyoming have all adopted self-settled trust legislation. *See* ALASKA STAT. § 34.40.110(A); COLO. REV. STAT § 38-40-111; DEL. CODE ANN. TIT. 12, §§ 3536(C), 3570-3576; HAW. REV. STAT., §§ 554G-1—G-12; MO. REV. STAT. § 456-005.505; N.H. REV. STAT ANN. §§ 564-B:5-505(C), 564-D:1-D:18; NEVADA REV. STAT. §§ 166.010-166.170; OKLA. STAT. TIT. 31, §§ 10-18; R.I. GEN. LAWS §§ 18-9.2-1—18-9.2-7; S.D. CODIFIED LAWS §§ 55-1-36, 55-16-1—55-16-17, 55-3-39, 55-3-41, 55-3-47; TENN. CODE ANN. §§ 35-16-101—35-16-112; UTAH CODE ANN. § 25-6-14; WYO. STAT. ANN. §§ 4-10-103, 4-10-506(b), 4-10-510—4-10-523.

[27] Arizona, Delaware, Florida, Michigan and Wyoming have all adopted inter vivos QTIP trust planning legislation. *See* ARIZ. REV. STAT. § 14-10505(E); DEL. CODE ANN. TIT. 12 § 3536(C)(2); FLA. STAT. § 736.0505(3); MICH. COMP. LAWS § 700.7506(4); WYO. STAT. ANN. § 4-10-506(e).

[28] Tax Relief Unemployment Insurance Reauthorization and Job Creation Act of 2010, 111 P.L. 312, 124 Stat. 3296 (Dec. 17, 2010) [hereinafter 2010 Tax Relief Act].

2013),[29] portability is available, and federal estate, generation skipping and gift tax rates are 35%. A number of articles have been written on how to best use the increased exemption, especially for those who are concerned that the exclusion may be reduced in the future.[30] Articles have also been written on whether it is prudent to rely on portability.[31]

Planning alternatives under the 2010 Tax Relief Act will differ based upon expectations of the future of the $5 million exemption and portability. Even if portability remains, it has a number of shortfalls.[32] For example, if the surviving spouse remarries and the new spouse also predeceases him or her, then the availability of the unused applicable exclusion amount is based upon the last deceased spouse. As a result, if the first predeceased spouse (Joan) left all of her assets outright to her husband (Sam), and then Sam remarries a wealthy woman (Mary) who already made full use of her applicable exclusion amount by making gifts to her children, then if Mary predeceases Sam, Sam will not benefit from portability. Sam's last deceased spouse had no unused exclusion amount.[33] Another shortfall of portability is that the unused exclusion amount is not tied to the consumer price index and thus is not indexed for inflation. The appreciation in value of assets placed in a credit shelter trust passes tax free to the ultimate beneficiaries. If a surviving spouse lives for an additional ten to twenty years and the assets inherited outright from the first spouse to die significantly appreciate in value, the estate tax on the appreciation upon the death of the surviving spouse could have been avoided if instead the assets were held in a credit shelter trust (to the extent the surviving spouse

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[29] *Id.* at 3298.

[30] *See* Carol G. Kroch et al., *Taking a Fresh Look at Lifetime Gift Planning Opportunities*, 38 EST. PLAN. 3 (Sept. 2011); Robert F. Sharpe, *Increased Exemption Amounts Create New Opportunities*, TRUSTS & EST, Mar. 1, 2011, http://subscribers.trustsandestates.com/philanthropy/estate_increased_exemption_amounts_0226/index.html (last visited Oct. 19, 2011); Diane Freda, *New Tax Law Shifts Focus of Estate Planning Techniques, Attorneys Say*, 29 DTR G-5, (Feb. 11, 2011); Jonathan G. Blattmachr et al., *Estates Planning After the 2010 Tax Relief Act: Big Changes, But Still No Certainty*, 114 J. OF TAXATION 68 (Feb. 2011); Steve R. Akers, Estate Planning Effects and Strategies Under the "Tax Relief ... Act of 2010", Address at the 45th Annual Heckerling Institute on Estate Planning (Jan. 2011), *in* 45th Annual Heckerling Institute on Estate Planning (Matthew Bender, Pub., 2011).

[31] *See generally* Louis A. Mezzullo, *Portability's Effect on Planning for Retirement Benefits*, BNA, Aug. 4, 2011, *available at* http://www.bna.com/portabilitys-effect-planning-n12884902983/ (last visited Oct. 19, 2011); Gregory D. Singer & Andrew Auchincloss, *Making Two Years Last a Lifetime*, 150 TRUSTS & EST. 30, 32-33 (Aug. 2011); Howard M. Esterces, *Should Portability Make One 'Fugeddabout' Credit Shelter Trusts?*, 85 PRACTICAL TAX STRATEGIES, 148 (Apr. 2011); Dennis I. Belcher, Samuel A. Donaldson, & Beth Shapiro Kaufman, Question and Answer Session at the 45th Annual Heckerling Institute on Estate Planning (Jan. 2011), *in* 45th Annual Heckerling Institute on Estate Planning (Matthew Bender, Pub., 2011); Deborah V. Dunn, *Bypass the Bypass Trust?*, 150 TRUSTS & EST. 24 (Feb. 2011); Carol A. Cantrell, The Power of Post-Mortem Estate Planning (Selected Issues for 2010 and 2011), Address at the 45th Annual Heckerling Institute on Estate Planning (Jan. 2011), *in* 45th Annual Heckerling Institute on Estate Planning (Matthew Bender, Pub., 2011).

[32] *See* Marty Shenkman & Bob Keebler, *Ten Portability Malpractice Traps Practitioners Should Consider* (Steve Leimberg's Estate Planning Newsletter #1880) Oct. 18, 2011, *available at* http://www.leimbergservices.com.

[33] *See* Blattmachr et al., *supra* note 30, at 80-81; Esterces, *supra* note 31, at 150-51.

had other assets available). Credit shelter trusts may also provide asset protection to trust beneficiaries. Thus, by using a credit shelter trust, the first spouse can assure that his or her wealth passes as he or she intends and appreciation on assets, as well as a cumulative increase in the credit shelter trust, may pass estate and generation-skipping transfer tax free to children and more remote descendants. The aforementioned benefits are not possible if portability is relied on and assets are conveyed outright to a surviving spouse.

Those who are willing to rely on portability may decide that owning the entire $10 million of assets jointly is a simple plan that avoids probate after the death of the first spouse, especially in states such as Florida that protect assets held by a husband and wife as tenants by the entirety from claims of general creditors that are not joint creditors.[34] Among the typical suggestions for a couple with a $10 million net worth, who prefer not to rely on portability, is to divide assets so both a husband and wife take advantage of their respective $5 million exemption. However, both holding assets in separate revocable trusts and holding the entire $10 million in joint names, even tenants by the entirety, could create potentially devastating asset protection consequences as described more fully below. Having each spouse create separate non reciprocal inter vivos QTIP trusts provides asset protection and assures the use of each spouse's applicable exclusion amount. If such inter vivos QTIP trusts are created in Arizona, Delaware, Florida, Michigan or Wyoming (referred to hereinafter as the "Inter Vivos QTIP Trust Jurisdictions"), the anticipated tax and asset protection benefits are significantly more likely to be achieved as compared to those inter vivos QTIP trusts created in states that have not modified their spendthrift trust statutes.[35]

B. Planning Using Inter Vivos QTIP Trusts

The Inter Vivos QTIP Trust Jurisdictions have modified their spendthrift trust statutes to provide that where an inter vivos QTIP election was made, then, after the death of the donor's spouse, any assets passing back into a trust for the initial donor spouse are deemed to have been contributed by the donor's deceased spouse and not by the donor.[36] The creation of inter vivos QTIP trusts thereby allows married couples to take advantage of one another's federal estate tax exemptions and, at the same time, to enhance asset protection planning. These statutes (referred to hereinafter as the

[34] For a discussion on tenants by the entirety, see Section V., *infra*.

[35] *See* ARIZ. REV. STAT. § 14-10505(E); DEL. CODE ANN. TIT. 12 § 3536(c)(2); FLA. STAT. § 736.0505(3); MICH. COMP. LAWS § 700.7506(4); WYO. STAT. ANN. § 4-10-506(e). Since 2009, all said statutes were amended to provide protection for inter vivos QTIP trusts. It may also be possible to utilize an inter vivos QTIP trust plan in one of the 13 self-settled asset protection trust jurisdictions referred to in Footnote 26, above.

[36] For example, see FLA. STAT. § 736.0505(3).

"Inter Vivos QTIP Spendthrift Statutes"), coupled with the 2010 Tax Relief Act, provide estate planners with a great planning opportunity.

1. Dennis and Debbie – An Example

In order to illustrate the planning possibilities of an inter vivos QTIP spendthrift trust plan, a hypothetical example is provided. Dennis and Debbie, both attorneys, are married with children and reside in Florida. Dennis and Debbie have accumulated a net worth of approximately $13.5 million, of which $3.5 million is equity in their Florida homestead, and $10 million is invested in a joint brokerage account (titled "tenants by the entirety"). Dennis and Debbie are willing to rely on estate tax portability to maintain a "simple" estate plan and benefit from asset protection provided by tenants by the entireties ownership.[37] Assuming Debbie dies in 2012 and Dennis in 2013, and that estate and gift tax rates and portability are both extended until 2013, no estate tax is due upon Debbie's death and the tax upon the death of Dennis, assuming portability, would be $1.225 million (Dennis' taxable estate of $13.5 million - $10 million applicable exclusion amount = $3.5 million x 35% tax rate = $1.225 million).[38] Although all of their assets are protected from creditors during their joint lifetimes (assuming all debts are owed to individuals as compared to the IRS or SEC,[39] they remain married to one another, had no joint debt and all property was held as tenants by the entirety or as their Florida homestead) upon the death of Debbie, all assets that pass to Dennis by operation of law, other than their Florida homestead, would be subject to the creditors of Dennis.[40] Understanding that Dennis and Debbie's current estate plan fails to take advantage of the estate tax exemption amount of the first spouse to die, in the event portability is not extended, and in order to possibly enhance the amount of assets that can pass free of tax upon the death of the surviving spouse by allowing the assets of the credit shelter trust to grow, their CPA suggests that Debbie's assets be re-titled so the revocable trust created by Dennis owns $5 million (thereby avoiding probate and taking advantage of his estate tax exemption if he dies first), and the revocable trust created by Debbie owns $5 million.[41] Each of their revocable trusts creates a testamentary credit shelter trust primarily for the benefit of the surviving spouse of the greatest amount that can pass free of estate tax upon the death of the first spouse, which trust is intended to pass free of estate tax upon the death of the surviving spouse.

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[37] For an explanation on tenants by the entirety, see Section V., *infra*.
[38] *See* Exhibit A.
[39] *See* discussion in Section V.C., *infra*.
[40] *Id.*
[41] *See* Exhibit B.

Dennis and Debbie's desire is to maintain access to all family wealth until the survivor of them passes away, but they do not mind having a portion of the funds held in trust for the surviving spouse, as long as the surviving spouse can serve as a co-trustee or as sole trustee during his or her lifetime, and as long as distributions can be made to the surviving spouse based upon an ascertainable standard (such as for his or her health, maintenance and support). Assuming they follow their CPA's suggestion and divide their assets so each has $5 million in their respective revocable trusts, none of the $10 million owned by their trusts would be protected from creditors while both spouses were married and living because assets in a revocable trust are not protected from creditors' claims.[42] Assuming Debbie predeceases Dennis and no claims are made against her estate, Debbie's assets can pass into a credit shelter spendthrift trust for Dennis, generally protected from the creditors of Dennis. During the lifetime of Dennis, $5 million or more (i.e., the assets held in the credit shelter trust for the benefit of Dennis as well as any growth and accumulated income) is protected from his creditors, but the $5 million held in the revocable trust created by Dennis remains subject to his creditors.[43] Based upon the assumptions above, upon his death, Dennis' estate would pay $1.225 million in estate taxes assuming no appreciation on his $5 million investments and his $3.5 million residence.[44]

Dennis and Debbie want a second opinion, so they consult with Mike, an attorney whose practice combines estate planning and asset protection. Mike explains that converting $10 million of their assets from tenants by the entirety into two $5 million revocable trust accounts changes the character of the assets from those that are protected from most potential creditors (as long as the debt was not a joint debt of Dennis and Debbie, and both were living and married to one another in a state that fully protects tenants by the entirety assets), and subjects the entire $10 million to claims of their respective creditors because assets in a revocable trust are unprotected.[45] Dennis and Debbie ask for alternatives that would allow each of them to take advantage of their estate tax exemptions

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[42] ARIZ. REV. STAT. § 14-10505(E); DEL. CODE ANN. TIT. 12 § 3536(c)(2); FLA. STAT. § 736.0505(3); MICH. COMP. LAWS § 700.7506(4); WYO. STAT. ANN. § 4-10-506(e). *See* Exhibit B.

[43] *See* Exhibit B.

[44] Dennis' Gross Estate ($8.5 million, $5 million of brokerage assets and $3.5 million in equity from homestead) – Applicable Exclusion Amount ($5 million) = Dennis' Taxable Estate ($3.5 million). Dennis' Estate Tax is $1.225 million ($3.5 million x 35%). *See* Exhibit B.

[45] FLA. STAT. § 736.0505(1)(a) ("The property of a revocable trust is subject to the claims of the settlor's creditors during the settlor's lifetime to the extent the property would not otherwise be exempt by law if owned directly by the settlor"). *See* Exhibit B.

while at the same time not subjecting their assets to exposure to the claims of future creditors.

Mike explains that as a result of the enactment of Florida's new inter vivos QTIP spendthrift statute, assuming Dennis and Debbie have no existing actual or contingent liabilities,[46] Dennis and Debbie can divide their $10 million tenants by the entireties brokerage account equally between them and create separate inter vivos QTIP trusts, taking care that the trusts are not reciprocal.[47] Inter Vivos QTIP Trust Jurisdictions provide a solution to many of Dennis and Debbie's tax and asset protection objectives. Rather than maintaining the assets in unprotected revocable trusts (and thereby subjecting $10 million of assets to potential future creditors), Dennis can create an inter vivos QTIP trust for Debbie and transfer $5 million of assets to the trust, and Debbie can do the same for Dennis.

Dennis would only be willing to create the trust for Debbie if he had reasonable assurances that, should Debbie predecease Dennis, he would have access to the $5 million (or such other amount as may be held in the trust upon Debbie's death). To maintain flexibility for future planning, the inter vivos QTIP trust can give Debbie a testamentary special power of appointment that could be exercised in favor of one or more of Dennis, their children, or a charity.[48] However, if Dennis wants to be certain that, should Debbie predecease him, the assets would be held in a trust for him, the QTIP trust could provide that if Dennis survives Debbie, assets remaining in Debbie's QTIP trust must pass in trust for the benefit of Dennis during his lifetime. The trust could provide a formula so, to the extent assets that were held in Debbie's trust can pass free of estate tax as a result of Debbie's applicable exclusion amount, they

[46] While Dennis and Debbie enjoy tenancy by the entireties protection of their jointly owned assets, once Debbie and Dennis separate their tenants by the entirety property so each of them owns one half in their own names, the tenancy by the entireties protection is lost. In the event either Debbie or Dennis had any outstanding creditors at that time, breaking the tenancy by the entirety would subject any assets held in the sole name of Debbie or Dennis to claims of their creditors and a conveyance by them to an inter vivos QTIP trust at a time where either of them is insolvent could be deemed a fraudulent conveyance, thereby subjecting the transfer to attachment or other creditors' remedies. *See* FLA. STAT. §§726.105; 726.108.

[47] This should only be done if Dennis and Debbie do not have existing debt because once assets held as tenants by the entirety are divided and retitled in their respective names, assets that previously were protected from creditors as tenants by the entirety (assuming no joint debt) would be subject to creditors' claims of Dennis and Debbie since they will have outright ownership of $5 million each prior to contributing such assets to the new QTIP trusts. Reciprocal trusts must be avoided. For an excellent article addressing the reciprocal trust issue in great detail, see Mitchell M. Gans, Jonathan G. Blattmachr & Diana S.C. Zeydel, *Supercharged Credit Shelter Trust*, 21 PROB. & PROP. 52, 57-62 (July/Aug. 2007).

[48] A special power of appointment provides the power holder with the right to distribute property, subject to the power, to a limited class of beneficiaries or alternatively to a broad class that excludes the power holder, the power holder's estate, the power holder's creditors, or the creditors of the power holder's estate. *See* I.R.C. § 2041.

would pass into a credit shelter trust for Dennis with any excess assets passing into a QTIP trust for Dennis so no estate tax would be payable upon Debbie's death.[49] Use of this technique assures that the assets held in the inter vivos QTIP trust for the benefit of Debbie are protected from her creditors during Debbie's lifetime because the QTIP trust is a spendthrift trust. Furthermore, upon Debbie's death, the assets remaining in her QTIP trust will be held in an asset-protected spendthrift trust for the benefit of Dennis (a credit shelter trust and/or a QTIP trust).[50]

Until enactment of the inter vivos QTIP trust statutes, assets passing from the inter vivos QTIP trust created by Dennis for Debbie back to Dennis at Debbie's death, whether based upon the terms of the original trust or through the exercise of a special power of appointment from Debbie, might have been thought to be subject to the claims of creditors of Dennis because he created the original trust.[51] In his defense against a creditor's challenge to the trust, Dennis would argue that Debbie, and not Dennis, should be considered as the donor of the trust after Debbie's death, so Dennis is not properly considered the donor of the trust passing to him upon Debbie's death. This argument would be consistent with

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[49] The mandatory reversion in favor of Dennis would be even more critical if he had children from a prior marriage and he wanted to be certain that upon Debbie's death the assets would: a) pass for his benefit if he survives Debbie; or b) to his children if he predeceases Debbie or disclaims the interest otherwise passing to him upon Debbie's death.

[50] This article assumes assets in a spendthrift trust are protected from general creditors. Exception creditors, such as the IRS, may circumvent spendthrift protection. *See* FLA. STAT. § 736.0503(2)

> To the extent provided in subsection (3), a spendthrift provision is unenforceable against: (a) A beneficiary's child, spouse, or former spouse who has a judgment or court order against the beneficiary for support or maintenance. (b) A judgment creditor who has provided services for the protection of a beneficiary's interest in the trust. (c) A claim of this state or the United States to the extent a law of this state or a federal law so provides.

Id.

[51] *See* ARIZ. REV. STAT. § 14-10505(A)(2) ("with respect to an irrevocable trust, a creditor or assignee of the settlor may reach the maximum amount that can be distributed to or for the settlor's benefit."); DEL. CODE ANN. TIT. 12 § 3536(a)

> A creditor of a beneficiary of a trust shall have only such rights against or with respect to such beneficiary's interest in the trust or the property of the trust shall be expressly granted to such creditor by the terms of the instrument that creates or defines the trust or by the laws of this State.

Id.; FLA. STAT. § 736.0505(1)(b) ("With respect to an irrevocable trust, a creditor or assignee of the settlor may reach the maximum amount that can be distributed to or for the settlor's benefit"). If the original donor of an inter vivos QTIP trust is also treated as the donor of the trust for his or her benefit after the death of the initial beneficiary spouse, under Florida law prior to § 736.0505(3), the donor's creditors could reach the trust assets in satisfaction of their claims; MICH. COMP. LAWS § 700.7506(1)(c) ("With respect to an irrevocable trust, a creditor or assignee of the settlor may reach no more than the lesser of the following:(i) The claim of the creditor or assignee. (ii) The maximum amount that can be distributed to or for the settlor's benefit exclusive of sums to pay the settlor's taxes during the settlor's lifetime"); WYO. STAT. ANN. § 4-10-506(a)(ii) ("With respect to an irrevocable trust without a spendthrift provision, a creditor or assignee of the settlor may attach the maximum amount that can be distributed to or for the settlor's benefit").

Treas. Reg. § 25.2523(f)-1(f), Example 11, which provides that assets held in an inter vivos QTIP trust for the benefit of the donor after the death of his or her spouse will not be includible in the donor's taxable estate under §§ 2036 and 2038 of the Internal Revenue Code.[52] Thus, Dennis and Debbie would argue that following the reasoning in the Treasury Regulation, the trust created for Dennis upon Debbie's death should not be considered settled by Dennis.[53]

However, if Dennis retained the right to the assets remaining in Debbie's trust upon her death should Debbie predecease Dennis, Dennis' creditors would argue such assets should be subject to the creditors of Dennis because he was the initial donor of the trust. Furthermore, even if the trust created by Dennis did not reserve an interest in favor of Dennis as described above, should Debbie predecease him, if Debbie had a testamentary special power of appointment that allows her to direct assets back to Dennis, those assets may be subject to his creditors as a result of the Relation Back Doctrine.

2. The Effect of the Relation Back Doctrine

If, upon her death Debbie exercises a special power to create a credit shelter or QTIP trust for Dennis (the original donor), the trust assets appointed to Dennis may be considered as if Dennis created his own trust rather than Debbie being treated as the creator of such trust. The creditor under the Relation Back Doctrine could argue: (i) the exercise of a special power of appointment constitutes a transfer "from the donor of the power, not from the donee;[54] and (ii) the power of appointment is "conceived to be merely an authority to the power holder to do an act for the creator of the power."[55] "The appointment is said to 'relate back' to the time of the creation of the power and to operate as if it had been originally contained in [the creator of the power's] will."[56] Cases involving the Relation Back Doctrine have typically been in conjunction with whether trust assets subject to a general power of appointment should be considered when determining fiduciary fees upon the death of the donee spouse who exercised such power.

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[52] Treas. Reg. § 25.2523(f)(1)(f), Ex. 11.
[53] *Id.*
[54] In re Estate of Wylie, 342 So.2d 996, 998 (Fla. 4th DCA 1977) (quoting RESTATEMENT (FIRST) OF PROPERTY § 318 comment (b) (1940)).
[55] American Law Institute, *Donative Transfers* vol. 2 §§ 11.1-24.4, *in* RESTATEMENT (SECOND) OF PROPERTY 4 (1986).
[56] *Id.*

In *In re Estate of Wylie*, a husband created a testamentary trust for his wife. At his death, wife received all the income from the trust for her life and had a general power of appointment over the corpus of the trust at her death.[57] The issue on appeal was whether the value of the husband's trust was includible in wife's estate for purposes of determining fiduciary fees because she exercised her general power of appointment by her last will and codicil in favor of her testamentary trustees, and the assets were distributed and paid to the trustees.[58] The court found the determinative question to be whether the power of appointment should be characterized as an interest in property or merely a mandate or authority to dispose of property.[59] The court noted that:

The doctrine of relation back, minimizing as it does the importance of the donee of the power, is the mainstay for that rule of law which treats the donee as a mere agent with no property interest. Although under attack by many commentators in the field of future interests, the prevailing view still remains that a general power of appointment is a mere mandate or authority to dispose of property and not an interest in property itself.[60]

In keeping with the historical origin of powers of appointment and the "spirit of the law," the court in *Wylie* held that the power of appointment was an authority to dispose of property and not an interest in property.[61]

Although none of the reported cases regarding the Relation Back Doctrine address its application to the donor of a QTIP or credit shelter trust who receives trust assets upon the death of the donee spouse through the exercise of a special power of appointment, Inter Vivos QTIP Trust Jurisdictions provide greater protection for inter vivos QTIP trust donors by avoiding any possible Relation Back Doctrine attack.[62]

3. Can an Inter Vivos Credit Shelter Trust Plan Provide Better Overall Results?

The inter vivos QTIP trust plan has limitations when compared to a similar plan using an inter vivos credit shelter gift to freeze estate tax values. For example, some attorneys have suggested planning to take advantage of the existing $5 million gift exemption since it

[57] In re Estate of Wylie, 342 So.2d at 996-97.
[58] *Id.* at 998.
[59] *Id.* at 999.
[60] *Id.* at 998.
[61] *Id.*
[62] *See* Section II.B.5., *infra*.

may expire (or be reduced to as little as $1 million) after 2012, or possibly earlier. By making gifts in 2012 to an inter vivos credit shelter trust using a taxpayer's remaining gift and estate tax exemption, the growth on any assets remaining in the inter vivos credit shelter trust will pass estate tax-free upon the death of the beneficiary spouse even if the estate tax exemption amount was only $1 million upon the date of death of the beneficiary spouse and even if the initial $5 million gift grew to significantly more within the credit shelter trust. The problem with using the inter vivos QTIP plan rather than a gift into a credit shelter type trust is that most Inter Vivos QTIP Trust Jurisdictions (i.e., Delaware, Florida, Michigan and Wyoming) require that a gift tax QTIP election be made to obtain the asset protection benefit (that the beneficiary spouse is considered the donor and not the initial donor of the inter vivos QTIP) upon the death of the initial donee spouse.[63] As a result, if the plan is to make the inter vivos credit shelter trust assets available for the surviving spouse who created the initial trust, there is a possibility such assets will be subject to estate tax inclusion under §§ 2036 or 2041 of the Internal Revenue Code, as the creditors of the initial donor spouse may be able to reach such assets upon the death of the first spouse. While Treas. Reg. § 25.2523(f)- 1(f), Example 11, provides that assets held in an inter vivos QTIP trust — for the benefit of the donor after the death of his or her spouse — will not be includible in the donor's taxable estate under §§ 2036 and 2038, no similar regulation exists for an inter vivos credit shelter trust. It would appear that the favorable treatment is provided by said Regulation based upon the fact that such assets are includible in the estate of the donee spouse under § 2044 of the Internal Revenue Code which is not the case with a credit shelter trust. Accordingly the tax treatment of assets reverting back to the original donor of a credit shelter trust may be subject to estate tax.

4. Arizona's Unique Statute May Create Asset Protection and Estate Tax Benefits (but it may not!)

Arizona Statutes § 14-10505(E) states:

> E. For the purposes of this section, amounts and property contributed to the following trusts are not deemed to have been contributed by the settlor, and a person who would otherwise be treated as a settlor or a deemed settlor of the following trusts shall not be treated as a settlor:

[63] *See* DEL. CODE ANN. TIT. 12 § 3536(c)(2); FLA. STAT. § 736.0505(3); MICH. COMP. LAWS § 700.7506(4); WYO. STAT. ANN. § 4-10-506(e).

> 1. An irrevocable inter vivos marital trust that is treated as qualified terminable interest property under section 2523(f) of the internal revenue code if the settlor is a beneficiary of the trust after the death of the settlor's spouse.
>
> 2. An irrevocable inter vivos marital trust that is treated as a general power of appointment trust under section 2523(e) of the internal revenue code if the settlor is a beneficiary of the trust after the death of the settlor's spouse.
>
> 3. An irrevocable inter vivos trust for the settlor's spouse if the settlor is a beneficiary of the trust after the death of the settlor's spouse.
>
> 4. An irrevocable trust for the benefit of a person, the settlor of which is the person's spouse, regardless of whether or when the person was the settlor of an irrevocable trust for the benefit of that spouse.
>
> 5. An irrevocable trust for the benefit of a person to the extent that the property of the trust was subject to a general power of appointment in another person.[64]

Unlike Florida, Michigan, Delaware and Wyoming, the Arizona statute provides that the initial donor of *any* irrevocable inter vivos trust created for the donor's spouse will not be deemed to have been contributed by the donor if the donor is the beneficiary of the trust after the death of the donor's spouse, even if there is no QTIP election.[65] As a result, under Arizona law, Debbie could have created an inter vivos credit shelter trust for Dennis and even if the trust assets reverted to Debbie in a credit shelter trust, upon the death of Dennis, those assets would not be deemed to have been contributed by Debbie. As such, the assets should retain protection from Debbie's creditors during her lifetime despite the fact that she created the initial trust and was the beneficiary of the trust upon the death of Dennis.

While at first glance the Arizona statute appears to create great asset protection and the possibility of enhanced estate tax benefits that are afforded to credit shelter trusts as compared to an inter vivos QTIP Trusts (i.e., all appreciation of assets in the credit

[64] ARIZ STAT. § 14-10505(E).
[65] *Id.*

shelter trust would avoid future estate taxes and regardless of whether the applicable exclusion amount is reduced the assets in a credit shelter trust should not be subject to estate tax inclusion), there are two potential pitfalls to the Arizona statute: (1) the trust needs to have its situs in Arizona and be subject to income tax there; and (2) there is no provision similar to IRS Treas. Reg. § 25.2523(f)- 1(f), Example 11 that assures that the initial donor will not be subject to tax under §§ 2036 or 2038 of the Internal Revenue Code. As a result, the IRS could take the position that despite state law, the initial donor has an interest under §§ 2036 and 2038 of the Internal Revenue Code, resulting in estate tax inclusion.

Providing the initial donee of a credit shelter trust a special power of appointment to direct the credit shelter assets back to the initial donor, as compared to retaining a reversion in the credit shelter trust in favor of the donor, may not change the estate tax consequences to the donor due to the Relation Back Doctrine described above.[66] As a result, assets passing from an inter vivos credit shelter trust back to a credit shelter trust for the initial donor may be considered to be held in a self-settled trust and therefore subject to estate tax inclusion.

Some have suggested the creation of the initial credit shelter trust in a jurisdiction that recognizes and protects self-settled asset protection trusts.[67] The IRS has ruled favorably for a trust created under Alaska law.[68] A thorough analysis of this issue is beyond the scope of this article. However, creation of a credit shelter trust, in one of the thirteen states that have enacted self-settled asset protection trusts, does not assure that trust assets will be excluded from the initial donor's gross estate when they are appointed back to the initial donor, especially if there was an implied agreement that the assets would revert to the donor and there is a pattern of distributions to the donor spouse. Another potential alternative is creation of a credit shelter trust in a foreign self-settled asset protection trust jurisdiction.

Based upon most clients' objective of obtaining the anticipated tax and asset protection results, the author prefers the Inter Vivos QTIP Trust Jurisdictions, or use of a combination of an inter vivos QTIP trust created by one spouse and a credit shelter trust created by another spouse where the QTIP assets will revert to the initial donor upon the death of the initial donee spouse and the assets of

[66] *See* In re Estate of Wylie, 342 So.2d at 998.
[67] *See* Kroch et al., *supra* note 30, at 14; Gans et al., *supra* note 47, at 59.
[68] *See* Gideon Rothschild et al., *IRS Rules Self-Settled Alaska Trust Will Not Be In Grantor's Estate*, 37 EST. PLAN 3, 13 (Jan. 2010).

the credit shelter trust pass to children (and not in trust for the initial donor spouse) upon the death of the donee spouse. Life insurance could be purchased on the life of the donee spouse of the credit shelter trust to replace assets that will pass to children upon the death of the donee spouse beneficiary of the credit shelter trust.

5. States Where Dennis and Debbie Could Create an Inter Vivos QTIP Trust Plan Without Concern of Relation Back or Self-Settled Trust Issues

There are tradeoffs that a client must consider to obtain greater certainty as to tax and asset protection results. Inter Vivos QTIP Trust Jurisdictions provide certainty that the anticipated asset protection results will be effectuated because these statutes explicitly provide that assets reverting to the initial donor as a result of the death of the initial donee are considered to have been contributed by the donor's spouse and not the donor. Under such statutes, if the inter vivos QTIP trust is properly drafted — and assuming the initial transfer to the trust was not a fraudulent conveyance — it is clear that the assets of the inter vivos QTIP trust described in the example above will be considered as if contributed to the trust by Debbie (the initial trust beneficiary) and not Dennis (the initial donor) and therefore, will not be subject to Dennis' creditors upon the death of Debbie. As long as the assets in the trust created by Dennis are not subject to the creditors of Dennis when such assets revert to Dennis, such assets should not be includible in the taxable estate of Dennis.[69] Thus using the inter vivos QTIP plan, $0 of assets will be subject to creditors' claims while both spouses are married and living, and $0 of assets should be subject to creditors upon death of first spouse or divorce.[70] Similar results may be available, using the thirteen states that have self-settled asset protection trust legislation, but only the Inter Vivos QTIP Trust Jurisdictions assure favorable results.[71]

6. Issues Requiring Analysis When Implementing an Inter Vivos QTIP Trust Plan

• Net Worth — Clients will appreciate the certainty of tax and asset protection results of creating an inter vivos QTIP trusts in Inter Vivos QTIP Trust Jurisdictions. However, for wealthier

[69] *See* Treas. Reg. § 25.2523(f)-1(d); Howard M. Zaritsky, Tax Planning for Family Wealth Transfers: Analysis With Forms ¶ 6.03[3][a], 6-12 (Thompson Reuters/WG/L, 4th ed. 2002 & Supp. Aug. 2011).

[70] The tax is similar to the CPA Tax Savings plan with the exception of the assets subject to creditors. Dennis' Gross Estate ($8.5 million, $5 million of brokerage assets and $3.5 million in equity from homestead) – Applicable Exclusion Amount ($5 million) = Dennis' Taxable Estate ($3.5 million) Dennis' Estate Tax is $1.225 million ($3.5 million x 35%). *See* Exhibit C.

[71] *See* Kroch et al., *supra* note 30, at 14. *See* Gans, Blattmachr & Zeydel, *supra*, note 47.

clients, creating an inter vivos credit shelter trust for a spouse could provide significant estate tax benefits under the 2010 Tax Relief Act because the assets held in an inter vivos credit shelter trust (including appreciation) will not be subject to tax upon the death of the donee spouse, whereas the inter vivos QTIP trust assets are subject to estate tax upon the death of the donee spouse based upon date of death values. If the inter vivos QTIP trust assets, when combined with the other assets of the donee spouse, exceed the available estate tax exemption for the year of death, additional estate taxes will be incurred. Wealthier clients may be willing to each create trusts for their children with their $5 million gifting exemption (or such lesser amount based upon prior taxable gifts). Alternatively, couples with children who are not willing to lose the ability to benefit from $10 million of gifts may consider the creation of one inter vivos credit shelter trust that could benefit the donee spouse during his or her lifetime (at the discretion of the trustee) and allow for invasions for children and grandchildren, and one inter vivos QTIP trust. The credit shelter trust assets can pass to children or grandchildren upon the death of the donee spouse. The donee spouse of the credit shelter trust could create an inter vivos QTIP trust for the other spouse, thereby reserving a remainder interest in trust in an Inter Vivos QTIP Trust Jurisdiction. Both spouses will benefit from at least $5 million held in trust until they both have passed away (i.e., the QTIP assets will benefit the donee spouse during the lifetime of the donee spouse and then pass, in trust, to the initial donor of the inter vivos QTIP trust for the lifetime of such donor).

• Jurisdiction — The trust should be created in an Inter Vivos QTIP Trust Jurisdiction or possibly in a state that recognizes self-settled asset protection trusts assuming the structure complies with the self-settled asset protection trust statutes.

• Reciprocal Trusts — If both spouses create an inter vivos QTIP trust, there is a possibility that the IRS could take the position that they were reciprocal.[72] Avoidance of reciprocal trust attacks may be accomplished by allowing a considerable amount of time lapse between the creation of the husband's inter vivos QTIP trust and the wife's inter vivos QTIP trust, and by having different dispositive provisions in the trusts, for example: providing for different trustees, different beneficiaries upon the death of the donee spouse, a special power in favor of certain beneficiaries in each trust, or not providing a special power upon the death of the donee spouse at all in one of the trusts.[73] Arizona has addressed the

[72] For a thorough analysis of reciprocal trusts, see Gans, Blattmachr & Zeydel, *supra*, note 47.
[73] *Id.*

reciprocal trust dilemma by enacting Arizona Revised Statutes § 14-10505(E)(4) that, in conjunction with § 14-10505(E), attempts to provide protection from a reciprocal trust attack when spouses create irrevocable trusts for one another.[74] Planners need to review the reciprocal trust issues carefully if they intend to create similar irrevocable trusts for both a husband and a wife, and state laws such as Arizona should be reviewed to see whether other states should consider similar enactments.

• Divorce — A number of important issues need to be considered before proceeding with creation of the inter vivos QTIP trust. Once created, the inter vivos QTIP trust is irrevocable for the lifetime of the donee spouse. A trust will not qualify for the gift tax marital deduction if the spouse's interest in the trust automatically terminates in the event of divorce.[75] As a result, even after divorce, the donee spouse will have the benefit of the trust assets. One planning technique may be to limit principal invasions in the event of dissolution of marriage so that, after divorce, only income distributions will be mandated in favor of the donee spouse without the consent of a "special trustee." Will the assets in the trust be considered for purposes of determining elective share rights of a surviving spouse? Would the value of assets in the inter vivos QTIP trust be considered in the event of a subsequent dissolution of marriage of the donor and donee spouse? If so, will the terms of discretionary distributions provided in the trust be considered in determining the value of the trust for purposes of computing the division of assets? Some of these issues could be dealt with if each spouse created an inter vivos QTIP trust for the benefit of the other spouse. It may be best to include a family law attorney as part of the planning. If feasible, clients may consider entering into a postnuptial agreement to address how assets in the inter vivos QTIP trust will be treated in the event of a divorce.

C. Conclusion

When integrating inter vivos QTIP trust planning with the current provisions of the 2010 Tax Relief Act, estate planners must keep in mind that after December 31, 2012 or possibly earlier, estate tax rates and exemptions may be significantly less favorable.[76] If Congress decides not to act, the estate tax exemption would drop to $1 million in 2013 and the estate tax rate would increase to 55%; the gift tax rate would increase to 55% with a $1 million exemption; portability would be eliminated; and the generation skipping tax would increase to a flat 55% with a $1 million

[74] ARIZ. REV. STAT. § 14-10505(E).
[75] Treas. Reg. § 25.2523(f)-1(c)(1)(i).
[76] 2010 Tax Relief Act, *supra* note 28, at 124 Stat. 3298.

exemption, indexed for inflation.[77] If that were to occur, the asset protection benefits of the inter vivos QTIP plan would most likely be dwarfed by the loss of potential for estate tax savings that could have been achieved using other asset protection techniques such as the creation of inter vivos credit shelter trusts where assets pass to children upon the death of the donee spouse, or using a self-settled asset protection trust situs for those clients who understand potential IRS attacks. While many questions exist, there is no question that clients should be advised of the benefits of restructuring their assets to maximize asset protection and use of the currently available applicable exclusion amount. Inter vivos QTIP trust planning in an Inter Vivos QTIP Trust Jurisdiction is one alternative that should be considered.

III. LP and LLC Situs Issues: Charging Order Protection

A. Introduction

Limited Partnerships ("LP") and LLC's have been touted as asset protection techniques as well as for estate planning and family planning.[78] The major benefit touted for asset protection is that if a partner or member of a partnership or LLC is subject to a personal judgment, the typical remedy is a charging order. The creditor typically cannot become a partner (replacing the debtor partner) or a member (replacing the debtor member). Assuming the other partners or members are cooperative with the debtor partner or member, the partnership or LLC may decide not to make distributions for so long as the charging order exists. As a result, the creditor holding the charging order may become frustrated and seek court intervention. Many states such as Delaware do not differentiate between charging order protection for single-member and multimember LLCs.[79] A

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[77] *See* I.R.C. §§ 2001, 2502, 2631, 2641.

[78] *See* Thomas O. Wells, *Asset Protection Provided With Florida Business Entities*, *in* ASSET PROTECTION IN FLORIDA 4-1 (LexisNexis/Fla. Bar 2d ed., 2011); Richard A. Behrendt, *Transfer of Interest in FLPs*, 150 TRUSTS & EST. 38 (Aug. 2011); Richard B. Robinson, Escape From the World of FLPs, Address at the 44th Annual Heckerling Institute on Estate Planning (Jan. 2010), *in* 44th Annual Heckerling Institute on Estate Planning (Matthew Bender, Pub., 2010); Nelson, *supra* note 9; N. Todd Angkatavanich & Edward A. Vergara, *The FLP Quadrilogy*, 148 TRUSTS & EST. 16 (Dec. 2009); Barry A. Nelson, Asset Protection for Estate Planners, Address at the 43rd Annual Heckerling Institute on Estate Planning (Jan. 2009), in 43rd Annual Heckerling Institute on Estate Planning at 18-15-18-20 (Matthew Bender, Pub., 2009); Wells & Guso, *supra* note 9.

[79] DEL. CODE ANN. TIT 6 § 18-703:

> (a) On application by a judgment creditor of a member or of a member's assignee, a court having jurisdiction may charge the limited liability company interest of the judgment debtor to satisfy the judgment. To the extent so charged, the judgment creditor has only the right to receive any distribution or distributions to which the judgment debtor would otherwise have been entitled in respect of such limited liability company interest.
>
> (b) A charging order constitutes a lien on the judgment debtor's limited liability company interest.
>
> (c) This chapter does not deprive a member or member's assignee of a right under exemption laws with respect to the judgment debtor's limited liability company interest.

limited number of states have specifically addressed whether a creditor who holds a charging order but has no ability to demand distributions should have additional remedies or whether such creditor must sit patiently until a distribution is made or a negotiated settlement resolves the situation. Alabama, Alaska, South Dakota, Texas, Florida and most recently Nevada, state that a charging order is the exclusive remedy available to a creditor of a limited partner.[80] It has become apparent, as a result of *Olmstead v. FTC*, that courts will carefully analyze applicable state law of the partnership or LLC in question to determine whether a creditor having a judgment against a partner of a partnership or a member of an LLC will be limited to the charging order remedy or instead may foreclose on the debtor's interest in the partnership or LLC.

B. Olmstead v. Federal Trade Commission

Florida's Supreme Court held in *Olmstead* that a court may order a judgment debtor to surrender all right, title and interest in the debtor's single-member LLC, organized under Florida law, to satisfy an outstanding judgment.[81] The Florida Supreme Court said: "[s]pecifically, we conclude that there is no reasonable basis for inferring that the provision authorizing the use of charging orders under § 608.433 (4) establishes the sole remedy for a judgment creditor against a judgment debtor's interest in single-member LLC."[82] The majority opinion referred to *In re Albright*,[83] where a Colorado Bankruptcy Court rejected the argument that a bankruptcy trustee should be entitled to only a charging order with respect to a debtor's ownership of a single-member LLC. It held: "[b]ecause there are no other members in the LLC, the entire membership interest passed to the bankruptcy estate."[84]

1. Understanding Essential Terms

While this article is not intended to be a comprehensive analysis of charging orders, it is helpful to provide a general understanding of the essential terms that are the subject of *Olmstead* and similar cases, such as the definition of a charging order, and how some states have specifically legislated to provide clarity to avoid

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(d) The entry of a charging order is the exclusive remedy by which a judgment creditor of a member or of a member's assignee may satisfy a judgment out of the judgment debtor's limited liability company interest.

(e) No creditor of a member or of a member's assignee shall have any right to obtain possession of, or otherwise exercise legal or equitable remedies with respect to, the property of the limited liability company.

[80] ALA. CODE. § 10A-9-7.03; ALASKA STAT. § 32.11.340; FLA. STAT. § 620.1703; NEVADA REV. STAT. § 88.535; S.D. CODIFIED LAWS § 48-7-703; TEX. BUS. ORG. CODE § 153.256.

[81] Olmstead, 44 So.3d at 76.

[82] *Id.* at 83.

[83] 291 B.R. 538 (D. Colo. 2003).

[84] *Id.* at 540.

Olmstead-type litigation. Generally, "[a] charging order is a statutory procedure whereby a creditor of an individual member can satisfy its claim from the member's interest in the limited liability company as a protection of the other partners of the partnership or other members of the LLC."[85] Foreclosure is "[a] legal proceeding to terminate a mortgagor's interest in property..."[86] In a judicial foreclosure, a judge orders the sale of the member-debtor or partner-debtor's interest in the entity, resulting in the sale of the member/partner's entire interest in the LLC/partnership.[87] Both the Uniform Limited Partnership Act and the Revised Uniform Limited Liability Company Act, drafted by the National Conference of Commissioners on Uniform State Laws, provide for charging orders and specifically permit foreclosure.[88]

The *Olmstead* decision referred to inconsistencies under Florida law on the treatment of charging orders under Florida's Revised Uniform Limited Partnership Act of 2005,[89] Florida's Revised

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[85] BLACK'S LAW DICTIONARY (9th ed. 2009).

[86] *Id.*

[87] *See* Elizabeth M. Schurig & Amy P. Jetel, *A Shocking Revelation! Fact or Fiction? A Charging Order is the Exclusive Remedy Against a Partnership Interest*, 17 PROB. & PROP. 57 (Nov./Dec. 2003)

> From the creditor's perspective, a charging order is an unattractive remedy because the creditor will receive nothing if there are no distributions to the debtor partner... A charging order differs from a foreclosure: a foreclosure is permanent, but a charging order is in place only long enough to pay off the debt. A further difference is that the purchaser at a foreclosure enjoys the right to a proportionate share of the partnership's assets upon dissolution--increasing the creditor's chances of having the debt satisfied out of the partnership interest.

Id. at 58.

[88] *See* REV. UNIF.LTD. LIAB. CO. Act § 503(c) (2006)

> Upon a showing that distributions under a charging order will not pay the judgment debt within a reasonable time, the court may foreclose the lien and order the sale of the transferable interest. The purchaser at the foreclosure sale obtains only the transferable interest, does not thereby become a member, and is subject to Section 502.

Id.; UNIF. LTD. P'SHIP ACT § 703(b) (2001)

> A charging order constitutes a lien on the judgment debtor's transferable interest. The court may order a foreclosure upon the interest subject to the charging order at any time. The purchaser at the foreclosure sale has the rights of a transferee.

Id. See also FLA. STAT. § 620.1703 (indicating Florida's approach to charging orders and limited partnerships); FLA. STAT. § 608.433 (indicating Florida's approach to charging orders and LLCs). In both cases Florida did not adopt the express authority for a foreclosure remedy as provided in the uniform laws.

[89] FLA. STAT. § 620.1703. sub-section (1), for Florida Limited Partnerships, states:

> On application to a court of competent jurisdiction by any judgment creditor of a partner or transferee, the court may charge the partnership interest of the partner or transferable interest of a transferee with payment of the unsatisfied amount of the judgment with interest. To the extent so charged, the judgment creditor has only the rights of a transferee of the partnership interest.

(3) states:

> This section provides the exclusive remedy which a judgment creditor of a partner or transferee may use to satisfy a judgment out of the judgment debtor's interest in the

Uniform Partnership Act of 1995[90] and Florida's Limited Liability Company Act.[91] The disparity under Florida law is not unique and, as described below, applicable state laws should be examined to determine if similar inconsistencies could result in decisions limiting charging order protection such as in *Olmstead*. § 620.1703 of Florida's Revised Uniform Limited Partnership Act of 2005 ("Florida's LP Act") states that a charging order is the exclusive remedy by which a judgment creditor of a partner may satisfy a judgment and provides that other remedies, including (but not limited to) foreclosure on the partner's interest in the LP, are not available and may not be ordered by a court.[92] Florida Bar members with different areas of specialty worked on the drafting of Florida's LP Act. Based upon my review in 2004 of various state laws, I proposed that the drafting committee include the

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> limited partnership or transferable interest. Other remedies, including foreclosure on the partner's interest in the limited partnership or a transferee's transferable interest and a court order for directions, accounts, and inquiries that the debtor general or limited partner might have made, are not available to the judgment creditor attempting to satisfy the judgment out of the judgment debtor's interest in the limited partnership and may not be ordered by a court.

Id.

[90] FLA. STAT. § 620.8504 for Partnerships other than Limited Partnerships, states:

> (1) Upon application by a judgment creditor of a partner or of a partner's transferee, a court having jurisdiction may charge the transferable interest of the judgment debtor to satisfy the judgment. The court may appoint a receiver of the share of the distributions due or to become due to the judgment debtor in respect of the partnership and make all other orders, directions, accounts, and inquiries the judgment debtor might have made or which the circumstances of the case may require.
>
> (2) A charging order constitutes a lien on the judgment debtor's transferable interest in the partnership. The court may order a foreclosure of the interest subject to the charging order at any time. The purchaser at the foreclosure sale has the rights of a transferee.
>
> (3) At any time before foreclosure, an interest charged may be redeemed:
>
> (a) By the judgment debtor;
>
> (b) With property other than partnership property, by one or more of the other partners; or
>
> (c) With partnership property, by one or more of the other partners with the consent of all of the partners whose interests are not so charged.
>
> (4) This act does not deprive a partner of a right under exemption laws with respect to the partner's interest in the partnership.
>
> (5) This section provides the exclusive remedy by which a judgment creditor of a partner or partner's transferee may satisfy a judgment out of the judgment debtor's transferable interest in the partnership.

Id.

[91] FLA. STAT. § 608.433(4), for Limited Liability Companies, stated, before the 2011 amendment:

> On application to a court of competent jurisdiction by any judgment creditor of a member, the court may charge the limited liability company membership interest of the member with payment of the unsatisfied amount of the judgment with interest. To the extent so charged, the judgment creditor has only the rights of an assignee of such interest. This chapter does not deprive any member of the benefit of any exemption laws applicable to the member's interest.

Id.

[92] FLA. STAT. § 620.1703(3).

"exclusive remedy" and foreclosure prohibition provisions that were enacted. These provisions were based in significant part on the Alaska Uniform Limited Partnership Act.[93] At the time there was no significant opposition to providing strong charging order protection in Florida's LP Act.

Both the Alaska and Florida Acts state that the charging order provides the exclusive remedy which a judgment creditor of a partner (both general and limited partners) may use to satisfy a judgment out of the judgment debtor's interest in an LP. Where an individual serves as general partner of a Florida LP, such individual's creditors would be limited to a charging order against his or her general partnership interest. However, if the general partner of a Florida LP is a single-member LLC owned by an individual debtor, then the debtor would not be protected by § 620.1703(3) as that section only provides the exclusive remedy protection to a judgment creditor of a partner.[94] Where the general partner of an LP is an LLC, the creditors of the LLC members are not creditors of a partner of the partnership (i.e., the partner is the LLC and the debtor is a member of the LLC and not a partner of the partnership). As such, the LLC member's creditors are governed by the charging order provisions of § 608.433 of Florida's Limited Liability Company Act. Based upon *Olmstead* and new Florida Statutes § 608.433(5)-(8), no charging order protection is available to the sole member of an LLC.[95] Accordingly, an individual general partner of a Florida LP who has creditors benefits from charging order protection under Florida Statutes § 620.1703(3), whereas the sole member of an LLC that is the general partner of a Florida LP would not benefit from

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[93] ALASKA STAT. § 32.11.340(b)

> This section provides the exclusive remedy that a judgment creditor of a general or limited partner or of the general or limited partner's assignee may use to satisfy a judgment out of the judgment debtor's interest in the partnership. Other remedies, including foreclosure on the general or limited partner's partnership interest and a court order for directions, accounts, and inquiries that the debtor general or limited partner might have made, are not available to the judgment creditor attempting to satisfy the judgment out of the judgment debtor's interest in the limited partnership and may not be ordered by a court.

Id. See also ALASKA STAT. § 10.50.380 (dealing with LLCs).

> (c) This section provides the exclusive remedy that a judgment creditor of a member or a member's assignee may use to satisfy a judgment out of the judgment debtor's interest in the limited liability company. Other remedies, including foreclosure on the member's limited liability company interest and a court order for directions, accounts, and inquiries that the debtor member might have made, are not available to the judgment creditor attempting to satisfy a judgment out of the judgment debtor's interest in the limited liability company and may not be ordered by a court.

Id.

[94] FLA. STAT. § 620.1703.

[95] Fla. Stat. § 608.433(5)-(8); Olmstead, 44 So.3d at 83.

charging order protection as such sole member is not a partner in the Florida LP.[96]

A well drafted LP agreement will: (i) restrict an LLC general partner from conveying its membership interests, without the consent of the limited partners; and/or (ii) provide that a charging order against a sole member of the general partner LLC will cause the LLC to be disassociated from the LP as a general partner. Both alternatives will avoid the creditor who forecloses on the interest of the LLC general partner from gaining control over the partnership as general partner. Owning a general partnership interest directly under Florida law is clearly the better alternative to obtain charging order protection than owning said general partnership interest indirectly through a single-member LLC because the creditor of the sole member of the LLC can foreclose on the LLC and thereby obtain control of the partnership without careful partnership planning. Florida LPs having a single-member Florida LLC general partner may benefit from restructuring, described below (such as moving the situs of the LLC to a state where a charging order is the exclusive remedy against the sole member of an LLC or being certain the LLC is and remains a multimember LLC). As of November 2011, eleven states have exclusive remedy language and explicitly prohibit foreclosure as part of their LLC Acts and/or Limited Partnership Acts.[97]

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[96] It should be noted that if the individual general partner becomes a debtor in bankruptcy or executes an assignment for the benefit of creditors, the general partner would be dissociated from the limited partnership as a general partner. *See* FLA. STAT. § 620.1603(6). In such event if there is no other general partner, all of the limited partners may consent to continue the partnership and admit at least one general partner. However, if the individual general partner is also a limited partner, the requirement to obtain the consent of "all" the limited partners is unlikely to be satisfied. Therefore, it may still be preferable to use an LLC as a general partner provided the LLC is created in a jurisdiction where charging orders are the exclusive remedy and the LLC has at least one other member who is not a debtor in bankruptcy.

[97] See ALASKA STAT. § 10.50.380; ME. REV. STAT. ANN. tit. 31 § 1573; MICH. COMP. LAWS § 450.4507; NEVADA REV. STAT. § 86.401; N.J. REV. STAT. § 42:2B-45; OKLA. STAT. TIT. 18 § 2034; S.D. CODIFIED LAWS § 47-34A-504; TEX. BUS. ORG. CODE § 101.112; WYO. STAT. ANN. § 17-29-503, for LLC states Alaska, Maine, Michigan, Nevada, New Jersey, Oklahoma, South Dakota, Texas, and Wyoming. See ALA. CODE. § 10A-9-7.03; ALASKA STAT. § 32.11.340; FLA. STAT. § 620.1703; NEVADA REV. STAT. § 88.535; S.D. CODIFIED LAWS § 48-7-703; TEX. BUS. ORG. CODE § 153.256, for LP Act states Alabama, Alaska, Florida, Nevada, South Dakota, Texas. Note, while some states do not have exclusive remedy and foreclosure prohibition in their LLC statutes, court decisions in such states (including Delaware) have interpreted state law to provide such protection. *See* New Times Media LLC v. Bay Guardian Co., 2010 U.S. Dist LEXIS 64395 (D. Del. June 28, 2010). See *infra* note 104, for articles providing a summary of each state's charging order provisions; *infra* note 108, for articles relating to charging orders and state statutory language.

2. Attempts Prior to *Olmstead* to Create Continuity Between Charging Order Protection for Florida's LLCs and Partnerships was Unsuccessful

In 2006, the Asset Preservation Committee of the Real Property, Probate and Trust Law Section of the Florida Bar attempted to introduce exclusive remedy and prohibition against foreclosure language provisions, almost identical to those in § 620.1703 of the Florida Revised Uniform Limited Partnership Act of 2005, for LLCs and Florida general partnerships.[98] The proposal was supported by the Executive Counsel of the Real Property, Probate and Trust Law Section of the Florida Bar.[99] The explanation attached to the Legislative Position Request Form included a section entitled: "Extension of Charging Lien Limitation and Foreclosure Prohibition Against Partner and Member Interests in Other Partnerships and in Limited Liability Companies." The "White Paper" attached to the Florida Bar's "Legislative Position Request Form" describing the proposed legislation stated:

> The same policy concerns that caused the adoption of the limited remedy of a charging lien and prohibition of foreclosure apply equally to partner interests in general partnerships and in limited liability partnerships and member interests in limited liability companies. Accordingly, the proposed legislation would extend those features to the general and limited liability partnership and limited liability company statutes.[100]

The proposal was withdrawn when opposition to the policy being extended was expressed by those representing creditors, and this issue was never considered by the Florida Legislature. Based upon discussions with the Florida Bar's Chapter 608 LLC Drafting Task Force Chair Louis T. M. Conti and committee member Richard Comiter, in addition to the above described proposal initiated by the Florida Bar's Asset Protection Subcommittee, the Business Law Section Drafting Committee in 2006 proposed Amendments to the LLC Act that initially included "exclusive remedy" language to the LLC Act. The Business Law Section also decided not to proceed to the Florida Legislature in order to assure that other non controversial revisions to the LLC Act would be enacted.

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[98] Legislative Position Request Form Submitted By Real Property, Probate & Trust Law Section, Jan. 5, 2006, *available at* http://www.rpptl.org/Content/Committees/LegislativeReview/Creditor's_remedies_against_LP_and_LLLP_Interests.pdf[hereinafter Legislative Position].

[99] *Id.*

[100] Legislative Position, *supra* note 98, at 8.

3. Inconsistent Treatment for Limited Partnerships, General Partnerships, and LLCs may Have Caused Confusion in the Florida Supreme Court's *Olmstead* Majority Opinion; Other States' Laws Should be Reviewed

One significant reason provided in the *Olmstead* majority opinion supporting its conclusion was that Florida's LP Act specifically provided that a charging order is the exclusive remedy and foreclosure is not an available remedy, and Florida's Revised Uniform Partnership Act of 1995 specifically provided that the remedies described in § 620.8504 were exclusive, but no such exclusive language was provided in the Florida Limited Liability Company Act.[101] The majority opinion said:

> In this regard, the charging order provision in the LLC Act stands in stark contrast to the charging order provisions in both the Florida Revised Uniform Partnership Act and the Florida Revised Uniform Limited Partnership Act….[and] [a]lthough the core language of the charging order provisions in each of the three statutes is strikingly similar, the absence of an exclusive remedy provision set the LLC Act apart from the other two statutes.[102]

Based upon the disparity between the LLC and LP law, the majority opinion states: "[w]here the legislature has inserted a provision in only one of two statutes that deal with closely related subject matter, it is reasonable to infer that the failure to include that provision in the other statute was deliberate rather than inadvertent."[103] That might be a reasonable inference, but the justices did not have access to nor were they aware of the real story. As described above, Florida's Legislature never had the opportunity to determine whether Florida LLCs should have the same charging order exclusive remedy provisions as were enacted as part of Florida's LP Act as a result of conflicting interests of various committees of the Florida Bar.

4. *Olmstead* Decision and National Consequences

In recent years, a number of articles have been written suggesting the best states to form LPs and LLCs, taking into account asset

[101] Olmstead, 44 So.3d at 82.
[102] *Id.*
[103] *Id.*

protection.[104] Since legislation is continually changing on a statewide basis, many recent articles may already be outdated. For example, Nevada, Wyoming and Texas enacted protective charging order laws in 2011,[105] 2010[106] and 2009,[107] respectively.

The fact that a state may have favorable charging order protection within its limited partnership act does not necessarily mean that the state's LLC laws are equally beneficial. Carter Bishop, a Professor of Law at Suffolk University Law School, has written extensively on charging order issues.[108] He summarized the laws of each state and has distinguished those states that specify that a charging order is the exclusive remedy, those that are silent, and those that provide protection beyond exclusive remedy language (e.g., by stating that remedies such as foreclosure are specifically prohibited).[109] The Bishop articles referenced list the states that have favorable exclusive remedy and foreclosure limitation provisions. However in light of the pace of legislative changes in this area, no situs should be selected for an LP or LLC until current state law is verified.

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[104] *See* Mark Merric, Bill Comer, & Mark Monasky, *Forum Shopping for Favorable FLP and LLC Law: Part VII* (Steve Leimberg's Asset Protection Planning Newsletter #162) Sept. 14, 2010, *available at* http://www.leimbergservices.com; Mark Merric, Bill Comer, & Daniel G. Worthington, *Charging Order: What does sole or exclusive remedy mean?*, 149 TRUSTS & EST. 47, 48 (Apr. 2010) (listing the "Magnificent Seven" charging order states as Alaska, Delaware, Florida, New Jersey, Texas, Virginia and South Dakota); Daniel G. Worthington & Mark Merric, *Which Situs is Best?*, 149 TRUSTS & EST. 54 (Jan. 2010) (listing the top four jurisdictions for 2010 as South Dakota, Delaware, Alaska and Nevada); Nelson, *supra* note 78, at 18-34–18-35; Amy P. Jetel, Asset Protection in the Context of LPs and LLCs, (Steve Leimberg's Asset Protection Planning Newsletter #121) Jan. 31, 2008, *available at* http://www.leimbergservices.com (listing the "truly magnificent" states for LPs as Alaska, Florida and South Dakota, and for LLCs: Alaska, New Jersey and Oklahoma).

[105] NEVADA REV. STAT. § 86.401 (effective July 1, 2011).

[106] WYO. STAT. ANN. § 17-29-503 (effective July 1, 2010).

[107] *See* TEX. BUS. ORG. CODE § 101.112 (effective Sept. 1, 2009); TEX. BUS. ORG. CODE § 153.256 (effective Sept. 1, 2009).

[108] *See* Carter G. Bishop, *Desiderata: The Single Member Limited Liability Company Charging Order Statutory Lacuna*, STAN J. L. BUS. & FIN. (forthcoming 2011); Carter G. Bishop, *Fifty State Series: LLC & Partnership Transfer Statutes* (Suffolk University Law School Research Paper No. 10-25), *available at* http://ssrn.com/abstract=1621694; Carter G. Bishop, *Fifty State Series: LLC Charging Order Case Table* (Suffolk University Law School Research Paper No. 10-15), *available at* http://ssrn.com/abstract=1565595; Carter G. Bishop, *Fifty State Series: LLC Charging Order Statutes* (Suffolk University Law School Research Paper No. 10-03), *available at* http://ssrn.com/abstract=1542244; Carter G. Bishop, *A Jurisdictional & Governing Law Quagmire: LLC Charging Orders* (Journal of Business Entities, Forthcoming; Suffolk University Law School Research Paper No. 10-05), *available at* http://ssrn.com/abstract=1545855; Carter G. Bishop, *Reverse Piercing: A Single Member LLC Paradox*, 54 S.D. L. REV. 199 (2009); Carter G. Bishop, *Through the Looking Glass: Status Liability and the Single Member and Series LLC Perspective*, 42 SUFFOLK U. L. REV. 459 (2009); Carter G. Bishop, Thomas Geu, & Daniel S. Kleinberger, *Charging Orders and the New Uniform Limited Partnership Act: Dispelling Rumors of Disaster*, 18 PROB. & PROP. 30 (2004).

[109] *See id.*

5. Consequences of Providing Charging Order Protection to Single-Member LLCs

If states modify their LLC statutes to provide exclusive remedy protection and foreclosure prohibition for the sole member of a single-member LLC, creation of single-member LLCs may be as effective, at least for purposes of negotiation, as using a domestic or foreign self-settled asset protection trust in jurisdictions that sanction such trusts. Furthermore, the restrictions and administrative burdens of self-settled asset protection trusts (e.g., the need to have a trustee in the jurisdiction) could be avoided by using a single-member LLC in a jurisdiction that provides exclusive remedy and foreclosure prohibition, where the sole owner could serve as the sole manager, as long as there is at least some nexus within the jurisdiction in which the LLC is formed. It should be noted that if a self-settled asset protection trust is respected, a judgment creditor of the trust creator generally will have no interest therein. Yet, the trustee could have discretion to make distributions for the benefit of a debtor beneficiary, and upon the beneficiary's death, the beneficiary can designate successor beneficiaries through a limited power of appointment. Upon the death of the debtor beneficiary without designating the remainder beneficiary through the exercise of the power of appointment, the assets of the self-settled trust would pass to the remainder beneficiaries of such trust, free and clear of any creditors of the debtor.[110] However, with LLCs, even if the charging order is the exclusive remedy, should distributions be made to the LLC member, creditors would recover them as a result of the charging order. Furthermore, upon the death of the judgment debtor, his or her LLC membership interests remain an asset that will be subject to creditor's claims; although, subject to continued charging order protection. The practical consequences of the charging order protection being the exclusive remedy for an LLC or LP is that creditors are encouraged to negotiate a settlement with the debtor if the judgment creditor is unable to force distributions to the LLC member or limited partner through the courts. The sole member of an LLC will have exclusive authority to decide on the timing of

[110] One reason that a single-member LLC may be preferred over a self-settled asset protection trust is that under Bankruptcy Code § 548(e)(1)(A), a trustee of a bankruptcy estate may avoid any transfer made by the debtor within ten years of the date of the filing of a bankruptcy petition if the transfer was made to a self-settled trust or similar device. No such provision was adopted to specifically address transfers to a limited partnership. *See* In re Porco, 447 B.R. 590 (Bankr. S.D. Ill. 2011) (holding that the interpretation of "similar device" in Bankruptcy Code § 548 (e) was intended to capture self-settled trusts and as a result, did not apply to property held in an LLC). *See also* Alexander A. Bove. Jr. & Melissa Langa, *In re Porco: Case of First Impression Interprets Similar Device for Purposes of Section 548(e) of Bankruptcy Code* (Steve Leimberg's Asset Protection Planning Newsletter #184) Oct. 12, 2011, *available at* http://www.leimbergservices.com.

distributions. As a result, the charging order protection for single-member LLCs will also serve to safeguard the debtor's LLC assets and bring creditors to the negotiating table.

6. What Should States Do Now?

As a result of *Olmstead*, the Tax Section, Business Law Section and Real Property, Probate and Trust Law Section of The Florida Bar suggested a "Patch" to the LLC statute that was enacted and is retroactive.[111] It provides that a charging order is the exclusive remedy in Florida with respect to multimember LLCs but not single-member LLCs.[112] It would be prudent to form both single-member and multimember LLCs in states such as Wyoming and Nevada if protection of membership interests is an objective. Exclusive remedy and foreclosure protection is not provided in Florida for single-member LLCs.[113] Possibly, Carter Bishop's analysis was factored in when a compromise "Patch" was agreed to:

> The sensible statutory restrictions applicable to transfers of a membership in a multiple member limited liability company are justified and intuitive. Specifically, the rules that permit a member to freely transfer economic rights to future distributions while at the same time requiring the consent of the remaining members to admit the transferee as a member are appropriate to balance the reasonable expectations of members of a close business association. However, when applied to a SMLLC ["single-member LLC"], the same rules create a perverse and unexpected result….There are no other remaining partners to protect as in the case of a muti-member limited liability company. …Ultimately, these perverse results are best cured by statutory amendment. Preferably, every state would amend its SMLLC legislation to provide that upon the voluntary or involuntary transfer of the only economic interest in the SMLLC, the transferee will be admitted as a substituted member, with or without the consent of the only member.[114]

It appears that the *Olmstead* court did, as far as single-member LLCs go, reach the right result.

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[111] *See* 2011 Fla. Laws ch. 11-77 (approved May 31, 2011).
[112] FLA. STAT. § 608.433(5)-(6).
[113] *Id.*
[114] Bishop, *Reverse Piercing: A Single Member LLC Paradox*, *supra* note 108, at 231-32.

a. Recent Statutory Developments

Nevada and Wyoming specifically provide exclusive remedy protection to a judgment debtor who is the sole LLC member.[115] Florida is the only state to differentiate between single-member and multimember LLCs.[116] Other states, such as Delaware, that have exclusive remedy protection whether by statute or case law, are silent as to whether their protection extends to single-member LLCs. A reasonable argument can be made that because no exclusion is provided in statutes such as Delaware for single-member LLCs, exclusive remedy protection applies to them as well. Yet, as previously quoted from Carter Bishop, with a single-member LLC there are no remaining partners (or members) to protect. Those considering proposed legislative responses to *Olmstead* should be aware of the possibility of aggressive asset protection that could result if single-member LLCs had exclusive charging order protection similar to multimember LLCs. Single-member LLCs could be formed and the sole member could contribute all of his or her business and personal assets thereto. Would the sole member then benefit from the exclusive remedy charging order protection?[117]

There is a great disparity in the approach states have taken with respect to LLC charging orders. Wyoming restated its entire LLC Act effective July 1, 2010, to clarify prior state law that provided charging order protection as the exclusive remedy for LLCs, without differentiating between single-member and multimember LLCs.[118] Nevada recently enacted asset protection law changes favorable to debtors. Effective June 16, 2011, both Nevada's LP and LLC statutes (including single-member LLCs) provide that charging orders are the exclusive remedy.[119]

b. Recent Case Law Developments

What law should govern when a debtor owns an interest of an LLC or LP created in another state that provides greater

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[115] NEVADA REV. STAT. § 86.401(2) (2011); WYO. STAT. ANN. § 17-29-503(g) (2010).
[116] FLA. STAT. § 608.433(6).
[117] In Florida, homestead protection could be lost for property tax purposes and asset protection if the homestead was conveyed to a Florida partnership or LLC and therefore, Florida homestead should not be so conveyed even if single-member LLC charging order protection was provided. *See* Nelson, *supra* note, 47, at 18-30 – 18-34.
[118] WYO. STAT. ANN. § 17-29-503.
[119] NEVADA REV. STAT. §§ 86.401; 86.401(2)(a); 88.535.

charging order protection? Delaware LLCs are protected as a charging order is the exclusive remedy of a judgment creditor.[120] Recently, Delaware's LLC statute was tested in *American Institutional Partners LLC v. Fairstar Resources, Ltd.* ("*Fairstar*").[121] In *Fairstar*, Fairstar Resources LTD and Goldlaw PTY, LTD (collectively the "Creditors") obtained charging orders in a Utah state court against American Institutional Partners, LLC, AIP Resort Development, LLC and Peninsula Advisors LLC, LLCs formed under Delaware law, and Mark Robbins (collectively "Debtors").[122] Since Creditors sought to foreclose on the membership interests of Debtors, Debtors filed suit in Delaware, seeking a declaratory judgment that Creditors' foreclosures upon Debtors' membership interests were invalid under Delaware law.[123] Creditors responded by filing a Motion to Dismiss or Transfer Venue, arguing that Utah law applied.[124] In denying Creditors' motion, the Delaware court opined that even if the LLCs are registered to do business in Utah and have their principal places of business there, the Plaintiff's (Debtors) choice of forum outweighed the origin of the claim in Utah.[125] The court noted that factors in deciding whether the case should be transferred to Utah consisted of: preference of the plaintiff; preference of the defendant; where the plaintiff's claim arose; the physical condition and financial condition of the parties and the convenience of litigating in one jurisdiction as opposed to a different one; where the witnesses reside; where the documentary evidence is located; whether the judgment would be enforceable; practical consideration such as the ease and expense of trial; the caseload of the district court; local interests; public policy considerations; and whether a judge in one state may apply the law of the other state. Here, none of the factors stood out to tip the scale in favor of Creditors.[126] Although the Delaware LLC statute does not specifically prohibit foreclosure, this issue was addressed in the decision of *New Times Media LLC v. Bay Guardian Co*,[127] where the court stated that "Delaware law does not permit foreclosures on charging orders."[128]

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[120] DEL. CODE ANN. TIT 6 § 18-703.
[121] 2011 U.S. Dist. LEXIS 34385 (D.Del., Mar. 31, 2011).
[122] *Id.* at *1-4.
[123] *Id.* at *4.
[124] *Id.*
[125] *Id.* at *43
[126] Fairstar, 2011 U.S. Dist. LEXIS at *43-48.
[127] 2010 U.S. Dist LEXIS 64395.
[128] *Id.* at *8.

> *Fairstar* should serve as a potential warning for advisors who select a jurisdiction that may be more protected than the laws of their home state. Clients should be advised that the laws of the state of business or trust formation could be attacked where more favorable law exists in debtor's home state.[129]

C. Florida's Unique Approach and a Multitude of Issues to Consider

Florida's distinction between single-member and multimember LLCs whereby exclusive remedy protection is not available to the owner of a single-member LLC but is available to multimember LLCs is currently unique. Nevada and Wyoming specifically provide charging order protection to single-member and multimember LLCs.[130] While drafting a statute to distinguish between single-member LLCs and multimember LLCs and providing exclusive remedy and foreclosure protection to only multimember LLCs does not seem to be a daunting task, implementation is likely to be a challenge. As an example, will the courts consider an LLC to be a multimember LLC with a 99.99% member and a .01 % member a multimember LLC?[131] How could a statute be drafted that requires at least two significant or meaningful members that will not result in vast litigation? Should a safe harbor interest be provided that will create a statutory multimember LLC? Would the statute need to look through any business entity LLC members to determine whether beneficial ownership is entirely in one LLC member? Should the statute refer to a *de minimis* percentage of an LLC that would be disregarded in determining whether a single-member LLC exists? Should exclusive remedy protection be provided to single-member LLCs, but be subject to court oversight as provided, by way of example, in the revised Uniform Limited Liability Company Act which allows a court to foreclose and order the sale of the "transferable interest?"[132] Would such court discretion create uncertainty? The answers to the questions raised in this section are left to those who will need to devote significant time and effort to find an effective statutory solution. Each state will need to weigh its desire to be a business friendly jurisdiction against any policies to limit creditor protection. Any state law that differentiates between single-member and multimember LLCs may find it difficult to establish guidelines that would define single-member

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[129] *See* Viktoria A.D. Ziebarth, *Choice-of-Law Rules in Bankruptcy: An Opportunity for Congress to Resolve Conflicting Approaches*, 5 SEVENTH CIRCUIT REV. 309 (Spring 2010)

[130] WYO. STAT. ANN. § 17-29-503.

[131] *See* FLA. STAT. § 608.402(21) (defining an LLC member as "any person who has been admitted to a limited liability company as a member in accordance with this chapter and has an economic interest in a limited liability company which may, but need not, be represented by a capital account"). Due to the difficulties in what constitutes a member, it may be best to leave this issue to the courts, on a case by-case-basis, if single-member and multimember LLCs are provided different charging order protection.

[132] REV. UNIF. LTD. LIAB. CO. Act § 503(c) (2006).

and multimember LLCs in such a way as to not be subject to manipulation by creative debtors and their lawyers.

What is clear is that providing exclusive remedy and foreclosure protection for single-member LLCs is likely to result in an unanticipated asset protection vehicle that could exceed the asset protection benefits contemplated. States considering whether to enact provisions similar to Nevada or Wyoming may want to establish reasons, such as a requirement for a business purpose, to avoid unanticipated expansion of charging order protection for personal assets conveyed to single-member LLCs at the suggestion of creative asset protection attorneys. Possibly, states without domestic self-settled asset protection trust legislation may have an overall state policy against asset protection that would make it unlikely for such a state to pass legislation providing enhanced asset protection for single-member LLCs.

D. Conclusion

Based upon the discussion above, it is important to review state law before creating a partnership or LLC if asset protection is of any concern to a client. The *Olmstead* issue is for the most part resolved in Florida with multimember LLCs likely being treated in a similar fashion to Florida LPs. Actually, Florida's LP statute remains somewhat more protective than the LLC statute even after the 2011 "Patch" described above.[133] It is incumbent on planners to review their home state partnership and LLC statutes to determine whether partnerships and LLCs will benefit from charging order protection if created in a client's domicile state or whether a more conservative approach would be to create an LLC or partnership in a state where charging order protection is more certain. For Florida residents, creating a partnership under Florida's LP Act appears the safest alternative for asset protection. However, even after the *Olmstead* "Patch," due to the continued disparity (although minor) of creditor's rights for

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[133] *Compare* FLA. STAT. § 620.1703 (for LPs: "Other remedies, including foreclosure on the partner's interest in the limited partnership or a transferee's transferable interest and a court order for directions, accounts, and inquiries that the debtor general or limited partner might have made, are not available to the judgment creditor"), *with* FLA. STAT. § 608.433(5) For LLCs:

> Except as provided in subsections (6) and (7), a charging order is the sole and exclusive remedy by which a judgment creditor of a member or member's assignee may satisfy a judgment from the judgment debtor's interest in a limited liability company or rights to distributions from the limited liability company.

Id.; FLA. STAT § 608.433(6) (for single-member LLCs: "In the case of a limited liability company having only one member...a charging order is not the sole and exclusive remedy"); FLA. STAT. § 608.433(8) ("In the case of a limited liability company having more than one member, the remedy of foreclosure on a judgment debtor's interest in such limited liability company or against rights to distribution from such limited liability company is not available to a judgment creditor"). Also, since Florida Statutes § 608.402(21) requires an LLC member to have an economic interest in the LLC to be a member, if a creditor obtains a judgment against all members of a Florida LLC that exceeds the value of the members' LLC interests, the creditor could argue that the LLC should be dissolved under Florida Statutes §608.441(1)(d) because it has no members with an economic interest.

Florida partnerships and LLCs, Florida residents should consider creating LLCs in Delaware, Wyoming and possibly Nevada. The devil is in the details and states that have distinctions in their LP and LLC statutes similar to Florida could find themselves with court battles where those with judgments will try to foreclose on interests if they can find similar distinctions as described in *Olmstead*. There does not appear to be a good reason for state laws to distinguish between LP and LLCs with respect to charging order protection for multimember LLCs and LPs. The question as to whether states should provide charging order protection for single-member LLCs is more difficult. The author believes that because the concept of the charging order is to protect the continuing partnership partners or LLC members, that Florida's "Patch" approach makes sense. However, states such as Wyoming and Nevada have taken another direction. Applicable state laws should be reviewed to see if existing law corresponds with current state policy, and to determine whether state law includes charging order disparities similar to those discussed in *Olmstead*. Once the review is completed, state laws should be updated to avoid cases like *Olmstead* where variations in approaches for protecting partners and LLC members from creditors create unanticipated results. If charging order protection is an important objective, use of jurisdictions that have addressed charging order protection, codified the charging order protection and prohibit other remedies such as, but not limited to, foreclosure, rather than simply creating LLCs and partnerships in the debtor's home state, is the safest alternative.[134]

IV. Protecting the Future Inheritance

A. Introduction

Estate planning practitioners often incorporate asset protection planning tools such as spendthrift trusts and discretionary trusts, or a combination thereof.[135] A spendthrift trust restricts a beneficiary from assigning his or her interest and provides that creditors cannot reach beneficial interests in the instrument.[136] Spendthrift clauses prohibit most creditors from attaching trust assets and forcing distributions to satisfy the creditor claims. Many state statutes provide that certain creditors including those owed for child support, alimony and governmental claims retain the ability to enforce rights against a spendthrift trust. Thus, a spendthrift clause may

[134] This paper has not addressed whether the conversion of a single-member LLC created in Florida or any other state that does not recognize charging order protection for single-member LLC's to Nevada or Wyoming could be avoided as a fraudulent conveyance. The case law addressing such planning appears limited but it is likely that a creditor would put forth the fraudulent conveyance argument when faced with such facts. Stay tuned.

[135] RESTATEMENT (THIRD) OF TRUSTS § 58 (2003)(quoting comment a: "A spendthrift trust is to be distinguished from a discretionary trust but may or may not also contain discretionary interests…").

[136] *See* Bacardi v. White, 463 So.2d 218, 221 (Fla. 1985).

not protect the trust assets from the beneficiary's creditors in every instance.

Discretionary trusts often provide that the trustee, in the trustee's sole discretion, may determine whether or not a distribution will be made to a trust beneficiary and often also contain spendthrift clauses. The Uniform Trust Code ("UTC") "forbids a creditor from compelling a distribution from the trust, even if the trustee has failed to comply with the standard of distribution...the power to force a distribution due to an abuse of discretion or failure to comply with a standard belongs solely to the beneficiary."[137] Ascertainable standards are defined under the UTC and Florida Trust Code as standards relating to an individual's health, education, support or maintenance pursuant to §§ 2041(b)(1)(A) or 2514(c)(1) of the Internal Revenue Code.[138] Although the Restatement Third does not specifically define the term ascertainable standard as the UTC does, it states:

> [C]reditors may reach a beneficiary's right to receive the trust income or an annuity or unitrust payments. They may also attach a beneficiary's right to discretionary distributions, subject to the practical limitations described in § 60...Creditors may also reach a beneficiary's right to withdraw trust property or to demand distribution of a stated or formula amount..., including a power periodically to compel payments of stated or percentage amounts.[139]

Further, § 60 provides:

> [I]f the terms of a trust provide for a beneficiary to receive distributions in the trustee's discretion, a transferee or creditor of the beneficiary is entitled to receive or attach any distributions the trustee makes or is required to make in the exercise of that discretion after the trustee has knowledge of the transfer or attachment. The amounts a creditor can reach may be limited to provide for the beneficiary's needs (Comment c), or the amounts may be increased where the beneficiary either is the settlor (Comment f) or holds the discretionary power to determine his or her own distributions (Comment g).[140]

The public policy in favor of allowing for spendthrift trusts competes with public policy favoring payment of child support, alimony and governmental obligations. When analyzing the appropriateness of utilizing such trusts, it is important to consider variations among states' laws.

[137] UNIF. TRUST CODE § 504 cmt (2005).
[138] FLA. STAT. § 736.0103(3); UNIF. TRUST CODE § 103(2) (2005).
[139] RESTATEMENT (THIRD) OF TRUSTS § 56 (2003).
[140] RESTATEMENT (THIRD) OF TRUSTS § 60 (2003).

Establishing a trust domiciled in and governed by the laws of a particular jurisdiction could have significant benefits as compared to relying on the laws of the donor's home state when beneficiaries have or may have judgment creditors.

Spendthrift trusts and discretionary trusts are frequently a part of an estate plan to protect the inheritance of a beneficiary against claims made by creditors of the beneficiary. The UTC addresses the right of creditors against a debtor beneficiary's interest in spendthrift trusts and discretionary trusts.[141] § 502 of the UTC provides that creditors cannot compel a voluntary or involuntary transfer of the beneficiary's interests in a spendthrift trust.[142] § 504 provides that creditors cannot compel a distribution of a discretionary trust.[143] The UTC states that "whether or not a trust contains a spendthrift provision, a creditor of a beneficiary may not compel a distribution that is subject to the trustee's discretion, even if: (1) the discretion is expressed in the form of a standard of distribution; or (2) the trustee has abused the discretion."[144] The UTC provides for certain creditors who have greater powers to reach spendthrift and discretionary trust assets.[145] The UTC defines these creditors as exception creditors.[146] Each state that considered the adoption of the UTC weighed policy issues of allowing trust donors to protect the trust assets from its beneficiary's creditors as compared to protecting the rights of creditors such as: governments, children who have child support settlements, spouses and former spouses who may have judgments or their entitlements in the form of support. Some question whether their state's trust code should enhance a beneficiary's right to be a deadbeat dad. While the policy issues are beyond the scope of this article, planners need to be aware of the differences in state laws with respect to exception creditors so they may effectively advise their clients, especially those clients who advise that one or more of their children is subject to a judgment as a result of divorce or may be involved in a divorce. Spendthrift or discretionary trusts created in certain states are more protected than others, especially when it comes to judgments resulting from a divorce. If the parent's objective is to protect his child's inheritance from his or her former spouse, we as planners need to provide alternatives.

As states have considered whether to adopt the UTC's approach toward spendthrift and discretionary trusts and their exposure to claims made by creditors of trust beneficiaries, many have questioned whether such state's existing common law should be changed by the trust code provisions.

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[141] *See* UNIF. TRUST CODE §§ 501-504 (2005).
[142] UNIF. TRUST CODE § 502 (2005).
[143] UNIF. TRUST CODE § 504 (2005).
[144] UNIF. TRUST CODE § 504(B) (2005).
[145] UNIF. TRUST CODE § 503 (2005).
[146] UNIF. TRUST CODE, Art. 5 Creditor's Claims; Spendthrift and Discretionary Trust, General Comment (2005).

Florida law provides a good example of why creating a trust in a jurisdiction such as Nevada or South Dakota may provide significantly more protection for a divorced or divorcing child.

B. Example: Residential Developer Cannot Pay his Alimony Because he Cannot Make a Living

Divorced son Mark, a Florida domiciliary who has a large support obligation to a former spouse, was a successful Florida residential homebuilder who as a result of the existing market downturn, no longer has a source of income. Mark used all of his assets to satisfy bank guarantees on land which was stock piled for future development that lost significant value. Mark's father, a wealthy and elderly retiree ("Client") consults his adviser and asks whether the testamentary trust for Mark included in his existing estate plan could be reached by Mark's former wife who has a judgment against him in the form of support resulting from their divorce. Client states that when Mark was financially secure, Mark was making payments to his former spouse. However, like many others, Mark's ability to satisfy his debts was significantly curtailed when the value of his real estate vanished as did his capacity to earn a living as a developer. Client is helping to support Mark (hopefully temporarily) and wants the comfort that upon Client's death, Mark, and not Mark's former wife, would benefit from assets left in a spendthrift or discretionary trust for Mark.

Under Client's home-state law, both for support and discretionary trusts, assets held in a trust created by Client for Mark's benefit may be reached or attached by creditors, who have a judgment in the form of spousal support. Various states have enacted statutes governing creditor rights of beneficiaries who are subject to claims by exception creditors, and in certain limited circumstances, such as a claim by a state, the United States, or for child support or alimony, disbursements from spendthrift trusts may be garnished to enforce court orders or judgments.[147] However, as discussed below, the law is not clear in Florida as to whether an exception creditor can reach assets in a discretionary trust once the trustee is prepared to make a discretionary distribution.

Before enactment of the UTC, a number of cases addressed whether a creditor could garnish the interest of a beneficiary when an intended discretionary distribution was going to be made by the Trustees.[148] Under

[147] FLA. STAT. § 736.0503(2); UNIF. TRUST CODE § 503 (2005). *See* Mason v. Mason, 798 So.2d 895, 896-97 (Fla. 5th DCA 2001).

[148] *See* In re Bass, 171 F.3d 1016, 1028-29 (5th Cir. Tex. 1999)("courts can neither prevent or force the exercise of discretion by the trustee nor specify a particular exercise or otherwise interfere with or impinge on such discretion"); Bacardi, 463 So.2d at 222 (Fla. 1985)("If disbursements are wholly within the trustee's discretion, the court may not order the trustee to make such disbursements. However, if the trustee

the UTC, without a spendthrift provision, a creditor or assignee of the beneficiary of a trust other than a discretionary trust is ordinarily authorized "to reach the beneficiary's interest by attachment of present or future distributions to or for the benefit of the beneficiary or by other means."[149] However, the creditor generally cannot collect distributions to be made to a beneficiary of a discretionary trust.[150] Spendthrift provisions are effective so long as they restrain both voluntary and involuntary transfers of a beneficiary's interest.[151] The creditor's rights against a spendthrift trust are generally limited to circumstances whereby the beneficiary has a right to distributions.[152] Whether creditors can recover assets from a discretionary trust once a trustee is prepared to exercise discretion in favor of a beneficiary/debtor has and is likely to be subject to continued litigation.

C. Florida Trust Code and Case Law – *Barcardi* on the Rocks?

1. Florida Exception Creditors

In Florida, a spendthrift provision is unenforceable against a beneficiary's child, spouse or former spouse who has a judgment or court order for support or maintenance, a judgment creditor who has provided services for the protection of a beneficiary's interest in the trust and a claim of a state or the United States.[153]

2. Florida Case Law

Before enactment of Florida's Trust Code in 2006, *Bacardi v. White* provided Florida common law on the rights of a former spouse (wife) to assets in a spendthrift and discretionary trust, where wife had a judgment in the form of support against her ex-husband.[154] In *Bacardi*, the former spouse of donor's son was granted alimony.[155] After the son ceased paying the requisite amount of alimony, his ex-wife obtained a judgment for the unpaid balance.[156] In aid of execution on her judgments, the ex-wife served a writ of garnishment on the trustee of the spendthrift trust

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exercises its discretion and makes a disbursement, that disbursement may be subject to the writ of garnishment.").

[149] UNIF. TRUST CODE § 501 (2005). *See* FLA STAT. § 736.0501.

[150] *See* UNIF. TRUST CODE, § 504 cmt (2005). For case law and statutes regarding forcing distributions of a purely discretionary trust, see Mark Merric, *How to Draft Distribution Standards for Discretionary Dynasty Trusts*, 36 EST. PLAN 3, 8-10, fn 42-43 (Mar. 2009).

[151] FLA. STAT. § 736.0502; UNIF. TRUST CODE § 502(b) (2005).

[152] *See* Comments to UNIF. TRUST CODE §§ 503-504 (2005).

[153] FLA. STAT. § 736.0503(2).

[154] Bacardi, 463 So.2d at 223.

[155] *Id.* at 220.

[156] *Id.*

created by the father for benefit of the son.[157] The son and trustee asserted that under this spendthrift provision, the trust could not be garnished for the collection of alimony and attorney's fees.[158] The issue on appeal to the Florida Supreme Court was whether disbursements from spendthrift trusts could be garnished to satisfy court ordered alimony and attorneys' fees before such disbursements reach the debtor-beneficiary.[159] The Florida Supreme Court held that disbursements from spendthrift trusts, in certain limited circumstances, may be garnished to enforce court orders or judgments for alimony before such disbursements reach the debtor-beneficiary.[160]

Much of the *Bacardi* opinion centered on Florida's public policy in creating an exception to spendthrift trust provisions, specifically:

> This state has always had a strong public policy favoring the enforcement of both alimony and child support orders...We have weighed the competing public policies and, although we reaffirm the validity of spendthrift trusts, we conclude that in these types of cases the restraint of spendthrift trusts should not be an absolute bar to the enforcement of alimony orders or judgments. Florida's interest in the enforcement of these awards under certain limited circumstances is paramount to the declared intention of the donor and the restraint of a spendthrift trust.[161]

The court added:

> In not every case where someone is attempting to enforce alimony orders or judgment, however, will garnishment of a spendthrift trust be appropriate. This enforcement alternative *should be allowed only as a last resort.* If the debtor himself or his property is within the jurisdiction of this state's courts, the traditional methods of enforcing alimony arrearages may be sufficient. In this event, there would be no overriding reason to defeat the intent of the settlor.

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[157] Bacardi, 463 So.2d at220.
[158] *Id* at 220-21.
[159] *Id.* at 221.
[160] *Id.* at 223. See also Landmark First Nat'l Bank v. Haves, 467 So.2d 839, 840 (Fla. 4th DCA 1985). In review of a discretionary trust, in accord with *Bacardi v. White*, the court held that the creditor may be entitled to a continuing garnishment against the trust but that it will not be effective unless and until the trustee exercises discretion and elects to make payments to the beneficiary. The court may not order the trustee to make such disbursements.
[161] Bacardi, 463 So.2d at 222.

> Florida courts have a variety of methods available to enforce alimony and child support. When these traditional remedies are not effective, it would be unjust and inequitable to allow the debtor to enjoy the benefits of wealth without being subject to the responsibility to support those whom he has a legal obligation to support.[162]

It appears that the opinion in *Bacardi* was codified by Florida's Trust Code.[163] Florida Statutes § 736.0503(3) provides an exception to spendthrift provisions, as follows:

> Except as otherwise provided in this subsection and in s. 736.0504, a claimant against which a spendthrift provision may not be enforced may obtain from a court, or pursuant to the Uniform Interstate Family Support Act, an order attaching present or future distributions to or for the benefit of the beneficiary. The court may limit the award to such relief as is appropriate under the circumstances. Notwithstanding this subsection, the remedies provided in this subsection apply to a claim by a beneficiary's child, spouse, former spouse, or a judgment creditor described in paragraph (2)(a) or paragraph (2)(b) only as a last resort upon an initial showing that traditional methods of enforcing the claim are insufficient[164]

3. Did the Florida Trust Code Overrule *Bacardi* for Discretionary Trusts?

While it appears that Florida law allows certain creditors to garnish spendthrift trust distributions, it remains unclear whether exception creditors may garnish a beneficiary's interest in a discretionary trust. Florida Statutes § 736.0504 addresses discretionary trusts[165] and provides:

> Whether or not a trust contains a spendthrift provision, if a trustee may make discretionary distributions to or for the benefit of a beneficiary, a creditor of the beneficiary, including a creditor as described in s. 736.0503(2), may not: (a) Compel a distribution that is subject to the trustee's discretion;

[162] Bacardi, 463 So.2d at 222 (emphasis added).
[163] *See generally* FLA. STAT. § 736 (chapter effective July 31, 2007).
[164] FLA. STAT. § 736.0503(3).
[165] FLA. STAT. § 736.0504.

> or (b) Attach or otherwise reach the interest, if any, which the beneficiary might have as a result of the trustee's authority to make discretionary distributions to or for the benefit of the beneficiary.[166]

One reading Florida Statutes §§ 736.0503(2)(b) and 736.0504 may believe that a discretionary trust created for a beneficiary such as Mark would be protected and an exception creditor could not **attach or otherwise** reach Mark's interest.

The Florida Senate Analysis and Economic Impact Statement prepared prior to § 736.0504's enactment date, stated that "exception creditors may attach present or future distributions to or for the benefit of the beneficiary; they cannot compel distributions from or otherwise reach beneficial interests in discretionary trusts."[167] The terms "attach" or "reach" are not defined in the Florida Trust Code and lend themselves to a number of interpretations as to whether a creditor may be able to garnish the interest of a discretionary trust once the trustee, in the trustee's sole discretion, is ready to exercise its discretion to make a trust distribution to the beneficiary. The court in *Bacardi* did not need to address whether its ruling would apply equally to a discretionary trust. However, the *Bacardi* opinion states:

> We further limit this right of garnishment to disbursements that are due to be made or which are actually made from the trust. If, under the terms of the trust, a disbursement of corpus or income is due to the debtor-beneficiary, such disbursement may be subject to garnishment. *If disbursements are wholly within the trustee's discretion, the court may not order the trustee to make such disbursements. However, if the trustee exercises its discretion and makes a disbursement, that disbursement may be subject to the writ of garnishment….We also note that where a continuing garnishment is appropriate, the trustee, if it wishes to make payments to the debtor-beneficiary in excess of alimony then due, should seek court approval before it makes such payments. The court may then authorize such payments if sufficient assets remain in the trust or if*

[166] FLA. STAT. § 736.0504(2).

[167] Banking & Insurance Committee, Senate Staff Analysis and Economic Impact Statement on CS/SB 1170 at 23, Mar. 21, 2006, http://archive.flsenate.gov/data/session/2006/Senate/bills/analysis/pdf/2006 s1170.bi.pdf.

> *other provisions are made to secure the payment of alimony to the person who should receive it.*[168]

Although Florida practitioners may believe that the intent of the Florida legislature in its drafting of the Florida Trust Code was to follow *Bacardi*, an interpretation of the Florida Trust Code could leave an impression that an exception creditor could not garnish assets in a Florida discretionary trust even upon distribution to an exception creditor due to the phrase may not "attach or otherwise reach an interest."[169] When reading the Florida Trust Code in conjunction with *Bacardi*, a court could determine that if a trustee, in the trustee's sole discretion, decides to make a distribution, an exception creditor of the beneficiary should be able to garnish such distributions before they reach the beneficiary.

4. It is Safer to Create a Discretionary Trust in a State that Clearly Addresses Exception Creditors

Based upon *Bacardi*, it appears that although an exception creditor may attach a present or future distribution to or for the benefit of the beneficiary regardless of whether the trust contains a spendthrift provision; such exception creditor cannot compel distributions from or otherwise reach beneficial interests in discretionary trusts. In the event that the exception creditor could attach or otherwise reach distributions intended to be made by the trustee of a discretionary trust, then effectively, the donor's objective, to provide funds to the beneficiary and not to the beneficiary's former spouse, are thwarted. In Florida, the question as to whether an exception creditor can obtain a continuing garnishment over assets in a discretionary trust is likely to be determined by future case law or statutory clarification. For those desiring greater certainty that their beneficiaries (and not the beneficiary's former spouses) will benefit from trust assets, other jurisdictions such as Nevada or South Dakota should be considered. However, even Ohio law provides greater certainty than many other states.

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[168] Bacardi, 463 So.2d at 222-23 (emphasis added) (The Florida Trust Code preserves the ability for an exception creditor to reach Bacardi requirements that child support and alimony creditors reach a beneficiary's spendthrift interest "only as a last resort.").

[169] FLA. STAT. § 736.0504(2)(b). *See* Lerman v. Lerman, 2009 N.J. Super. Unpub. LEXIS 2093 (App.Div. Aug. 4, 2009) (quoting *Bacardi* in part, "The right of a third party to garnish assets of a beneficiary of a spendthrift trust is limited to disbursements from the trust and '[i]f disbursements are wholly within the trustee's discretion, the court may not order the trustee to make such disbursements.'").

D. Ohio Trust Code – Some Distinction

Like Florida, Ohio is modeled after the UTC and many of its provisions are similar. For example, the Ohio statutes governing spendthrift trusts mirror Florida and the UTC and seem to distinguish between the protections afforded to each type of trust.[170] Ohio differs from Florida and the UTC as it specifically differentiates between wholly discretionary trusts, discretionary trusts with spendthrift language, and discretionary trusts without spendthrift language. Ohio Revised Code Annotated § 5805.04(B) resembles Florida and the UTC in that creditors may not compel distribution subject to a trustee's discretion, even if that discretion is in the form of a standard. The Ohio Trust Code includes § 5805.03 which, unlike Florida or the UTC, differentiates wholly discretionary trusts from trusts that provide distributions subject to a standard. Ohio law states that "no creditor or assignee of a beneficiary of a wholly discretionary trust may reach the beneficiary's interest in the trust, or a distribution by the trustee before **its receipt** by the beneficiary...regardless of whether the terms of the trust include a spendthrift provision."[171] Ohio does have exceptions for a trust that is not wholly discretionary.[172] However, even for an Ohio trust that is not fully discretionary, the donor can explicitly provide in the trust that the beneficiary's child and spouse or both are excluded from benefiting from the Trust.[173] Furthermore, even without the express exclusion of a beneficiary's spouse or child, the exception under Ohio Revised Code Annotated § 5805.04(D) does not permit a court to order any distributions from a discretionary trust to satisfy a judgment or court order against the beneficiary for support of the

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[170] *Compare* OHIO REV. STAT. § 5805.01, *with* FLA. STAT. § 736.0502; UNIF. TRUST CODE § 502 (2005).

[171] OHIO REV. CODE ANN § 5805.03 (emphasis added).

[172] OHIO REV. CODE ANN § 5805.04(C)-(D).

> (C) Division (B) of this section does not apply to this state for any claim for support of a beneficiary in a state institution if the terms of the trust do not include a spendthrift provision and do include a standard for distributions to or for the beneficiary under which the trustee may make distributions for the beneficiary's support.
>
> (D) Unless the settlor has explicitly provided in the trust that the beneficiary's child or spouse or both are excluded from benefiting from the trust, to the extent a trustee of a trust that is not a wholly discretionary trust has not complied with a standard of distribution or has abused a discretion, both of the following apply:
>
> (1) The court may order a distribution to satisfy a judgment or court order against the beneficiary for support of the beneficiary's child or spouse, provided that the court may order the distributions only if distributions can be made for the beneficiary's support under the terms of the trust and that the court may not order any distributions under this division to satisfy a judgment or court order against the beneficiary for support of the beneficiary's former spouse.
>
> (2) The court shall direct the trustee to pay to the child or spouse the amount that is equitable under the circumstances but not more than the amount the trustee would have been required to distribute to or for the benefit of the beneficiary had the trustee complied with the standard or not abused the discretion.

Id.

[173] OHIO REV. CODE ANN § 5805.04 (D).

beneficiary's former spouse.[174] As indicated below, South Dakota and Nevada provide even greater protection to a beneficiary subject to an outstanding judgment from a spouse or former spouse for support.

E. A Comparison of South Dakota and Nevada to Florida, Ohio and the UTC

Based upon the example above, Mark's father believed the risk of enabling Mark's former spouse to reach assets in a Florida discretionary trust was too great. After reviewing the laws of various jurisdictions, including those that have adopted the UTC in some form, we limited our review to two jurisdictions to satisfy our Client's goals –Nevada and South Dakota.

1. South Dakota

The South Dakota statute leaves little room for misunderstanding. For example, unlike Florida where the word "reach" is not defined, South Dakota Codified Laws § 55-1-24(6) defines reach as follows: "to subject the distribution to a judgment, decree, **garnishment**, **attachment**, execution, levy, creditor's bill or other legal, equitable, or administrative process, relief, or control of any court, tribunal, agency, or other entity as provided by law."[175]

South Dakota Codified Laws § 55-1-25 specifically states "...the Legislature does not intend the courts to consult the Restatement (Third) of the Law of Trusts Articles § 50, § 56, § 58, § 59, or § 60."[176] South Dakota Codified Laws § 55-1-35 states that a declaration in a trust that the intent of the beneficiary "shall be subject to a spendthrift trust" is sufficient to restrain voluntary or involuntary alienation.[177] South Dakota Codified Laws § 55-1-35 additionally states:

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[174] OHIO REV. CODE ANN § 5805.04 (D)(1).

[175] S.D. CODIFIED LAWS § 55-1-24(6) (emphasis added).

[176] S.D. CODIFIED LAWS § 55-1-25.

> The common law distinction between a discretionary trust and a support trust and the dual judicial review standards related to this distinction shall be maintained. In the area of creditor rights, the Restatement of Trusts (Third) and the Uniform Trust Code creates many new positions of law as well as adopts many minority" positions of law. Sections 55-1-24 to 55-1-43, inclusive, affirmatively reject many of these positions. Therefore, the Legislature does not intend the courts to consult the Restatement (Third) of the Law of Trusts Articles § 50, § 56, § 58, § 59, or § 60 as approved by the American Law Institute of Uniform Trust Code Article 5 and Section 814(a) as approved by the National Conference of Commissioners on Uniform State Laws in 2004 with respect to subject matters addressed by §§ 55-1-24 to 55-1-43, inclusive.

Id.

[177] S.D. CODIFIED LAWS § 55-1-35.

> Regardless of whether a beneficiary has any outstanding creditor, a trustee of a spendthrift trust may directly pay any expense on behalf of such beneficiary and may exhaust the income and principal of the trust for the benefit of such beneficiary. No trustee is liable to any creditor for paying the expenses of a beneficiary of a spendthrift trust.[178]

2. Nevada

Nevada's spendthrift trust statute dates back to 1939, and was significantly enhanced in 1999 by enlarging the class of permitted beneficiaries of a spendthrift trust, and the types of spendthrift trusts to which the law of Nevada applied.[179] There is no statutory allowance for exception creditors and Nevada specifically disallows claims of spouses, former spouses, children, or dependents as Nevada Revised Statutes § 166.090 provides that a "[p]rovision for the beneficiary will be for the support, education, maintenance and benefit of the beneficiary alone, and without reference to or limitation by the beneficiary's needs, station in life, or mode of life, or the needs of any other person, whether dependent upon the beneficiary or not."[180] Nevada Revised Statutes § 166.080 adds that "[t]he beneficiary or beneficiaries of such trust shall be named or clearly referred to in the writing. No spouse, former spouse, child or dependent shall be a beneficiary unless named or clearly referred to as a beneficiary in the writing."[181]

The Trustee's exercise of his or her discretion in a discretionary trust can only be reviewed if the trustee acts "dishonestly, with improper motive or fails to act."[182] "Regardless of whether a beneficiary has an outstanding creditor, a trustee of a discretionary interest may directly pay any expense on the beneficiary's behalf and may exhaust the income and principal of the trust for the benefit of such beneficiary."[183] Furthermore, creditors have an almost impossible task at trying to get a Nevada court to force a trustee to make a distribution out of a discretionary trust, as Nevada Revised Statutes § 163.417 provides:

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[178] S.D. CODIFIED LAWS § 55-1-35.
[179] *See* Assembly Bill 469, as introduced, Mar. 10, 1999, *available at* http://www.leg.state.nv.us/Session/70th1999/bills/AB/AB469.pdf.
[180] NEV. REV. STAT. § 166.090(1).
[181] NEV. REV. STAT. § 166.080.
[182] NEV. REV. STAT. § 163.419(1).
[183] NEV. REV. STAT. § 163.419(4).

> 1. A creditor may not exercise, and a court may not order the exercise of:
> (a) A power of appointment or any other power concerning a trust that is held by a beneficiary;
> (b) Any power listed in NRS 163.5553 that is held by a trust protector as defined in NRS 163.5547 or any other person;
> (c) A trustee's discretion to:
> (1) Distribute any discretionary interest;
> (2) Distribute any mandatory interest which is past due directly to a creditor; or
> (3) Take any other authorized action in a specific way; or
> (d) A power to distribute a beneficial interest of a trustee solely because the beneficiary is a trustee...
> 3. A settlor may provide in the terms of the trust instrument that a beneficiary's beneficial interest may not be transferred, voluntarily or involuntarily, before the trustee has delivered the interest to the beneficiary.[184]

3. Commentators' Views

At least one treatise has suggested, "[t]o provide protection against a claim for support of a beneficiary's spouse and children, the situs of the trust should be either Nevada or a foreign jurisdiction that has similar laws."[185] "Nevada deviates from the general rule by providing that a beneficiary's interest in a spendthrift trust is protected from support claims. Accordingly, one can use a Nevada situs trust for a beneficiary that is likely to be subject to these kinds of claims"[186] Mark Merric, in his three part analysis in *Estate Planning Magazine* entitled *Discretionary Dynasty Trust*, points to South Dakota as the discretionary trust leader.[187]

F. Where Does Client's Trust Belong?

Ultimately, our Client created a discretionary trust in Nevada, as the Nevada statute prohibits a judgment creditor in the form of spousal and child support from reaching trust assets or distributions therefrom. Nevada law addressed Client's concern, whereas under Florida law, it appears an

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[184] NEV. REV. STAT. § 163.417(1), (3).
[185] Peter Spero, Bolstering Protective Trusts to Maximize Protection Against All Claims, in ASSET PROTECTION: LEGAL PLANNING, STRATEGIES AND FORMS ¶ 6.12[2] (2011 ed.).
[186] *Id.* at ¶ 6.12[2][c].
[187] Mark Merric, Michael J. Bland & Mark Monasky, *Beware of Federal Super Creditors*, 149 TRUSTS & EST. 14 (July 2010); Worthington & Merric, *supra* note 104; Mark Merric, *How to Draft Discretionary Dynasty Trusts – Part 3*, 36 EST. PLAN. 13, 22 (Apr. 2009).

argument can be made that based upon *Bacardi*, Mark's exception creditors could potentially obtain a garnishment of distributions once made by the trustee. South Dakota has an excellent statute but Client's trust company had an office in Nevada and Client committed to maintaining the fiduciary relationship. Nevada specifically permits payments from the trust directly for the beneficiary's benefit and specifically states that no spouse or former spouse shall be considered a beneficiary unless clearly named or referred to as such.

G. Conclusion

As states grapple with how exception creditors are treated for spendthrift and discretionary trusts, it is likely that there will be significant distinctions in the level of protection for beneficiaries of trusts created within the United States. If Florida's experience is not unique, remedies provided to exception creditors of spendthrift trusts and discretionary trusts will vary. As new trust codes are enacted, issues such as the rights of an exception creditor to a continuing garnishment of a discretionary trust may come into dispute. Other states should learn from Florida's experience, consider South Dakota and Nevada law, and then determine what their state's policy and law should be for exception creditors of spendthrift and discretionary trusts. Planners should advise their clients of the differences in treatment of exception creditors, especially when clients consult their lawyers as to how to protect their children from potential judgments in the form of support against their children.[188]

V. Tenancy by the Entireties Protection

A. Introduction

Tenancy by the Entirety is a form of ownership historically available to married couples where property is deemed to be held by a single, indivisible marital unit. This form of property ownership still exists in at least twenty-five states and the District of Columbia, some in its historic form and others in a modified form.[189] States that provide full tenancy by the entirety ownership protect such property from the creditors of one spouse. Due to the inseverable nature of tenancy by the entirety ownership, the creditors of one spouse cannot access the tenancy by the entirety property because it would interfere with the ownership rights of the non-debtor spouse. This section addresses how tenants by the entirety is properly created, limitations on its protection, the types of property that can be protected and how to plan using tenants by the entirety protection

[188] For a recent case alluding to the fact that the creditor's choice of law may not apply in certain situations, see discussion of Fairstar Resources, Ltd., 2011 U.S. Dist. LEXIS 34385 in Section III.B.6.b, *supra*. Alaska is another state that provides debtors protection from exception creditors. *See also* ALASKA STAT. § 34.40.110.

[189] *See* Exhibit E.

even if a couple's home state does not provide tenants by the entirety protection.

B. Formation

The following example is based upon Florida law. Many of the provisions are similar to other tenants by the entirety jurisdictions but each state has unique provisions that must be carefully reviewed. In Florida, tenancy by the entirety is a form of legal ownership possessing the five characteristics present in a joint tenancy, combined with the unity of marriage: unity of possession (joint ownership and control); unity of interest (the interests must be identical); unity of title (the interests must have originated in the same instrument); unity of time (the interest must have commenced simultaneously); and the characteristic of survivorship (ownership inures solely to the surviving owner following the co-owner(s)'s death and is not devisable).[190] In Florida, one spouse can create a tenancy by the entirety in real property by deeding the property in the names of both spouses and still benefit from tenants by the entirety protection notwithstanding the lack of unity of time or title.[191] Effective October 1, 2008, Florida has a similar provision for joint bank accounts so that one spouse can retitle a bank account in the name of husband and wife as tenants by the entirety and retain protection.[192]

Until the October 1, 2008, banking revision, the Florida Supreme Court decision in *Beal Bank v. Almand and Associates* first enumerated that if a bank account is held by both spouses and the six unities exist, a rebuttable presumption arises that the account is held as tenants by the entireties.[193] The *Beal* decision did not definitively address the lower court's interpretation that a spouse's name could not be added to a bank account, after one spouse had already opened the account, to create a valid tenancy by the entirety.[194] The name cannot be subsequently added because the unities of time <u>and</u> title are lacking.

In a case following the October 1, 2008 amendment but applying law prior to enactment, the court in *In re Aranda*,[195] addressed whether a bank

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[190] *See* Beal Bank v. Almand & Assocs., 780 So.2d 45, 52 (Fla. 2001).

[191] FLA. STAT. § 689.11. *See* Buzby-Walt, *supra* note 10, at 53.

> Attorneys' Title Insurance Fund, Inc., Title Note 17.01.01 (Rev. 12/93), confirms that a straw man conveyance is not necessary with respect to real property. The Fund cites Florida National Bank v. Gann, 101 So. 2d (Fla. 2d DCA 1958), and LaPierre [LaPierre v. Kalergis, 251 So.2d 885 (Fla. 1st DCA 1971), *aff'd* 257 So.2d 33], and the fact that the Florida Supreme Court affirmed LaPierre and found that the four unities were present despite the absence of a straw man.

Id.

[192] FLA. STAT. § 655.79.

[193] Beal Bank, 780 So.2d at 58-59.

[194] *Id.* at 49, FN 2.

[195] 2011 Bankr. LEXIS 108 (Bankr. S.D. Fla. Jan. 10, 2011).

account lacking the unities of time and title was a tenancy by the entirety when one spouse opened a single-party account alone and later added the other spouse as a co-owner.[196] The court held that where a spouse does not acquire his or her interest in an account at the same time as the other spouse, the bank account is not held as a tenancy by the entirety because the unity of time is not present.[197] Although the spouses signed a second signature card and deposited all funds in the account following the signing of the second card, the court stated that the relevant time for establishing tenants by the entirety ownership is when the account was originally opened and that the spouses did not allege that any funds they deposited into the account were traceable to tenancy by the entirety property.[198]

In 2008, Florida Statutes § 655.79 was modified to state: "[a]ny deposit or account made in the name of two persons who are husband and wife shall be considered a tenancy by the entirety unless otherwise specified in writing."[199] It appears that the decision of *Aranda* would be different if the facts occurred after enactment of Florida Statutes § 655.79. Traps exist for those who believe they hold title as tenants by the entirety. A creative creditor attorney should carefully investigate the effectiveness of the claimed entirety protection. Applicable state law must be carefully reviewed to distinguish rules for real property. Advisors should not rely on a client's representation that assets are titled as tenants by the entirety without verifying the required unities were present when title was taken under applicable state law.

C. Creditors' Claims

Generally, only creditors of both spouses jointly can reach tenancy by the entirety property. However, the US Supreme Court decided in *U.S. v. Craft*,[200] that the IRS was able to reach tenants by the entirety property even though one spouse, and not both, owed the debt.[201] Subsequent cases

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[196] In re Aranda, 2011 Bankr. LEXIS 108 at *1-4.

[197] *Id.* at *6.

[198] *Id.* at *8-9.

[199] FLA. STAT. § 655.79(1)

> Unless otherwise expressly provided in a contract, agreement, or signature card executed in connection with the opening or maintenance of an account, including a certificate of deposit, a deposit account in the names of two or more persons shall be presumed to have been intended by such persons to provide that, upon the death of any one of them, all rights, title, interest, and claim in, to, and in respect of such deposit account, less all proper setoffs and charges in favor of the institution, vest in the surviving person or persons. Any deposit or account made in the name of two persons who are husband and wife shall be considered a tenancy by the entirety unless otherwise specified in writing."

Id.

[200] 535 U.S. 274 (2002).

[201] It would appear that Craft could also apply to federal cases that involve either a federal lien or restitution order permitting the use of remedies provided under the Internal Revenue Code to enforce the lien or restitution order (See In re Dahlman, 304 B.R. 892 (Bankr. M.D. Fla., 2003)). In Popky v. US, 419 F. 3d 242 (3rd Cir. 2005), the court also held that a federal tax lien could attach to the husband's interest in

have limited the court's decision in *Craft* to apply only to federal tax liens. In *In re Knapp*,[202] the bankruptcy trustee tried to reach property held by the debtor as tenants by the entirety. Citing *Craft*, the trustee argued that the Supreme Court decision in *Craft* should bring property held as tenants by the entirety within the reach of a bankruptcy trustee to satisfy debts of an individual debtor.[203] The Bankruptcy Court held that the tenants by the entirety property held with a non-debtor spouse was not available to satisfy an unsecured debt owed solely in the name of one spouse.[204] The opinion states, "[f]ederal tax creditors are unique in that they are endowed by federal statute with certain powers which allow them to collect tax debts against property most creditors cannot reach."[205] The court in *In re Ryan*,[206] stated "*Craft* gives no indication the reasoning should be extended beyond federal tax law."[207] Despite the narrowness of the decision in *Craft*, practitioners should be aware that the federal government may be able to reach tenants by the entirety property, even if only one spouse is the debtor. For example, the SEC now joins the IRS in having the ability to reach tenants by the entirety assets, (see discussion in Section VI., below).

Section 6321 of the Internal Revenue Code provides that:

> If any person liable to pay any tax neglects or refuses to pay the same after demand, the amount (including any interest, additional amount, addition to tax, or assessable penalty, together with any costs that may accrue in addition thereto) shall be a lien in favor of the United States upon all property and rights to property, whether real or personal, belonging to such person.[208]

Courts use a two-step process in deciding the scope of a federal tax lien: (1) looking to state law to see what legal interests it creates for the taxpayer; and (2) looking to federal law to decide whether those interests constitute property or rights to property that the federal tax lien can latch

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tenants by the entirety property and force the sale with a distribution to the husband and wife of equal sales proceeds under Pennsylvania law.

[202] 285 B.R. 176 (Bankr. M.D.N.C., 2002).

[203] *Id.* at 178.

[204] *Id.* at 182-83.

[205] *Id.* at 181.

[206] 282 B.R. 742 (U.S. Dist. Ct. R.I., 2002).

[207] *Id.* 750. For other post *Craft* cases that held entirety ownerships effective where non IRS creditor, see In re Kelly, 289 B.R. 38, 43-45 (Bankr. D. Del. 2003) (bankruptcy creditor cannot attach debtor's interest in tenancy by the entireties property); Walters v. Leech, 279 Mich. App. 707, 716-19 (Mich. Ct. App. 2008) (child support liens could not be imposed against property held as tenancy the entireties); In re Brannon, 476 F.3d 170, 176-77 (3d Cir. Pa. 2007) (bankruptcy trustee bound by state law shielding tenancy by the entireties property from bankruptcy claim).

[208] I.R.C. § 6321.

onto.[209] "[F]ederal law looks past state law labels to determine whether that state law is truly defining the scope of property rights or instead creating a preference regime."[210] "The role of state law is thus very slim in determining the scope of the federal tax lien."[211] The Supreme Court in *Craft* stated that an "interpretation of 26 U.S.C. §6321 is a federal question, and in answering that question, we are in no way bound by state courts' answers to similar questions involving state law… exempt status under state law does not bind the federal collector."[212] *Craft* is cited for authority that "the government's need to collect taxes must trump the protection of entireties interests…federal tax liens may attach to property interests held in tenancy by the entirety."[213]

> [I]t is irrelevant that the highest court of a state holds that those enforceable rights are not property for state law purposes. The federal tax lien will nonetheless stick to those legal interests, with consequences determined by federal law and with federal law controlling how the IRS may enforce the lien.[214]

Even though other courts have limited *Craft* to matters solely pertaining to federal tax liens,[215] Judge Middlebrooks in the case of *SEC v. Solow* (discussed in detail in Section VI., below),[216] takes another approach to allow the SEC to become a super-creditor; his opinion states that disgorgement is the "remedy of the people;" "[a] disgorgement order is more like an injunction for the public interest than a money judgment…[i]t is this feature, the similarity to an injunction, that allows disgorgement orders, unlike judgments, to be enforced by civil contempt."[217] Unlike other remedies at law, the "[c]ourt has broad equitable powers to reach assets otherwise protected by state law to satisfy disgorgement… a district court can ignore state law exemptions as well as other state law limitations on the ability to collect a judgment in fashioning a disgorgement order."[218]

Disgorgement is the "act of giving up something (such as profits illegally obtained) on demand or by legal compulsion."[219] It is common in insider

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[209] *See* Aquilino v. U.S., 363 U.S. 509, 512-14 (1960).
[210] Bryan Camp, *Protecting Trust Assets from the Federal Tax Lien*, 1 EST. PLAN. & CMTY. PROP. L.J. 295, 301 (2008-09).
[211] *Id.* at 308.
[212] Craft, 535 U.S. at 288 (quoting in part Drye v. U.S., 528 U.S. 49, 59 (1999)).
[213] In re Hutchins, 306 B.R. 82 (Bankr. D. Vt. 2004).
[214] Camp, *supra* note 210, at 309.
[215] For the judicially imposed to limits on *Craft* to date, see discussion in note 207, *supra*.
[216] 682 F. Supp.2d 1312 (S.D. Fla. 2010).
[217] *Id.* at 1324 (quoting Steffen v. Gray, Harris & Robinson, P.A., 283 F. Supp.2d 1272, 1282 (M.D. Fla. 2003)).
[218] *Id.*
[219] BLACK'S LAW DICTIONARY, *supra* note 85.

trading cases, as well as other SEC cases, and is primarily used to deny the wrongdoer the fruits of ill-gotten gains and ensure that the wrongdoer will not profit from violating the securities laws.[220] "It is common for disgorgement of the funds to provide restitution to injured investors."[221]

Disgorgement is one of the ancillary reliefs fashioned by the SEC and the courts.[222] "Refusal to comply with orders of ancillary relief [such as a disgorgement order] can result in contempt of court and also can form the basis of incarceration."[223] "In an SEC enforcement action, the district court has the authority, through its equitable jurisdiction, to fashion an appropriate remedy on a proper showing of a securities violation... The ultimate remedies available to the court include disgorgement, restitution, and rescission."[224] There is a presumption that a district court has broad discretion in using a disgorgement order,[225] but is disgorgement broad enough to ignore state law exemptions as Judge Middlebrooks held?

In *SEC v. Huffman*,[226] the court held that disgorgement was not a debt under the Federal Debt Collection Procedures Act of 1990, and thus, the "defendants could not avail themselves of state law exemptions under the Debt Act."[227] Interestingly though, the court went on to say that "[t]his is not to say, however, that such exemptions may never be taken into account by the court… [and the court] may decide that some property should be exempt from such an order and may take state law as its guide"[228] In *SEC v. Musella*,[229] another disgorgement case, the court took a firmer stance than *Huffman* by stating that "the extent to which Mr. DeAngelis' assets and income would be exempt from attachment under New York law does not alter his duty to pay the amount he owes under the order."[230]

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[220] THOMAS LEE HAZEN, TREATISE ON THE LAW OF SECURITIES REGULATION VOL. 5 at 25-27 (5th ed., 2005).
[221] *Id.*
[222] *Id.* at 22-24. Other such remedies include:

> [T]he appointment of an independent majority on the board of directions, the appointment of a receiver, prohibitions against exercising voting control in a proxy battle, the appointment of 'special professionals' to assure compliance with securities laws, the imposition of additional reporting requirements, fashioning of orders designed to protect remaining assets, and prohibitions against continued participation as an officer or director of any public company.

Id.
[223] *Id.* at 24.
[224] SEC v. Comcoa Ltd., 887 F. Supp. 1521, 1524 (S.D. Fla. 1995).
[225] *See* SEC v. Huffman, 996 F.2d 800, 803 (5th Cir. 1993).
[226] Huffman, 996 F.2d at 803.
[227] *Id.*
[228] *Id.*
[229] 818 F. Supp 600 (S.D. N.Y. 1993).
[230] *Id.* at 602.

In *In re Musolino*,[231] another case cited in the *Solow* opinion, a bankruptcy creditor argued that a debtor's ownership rights in tenancy by the entireties property should be brought into a bankruptcy administration under the *Craft* precedent.[232] The court refused to extend the holding in *Craft* to creditors attempting to attach the property owned by a Chapter 13 bankruptcy debtor because of the unique nature of the powers granted to the IRS under federal law through the Supremacy Clause.[233] If other courts ultimately decide to follow *Solow*, besides the Eleventh District, then where is the line to be drawn for which federal agencies or quasi-federal actions can receive super-creditor status? It seems that the *Musolino* court offers sound reasoning why other agencies, other than the IRS, should not be afforded the ability to circumvent tenancy by the entireties protection as well as other state law exemptions. The court noted that "[t]he Supreme Court has expressed its 'deep reluctance to interpret a statutory provision so as to render superfluous other provisions in the same enactment.'"[234] Thus, where *Craft* extended a remedy to the IRS for use of § 6321 of the Internal Revenue Code to permit an attachment of a lien to property rights, a court could not extend a creditor's remedy and render other statutes superfluous, such as what the creditor tried to do with § 522 (b)(2)(B) of the Bankruptcy Code in *Musolino*, by pointing to *Craft* as authority that creditors, whether government agencies or a lay person, hold power to subvert state exemptions.

D. Holding Property as Tenants by the Entirety Can Protect Assets From Certain Creditors

Other than the IRS and other potential "super-creditors" as in *Solow*, property held as tenants by the entirety is only subject to the creditor claims of both spouses, and cannot be reached by the creditors of one spouse alone. Therefore, if only one spouse is indebted, that spouse's creditors cannot reach tenants by the entirety assets protected under certain state law. These states are known as "full bar" jurisdictions as contrast from "modified bar" jurisdictions that give parity to the other spouse so that he or she can alienate part of the tenancy during his or her lifetime, and thus be subject to a degree of creditor attachment, regardless of whether the innocent spouse played any role in acquiring the debt.[235] Depending on the total assets of the couple, this can protect a significant portion of the couple's assets.

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[231] 391 F.3d 1295 (11th Cir. Fla. 2004).
[232] In re Musolino, 391 F.3d at 1297. Note, this was cited as In re Sinreich, 391 F.3d 1295 (11th Cir. 2004) in the *Solow* opinion.
[233] *Id.* at 1297-98.
[234] *Id.* at 1298 (quoting Circuit City Stores, Inc. v. Adams, 532 U.S. 105, 113 (2001)).
[235] *See* Frederick R. Franke, Jr., *Asset Protection and Tenancy by the Entirety*, 34 ACTEC J. 209, 212 (Spring 2009).

To stop individuals who are on the verge of filing for bankruptcy from moving their wealth to states with laws that might better help them keep their assets (such as liberal homestead, annuity and similar exemptions), the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (the "2005 Bankruptcy Act") created two holding period requirements.[236] To qualify for a state's homestead exemption with property worth more than $125,000, an individual must own that property for 1,215 days before filing for bankruptcy.[237] There is also a residency requirement of 730 days, pre-bankruptcy filing, to take advantage of a state's other exemptions — including life insurance, annuities and retirement plans.[238]

Since the 2005 Bankruptcy Act was adopted, there have been cases across the country involving homeowners who failed to satisfy either one, or both, of these holding periods. In at least seven cases, described below (four bankruptcy cases in Florida, one bankruptcy case in Illinois, one bankruptcy case in Texas and one U.S. Court of Appeals for the Fifth Circuit case), decided since January 2006, homeowner debtors were able to retain all or a portion of the value of their homes after a bankruptcy proceeding despite the duration of their new domicile because said homes were titled as tenants by the entirety and the court concluded that § 522(b)(3)(B) of the Bankruptcy Code did not require a mechanical residency formula to obtain its benefits.[239]

1. Importing the Asset Protection Benefits of Tenants by the Entirety to States That Do Not Offer Tenants by the Entirety Protection

Those residing in states that do not recognize tenants by the entirety protection may be surprised to find that by purchasing real property in states that do recognize tenants by the entirety protection, the asset may be protected in bankruptcy or in state law proceedings if the judgment is against only one spouse. Generally, states create and determine the property rights of assets.[240] Based upon a series of Bankruptcy Court decisions, it appears that persons domiciled in a state that does not recognize tenants by the entirety protection may be able to import the law of a state that

[236] 11 U.S.C. §§ 522(b)(3), 522(p).
[237] 11 U.S.C. § 522(p)(1).
[238] 11 U.S.C. § 522(b)(3)(A). 11 U.S.C. § 522(o) and § 548(e) provide a ten year look-back for property disposed of to acquire a homestead or residence if the debtor had intent to hinder, delay or defraud a creditor or to avoid a transfer by the debtor to a self-settled trust or "similar device" with the intent to hinder, delay or defraud any entity to which the debtor, on or before the date that such transfer was made, was or became indebted.
[239] *See* In re Garrett, 429 B.R. 220 (Bankr. S.D. Tex 2010); In re Holland, 2009 Bankr. LEXIS 2890 (Bankr. N.D. Ill. Sept. 3, 2009); In re Cauley, 374 B.R. 311 (Bankr. M.D. Fla. 2007); In re Reinhard, 377 B.R. 315 (Bankr. N.D. Fla. 2007); In re Rogers, 513 F.3d 212 (5th Cir. Tex. 2008); In re Schwarz, 362 B.R. 532 (Bankr. S.D. Fla. 2007); In re Zolnierowicz, 380 B.R. 84 (Bankr. M.D. Fla 2007), *infra*.
[240] Barnhill v. Johnson, 503 U.S. 393, 398 (1992); Butner v. U.S., 440 U.S. 48, 55 (1979).

recognizes tenants by the entirety by purchasing real property (or even possibly intangible property) in that state, regardless of whether the state is a full or modified bar state.

Section 522(b)(3)(B) of the Bankruptcy Code provides an exemption for "any interest in property in which the debtor had, immediately before the commencement of the case, an interest as a tenant by the entirety or joint tenant to the extent that such interest as a tenant by the entirety or joint tenant is exempt from process under applicable non-bankruptcy law."[241] In the case of *In re Cochrane*, "the situs of the asset that is held by a debtor in bankruptcy as a tenant by the entireties is the sole determinant of whether § 522(b)(2)(B) of the Bankruptcy Code[242] can protect it from the claims of the bankruptcy estate."[243] It may be possible that a federal choice of law standard could instead apply that looks to the jurisdiction with the most significant relationship to the action instead of relying solely on the situs of the real property.[244]

In *In re Cauley*, debtor, a Delaware domiciliary at the time of his bankruptcy petition (yet during the 730 day period immediately preceding his petition, had lived in Alabama, Florida and Louisiana), claimed Florida real property held as tenants by the entirety was exempt from bankruptcy claims under § 522(b)(3)(B) of the Bankruptcy Code.[245] Although the bankruptcy trustee argued that tenants by the entirety protection is only afforded to Florida residents, the court disagreed, stating, "...the Court has not found any authority to support the proposition that an individual claiming Florida real property exempt as tenancy by the entireties must be a resident of Florida. The Court finds no such requirement exists."[246] This ruling appears to have provided debtors in states that do not provide tenants by the entirety protection the power to utilize the laws of another state, more protective of tenants by the entirety

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[241] 11 U.S.C. § 522(b)(3)(B).

[242] § 522(b)(2)(B) of the Bankruptcy Code in 1995 was adopted as § 522(b)(3)(B) of the Bankruptcy Code of 2005.

[243] In re Cochrane, 178 B.R. at 1020.

> Since the real estate at issue is located within the state of Florida, and Florida law can protect property held in tenancy by the entireties from the claims of at least certain of the owner's creditors, the possibility that the Debtor was not "domiciled" in Florida as of the commencement of this case does not in itself defeat his right to assert that protection.

Id.

[244] *See* In re Segre's Iron Works, Inc., 258 B.R. 547 (Bankr. D. Conn. 2001) (holding that New York law applied to a Connecticut resident filling bankruptcy in Connecticut because the relevant acts giving rise to the claim occurred in New York, and New York had an overriding interest in protecting its residents through the enactment of the relevant law at issue); Frederick R. Franke, Jr., Presentation to the Asset Protection Committee at the ACTEC 2009 Fall Meeting, Choice of Law: Tenancy By The Entirety Across State Lines 2 (Fall 2009). *See also* Ziebarth, *supra* note 129.

[245] In re Cauley, 374 B.R. at 313.

[246] *Id.* at 316.

property by purchasing tenants by the entirety property in states such as Florida.[247]

In *In re Zolnierowicz*, an Illinois debtor moved into a Florida condominium purchased more than ten years before establishing domicile in Florida.[248] The debtor did not satisfy the 730-day pre-bankruptcy filing holding period promulgated by § 522(b)(3)(B) of the Bankruptcy Code so Illinois exemptions applied in bankruptcy court.[249] In holding that the debtor's property was exempt notwithstanding the debtor's domicile for bankruptcy purposes, the court quoted *In re Schwarz*:

> Florida real property owned by a Florida-domiciled Debtor is exempt from administration as property of the estate regardless of when the debtor became a Florida domiciliary if the debtor had, immediately before the commencement of the case, an interest in that property held in a tenancy by the entireties with a spouse.[250]

In *In re Garrett*, Dean and Caroline Garrett ("Debtors") were North Carolina residents from December 2006 to February 2008.[251] In March 2008, they moved to Texas and on July 2, 2009, the Debtors filed for bankruptcy claiming exemptions under North Carolina's exemption laws for their Texas residence.[252] The Debtors claimed exemptions pursuant to §§ 522(b)(3)(A) and (b)(3)(B) of the Bankruptcy Code, arguing that the full value of their Texas residence was exempt as property owned as tenants by the entireties under North Carolina law.[253] The court held that North Carolina's exemptions applied under § 522(b)(3)(A) of the Bankruptcy Code and the Debtors were entitled to an exemption of $70,000, reflecting the amount of the exemption under North Carolina law ($35,000 per debtor).[254] The Debtors were not entitled to an exemption equal to the full value of their Texas residence under § 522(b)(3)(B) of the Bankruptcy Code because

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[247] *See* In re Garrett, 429 B.R. 220 (applying North Carolina's exemptions for tenants by the entirety ownership to Texas debtors seeking a bankruptcy exemption for the debtors' Texas property); In re Holland, 2009 Bankr. LEXIS 2890 (applying a bankruptcy exemption to an Illinois debtor for property owned as tenants by the entirety under Florida law); Nelson, *Florida Surprise*, *supra* note 8.
[248] In re Zolnierowicz, 380 B.R. at 85.
[249] *Id.* at 86.
[250] *Id.* at 87.
[251] In re Garrett, 429 B.R. at 222.
[252] *Id.*
[253] *Id.*
[254] *Id.* at 241.

Texas law, and not North Carolina law applied.[255] In coming to its conclusion, the court stated:

> Section 522(b)(3)(B) provides that a debtor may exempt "any interest in property in which the debtor had, immediately before the commencement of the case, an interest as a tenant by the entirety or joint tenant to the extent that such interest as a tenant by the entirety or joint tenant is exempt from process under applicable nonbankruptcy law . . . ." 11 U.S.C. § 522(b)(3)(B).[256]

The court stated further that "[u]nlike the 730 and 180 day requirements found in § 522(b)(3)(A), there is no mechanical formula for determining the applicable nonbankruptcy law under § 522(b)(3)(B)."[257] In *Garrett*, the debtors owned property in Texas; a state that does not recognize tenants by the entirety. Based upon the duration of their residence in Texas before filing for bankruptcy (less than 730 days immediately preceding the filing of their bankruptcy petition), North Carolina law bankruptcy exemptions applied. However, the Court noted that with respect to § 522(b)(3)(B) of the Bankruptcy Code, there is no mechanical formula for determining the applicable non-bankruptcy law. Following *In re Cochrane*, the court in *Garrett* concluded that the law of the situs of the real estate controlled whether tenancy by the entirety protection applied.[258] Since Texas does not recognize tenants by the entirety, the real property in Texas was not protected.

2. Can Tenancy by the Entirety Protection be Extended to Real Property Situated in States that do not Recognize it?

Those domiciled in a state that recognizes tenants by the entirety protection for intangible assets may be able to obtain asset protection for their real estate situated in states that do not recognize such protection. For example, a Florida domiciliary wants to purchase a home in Colorado that does not recognize tenancy by the entirety. Based upon *In re Cochrane* and as restated in *In re Garrett*, the applicable bankruptcy law of the situs of the asset claimed as tenancy by the entirety is applied in a bankruptcy proceeding.[259] As a result, a Florida resident purchasing Colorado real estate as tenants by the entirety will not have protection in a

[255] In re Garrett, 429 B.R. at 241.
[256] *Id.* at 239.
[257] *Id.* at 240.
[258] *Id.*
[259] *Id.* at 240.

bankruptcy proceeding as Colorado does not recognize such protection. However, if instead the Florida resident formed an LLC in Florida or Delaware (both states recognize tenants by the entirety), would the situs of the property be the residence of the debtor as the asset (an LLC that owns the Colorado real estate) is now an interest in the LLC, an intangible?[260]

3. Tenants by the Entirety Ownership May (But Without Certainty) Protect More Than Real Property

Section 522(b)(3)(B) of the Bankruptcy Code may not apply to protect just real property. The court in *In re Schwarz* found that "This exemption provision applies by its clear and unambiguous terms not merely to homestead property or to property that is the debtor's domicile, but to **all** property owned by a debtor in a tenancy by the entireties, if such property is exempt from process under state law."[261]

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[260] *See* Acme Contr., Ltd. v. Toltest, Inc., 2008 U.S. Dist. LEXIS 77747, *16 (E.D. Mich. Oct. 3, 2008)

> Numerous courts have observed that the situs of intangible property is, in truth, a legal fiction... Various courts have also found that intangible property may have more than one situs. In addition, the same intangible property may be deemed to have one situs for a particular purpose, yet another situs for a different purpose.

Id.; In re Iroquois Energy Mgmt., LLC, 284 B.R. 28, 31 (Bankr. W.D.N.Y. 2002) ("defining rights to intangible property, New York looks to the law of the situs of those assets. The determination of that situs, however, will depend upon considerations of justice and convenience"); In re Shelton, 2001 Bankr. LEXIS 2213, *17-18 (Bankr. D. Idaho Oct. 12, 2001)

> [S]everal possible locations can be ascribed to intangible assets. Among these are the debtor's domicile or tax residence, and the place(s) where the account or contract obligor can be pursued. It appears to the Court that the question is, at bottom, a factual one. The nature of the asset in question, and its specific traits as property, are critical to divining its location for venue purposes.

Id.; Severnoe Sec. Corp. v. London & Lancashire Ins. Co., 174 N.E. 299, 300 (N.Y. 1931). Quoting Justice Cardozo:

> The situs of intangibles is in truth a legal fiction, but there are times when justice or convenience requires that a legal situs be ascribed to them. The locality selected is for some purposes, the domicile of the creditor; for others, the domicile or place of business of the debtor, the place, that is to say, where the obligation was created or was meant to be discharged; for others, the place where the debtor can be found. At the root of the selection is generally a common sense appraisal of the requirements of justice and convenience in particular conditions.

Id.

[261] In re Schwarz, 362 B.R. at 534 (holding that the 730-day residency requirement of the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 did not apply to property held as tenants by the entirety for Florida domiciliaries). The court additionally stated in footnote 2 of its opinion:

> Congress determined to leave wholly intact the preexisting blanket exemption available to debtors who own property in a tenancy by the entireties form if applicable nonbankruptcy law would exempt that property from process. The range of property so exempt under Florida law is extremely broad and encompasses far more than homestead property alone.

Id.

a. Notes and Banking

The rules governing financial accounts and instruments are somewhat conflicting.[262] *Farmers Exchange Bank v. Metro Contracting Services, Inc.*,[263] involved the president of a corporation's execution of two promissory notes as collateral for two loans for a Missouri corporation which he and his wife owned.[264] The president also executed a personal guaranty in the name of himself and his wife (collectively the "debtors"); it was undisputed that the wife's name was forged by her husband.[265] Later, the president was notified that he defaulted on the promissory notes.[266] The issue was whether the debtors owned the promissory notes as tenants in common under Kansas law or tenants by the entirety under Missouri law, so as to determine whether the notes were subject to attachment and execution to satisfy the judgment creditor's judgment. While Kansas does not recognize a tenancy by the entireties, Missouri does. Although the debtors were Kansas domiciliaries at the time the promissory notes were executed, their corporation was formed under Missouri law which additionally, was also the place with the most contacts associated with the debt.[267] In finding for the judgment creditor, the court applied Kansas law and found that the debtors' interests in the note were as tenants in common.[268] In coming to this conclusion, the court applied the conflict of laws doctrine "...which calls for implementation of the relevant policies of the state with the dominant interest in the determination of the particular issue. Except in rare circumstances, this state will be the state where the spouses were domiciled at the time the movable was acquired."[269]

In *In re Robedee*,[270] a debtor from New York held a bank account in Florida as tenants by the entirety. After establishing domicile in Florida, the debtor filed for bankruptcy and claimed the Florida account exempt under

[262] *See* Franke, Jr., *supra* note 244, at 10.
[263] 107 S.W.3d 381 (Mo. 2003).
[264] *Id.*
[265] *Id.* at 386.
[266] *Id.*
[267] *Id.* at 394.
[268] *Id.*
[269] Farmers Exchange Bank, 107 S.W.3d at 392-93. *See also* In re Goldstein, 66 B.R. 909 (Bankr. W.D. Pa. 1986)(applying the forum state's conflict of laws rule in finding that New Jersey had the greatest connection to a note held by spouses).
[270] 367 B.R. 901 (Bankr, S.D. 2007).

§ 522(b)(3)(B) of the Bankruptcy Code.[271] The court, following its opinion in *Schwarz*, agreed with the debtor, stating that there is no difference whether the property at issue is real property or personal property under § 522(b)(3)(B) of the Bankruptcy Code, and once the property was held as tenants by the entirety by a Florida domiciliary it was exempt under Florida law (and therefore exempt under § 522(b)(3)(B) of the Bankruptcy Code).[272]

b. Tangible Personal Property

Generally, the debtor's domicile at the time the tangible personal property was acquired controls whether it is protected through tenants by the entirety ownership. In *In Re Kirshner*,[273] a New Jersey debtor moved to Florida before filing his bankruptcy petition in New Jersey.[274] The New Jersey bankruptcy case was subsequently transferred to Florida. The debtor claimed an exemption for certain tangible personal property owned with his wife as tenants by the entirety, specifically for household goods and furnishings.[275] The trustee argued that because New Jersey does not recognize tenancy by the entireties ownership and the tangible personal property was acquired while the debtor resided in New Jersey, the debtor and his wife could not have had the intent required to create a tenancy by the entireties.[276] Although the court pointed out that New Jersey recognized a tenancy by the entirety to the extent that a written instrument was used to create it, the debtor and his wife had not done so, and thus, the household goods and furnishings were not held as husband and wife, tenants by the entirety.[277] Similarly, in *Blackwell v. Lurie*,[278] a sketch acquired by a debtor with his wife as tenants by the entirety in Missouri was protected by the New Mexico Court of Appeals' application of the laws of Missouri, instead of the laws of New Mexico, because Missouri recognized tenants by the entirety ownership.[279]

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[271] In re Robedee, 367 B.R. at 905.
[272] *Id.* at 907.
[273] 2007 Bankr. LEXIS 3779 (Bankr. S.D. Fla. Oct. 30, 2007).
[274] *Id.* at *2.
[275] *Id.* at *16.
[276] *Id.* at *20.
[277] *Id.* at 21-22.
[278] 71 P.3d 509 (N.M. 2003).
[279] *Id.* at 511-12. The trustee argued that New Mexico or Montana law (of which neither state recognizes tenants by the entirety) controlled because the sketch was on consignment to an art gallery in New Mexico and the debtors were domiciled in Montana. However, the sketch was acquired by the debtors as husband

E. Using Life Insurance to Protect Tenants by Entirety Ownership

Because death (or divorce) terminates tenants by the entirety ownership, property previously so titled can be reached upon death of one spouse if the debtor spouse survives the non-debtor spouse since the debtor spouse inherits all tenants by the entirety property by operation of law, and therefore has full title to the property which can be reached by the debtor spouse's creditors. To protect clients from the risk of the untimely death of a non-debtor spouse where the husband and wife are relying on tenants by the entirety protection for significant assets, practitioners should consider wealth replacement through life insurance on the non-debtor spouse using an Irrevocable Life Insurance Trust that provides for discretionary distributions to the debtor spouse, possibly along with other family members, and a spendthrift clause. While the tenants by the entirety assets received by the surviving debtor spouse can be reached by the creditors of the surviving spouse, the life insurance proceeds paid to the trustee of said Irrevocable Life Insurance Trust for the benefit of the debtor spouse can "replace" the potential loss of the tenants by the entirety assets that became unprotected upon the death of the first spouse to die.

F. Conclusion

Tenants by the entirety ownership provides great asset protection for husbands and wives domiciled in states that recognize such benefits. Based upon the discussion above, it appears that residents of states that do not have tenants by the entirety may still purchase real estate in states where tenants by the entirety protection is provided and benefit from tenants by the entirety protection. Persons living in states that recognize tenants by the entirety protection for tangible and intangible assets may be able to create an LLC, LP or corporation to take title to real property outside of the domicile state and thereby retain tenants by the entirety protection by converting real property into an intangible asset. Properly structured life insurance serves as a hedge for those relying on tenants by the entirety protection.

VI. The Consequences of Overly Aggressive Planning

A. Introduction

Those engaged in structuring an asset protection or estate plan need to advise clients that should a problem arise, their planning will come under

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and wife while they lived in Missouri, and under the time-and-manner-of-acquisition rule, the New Mexico court applied Missouri law. *Id.* at 3. *See also* Goldman v. Dzikowski, 2006 U.S. Dist. LEXIS 97009 (S.D. Fla. Mar. 6, 2006) (applying Arizona law to find that certain property, including artwork and pictures worth $5,770.00, was not exempt from the debtor's bankruptcy estate because Arizona, a community property jurisdiction, does not recognize a tenancy by the entirety and the debtor and his wife acquired the artwork and pictures while residing in Arizona).

intense scrutiny. Not only will the timing of any transfers be examined, but also courts will consider whether: (i) assets claimed to be titled in a protected format are in fact so titled; and (ii) assets claimed to be protected through trusts, partnerships or LLC's, have been properly transferred to the trust, partnership or LLC and administered in an arm's length format rather than as the alter ego of the debtor. Debtors subject to a judgment should anticipate a series of information requests from creditor lawyers whose clients have typically won a hard fought contested legal battle. A team of forensic accountants are likely to be authorized by the court to pay a visit to the debtor subject to the judgment, to examine all of the debtor's relevant bank, accounting and financial records. Most likely, a timeline of all transfers by the debtor will be created by both the debtor and the creditor to bolster their respective positions as to the effectiveness of any asset protection planning and the debtor's financial condition at the time the transfers were made. An effective creditor's attorney will leave no stone unturned.

Clients who combine asset protection planning with estate planning want a reasonable assurance that the techniques used are time tested and are likely to be effective. It is only reasonable for expectations to be significantly higher when the client is planning defensively without any pending or reasonably anticipated claims. With the vast number of potential asset protection alternatives available, planning for those who have no existing or pending claims should have strong statutory or case law protection. Many asset protection techniques provide significant benefits in addition to asset protection and should be considered as part of a diversified approach to estate planning and asset protection. Some alternatives and their business benefits are described below:

ASSET PROTECTION TECHNIQUE	***BENEFITS OUTSIDE OF ASSET PROTECTION***
Annuities	Secures a retirement benefit tax deferred.
Qualified Retirement Plans	Secures a retirement plan benefit tax deferred.
Cash Surrender Value of Life Insurance	Provides a death benefit to family if premature death. Tax deferred accumulations. Cash value can be borrowed.
Homestead	Provides a safe place for family to live and over time, generally an appreciating asset.
Family Limited Partnerships/LLCs	Provides a format for including younger generations in family business and investing. Provides potential transfer tax benefits as a result of discounts.
Inter Vivos QTIP Trusts	Provides a way to transfer assets to a spouse to take advantage of the applicable exclusion amount and the return of gifted assets (via a tax and asset protected trust) should donee spouse predecease donor spouse, and provides distributions of QTIP assets upon death

	of donee spouse to descendants of trust creator.
Tenants by the Entirety	Probate avoidance upon death of first spouse.
Self-Settled Domestic and Foreign Asset Protection Trusts	Provides investment diversification, private placement life insurance opportunities and participation in investments not otherwise available to U.S. investors.[280]

Many of these techniques are referred to in articles and Heckerling presentations of the past.[281]

From time to time, we may be confronted with clients who are already being sued or may in fact have a judgment against them. Is it too late to consider the asset protection techniques discussed earlier in this article? Is there anything ethically we can do to protect them? Is it proper for us to say sorry, but there is nothing I can do...it is too late to help you now? Do we have exposure for helping? Do we have exposure for not helping?

B. Jamie Solow

The January 2010 case of Jamie L. Solow ("Solow") should serve as a lesson to the estate planning community, and at the very least, encourage lawyers to rethink some of their planning techniques. Defendant Solow engaged in a fraudulent trading scheme involving inverse floating rate collateralized mortgage obligation, and subsequently, the Securities and Exchange Commission ("SEC") obtained a jury verdict convicting Solow of violating § 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5; § 17(a) of the Securities Act of 1933.[282] The jury verdict was rendered

[280] *See* Duncan E. Osborne, *Introduction to Offshore Trusts*, *in* ASSET PROTECTION: DOMESTIC AND INTERNATIONAL LAW AND TACTICS §19:3 (2011 ed.).

[281] For annuities, see Louis A. Mezzullo, Lifetime Transfers: Installment Sales to Grantor Trusts, GRATs, and Other Techniques, Address at the 45th Annual Heckerling Institute on Estate Planning (Jan. 2011), *in* 45th Annual Heckerling Institute on Estate Planning (Matthew Bender, Pub., 2011). For qualified retirement plans and LLCs, see Steven J. Oshins, Asset Protection Other Than Self-Settled Trusts: Beneficiary Controlled Trusts, FLPs, LLCs, Retirement Plans and Other Creditor Protection Strategies, Address at the 39th Annual Heckerling Institute on Estate Planning (Jan. 2005), *in* 39th Annual Heckerling Institute on Estate Planning (Matthew Bender, Pub., 2005). For life insurance planning, see Donald O. Jansen, Life Insurance and Charities-The Basics, Advanced and Over the Edge, Address at the 45th Annual Heckerling Institute on Estate Planning (Jan. 2011), *in* 45th Annual Heckerling Institute on Estate Planning (Matthew Bender, Pub., 2011). For family limited partnerships, see Richard B. Robinson, Escape From the World of FLPs, Address at the 44th Annual Heckerling Institute on Estate Planning (Jan. 2010), *in* 44th Annual Heckerling Institute on Estate Planning (Matthew Bender, Pub., 2010). For QTIP trusts, see M. Read Moore, Neil T. Kawashima, & Joy M. Miyasaki, Estate Planning for QTIP Trust Assets, Address at the 44th Annual Heckerling Institute on Estate Planning (Jan. 2010), *in* 44th Annual Heckerling Institute on Estate Planning (Matthew Bender, Pub., 2010). For tenants by the entirety and homestead, see Nelson, *supra* note 78. For self-settled domestic and foreign asset protection trusts, see Richard W. Nenno, Choosing and Rechoosing the Jurisdiction for a Trust, Address at the 40th Annual Heckerling Institute on Estate Planning (Jan. 2006), *in* 40th Annual Heckerling Institute on Estate Planning (Matthew Bender, Pub., 2006).

[282] Solow, 682 F. Supp.2d at 1314.

on January 31, 2008, and four days later, Solow's wife, Gina P. Solow, retained a law firm specializing in asset protection to execute a $1,187,500 mortgage on the couple's Fort Lauderdale residence and a $5,261,289 mortgage on their Hillsboro Beach residence.[283] Gina Solow's attorneys argued that they could legally do the asset protection planning because the Solows' Hillsboro Breach residence had been owned as tenants by the entireties since 2002, long before the judgment against Jamie had been rendered, and the Fort Lauderdale residence was purchased by a corporation owned 100% by Gina Solow, Jaime Solow never had any legal ownership in the property.[284]

Florida case law supports the position that the transfer of exempt property into other protected forms cannot be set aside even if the debtor has actual intent to defraud. In Sneed v. Davis,[285] the court stated:

> [A] debtor in disposing of property can commit a fraud on creditors only by disposing of such property as the creditor has a legal right to look for satisfaction of his claim, and hence a sale, gift, or other disposition of property which is by law absolutely exempt from the payment of the owner's debt cannot be impeached by creditors as in fraud of their rights. Creditors have no right to complain of dealings with property which the law does not allow them to apply on their claims, even though such dealings are with a purpose to hinder, delay, or defraud them.[286]

The final judgment, issued on May 14, 2008, found Solow liable for $2,646,485.99, together with prejudgment interest of $778,302.91, for a total of $3,424,788.90, in disgorgement.[287] The SEC filed an Order to Show Cause why Defendant Jamie L. Solow should not be held in contempt of court on June 4, 2009, alleging that Solow purposefully dissipated his assets in order to avoid paying the court's final judgment.[288] The court, in an opinion issued on January 14, 2010, by Judge Donald M. Middlebrooks, found Solow to be in Contempt of Court and ordered him to surrender to U.S. Marshals and be taken into custody by January 25, 2010.[289] Middlebrooks stated disgorgement "operate[s] to wrest ill-gotten gains from the hands of a wrongdoer,"[290] and the "Court has broad equitable powers to reach assets protected by state law to satisfy a

[283] Solow, 682 F. Supp.2d at 1316.
[284] *Id.* at 1317-20.
[285] 135 Fla. 271 (Fla. 1938).
[286] *Id.* at 276-77.
[287] Solow, 682 F. Supp.2d at 1314.
[288] *Id.* at 1313.
[289] *Id.* at 1334.
[290] *Id.* at 1324 (quoting Steffen v. Gray, Harris & Robinson, P.A., 283 F. Supp.2d at 1282).

disgorgement."[291] Thus, the disgorgement order eliminated any tenants by the entireties protection usually afforded a married couple taking title to property in Florida.[292] As a result, the planning with Solow's tenants by the entirety assets that would have been permitted under Florida law through *Sneed*, was rendered ineffective by the SEC's disgorgement order. The court was empowered to issue the contempt order. Solow surrendered himself into custody on February 1, 2010, and remained incarcerated until June 4, 2010.[293]

Solow's circumstances should serve as a lesson for attorneys who integrate asset protection planning with estate planning because they illustrate that planning following an adverse judgment will be subjected to intense and creative legal attacks (such as disgorgement). Whether attorneys who participate in asset protection planning can be subject to liability or bar sanctions for assisting debtors with planning that may be considered improper is a matter of some dispute and state laws in the area of asset protection planning vary. Despite thorough analysis of the law and case precedent, there is surprisingly sparse authority, one way or the other, to determine the exposure of an asset protection attorney practicing post-judgment planning. Although no case unequivocally results in attorney liability, many of them have expressed the possibility of that exposure.

In *Freeman v. First Union National Bank*,[294] the Florida Supreme Court decided whether the Florida Uniform Fraudulent Transfer Act ("FUFTA") created a cause of action for damages in favor of a creditor against an aider or abettor to a fraudulent transaction. The case stemmed from a suit brought against First Union by victims of a ponzi scheme.[295] The victims alleged that despite First Union's knowledge of litigation instituted against one of its clients, it continued to permit its client to transfer millions of dollars offshore.[296] After reviewing FUFTA, the Court concluded that it "was not intended to serve as a vehicle by which a creditor may bring a suit against a non-transferee party (like First Union in this case) for monetary damages arising from the non-transferee party's alleged aiding-abetting of a fraudulent money transfer."[297]

In *Freeman*, the court in dicta stated "[w]e caution that our answer to the certified question in this case is confined to the context of FUFTA. We do not address whether relief is available under any other theory of liability or

[291] Solow, 682 F. Supp.2d at 1325.
[292] *Id.* at 1325-26.
[293] SEC v. Solow, Order Modifying Order of Civil Contempt and Directing Release from Incarceration, 06-81041-CIV-Middlebrooks/Johnson at 1 (S.D. Fla. June 4, 2010).
[294] 865 So.2d 1272 (Fla. 2004).
[295] *Id.* at 1273-74.
[296] *Id.* at 1274.
[297] *Id.* at 1277.

cause of action."[298] In *Chepstow Limited v. Hunt*,[299] the court was confronted with the question as to whether a non-transferee could be subject to actual or punitive damages for knowingly aiding and abetting a debtor to carry out a fraudulent transfer under Georgia law. The court held that there was no provision within the Georgia Code that permitted a cause of action against "a third party who aids and abets a debtor in carrying out a fraudulent transfer is liable for it even though it is neither a debtor nor a transferee."[300] It then cited Freeman for the proposition that "FUFTA was not intended to serve as a vehicle by which a creditor may bring a suit against a non-transferee party … for monetary damages arising from the non-transferee party's alleged aiding-abetting of a fraudulent money transfer."[301] However, the court went a step further than Freeman and actually stated that there was a cause of action under Georgia law against a non-transferee third party "where the allegations are, as here, that they conspired with the debtor to defraud the creditor by hindering its collections of an outstanding debt..."[302] Instead of basing liability on the status of a transferee, liability was based upon status as a co-conspirator who assisted the debtor in defrauding a creditor.

Similarly, in the 2003 case of *Morganroth & Morganroth v. Norris, McLaughlin & Marcus, P.C.*,[303] the United States Court of Appeals for the Third Circuit remanded to the district court in New Jersey whether the defendants, who were attorneys, knowingly and intentionally participated in a client's unlawful conduct to hinder, delay and/or fraudulently obstruct the enforcement of a judgment.[304] The appeals court said such a finding would satisfy a claim for creditor fraud against the lawyer under New Jersey law.[305] Based upon Chepstow, Morganroth and the cautionary language in Freeman, planners should be aware that creditors are likely to bring actions based upon theories of law outside of FUFTA such as creditor fraud or as a co-conspirator in a fraudulent transfer.[306]

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[298] Freeman, 865 So.2d at 1275.
[299] 381 F.3d 1077 (11th Cir. 2004).
[300] *Id.* at 1089.
[301] *Id.* at 1089, FN 7 (quoting Freeman, 865 So.2d at 1277).
[302] *Id.* at 1090.
[303] 331 F.3d 406 (3rd Cir. 2003).
[304] Morganroth, 331 F.3d at 408.
[305] *Id.* at 414.
[306] *See* In re Harwell, 2011 Bankr. LEXIS 3687 (Bankr. M.D. Fla. Sept. 30, 2011) (holding that an attorney did not act in good faith and was not an innocent participant to his client's fraudulent actions). Debtor had a judgment rendered against him and in post-judgment interrogatories, did not disclose that he was to receive a settlement in the near future. The attorney received the settlement funds from the debtor's settlement and at the debtor's directions, he transferred the funds from his trust account to the debtor's family members, other third parties, and the debtor himself. Although the attorney argued that the funds belonged to his client and that he only disbursed the funds as directed by his client (thereby acting in the attorney's fiduciary capacity), the court stated that the attorney could:

> [M]ake no credible argument that he was an unwitting or innocent participant in the transfers made by Mr. Harwell. He knew that transfers were intended to get the money

C. Peter G. Rogan – 2011 Case Where Attorney Indicted

Peter G. Rogan ("Rogan") and his attorney, Frederick M. Cuppy ("Cuppy") were indicted by a federal grand jury in March 2010, for Conspiracy to Obstruct Justice, Perjury and Obstruction of Justice.[307] Rogan was involved in an alleged Medicare and Medicaid fraud scheme throughout his affiliation as the chief executive officer with Edgewater Medical Center, a hospital in Chicago, Illinois ("hopsital").[308] Rogan secured Dexia Crédit Local ("Dexia") to guarantee a hospital bond debt in June 1998.[309] Once Rogan's fraud was uncovered, the federal government instituted litigation against him under the federal False Claims Act in May 2002.[310] Additionally, the government stopped making Medicare and Medicaid payments to the hospital, and Dexia was required to pay $55 million on the hospital's behalf to satisfy obligations to bondholders.[311] Later in November 2002 with the hospital in bankruptcy and Dexia unable to obtain reimbursement from it, Dexia sued Rogan and his management partners for fraud, conspiracy and other torts.[312] On September 29, 2006, the court entered a judgment against Rogan in favor of the United States for $64,259,032.[313] Likewise on May 3, 2007, Dexia obtained a default judgment against Rogan and his partner companies for $124,280,712.[314]

Throughout the 1990s, Rogan took steps to conceal and protect millions of dollars in assets that he acquired over a span of thirty years in the healthcare and hospital fields.[315] In 1992, Rogan and his wife set up three trusts in Florida for their children.[316] The trusts received money from Rogan's initial sale of the hospital in 1994 and received millions of dollars throughout Rogan's continued operation of the hospital from 1994 to 1997.[317] In June of 1997, Rogan formed three more trusts for his children

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> away from Mr. Hill's collection efforts. He knew a judgment had been entered. He knew that the transferees were either Mr. Harwell himself or family members or other third parties. The transactions were unusual in his practice, as he and his office manager testified. In fact, in a sense, he went beyond the call of duty when, on his own notion, he obtained cashier's checks, something he'd never done before for any client, to ensure that there would be absolutely no money left to be applied toward Mr. Hill's judgment.

Id.

[307] U.S. v. Peter G. Rogan & Frederick M. Cuppy, Grand Jury Charge, 11-mj-6511-RSR (N.D. Ill. Sept. 28, 2011)[hereinafter Rogan & Cuppy Grand Jurry Charge].

[308] Dexia Crédit Local v. Rogan, 629 F.3d 612, 617 (7th Cir. Ill. 2010).

[309] *Id.*

[310] *Id.*

[311] *Id.*

[312] *Id.*

[313] Rogan & Cuppy Grand Jurry Charge, *supra* note 307, at 6.

[314] *Id.* at 7.

[315] Rogan, 629 F.3d at 618.

[316] *Id.*

[317] *Id.*

under Belizean law. Those trusts were funded with interests in several of his companies.[318]

Rogan's tie-in to asset protection and estate planning stems from the Bahamian trust Rogan created in 1996, the "Peter G. Rogan Irrevocable Trust 001."[319] Rogan was advised by Cuppy and an unidentified Florida attorney in creating, establishing the terms and choosing the location of the trust.[320] By 2002, the trust owned approximately $28 million in assets.[321] Following the judgments by the U.S. and Dexia, both took steps to collect their judgments. **Rogan and Cuppy allegedly committed multiple counts of perjury and obstruction of justice following the U.S.'s and Dexia's efforts to seek information in conjunction with their efforts to discover assets pertaining to Rogan's Bahamian Trust**.[322] The federal grand jury indictment was unsealed with a date of September 28, 2011.[323] The indictment states that Cuppy lied under oath about directly communicating with trust employees regarding information requests and causing the trustee to distribute approximately $6.5 million from the Trust to accounts in Rogan's wife's name during the pendency of litigation in both the government's and Dexia's cases-in-chief.[324] Cuppy testified that he never communicated with the trust company and that he never had control over the funds of the trust.[325] The attorney's alleged participation in the client's conduct sends out red flags to others. Not only was this attorney allegedly participating in the fraud during the litigation in question, but he allegedly lied about it under oath in affidavits and in court.

> Rogan and Cuppy made and caused to be made incomplete, inaccurate, and misleading statements to the Court, the United States, and Dexia about the nature, operation, and control of the Rogan Trust, its assets, and distributions... Cuppy filed and caused to be filed with the Court a declaration containing incomplete, inaccurate, and misleading assertions; Rogan and Cuppy provided incomplete inaccurate, and misleading testimony in depositions; Cuppy provided incomplete, inaccurate, and misleading testimony in a hearing before the Court; and

[318] Rogan, 629 F.3d at 618.
[319] Rogan & Cuppy Grand Jurry Charge, *supra* note 307, at 2.
[320] *Id.*
[321] *Id.* at 1.
[322] *Id.* at 17-29 (emphasis added).
[323] *See* Martha Neil, *Lawyer and Ex-Client Charged in Perjury and Obstruction Case re Failed Hospital and Offshore Trust*, ABA J., Oct. 4, 2011, http://www.abajournal.com/news/article/ex-owner_of_chicago_hospital_a_lawyer_in_fla._is_charged_with_perjury/ (last visited Nov. 3, 2011).
[324] Rogan & Cuppy Grand Jurry Charge, *supra* note 307, at 5-16.
[325] *Id.* at 15.

> Rogan and Cuppy caused the Trustee to withhold and otherwise not produce Trust-related documents.[326]

As evidenced by the quoted provision of the indictment, Mr. Cuppy found himself in a very uncomfortable position as the planning he designed came under intense scrutiny.

Many estate planning attorneys tout the benefits of offshore trusts and other asset protection techniques. Although such planning generally serves legitimate legal purposes, asset protection and estate planning become especially suspect in the eyes of the court when planning is initiated after a problem occurs. The trend from cases like *Solow* and *Rogan* is to punish the defendant harshly and attorneys are not immune as was the case when Mr. Cuppy was indicted. Lawyers need to be aware of potential exposure.

D. *In Re Mortensen* – 2011 Case Where Transfer to Debtor's Self-Settled Alaska Asset Protection Trust Ruled Fraudulent

The unpublished decision of *In re Mortensen*[327] held that the debtor, who created an Alaska self-settled asset protection trust in 2005, made a fraudulent conveyance to the trust that could be set aside under § 548(e) of the Bankruptcy Code's ten year limitations period.[328] Husband (the "Debtor") and Wife purchased 1.25 acres of remote, unimproved real property located near Seldovia, Alaska (the "Seldovia" property).[329] Debtor and Wife divorced, with Debtor receiving the Seldovia property.[330] Following the divorce decree, Debtor's income fluctuated substantially.[331] Debtor transferred the Seldovia property to a self-settled Alaska asset protection trust.[332] The express purpose of creating the trust was "to maximize the protection of the trust estate or estates from creditors' claims of the Grantor or any beneficiary and to minimize all wealth transfer taxes."[333] Debtor and his descendants were the trust beneficiaries.[334] Four years after the trust was registered, Debtor filed his petition for bankruptcy with over $250,000 in credit card debt and over $8,000 in medical debt.[335] Debtor disclosed the creation of the Alaska trust on his statement of financial affairs.[336]

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[326] Rogan & Cuppy Grand Jurry Charge, *supra* note 307, at 12.
[327] In re Mortensen, A09-00565-DMD (Bankr. D. Alaska May 26, 2011).
[328] *Id.* at 19-20.
[329] *Id.* at 2.
[330] *Id.* at 2-3.
[331] *Id.* at 4.
[332] *Id.* at 5.
[333] In re Mortensen, A09-00565-DMD at 5.
[334] *Id.*
[335] *Id.* at 9.
[336] *Id.* at 10.

Debtor submitted an affidavit at the time of the trust's creation alleging that he was solvent and not trying to defraud creditors by creating the trust.[337] The bankruptcy trustee alleged that Debtor failed to establish a valid asset protection trust under Alaska law, claiming Debtor was insolvent when the trust was created.[338] The Court disagreed with the Trustee and held that under Alaska law, Debtor was solvent at the time the trust was created.[339]

Additionally, the trustee argued that the transfer of the Seldovia property to the asset protection trust should be set aside as fraudulent under § 548(e) of the Bankruptcy Code.[340] The Court, in agreeing with the Trustee, characterized Debtor's trust as a self-settled trust within the purview of § 548(e) of the Bankruptcy Code.[341] The Court reasoned that § 548(e) of the Bankruptcy Code was enacted to close the self-settled trusts loophole by avoiding any transfer of an interest of the debtor in property that was made on or within ten years before the date of the filing of a bankruptcy petition where the transfer was made to a self-settled trust, by a debtor, where the debtor was a beneficiary, and the debtor made such transfer with intent to hinder, delay, or defraud.[342] The Debtor transferred the Seldovia property to his own self-settled trust, and was a beneficiary of the trust. The Court went on to allege that Debtor transferred the property with actual intent to hinder, delay, or defraud his creditors because the trust's express purpose was to hinder, delay and defraud present and future creditors,[343] he was in debt when he placed the property in trust[344] and he used the trust for activities having no relationship to the trust's alleged purpose of "preserving the Seldovia property for his children" such as pledging it as collateral for making stock market investments and making a car loan to an acquaintance.[345] The opinion, in ruling a fraudulent transfer was made, states that the debtor "....was experiencing 'financial carnage' from his divorce. Comparing his low income to his estimated overhead...Mortensen was well 'under water' when he sought to put the Seldovia property out of reach of his creditors by placing it in the trust."[346]

VII. Conclusion

Economic times have created hardships for many previously successful real estate developers, business owners and investors. Other professionals have found themselves with malpractice claims or in other civil litigation. Estate planning

[337] In re Mortensen, A09-00565-DMD at 6.
[338] *Id.* at 10.
[339] *Id.* at 13.
[340] *Id.*
[341] *Id.* at 15.
[342] 11 U.S.C. § 548(e)(A)-(D).
[343] In re Mortensen, A09-00565-DMD at 17.
[344] *Id.*
[345] *Id* at 19.
[346] *Id.* at 17.

attorneys are asked whether they can initiate planning to assist those who are immersed with contingent or actual judgments. This Article described the benefits of initiating asset protection planning as part of the estate planning and business planning process when the client is solvent and/or to enhance protection of property that is already protected from creditor's claims. As described above, selection of a jurisdiction to form partnerships, LLCs, trusts and to acquire real estate investments could have significant consequences if a person is ultimately subject to a judgment. Planning well in advance will avoid the adverse consequences illustrated in the *Solow* and *Mortensen* cases. Any attorney involved with asset protection should understand that he or she and his or her clients are likely to be subject to intense scrutiny should a judgment be rendered against the client. *Rogan* should serve as a warning to any attorney who is considering overly aggressive planning.

EXHIBITS

EXHIBIT A
Debbie and Dennis– Tenancy by the Entireties Plan

	Debbie	Dennis	T by E
Upon Debbie's Death, Estate Lapses House – Protected Homestead			$3.5 M
Brokerage			$10 M
TOTAL			$13.5 M
Debbie's Gross Estate Assuming She Dies First			$6.75 M
MARITAL DEDUCTION			$6.75 M
Debbie's Taxable Estate			$0
Debbie's Tax			$0

	Debbie	Dennis	T by E
UPON DENNIS' DEATH			
Dennis' Gross Estate			$13.5 M
Less Applicable Exclusion Amount (assuming portability)			($10 M)
Dennis' Taxable Estate			$3.5 M
Dennis' Tax			$1.225 M
Assets subject to creditors while both married and living			$0
Assets subject to creditors upon death of 1st spouse or divorce			$10 M

EXHIBIT B
Debbie and Dennis– CPA's Tax Savings Plan

	Debbie's Revocable Trust	Dennis' Revocable Trust	T by E
Upon Debbie's Death House – Protected Homestead			$3.5 M
Brokerage	$5 M	$5 M	
TOTAL	$5 M	$5 M	$3.5 M
Debbie's Gross Estate Assuming She Dies First	$6.75 M		
Debbie's Share of Homestead to Dennis Outright	($1.75 M)		
MARITAL DEDUCTION	$1.75 M		
Debbie's Taxable Estate	$5 M		
Less Applicable Exclusion Amount	($5 M)		
Debbie's Tax	$0		

	Debbie's Revocable Trust	Dennis' Revocable Trust	T by E
UPON DENNIS DEATH			
Dennis' Gross Estate	$8.5 M		
Less Applicable Exclusion Amount (assuming portability)	($5 M)		
Dennis' Taxable Estate	$3.5 M		
Dennis' Tax	$1.225 M		
Savings Compared to Tenancy by the Entireties	$0		
Assets subject to creditors while both married and living			$10 M
Assets subject to creditors upon death of 1st spouse or divorce Assuming assets pass into spendthrift trust for surviving spouse upon death of 1st spouse			$5 M

Homestead	**$3.5 M**
Brokerage Assets	**$ 5 M**

EXHIBIT C
Debbie and Dennis– Inter Vivos QTIP

	Debbie's QTIP	Dennis' QTIP	T by E
Upon Debbie's Death House – Protected Homestead			$3.5 M
Brokerage	$5 M	$5 M	
TOTAL	$5 M	$5 M	$3.5 M
Debbie's Gross Estate Assuming She Dies First	$6.75 M		
Debbie's Share of Homestead to Dennis' Marital Deduction	($1.75 M)		
MARITAL DEDUCTION	$1.75 M		
Debbie's Taxable Estate	$5 M		
Less Applicable Exclusion Amount	($5 M)		
Debbie's Tax	$0		

	Debbie's QTIP	Dennis' QTIP	T by E
UPON DENNIS' DEATH			
Homestead	$3.5 M		
QTIP Trust from Debbie	$5 M		
Dennis' Gross Estate	$8.5 M		
Less Applicable Exclusion Amount (assuming portability)	($5 M)		
Dennis' Taxable Estate	$3.5 M		
Dennis' Tax	$1.225 M		
Assets subject to creditors while both married and living			$0
Assets subject to creditors upon death of first spouse or divorce			$0

EXHIBIT D
Comparison of Benefits of Inter Vivos QTIP

	Tenancy by the Entirety Plan	Tax Plan	Benefits of QTIP Plan
Technique	T by E	Tax Savings Plan	Funded Inter Vivos QTIP
Securities Protected While Both Living	$10 M	$0	$10 M
Securities Protected Upon Death of 1st Spouse	$0	$5 M	$10 M
Tax Paid Upon Death of Spouse (assuming portability)	$1.225 M	$1.225 M	$1.225 M

EXHIBIT E
Tenancy by the Entireties

States	Statutes Referencing	Case Law Referencing (If necessary)	Recognize? (Yes or No)
Alabama		*Donegan v. Donegan*, 15 So. 823, 824 (1893) ("...the reason of the rule of the common law, that they should take by entirety,--per tout, not per my,--has ceased to exist."). *First Nat'l Bank v. Lawrence*, 101 So. 663, 663-64 (Ala. 1924) ("As a result of our statutory system joint owners of property, real or personal, including husband and wife, holding by inheritance, grant, devise or gift, become tenants in common, each owning a moiety, which, upon death, passes under the statute of descents and distributions. There is no survivorship as an incident to such estate.").	No
Alaska (1)	ALASKA STAT. § 34.15.140(a)		Yes
Arizona	ARIZ. REV. STAT. ANN. §25-211	*Sigmund v. Rea*, 226 Ariz. 373, 376 (Ariz. Ct. App. 2011) ("The notion that married persons in Missouri hold property as "one person" is wholly different from the model of community property, under which a separate entity -- the community -- owns property, realizes the fruits of the spouses' efforts and bears the burden of the debts they each may incur.").	No
Arkansas (2)		*Ford v. Felts*, 624 S.W.2d 449 (Ark. Ct. App. 1981) ("Arkansas follows the rule that a homestead may be acquired in land held by a husband and wife as tenants by entireties.").	Yes
California		*Tischhauser v. Tischhauser*, 298 P.2d 551, 553 (Cal. App. 2d Dist. 1956) ("At respondent's behest and without knowledge or consent of appellant wife, the title to the ranch	No

States	Statutes Referencing	Case Law Referencing (If necessary)	Recognize? (Yes or No)
		was placed in the spouses as tenants by the entirety, a common law estate recognized by Oregon law, one which does not exist in California.”).	
Colorado	COLO. REV. STAT. § 38-31-201		No
Connecticut	CONN. GEN. STAT. § 47-14a		No
Delaware (3)		*Citizens Sav. Bank, Inc. v. Astrin*, 61 A.2d 419, 421 (Del. Super. Ct. 1948) (“...it appears that the only property involved in this litigation is the real estate owned by the bankrupt and his wife as tenants by the entirely. In Delaware, this type of ownership retains most, if not all, of its common law features.”).	Yes
District of Columbia (x)		*Travis v. Benson*, 360 A.2d 506, 509 (D.C. 1976) (“Although tenancy by the entirety has been eliminated in many states, it is still recognized in the District of Columbia.”).	Yes
Florida (4)	FLA. STAT. § 655.79.	*Beal Bank v. Almand & Assocs.*, 780 So.2d 45 (Fla. 2001).	Yes
Georgia		*State v. Jackson*, 399 S.E.2d 88, 91 (1990) ("While the doctrine of survivorship as applied to joint tenancies has been distinctly abolished and does not exist in this State, there is no law of this State that we are aware of which prevents parties . . . from expressly providing that an interest in property shall be dependent upon survivorship."). *Spurlock v. Commercial Banking Co.*, 227 S.E.2d 790, 794 (Ga. Ct. App. 1976) (“Because of the abolition of joint tenancies, the interest created in a joint account or savings certificate with right of survivorship is a life estate with an alternative contingent remainder in fee simple.”).	No

States	Statutes Referencing	Case Law Referencing (If necessary)	Recognize? (Yes or No)
Hawaii (5)	HAW. REV. STAT. § 509-2		Yes
Idaho		*In re Antonie*, 432 B.R. 843, 851 (Bankr. D. Idaho 2010) ("Debtor does not hold her interest in the mobile home by 'entirety.' And it has long been the law in Idaho that property jointly-owned with another is subject to the claims of the co-owners' creditors.").	No
Illinois (6)	750 ILL. COMP. STAT. 65/22		Yes
Indiana (7)	IND. CODE ANN. § 32-17-3-1		Yes
Iowa		*Fay v. Smiley*, 207 N.W. 369, 371 (Iowa 1926) ("Assuming, for the purpose of this division of this opinion, that this deed, in the eyes of the common-law rule, would create an estate in entirety, we have to say that such a construction has never been recognized under the Iowa practice, and when attempts have been made to induce the court to make such construction, it has refused to do so. In the case of Hoffman v. Stigers, 28 Iowa 302, an attempt was made to have this court recognize an estate in entirety, and this was refused.").	No
Kansas	K.S.A. § 58-501		No
Kentucky (8)	KY. REV. STAT. ANN. § 381.050		Yes
Louisiana	LA. C.C. ART. 3526; POWELL ON REAL PROPERTY 7-52, §52.01 (Matthew Bender, Pub., 2011) ("Louisiana. Tenancy by the entirety does not appear in state statutes or cases which, given the state's civil law heritage, is not surprising.").		No
Maine		*In re Peters*, 2003 Bankr. LEXIS 1335 (Bankr. E.D. Pa. Oct. 7, 2003) ("...property may not be owned as tenants by entireties in Maine. Poulson v. Poulson, 145 Me. 15, 70 A.2d 868 (1950) (tenancy by entirety has not existed in Maine since 1844).").	No
Maryland (9)	MD. REAL PROP. CODE ANN		Yes

States	Statutes Referencing	Case Law Referencing (If necessary)	Recognize? (Yes or No)
	§ 4-108		
Massachusetts(10)	MASS. ANN. LAWS ch. 209 § 1		Yes
Michigan (11)		*Butler v. Butler*, 332 N.W.2d 488, 490 (Mich. Ct. App. 1983) ("...the common law remains the law of Michigan, stated: "In this State, where the common law is unchanged by statute, a conveyance to husband and wife conveys an estate in entirety, but may create one in joint tenancy or in common, if explicitly so stated in the deed").	Yes
Minnesota		*Wilson v. Wilson*, 45 N.W. 710, 711 (Minn. 1890) ("It would seem as though, the reason for the rule having ceased, and unity, so far as rights of property are concerned, no longer existing, the wife being as capable of taking and holding property as though she were unmarried, and she and her husband being no more considered as one person in the law as to property, there could no longer be any foundation for the rule. And the statute has very clearly abolished that sort of tenancy -- that is, by the entirety.").	No
Mississippi (12)	MISS. CODE ANN. § 89-1-7		Yes
Missouri (13)	MO. REV. STAT. § 442.025		Yes
Montana	MONT. CODE ANNO., § 70-1-306	*Lurie v. Sheriff of Gallatin County*, 999 P.2d 342, 345 (Mont. 2000) ("Accordingly, we hold that the estate by the entireties is not a permissible mode of ownership of property in Montana.").	No
Nebraska		*Sanderson v. Everson*, 141 N.W. 1025, 1026 (Neb. 1913) ("...the law of title by entireties does not exist in this state.").	No
Nevada	NEV. REV. STAT. § 123.030		No
New Hampshire		*Estate of Croteau v. Croteau*, 722 A.2d 464, 466 (N.H. 1998) ("A	No

States	Statutes Referencing	Case Law Referencing (If necessary)	Recognize? (Yes or No)
		divorce would automatically sever only a tenancy by the entirety, a form of ownership whose attributes are not recognized in New Hampshire.”).	
New Jersey (14)	N.J. STAT. ANN. § 46:3-17.4		Yes
New Mexico	N.M. STAT. ANN § 40-3-2		No
New York (15)	NY CLS REAL PROP. § 240-b		Yes
North Carolina (16)	N.C. GEN. STAT §39-13.3		Yes
North Dakota	N.D. CENT. CODE §47-02-08	*Renz v. Renz*, 256 N.W.2d 883, 885 (N.D. 1977) (“...North Dakota estates by the entirety have never been recognized.”).	No
Ohio (17)	OHIO REV. CODE ANN. § 5302.21	*Cent. Benefits Mut. Ins. Co. v. Ris Adm'Rs Agency*, 637 N.E.2d 291, 293 (Ohio 1994) (“Sub.S.B. No. 201, effective April 4, 1985, enacted the current version of R.C. 5302.17 and replaced the tenancy by the entireties with a survivorship tenancy. 140 Ohio Laws, Part I, 545, 556-557. However, Sub.S.B. No. 201 also enacted R.C. 5302.21, which provides that tenancies by the entireties created under former R.C. 5302.17 continue to be valid.”).	Yes
Oklahoma (18)	OKLA. STAT. tit. 60 § 74		Yes
Oregon (19)	OR. REV. STAT § 91.020	*Brownley v. Lincoln County*, 343 P.2d 529, 531 (Or. 1959) (“We have recognized in this state a form of concurrent ownership in real property by husband and wife which we have denominated a tenancy by the entirety...”).	Yes
Pennsylvania (20)	69 PA. STAT. ANN.§ 541		Yes
Rhode Island (21)		*Bloomfield v. Brown*, 25 A.2d 354, 359 (R.I. 1942) (“The possibility of creating an estate by entirety has not been removed by the married women's act, provided that the intention to create such an estate	Yes

States	Statutes Referencing	Case Law Referencing (If necessary)	Recognize? (Yes or No)
		clearly appears in the conveyance.”).	
South Carolina	S.C. CODE ANN. § 27-7-40		No
South Dakota	S.D. Codified Laws § 25-2-3	*Schimke v. Karlstad*, 208 N.W.2d 710, 714 (S.D. 1973) (“With this long-standing history of legislation we conclude that estates by entireties have never been recognized as the law of this state.”).	No
Tennessee (22)	TENN. CODE ANN. §66-1-109		Yes
Texas		*In re Garrett*, 429 B.R. 220, 240 (Bankr. S.D. Tex. 2010) (“’Texas does not recognize tenancies by the entirety.’”).	No
Utah	UTAH CODE ANN. § 57-1-5 (7)		No
Vermont (23)	VT. STAT. ANN. tit.15 § 67		Yes
Virginia (24)		*Rogers v. Rogers*, 512 S.E.2d 821, 822 (Va. 1999) (“We have stated, clearly and without equivocation, that real property held as tenants by the entireties is exempt from the claims of creditors who do not have joint judgments against the husband and wife.”).	Yes
Washington	WASH. REV. CODE ANN. § 64.28.010		No
West Virginia		*Wartenburg v. Wartenburg*, 100 S.E.2d 562, 565 (W. Va. 1957) (“The rights of survivorship do not depend on the continued existence of common law estates by entireties. Such estates were created and existed at common law only by virtue of a fiction, a fiction not recognized in this State... effect of the statutes mentioned, especially Code, 36-1-19, we believe, completely abolishes common law	No

States	Statutes Referencing	Case Law Referencing (If necessary)	Recognize? (Yes or No)
		estates by entireties.”).	
Wisconsin		*Estate of Richardson v. Estate of Richardson*, 282 N.W. 585, 587 (Wis. 1938) (“Estates by entirety do not exist under the law of this state.”).	No
Wyoming (25)	WYO. STAT. ANN. § 34-1-140		Yes

LAW OFFICES OF
NELSON & NELSON, P.A.

2012 Gift Suitability Analysis

July 26, 2012

This information has been prepared in accordance with Circular 230. Please review the following paragraph before reading this e-mail or it's attachments.

No one, without our express prior written permission, may use any part of this letter in promoting, marketing or recommending an arrangement relating to any federal tax issue. Furthermore, it may not be shared with any other person without our prior written consent other than as required by law or by ethical rules. However, this prohibition on sharing this letter does not preclude you from sharing with others the nature of this transaction or the fact that you consummate it.

Introduction

2012 provides a unique opportunity for making gifts using the federal estate, gift and generation skipping transfer ("GST") tax exemption of $5,120,000 (reduced by any prior use of such exemption). Unless Congress takes action, the exemption decreases to $1 Million on January 1, 2013 and there is a possibility that those who miss the opportunity will have lost the ability to make significant tax free gifts. Based upon the existing estate and gift tax rate of 35%, the additional taxes from not taking advantage of the gift exemption of $5.12 Million that could expire on January 1, 2013 as compared to the $1 Million gift tax exemption that is scheduled to be effective on January 1, 2013 could be over $1.4 Million. If estate, gift and GST tax rates are increased to 45%, additional taxes from not taking advantage of the $5.12 million tax exemption could be over $1.8 Million. For couples who each retain their $5.12 Million of remaining gift tax exemption (total of $10.24 Million), the potential gift tax savings by making use of the 2012 exemption could be as much as $3.7 Million (assuming the gift tax exemption is reduced to $1 Million and gift tax rates increased to 45%). These computations disregard the tax benefits of removing future appreciation on assets gifted from future estate, gift and GST taxes.

If you believe you can afford to make gifts in 2012, you must carefully select assets to gift and understand the consequences if such gifts are determined to be undervalued in the event of an IRS audit. Whether to proceed with 2012 gifting depends in part on your risk tolerance after: (i) considering the possibility of valuation increases of the gifted assets should the IRS audit your gift tax return; and (ii) whether you are willing to incur the time or expense to defend a gift tax audit. Some may prefer to "reserve" some unused exemption to offset any potential IRS audit adjustment of the gift tax valuation. However, this approach has pitfalls. To the extent the full $5.12 Million of gifting exemption was not used and the federal exemption is reduced, the "reserve" may be wasted as, once the exemption is reduced, it cannot be used, even if there is no gift tax audit or adjustment of prior gifts. Although gifts can be made using one of a number of formulas, which have been recognized in recent court decisions and limit the value of assets gifted to avoid taxable gifts should the IRS challenge valuation of gifted assets, the IRS has yet to acquiesce to these court decisions. Accordingly, we need to understand your willingness to pay gift taxes or defend the valuation of assets you gift in 2012 in the event of a gift tax audit even if formula gifts are used.

* * *

The following list of questions is provided to facilitate our discussions and assist you to make the best year end 2012 gifting decision based upon your unique facts:

1) Previous Use of Federal Estate, Gift and GST Exemption:

Have you previously made full use of your federal estate, gift and GST tax exemption ($5.12 Million if single, $10.24 Million if married) by making prior taxable gifts?

It is critical that this question be answered accurately to avoid unanticipated gift tax. It is possible that you made a prior taxable gift by consenting to a split gift election with your spouse (or even a former spouse) and signing a prior gift tax return treating 50% of gifts made by your spouse (or prior spouse) as if they were made by you and not by your spouse. If recent gifts were made by you that were reported on a federal gift tax return, it may also be possible for the IRS to audit the return and increase values of assets gifted and reported on the return. Any such audit adjustment could result in reducing the amount of gift exemption available to you in 2012 to offset gift taxes.

If no, read on. If yes, you cannot make additional tax free gifts in 2012.

2) To save future estate, gift and GST taxes, would you be willing to make 2012 gifts of up to $5.12 Million (single), $10.24 Million (jointly with spouse) if such gifts can be made free of gift taxes if you and your spouse would have no access to such funds, regardless of any reversal in your financial position?

If no, read on. If yes, contact our office/your tax advisor.

3) To save future estate, gift and GST taxes, would you make 2012 gifts of up to $5.12 Million into a trust for your spouse (and possibly your children) where your spouse and children may receive distributions at the discretion of the trustee (you may not be a beneficiary or a trustee). Upon the death of your spouse, the trust assets will be held exclusively for your children (they will not pass back to you even if you survive your spouse).

If no, read on. If yes, contact our office/your tax advisor.

4) To save future estate, gift and GST taxes, would you make 2012 gifts of up to $5.12 Million into a trust for your spouse (and possibly your children) in 2012 where your spouse and children may receive distributions at the discretion of the trustee, (you are not a beneficiary or trustee). Upon your spouse's death, your spouse can decide on whether all or any portion of the assets in the trust revert into a new trust created by your spouse for your benefit and in such event, an independent trustee will determine the extent of distributions to you?

If no, read on. If yes, contact our office/your tax advisor.

5) To save future estate, gift and GST taxes, would you make a 2012 gift into a trust designating your spouse and children as discretionary beneficiaries but providing that on a predetermined future date, the assets are distributed outright or in trust for your children if your net worth is at least a specified value determined upon creation of the trust that you believe would result in you having sufficient assets outside the trust to provide for you and your spouse for the rest of your life?

If no, read on. If yes, contact our office/your tax advisor.

6) Would your spouse be willing to initiate gift planning similar to the plans described in questions 2-5, above, but where you are the potential beneficiary so that if you and your spouse have not made use of your gifting exemptions, you could each gift $5.12 Million into trusts for one another before year end for a total of $10.24 Million providing that there are material differences in the trusts?

If no, read on. If yes, contact our office/your tax advisor.

7) To save future gift, estate and GST Taxes, would you make a 2012 gift into a trust in one of a number of states that have enacted self-settled asset protection trust legislation (such as but not limited to Alaska, Delaware, South Dakota and Nevada) where you, along with your spouse (and possibly your children) are potential beneficiaries understanding

that the IRS could argue that your inclusion as a potential trust beneficiary could result in the IRS asserting that all trust assets should be included in your estate upon your death (especially if the trustee has exercised its power to make regular distributions to you during your lifetime)? If you prefer greater certainty then you should consider making gifts as described in questions 2-5.

If yes, contact our office/your tax advisor so we can discuss options.

* * *

If you answered yes to any of the above questions, it is critical that you contact our office or your tax advisor promptly. You will need to discuss the benefits and drawbacks of the gifting alternatives that you may be interested in, and documents must be drafted, executed and funded before year end. Many will want to make 2012 gifts and time constraints will likely limit the ability of most tax advisors to assist those who wait until late in the year to begin planning.

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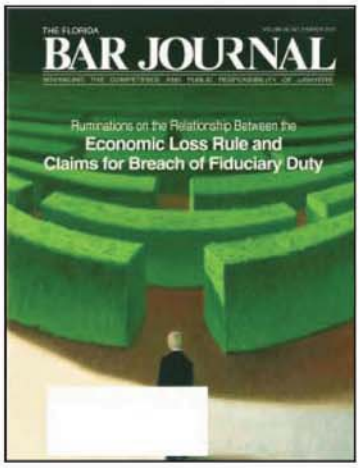
by Barry A. Nelson



Bacardi on the Rocks

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Those drafting estate planning documents frequently hear that one objective of a parent who wants all or a portion of a child's inheritance to pass into a trust, rather than outright, is to prevent the child's spouse from reaching such assets in the event of divorce. Beneficiaries of Florida trusts (as well as their lawyers) may be surprised that even when a discretionary trust is created to protect a child's inheritance, a former spouse may have rights as an exception creditor to reach trust assets that are protected from creditors, such as one holding a judgment resulting from a car accident, physician, or other professional malpractice or tort. Attorneys advising their clients that a discretionary trust governed by Florida law will protect a child's inheritance in the event of divorce, should a spouse or former spouse obtain a judgment in the form of support against such child as a result of a divorce, may be misguided.

This article explores discretionary and spendthrift trusts under the Florida Trust Code.[1] In the author's opinion, while it is clear that the Florida Supreme Court case of *Bacardi v. White*, 463 So. 2d 218 (Fla. 1985), was followed when the Florida Trust Code was enacted with respect to a spendthrift trust, it is unclear whether *Bacardi* was followed with respect to a Florida discretionary trust.[2] One reading F.S. §736.0504 may reasonably believe that a spouse with a judgment resulting from divorce cannot reach or otherwise attach the interest of their former spouse in a discretionary trust created under Florida law. However, based upon the discussion below, the author believes Florida Statutes should be clarified to reflect whether *Bacardi* was intended to be followed when the Florida Trust Code was enacted in 2006 or whether *Bacardi* is on the "rocks" for a discretionary trust.

Example: Residential Developer Cannot Pay Alimony Because He Cannot Make a Living

The following example is referred to throughout the remainder of this article. Divorced son Mark, a Florida domiciliary, who has a large support obligation to a former spouse, was a successful Florida residential homebuilder. As a result of the existing market downturn, Mark no longer has a source of income. Mark used all of his assets to satisfy bank guarantees on land that he stockpiled for future development. The land lost significant value, and Mark settled with his mortgage lender by using all of his liquidity in exchange for a release. Mark's father, Jack, a wealthy and elderly retiree, consults his adviser and asks whether the testamentary trust for Mark included in his existing estate plan could be reached by Mark's former wife who, as a result of Mark's inability to satisfy his unpaid alimony obligation to her, received a judgment against Mark in the form of support. Jack states that when Mark was financially secure, Mark was making timely payments to his former wife. However, like many others, Mark's ability to satisfy his debts was significantly curtailed when the value of his real estate vanished along with his capacity to earn a living as a developer. Jack is helping to support Mark (hopefully temporarily) and wants the comfort that upon Jack's death, Mark, and not Mark's former wife, would benefit from assets left in a discretionary trust for Mark.

Jack inquired about the benefits of using a spendthrift trust and/or a discretionary trust. He was advised that Mark's wife would be considered an "exception creditor" and could reach Mark's trust if it was a spendthrift trust. Jack was advised that Mark needed a discretionary trust. Jack asked his adviser to explain the difference between a spendthrift trust and a discretionary trust and whether either of them would protect Mark against his wife's judgment.

Distinction Between "Spendthrift Trusts" and "Discretionary Trusts"

• *Spendthrift Trusts* —

> Florida law recognizes the validity of spendthrift trusts.... A spendthrift trust is a trust "created with a view of providing a fund for the maintenance of another, and at the same time securing it against his own improvidence or incapacity for self-protection."...When a trust includes a valid spendthrift provision, a beneficiary may not transfer his interest in the trust and a creditor or assignee of the beneficiary may not reach any interest or distribution from the trust until the beneficiary receives the interest....[3]

In Florida, a spendthrift provision is unenforceable against a beneficiary's child, spouse, or former spouse who has a judgment or court order for support or maintenance, a judgment creditor who has provided services

interest in the trust, and a claim of a state or the United States.[4]

• *Discretionary Trusts* — Discretionary trusts often provide that the trustee, in the trustee's sole discretion, may determine whether a distribution will be made to a trust beneficiary. A discretionary trust often contains a spendthrift clause. A discretionary trust typically provides that distributions are "subject to the trustee's discretion whether or not the discretion is expressed in the form of a standard [an ascertainable standard] of distribution...."[5] Ascertainable standards are defined under the UTC and Florida Trust Code as standards relating to an individual's health, education, support, or maintenance pursuant to IRC §§2041(b)(1)(A) or 2514(c)(1).[6] When a trust document provides the trustee with complete discretion over distributions, a creditor may only reach those distributions the trustee chooses to make.[7] The creditor cannot compel a distribution.[8]

The *Restatement Second* distinguishes discretionary trusts from spendthrift trusts as follows:

> [A discretionary trust] is to be distinguished from a spendthrift trust and from a trust for support. In a discretionary trust it is the nature of the beneficiary's interest rather than a provision forbidding alienation which prevents the transfer of the beneficiary's interest. The rule stated in this [s]ection is not dependent upon a prohibition of alienation by the settlor; but the transferee or creditor cannot compel the trustee to pay anything to him because the beneficiary could not compel payment to himself or application for his own benefit.[9]

Florida Trust Code and Case Law

• *Florida Spendthrift Trusts and Florida Exception Creditors* — If the terms of a trust provide "that the interest of a beneficiary is held subject to a spendthrift trust, or words of similar import...," the terms are "sufficient to restrain both voluntary and involuntary transfer of the beneficiary's interest."[10]

> A beneficiary may not transfer an interest in a trust in violation of a valid spendthrift provision and, except as otherwise provided in this part, a creditor or assignee of the beneficiary may not reach the interest or a distribution by the trustee before receipt of the interest or distribution by the beneficiary.[11]

• *Florida Case Law* — Before enactment of Florida's Trust Code in 2006, *Bacardi* provided Florida common law on the rights of a former spouse (wife) to assets in a spendthrift and discretionary trust where the wife had a judgment in the form of support against her ex-husband.[12] Of great importance, and as discussed more fully below, the *Bacardi* case distinguished in its opinion the consequences of assets held in a spendthrift trust from assets held in a discretionary trust. In *Bacardi*, the former spouse of donor's son was granted alimony.[13] After the son ceased paying the requisite amount of alimony, his ex-wife obtained a judgment for the unpaid balance.[14] In aid of execution on her judgments, the ex-wife served a writ of garnishment on the trustee of the spendthrift trust created by the father for benefit of the son.[15] The son and trustee asserted that under the trust's spendthrift provision, the trust could not be garnished for the collection of alimony and attorneys' fees.[16] The issue on appeal to the Florida Supreme Court was whether disbursements from spendthrift trusts could be garnished to satisfy court-ordered alimony and attorneys' fees before such disbursements reach the debtor-beneficiary.[17] The Florida Supreme Court held that disbursements from spendthrift trusts, in certain limited circumstances, may be garnished to enforce court orders or judgments for alimony before such disbursements reach the debtor-beneficiary.[18]

Much of the *Bacardi* opinion centered on Florida's public policy in creating an exception to spendthrift trust provisions, specifically:

> This state has always had a strong public policy favoring the enforcement of both alimony and child support orders....We have weighed the competing public policies and, although we reaffirm the validity of spendthrift trusts, we conclude that in these types of cases the restraint of spendthrift trusts should not be an absolute bar to the enforcement of alimony orders or judgments. Florida's interest in the enforcement of these awards under certain limited circumstances is paramount to the declared intention of the donor and the restraint of a spendthrift trust.[19]

The court added:

> In not every case where someone is attempting to enforce alimony orders or judgment, however, will garnishment of a spendthrift trust be appropriate. This enforcement alternative *should be allowed only as a last resort.* If the debtor himself or his property is within the jurisdiction of this state's courts, the traditional methods of enforcing alimony arrearages may be sufficient. In this event, there would be no overriding reason to defeat the intent of the settlor. Florida courts have a variety of methods available to enforce alimony and child support. When these traditional remedies are not effective, it would be unjust and inequitable to allow the debtor to enjoy the benefits of wealth without being subject to the responsibility to support those whom he has a legal obligation to support.[20]

It appears that the opinion in *Bacardi* was codified by Florida's Trust Code.[21] F.S. §736.0503(3) provides an exception to spendthrift provisions, as follows:

> Except as otherwise provided in this subsection and in s. 736.0504, a claimant against which a spendthrift provision may not be enforced may obtain from a court, or pursuant to the Uniform Interstate Family Support Act, an order attaching present or future distributions to or for the benefit of the beneficiary. The court may limit the award to such relief as is appropriate under the circumstances. Notwithstanding this subsection, the remedies provided in this subsection apply to a claim by a beneficiary's child, spouse, former spouse, or a judgment creditor described in paragraph (2)(a) or paragraph (2)(b) only as a last resort upon an initial showing that traditional methods of enforcing the claim are insufficient.[22]

• *Did the Florida Trust Code Overrule* Bacardi *for Discretionary Trusts?* —When Florida enacted the Florida Trust Code in 2006, it included separate statutes for spendthrift trusts (§§736.0502 and 736.0503) and discretionary trusts (§736.0504). These statutes provide different rights to creditors. Florida law is clear that a spendthrift provision is unenforceable against exception creditors including a trust beneficiary's child, spouse, or former spouse who has a judgment for support or maintenance.[23] This article considers whether an exception creditor, such as a beneficiary's child, spouse, or former spouse, can reach a beneficiary's interest in a discretionary trust before such assets reach the beneficiary.

An attorney may believe that the exceptions to spendthrift protection under F.S. §736.0503(2) (entitled "Exceptions to Spendthrift Provision") could be avoided by creating

a discretionary trust. A quick and literal reading of F.S. §736.0504 (entitled "Discretionary Trusts; Effect of Standard") could lead an uninformed attorney and client to the conclusion that trust assets left to a client in a discretionary trust in Florida are protected from even a creditor holding a judgment in the form of support because although the creditor may be an exception creditor and, therefore, able to reach assets in a spendthrift trust, §736.0504(2) states:

> Whether or not a trust contains a spendthrift provision, if a trustee may make discretionary distributions to or for the benefit of a beneficiary, a creditor of the beneficiary, including a creditor as described in s. 736.0503(2), may not: (a) Compel a distribution that is subject to the trustee's discretion; or (b) Attach or otherwise reach the interest, if any, which the beneficiary might have as a result of the trustee's authority to make discretionary distributions to or for the benefit of the beneficiary.[24]

The critical issue is whether F.S. §736.0504(2) means a spouse holding a judgment in the form of support cannot 1) force a distribution from a discretionary trust for the benefit of the spouse holding the judgment; and/or 2) garnish or otherwise reach or attach distributions from the discretionary trust before they are in the hands of the beneficiary.

While Florida law allows certain creditors to attach present or future distributions from Florida spendthrift trusts to or for the benefit of a beneficiary under limited circumstances,[25] the author believes it is uncertain whether exception creditors may garnish a beneficiary's interest in a Florida discretionary trust.

F.S. §§736.0503(2)(b) and 736.0504 may provide support to the position that a discretionary trust created for a beneficiary, such as Mark in our example, would be protected (*i.e.*, a creditor cannot attach or otherwise reach the interest of a beneficiary as a result of the trustee's authority to make discretionary distributions to or for the benefit of the beneficiary).[26] Based upon such position, an exception creditor could not attach or otherwise reach Mark's interest in a discretionary trust at least until Mark received his distribution from the trust. However, the terms "attach" or "reach" are not defined in the Florida Trust Code and lend themselves to a number of interpretations as to whether a creditor may be able to garnish the interest of a discretionary trust once the trustee, in the trustee's sole discretion, is ready to exercise its discretion to make a trust distribution to the beneficiary.

• *A Discretionary Trust May Be Subject to a Writ of Garnishment* —The court in *Bacardi* did not need to address how its ruling should apply to discretionary trusts. However, it did. The Florida Supreme Court opinion in *Bacardi* states:

> We further limit this right of garnishment to disbursements that are due to be made or which are actually made from the trust. If, under the terms of the trust, a disbursement of corpus or income is due to the debtor-beneficiary, such disbursement may be subject to garnishment. *If disbursements are wholly within the trustee's discretion, the court may not*

order the trustee to make such disbursements. However, if the trustee exercises its discretion and makes a disbursement, that disbursement may be subject to the writ of garnishment....We also note that where a continuing garnishment is appropriate, the trustee, if it wishes to make payments to the debtor-beneficiary in excess of alimony then due, should seek court approval before it makes such payments. The court may then authorize such payments if sufficient assets remain in the trust or if other provisions are made to secure the payment of alimony to the person who should receive it.[27]

Although Florida practitioners may believe that the intent of the Florida Legislature in its drafting of the Florida Trust Code was to follow *Bacardi*, with respect to both spendthrift trusts and discretionary trusts, an interpretation of the Florida Trust Code could leave an impression that an exception creditor could not garnish, attach, or otherwise reach assets held in a Florida discretionary trust, even upon distribution to a beneficiary subject to a judgment in favor of an exception creditor due to the phrase may not "attach or otherwise reach an interest."[28] When reading the Florida Trust Code in conjunction with *Bacardi*, a court could determine that once a trustee, in the trustee's sole discretion, decides to make a distribution, an exception creditor of the beneficiary should be able to garnish such distributions before they reach the beneficiary. As noted below, Nevada and South Dakota have provided additional clarity in their statutes that specifically prohibit exception creditors from reaching discretionary trust assets.

• *Members of the Florida Trust Code Drafting Committee Have Different Views on Whether* Bacardi *Still Controls Discretionary Trusts* — Attorneys involved in drafting the Florida Trust Code who are leaders in the Real Property, Probate and Trust Law Section of The Florida Bar have differing views on whether §736.0504 was intended to overrule *Bacardi* with respect to discretionary trusts. In preparation of this article, a number of the Florida Trust Code Committee members were asked whether an exception creditor could obtain a continuing garnishment against a beneficiary of a Florida discretionary trust. Excerpts from some of their responses are included below:

1) Regardless of the effect on *Bacardi*, I think the legislative result under the existing statute was fully intended.

2) [Section] 736.0504 differs substantially from the UTC version. The difference flowed from the fact that the UTC has an exception for exception creditors of [beneficiaries] of discretionary trusts when the trustee has breach [sic] with regard to a standard for distribution. There was a lot of controversy over this and the committee decided that we did not want the UTC approach. To buttress the fact that we were not following the UTC, we beefed up our version of 736.0504 to clarify that the creditor protection inherent in a discretionary trust flows from the nature of the trust regardless of the presence of a spendthrift provision, that it does not matter if the discretion is modified by a standard, or whether that trustee has breached or whether the creditor is or is not an exception creditor. So, no rights to a garnishment (the UTC and FTC use the term "attachment") of future distributions. That said, it does not necessarily follow that if the trustee exercises discretion to make a distribution, the creditor cannot reach that particular distribution before it hits the hands of the beneficiary. Common law allows this in some states and the effect is to give the creditor the ability to cut off the beneficiary's water, so to speak.... All of this does not affect the fact, however, that no creditor can get a continuing writ of garnishment with respect to a beneficiary's interest in any kind of discretionary trust as that term is defined in 736.0504....

3) Maybe I am missing the point, but I don't see a problem with the statutes, nor do I see that they override *Bacardi*. The beginning point in the statute is in 736.0503.... That language is explicitly clear. A court can grant a continuing writ with respect to future distributions made by the trustee. The last sentence applies the last resort holding of *Bacardi*. [Section] 736.0504(2) does not change or override that rule,...736.0504(2) says that no creditor can compel a discretionary distribution, and no creditor can attach the beneficiary's interest in the trust. A beneficial interest in the trust is not the same as a distribution made by the trustee. A former spouse of the beneficiary can get a continuing writ that will require the trustee to withhold future distributions (whether discretionary or not) from the beneficiary, but that former spouse cannot compel the trustee to make a distribution, nor can that former spouse attach the beneficiary's beneficial interest in the trust. What am I missing?

4) As I recall, the intention of the RPPTL Section committee was not to change the law as set forth in *Bacardi*....

5) I would suggest that on a textualist reading of §736.0504, one cannot escape the conclusion that exception creditors cannot obtain a continuing garnishment or any other remedy against a discretionary trust under current law. Compare the sections: §736.0501, applicable to an income trust, allows general creditors of a beneficiary to satisfy their claims either by a continuing garnishment or "by other means," presumably a reference to acceleration. [Section] 736.0503, applicable to a spendthrift trust, allows exception creditors to satisfy their claims by a continuing garnishment only (no reference to "other means"), and only as a last resort (codifying *Bacardi*). Finally, §736.0504, applicable to a discretionary trust, makes no provision for satisfaction of exception creditors' claims at all. This conclusion is further reinforced when one compares §736.0504 with its analogue in the Uniform Trust Code (on which §736.0504 is based). UTC §504(c), applicable to a discretionary trust, creates a remedy for exception creditors. The drafters of §736.0504 omitted the language creating that remedy.... [I]f the committee intended a different result, then §736.0504 needs to be amended.

6) I did find my heavily highlighted and annotated copy of... Scrivener's Summary dated January 17, 2006, which a number of us on the committee often have treated as the "legislative history" of the FTC.... Summary concludes that in one sense, at least, an effort was made to expand *Bacardi* by adding another category of exception creditor and by requiring of the exception creditor(s) only an initial showing, and not a continuing showing, that traditional remedies are inadequate in order to allow attachment of distributions.... But as to your highlighted excerpt below from *Bacardi*, I don't see .0504(2) overriding the court. I read the statute as simply reasserting the rule that if only discretionary distributions are in play, the creditor, including an exception creditor, can reach only actual distributions made, and that the court's order can neither compel distributions nor allow the exception creditor to reach in and obtain assets. To this end...suggests in both the summary and The Florida Bar *Journal*, "The fact that spendthrift clauses are unenforceable against exception creditors means only that these creditors have remedies against a beneficiary's interest similar to those of creditors of beneficiaries with interests in a trust that does not include a spendthrift provision. That is, exception creditors may attach present or future distributions to or for the benefit of the beneficiary; they cannot compel distributions from or otherwise reach beneficial interests in discretionary trusts...."

7) My recollection of the discussions, growing fainter by the day, is that we did *not* intend to override *Bacardi*.

8) I have now had a look at creditors' rights against a discretionary trust in FL. I thought that this problem might benefit from statutory clarification, but in fact none is needed: F.S. §736.0504(2)(b) clearly provides that general creditors cannot file a continuing garnishment — being the

functional equivalent of a charging order — against a discretionary trust. Because the Florida Trust Code (following the UTC) also collapses support trusts into the discretionary trust category, we have no legal uncertainty to worry about.

9) This is complicated by the fact that 736.0503(2) creditors (the "preferred creditors") are entirely different animals with entirely different means of enforcing their claims. With respect to 736.0503(2)(a), preferred creditors (child, spouse, etc.) who would enforce their claims by writ of garnishment, it is easy to conclude that 736.0504(2)(b) means that a creditor cannot reach such a beneficiary's interest merely because a trustee has authority to make discretionary distributions when such a distribution is not being made.... A writ of garnishment operates entirely differently, and I think that writ is permissible against a trustee by the creditors specified in 736.0503(2)(a). A writ of garnishment would not operate unless a distribution is actually made by the trustee to the trust beneficiary, so that writ by the (2)(a) permitted persons would not violate 736.0504(2)(b). This preserves the law of *Bacardi*, which was intended. I presume the specified creditors could get a continuing writ of garnishment, so that the first dollars distributed would go to satisfy their claims. Beyond those claims, there could be additional discretionary funds distributed to a trust beneficiary, and other creditors could not reach those funds (until, I assume, the funds are actually in the hands of the beneficiary). I think the purpose of 736.0503(2)(a) is to make sure that discretionary distributions be first used to pay those specified creditors by way of garnishment, thus, preserving *Bacardi*....

• *It Is Safer to Create a Discretionary Trust in a State that Clearly Addresses Exception Creditors* — Based upon *Bacardi* and the "unofficial and independent" comments by members of the trust code drafting committee, it appears that although an exception creditor may attach a present or future distribution to or for the benefit of the beneficiary of a trust other than a discretionary trust, regardless of whether the trust contains a spendthrift provision, such exception creditor cannot compel distributions from or otherwise reach beneficial interests in discretionary trusts. In the event that the exception creditor could attach or otherwise reach distributions intended to be made by the trustee of a discretionary trust, then effectively, the donor's objective, to provide funds to the beneficiary and not to the beneficiary's former spouse, are thwarted. In Florida, the question as to whether an exception creditor can obtain a continuing garnishment over assets in a discretionary trust is likely to be determined by future case law or statutory clarification. For those desiring greater certainty that their beneficiaries (and not the beneficiary's former spouses) will benefit from trust assets under existing law, other jurisdictions, such as Nevada or South Dakota, should be considered. Some of the distinctions in Nevada and South Dakota are discussed below. Florida's statute may benefit from clarification, but the first decision is whether the policy discussed in *Bacardi*[29] should continue to be the law of Florida for discretionary trusts.

A Comparison of South Dakota and Nevada to Florida

• *South Dakota* — The South Dakota statute leaves little room for misunderstanding. For example, unlike Florida, where the word "reach" is not defined, South Dakota Codified Laws §55-1-24(6) states a creditor cannot reach assets in a discretionary trust and defines reach as follows: "[T]o subject the distribution to a judgment, decree, *garnishment, attachment*, execution, levy, creditor's bill or other legal, equitable, or administrative process, relief, or control of any court, tribunal, agency, or other entity as provided by law."[30]

South Dakota Codified Laws §55-1-35 states that a declaration in a trust that the intent of the beneficiary "shall be held subject to a spendthrift trust" is sufficient to restrain voluntary or involuntary alienation.[31] South Dakota Codified Laws §55-1-35 additionally states:

> Regardless of whether a beneficiary has any outstanding creditor, a trustee of a spendthrift trust may directly pay any expense on behalf of such beneficiary and may exhaust the income and principal of the trust for the benefit of such beneficiary. No trustee is liable to any creditor for paying the expenses of a beneficiary of a spendthrift trust.[32]

South Dakota states that a beneficiary's support interest does not rise to the level of a property interest.[33] "If the trust contains a spendthrift provision, notwithstanding the beneficiary's right to force a distribution with regard to a mandatory or support interest, no creditor may force a distribution [nor reach a present or future support distribution] with regard to a mandatory or support interest."[34] Even if a beneficiary has an outstanding creditor, the trustee of a mandatory or support interest "may directly pay any expense on behalf of such beneficiary. No trustee is liable to any creditor for paying the expenses of a beneficiary of a mandatory or support interest."[35]

Further, a discretionary interest is explicitly defined as a "mere expectancy" in South Dakota: "No creditor may force a distribution with regard to a discretionary interest. No creditor may require the trustee to exercise the trustee's discretion to make a distribution with regard to a discretionary interest."[36] A South Dakota court cannot:

> [O]rder a fiduciary to change a decision to exercise or not to exercise a discretionary power conferred by this chapter unless it determines that the decision was an abuse of the fiduciary's discretion. A fiduciary's decision is not an abuse of discretion merely because the court would have exercised the power in a different manner or would not have exercised the power.[37]

• *Nevada* — Nevada's spendthrift trust statute dates back to 1939 and was significantly enhanced in 1999 by enlarging the class of permitted beneficiaries of a spendthrift trust and the types of spendthrift trusts to which the law of Nevada applied.[38] There is no statutory allowance for exception creditors, and Nevada specifically disallows claims of spouses, former spouses, children, or dependents. Nevada Revised Statutes §166.090 provides that a "[p]rovision for the beneficiary will be for the support, education, maintenance and benefit of the beneficiary alone, and without reference to or limitation by the beneficiary's needs, station in life, or mode of life, or the needs of any other person, whether dependent upon the beneficiary or not."[39] Nevada Revised Statutes §166.080 adds that "[t]he beneficiary or beneficiaries of such trust shall be named or clearly referred to in the writing. No spouse, former spouse, child, or dependent shall be a beneficiary unless named or clearly referred to as a beneficiary

in the writing."[40]

The trustee's exercise of his or her discretion in a Nevada discretionary trust can only be reviewed if the trustee acts "dishonestly, with improper motive or fails to act."[41] "Regardless of whether a beneficiary has an outstanding creditor, a trustee of a discretionary interest may directly pay any expense on the beneficiary's behalf and may exhaust the income and principal of the trust for the benefit of such beneficiary."[42] Furthermore, creditors have an almost impossible task at trying to get a Nevada court to force a trustee to make a distribution out of a discretionary trust. Nevada Revised Statutes §163.417 provides:

1. A creditor may not exercise, and a court may not order the exercise of:

(a) A power of appointment or any other power concerning a trust that is held by a beneficiary;

(b) Any power listed in NRS 163.5553 that is held by a trust protector as defined in NRS 163.5547 or any other person;

(c) A trustee's discretion to:

(1) Distribute any discretionary interest;

(2) Distribute any mandatory interest which is past due directly to a creditor; or

(3) Take any other authorized action in a specific way; or

(d) A power to distribute a beneficial interest of a trustee solely because the beneficiary is a trustee....

***

3. A settlor may provide in the terms of the trust instrument that a beneficiary's beneficial interest may not be transferred, voluntarily or involuntarily, before the trustee has delivered the interest to the beneficiary.[43]

Where Does the Client's Trust Belong?

Ultimately, based upon the facts described in the example above, Jack created a discretionary trust in Nevada, as the Nevada statute prohibits a judgment creditor in the form of spousal and child support from reaching trust assets or distributions therefrom. Nevada law addressed Jack's concern, whereas under Florida law, it appears an argument can be made that based upon *Bacardi*, Mark's exception creditors could potentially obtain a garnishment of distributions once made by the trustee. Nevada specifically permits payments from the trust directly for the beneficiary's benefit and specifically states that no spouse or former spouse shall be considered a beneficiary unless clearly named or referred to as such.

Conclusion

Remedies provided to exception creditors of spendthrift trusts and discretionary trusts vary from state to state. As new trust codes are enacted, issues such as the rights of an exception creditor to a continuing garnishment of a discretionary trust may come into dispute. It appears that Florida law could benefit from clarification on whether the beneficiary of a discretionary trust can be subject to a continuing garnishment that would cut the beneficiary off from any distributions the trustee decides to make. South Dakota and Nevada statutes provide greater clarity. Florida should consider its policy for exception creditors of discretionary trusts. If *Bacardi* is still intended to be the law for discretionary trusts, F.S. §736.0504 should be clarified. Attorneys practicing in Florida should

advise their clients of the differences in treatment of exception creditors, especially when clients consult their lawyers as to how to protect their children or other beneficiaries from potential judgments in the form of support.[44] Until Florida law is clarified, advisors should consider using trusts in states such as Nevada and South Dakota if judgments resulting from divorce are likely against trust beneficiaries.❑

[1] *See* FLA. STAT. §§736.0502 and 736.0504.

[2] *Bacardi*, 463 So. 2d at 221.

[3] *Miller v. Kresser*, 34 So. 3d 172, 175 (Fla. 4th D.C.A. 2010). *See also* FLA. STAT. §§736.0502, 736.0503, and 736.0506.

[4] FLA. STAT. §736.0503(2).

[5] FLA. STAT. §736.0504(1).

[6] FLA. STAT. §736.0103(3).

[7] FLA. STAT. §736.0504(2). *See also Miller*, 34 So. 3d at 176.

[8] FLA. STAT. §736.0504(2).

[9] RESTATEMENT (SECOND) OF TRUSTS §155, comment b. (1959).

[10] FLA. STAT. §736.0502(2).

[11] FLA. STAT. §736.0502(3).

[12] *Bacardi*, 463 So. 2d at 219-220.

[13] *Id.* at 220.

[14] *Id.*

[15] *Id.*

[16] *Id* at 220-21.

[17] *Id.* at 220.

[18] *Bacardi*, 463 So. 2d at 222. *See also Landmark First Nat'l Bank v. Haves*, 467 So. 2d 839, 840 (Fla. 4th D.C.A. 1985). In review of a spendthrift trust, in accord with *Bacardi*, the court held that the creditor may be entitled to a continuing garnishment against the trust, but that it will not be effective unless and until the trustee exercises discretion and elects to make payments to the beneficiary. The court may not order the trustee to make such disbursements.

[19] *Bacardi*, 463 So. 2d at 222.

[20] *Id.* (emphasis added).

[21] *See generally* FLA. STAT. §736 (chapter effective July 31, 2007).

[22] FLA. STAT. §736.0503(3).

[23] FLA. STAT. §736.0503(2).

[24] FLA. STAT. §736.0504(2).

[25] FLA. STAT. §736.0503(3)

[26] FLA. STAT. §736.0504(2)(b).

[27] *Bacardi*, 463 So. 2d at 222-23 (emphasis added) (The Florida Trust Code preserves the ability for an exception creditor to reach *Bacardi* requirements that child support and alimony creditors reach a beneficiary's spendthrift interest "only as a last resort.").

[28] FLA. STAT. §736.0504(2)(b). *See Lerman v. Lerman*, 2009 N.J. Super. Unpub. LEXIS 2093 (App. Div. Aug. 4, 2009) (quoting *Bacardi* in part, "The right of a third party to garnish assets of a beneficiary of a spendthrift trust is limited to disbursements from the trust and '[i]f disbursements are wholly within the trustee's discretion, the court may not order the trustee to make such disbursements.'").

[29] *See Bacardi*, 463 So. 2d at 222 ("This state has always had a strong public policy favoring the enforcement of both alimony and child support orders....We have weighed the competing public policies and, although we reaffirm the validity of spendthrift trusts, we conclude that in these types of cases the restraint of spendthrift trusts should not be an absolute bar to the enforcement of alimony orders or judgments. Florida's interest in the enforcement of these awards under certain limited circumstances is paramount to the declared intention of the donor and the restraint of a spendthrift trust.").

[30] S.D. CODIFIED LAWS §55-1-24(6) (emphasis added).

[31] S.D. CODIFIED LAWS §55-1-35.

[32] *Id.*

[33] S.D. CODIFIED LAWS §55-1-42.

[34] *Id.*

[35] *Id.*

[36] S.D. CODIFIED LAWS §55-1-43(1)-(2).

[37] S.D. CODIFIED LAWS §55-13A-105(a).

[38] *See* Assembly Bill 469, as introduced, Mar. 10, 1999, *available at* http://www.leg.state.nv.us/ Session/70th1999/bills/AB/AB469.pdf.

[39] NEV. REV. STAT. §166.090(1).

[40] NEV. REV. STAT. §166.080.

[41] NEV. REV. STAT. §163.419(1).

[42] NEV. REV. STAT. §163.419(4).

[43] NEV. REV. STAT. §§163.417(1) and (3).

[44] Alaska is another state that provides debtors protection from exception creditors. *See also* ALASKA STAT. §34.40.110. For a recent case alluding to the fact that the creditor's choice of law may not apply in certain situations, *see American Institutional Partners LLC v. Fairstar Resources, Ltd.*, 2011 U.S. Dist. LEXIS 34385 (D. Del., Mar. 31, 2011). In *Fairstar*, Fairstar Resources, LTD, and Goldlaw PTY, LTD (collectively the "creditors") obtained charging orders in a Utah state court against American Institutional Partners, LLC, AIP Resort Development, LLC, and Peninsula Advisors, LLC, LLCs formed under Delaware law, and Mark Robbins (collectively "debtors"). Since the creditors sought to foreclose on the membership interests of the debtors, the debtors filed suit in Delaware, seeking a declaratory judgment that the creditors' foreclosures upon the debtors' membership interests were invalid under Delaware law. Creditors responded by filing a motion to dismiss or transfer venue, arguing that Utah law applied. In denying creditors' motion, the Delaware court opined that even if the LLCs are registered to do business in Utah and have their principal places of business there, the plaintiff's (debtors) choice of forum outweighed the origin of the claim in Utah. The court noted that factors in deciding whether the case should be transferred to Utah consisted of preference of the plaintiff; preference of the defendant; where the plaintiff's claim arose; the physical condition and financial condition of the parties and the convenience of litigating in one jurisdiction as opposed to a different one; where the witnesses reside; where the documentary evidence is located; whether the judgment would be enforceable; practical considerations, such as the ease and expense of trial; the caseload of the district court; local interests; public policy considerations; and whether a judge in one state may apply the law of the other state. Here, none of the factors stood out to tip the scale in favor of creditors.

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This column is submitted on behalf of the Real Property, Probate and Trust Law Section, George Joseph Meyer, chair, and William P. Sklar and Kristen Lynch, editors.

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by Barry A. Nelson and Richard R. Gans

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New §736.0505(3) Assures Tax/Asset Protection of Inter Vivos QTIP Trusts

Effective July 1, 2010, new F.S. §736.0505(3) allows married couples to take advantage more easily of one another's estate tax exemptions and, at the same time, to enhance asset protection planning.[1] Before enactment of the new statutory provision, it was unclear whether assets contributed to an inter vivos QTIP trust by one spouse that pass in trust for the benefit of the initial donor upon the death of the donor's spouse would be subject to the claims of the donor spouse's creditors, and, therefore, includible in the donor spouse's estate under I.R.C. §2041.[2] The new statute clarifies the asset protection and estate tax benefits of inter vivos QTIP trust planning. As described below, inter vivos QTIP trust planning can be enhanced if trusts are created by both the husband and wife, but only if the two trusts are not reciprocal.[3]

Example

The following example illustrates this technique: Bob and Judy, both attorneys, have been married for 28 years and have four children. Bob and Judy have accumulated a net worth of approximately $13.5 million, of which $3.5 million is equity in their Florida homestead, and $10 million is invested in a joint brokerage account (titled "tenants by the entirety"). Assuming estate taxes are reinstated and the estate tax exemption amount stays at $3.5 million (its 2009 level), Bob and Judy are significantly underutilizing their estate tax exemption amounts. Exhibit 1 shows estate taxes due upon the death of Bob and Judy and the amount of their assets that would be protected from their creditors during their joint lifetimes (assuming they remain married to one another) and upon the death of the first spouse. All jointly held assets pass outright by operation of law to the surviving spouse.

Understanding that Bob and Judy's current estate plan fails to take advantage of the estate tax exemption amount of the first spouse to die, their CPA suggests that Judy's assets be retitled so Bob has $5 million in his revocable trust (thereby avoiding probate and taking advantage of his estate tax exemption if he dies first), and Judy has $5 million in her revocable trust. Each of their revocable trusts directs that an estate tax-exempt gift of the greatest amount that can pass free of estate tax be used to create a trust for the surviving spouse; this trust is intended to pass free of estate tax upon the death of the surviving spouse.

Bob and Judy's desire is to maintain access to all family wealth until the survivor of them passes away, but they do not mind having a portion of the funds held in trust for the surviving spouse, as long as the surviving spouse can serve as a co-trustee or as sole trustee during his or her lifetime, and as long as distributions can be made to the surviving spouse based upon an ascertainable standard (such as for his or her health, maintenance, and support).

Bob and Judy want to confirm their CPA's recommendation, so they consult with their estate planning attorney, Lauren, whose practice combines estate planning with asset protection advice. Lauren explains that converting $10 million of their assets from tenants by the entirety by dividing those assets equally between their respective revocable trusts changes the character of the assets from those that are protected from potential creditors (as long as the debt was not a joint debt of Bob and Judy, and both were living and married to one another), and subjects the entire $10 million to claims of their creditors because assets in a revocable trust are unprotected.[4]

Exhibit 2 shows estate taxes due upon the death of Bob and Judy and the amount of the assets that would be protected from their creditors during their joint lifetimes and upon the death of the first spouse, assuming they follow their CPA's suggestion. Bob and Judy ask for alternatives that would allow each of them to take advantage of their estate tax exemptions while at the same time not subjecting their assets to exposure to the claims of future creditors.

F.S. §763.0505(3) to the Rescue

The new statute provides as follows:

> (3) Subject to the provisions of s. 726.105 [This is a reference to Florida's fraudulent transfer statute], for purposes of this section, the assets in:
>
> (a) A trust described in s. 2523(e) of the Internal Revenue Code of 1986, as amended, or a trust for which the elec-

tion described in s. 2523(f) of the Internal Revenue Code of 1986, as amended, has been made; and

(b) Another trust, to the extent that the assets in the other trust are attributable to a trust described in paragraph (a), shall, after the death of the settlor's spouse, be deemed to have been contributed by the settlor's spouse and not by the settlor.[5]

As a result of the enactment of §736.0505(3), Bob and Judy can divide the $10 million tenants by the entireties brokerage account equally between them and create separate inter vivos QTIP trusts, taking care that the trusts are not reciprocal.[6] Inter vivos QTIP trusts take advantage of new F.S. §736.0505(3) to provide a solution to many of Bob and Judy's tax and asset protection objectives. Rather than maintaining the assets in unprotected revocable trusts (and thereby subjecting $10 million of assets to potential future creditors), assume that Bob created an inter vivos QTIP trust for Judy and transferred $5 million of assets to the trust. Also assume that Bob would only be willing to create the trust for Judy if he had reasonable assurances that, should Judy predecease Bob, he would have access to the $5 million (or such other amount as may be held in the trust upon Judy's death). To maintain flexibility for future planning, the inter vivos QTIP trust can give Judy a testamentary special power of appointment that could be exercised in favor of one or more of Bob, their children, or a charity.[7] However, if Bob wants to be certain that, should Judy predecease him, the QTIP trust assets will pass in trust for Bob's benefit, he could draft the inter vivos QTIP trust to require that, should Judy predecease him, the QTIP trust assets would pass into an estate tax-exempt trust for Bob (to the extent of Judy's estate tax exemption amount, as of her date of death), and if Bob survives her, with any remaining assets passing into a testamentary QTIP trust for Bob.[8] Use of this technique assures that the assets held in the inter vivos trust for the benefit of Judy are protected from her creditors during Judy's lifetime because the QTIP trust is a spendthrift trust.

Upon Judy's death, the assets remaining in the trust will be held in an asset-protected spendthrift trust for Bob's benefit (an estate tax exempt trust) under the terms of the inter vivos QTIP trust.[9] Until F.S. §736.0505(3) was enacted, assets passing from the trust back to Bob at Judy's death might have been thought to be subject to the claims of Bob's creditors because Bob created the original trust.[10] Bob would have argued that Judy, and not Bob, should be considered as the donor of the trust after Judy's death, so Bob is not properly considered a beneficiary of a trust that he created. This argument would be consistent with IRS Treas. Reg. §25.2523(f)- 1(f), Example 11, which provides that assets held in an inter vivos QTIP trust — for the benefit of the settlor after the death of his or her spouse — will not be includible in the settlor's taxable estate under Code §§2036 and 2038. Thus, following the tax ownership reasoning, the trust created for Bob upon Judy's death should not be considered settled by Bob.[11]

F.S. §736.0505(3) makes it un-

necessary to analogize to federal estate tax concepts. Under the new statute, if the inter vivos QTIP trust is properly drafted — and assuming the initial transfer to the trust was not a fraudulent conveyance — it is now clear under Florida law that the assets of the inter vivos QTIP trust described in the example above will not be subject to the creditors of the initial donor (Bob) upon the death of the initial donee spouse (Judy), and that the assets passing in trust for Bob's benefit after Judy's death will not be includible in Bob's estate.

Potential Pitfalls

There are a number of issues and traps that must be considered when creating an inter vivos QTIP trust, some of which are described briefly below.

• *Jurisdiction* — The trust must be created in a jurisdiction in which assets that benefit the initial donor spouse in a protected trust will be protected from creditors' claims (as is the case in Florida as a result of new F.S. §736.0505(3)).

• *Reciprocal Trusts* — If both spouses create an inter vivos QTIP trust, there is a possibility that the IRS could take the position that they were reciprocal.[12] Avoidance of reciprocal trust attacks can be accomplished by allowing a considerable amount of time lapse between the creation of the husband's inter vivos QTIP trust and the wife's inter vivos QTIP trust, and by having different dispositive provisions in the trusts, for example: providing for different trustees, different beneficiaries upon the death of the donee spouse, a special power in favor of certain beneficiaries in each trust, or not providing a special power upon the death of the donee spouse at all in one of the trusts. Arizona has addressed the reciprocal trust dilemma by enacting Arizona Revised Statutes §14-10505(E)(4) that, in conjunction with §14-10505(E), provides that a person who would otherwise be treated as a settlor or deemed a settlor of a trust should not be treated as settlor with respect to an irrevocable inter vivos trust created by the settlor's spouse for the benefit of the settlor, regardless of whether or when the settlor also created an irrevocable inter vivos trust with respect to which such spouse is a beneficiary.[13]

• *Divorce* — A number of important issues need to be considered before proceeding with creation of the inter vivos QTIP trust. Once created, the inter vivos QTIP trust is irrevocable for the lifetime of the donee spouse, and the trust will not qualify for the gift tax marital deduction if the spouse's interest in the trust automatically terminates in the event of divorce. As a result, even after divorce, the donee spouse will have the benefits of the trust assets. One planning technique may be to limit principal invasions in the event of dissolution of marriage so that, after divorce, only income distributions will be mandated without the consent of a "special trustee." Will the assets in the trust be considered for purposes of determining elective share rights of a surviving spouse? Would the value of assets in the inter vivos QTIP trust be considered in the event of a subsequent dissolution of marriage of the donor and donee spouse? If so, will the terms of discretionary distributions provided in the trust be considered in determining the value of the trust for purposes of computing the division of assets? Some of these issues could be dealt with if each spouse created an inter vivos trust for the benefit of the other spouse.

Conclusion

Inter vivos QTIP trusts can provide very effective tax planning and asset protection benefits, but only if there is certainty about the rights of the creditors of the initial settlor in the trust assets. Florida may be the best state in which to create such a trust, if a sufficient nexus exists to invoke Florida law. Newly enacted F.S. §736.0505(3) provides certainty that assets in an inter vivos QTIP trust that pass in trust after the death of the beneficiary spouse to the initial donor will not be subject to the creditors of the initial donor spouse; combine this with the fact that Florida has no state income or intangible taxes, and it may be an unbeatable combination. Inter vivos QTIP trusts that can continue in trust for the benefit of the initial settlor after the death of a spouse can provide the following benefits: 1) reduction or elimination (depending upon the values of assets and the applicable estate tax exemption

amounts) of estate taxes in the estates of both spouses; 2) protection of the trust assets from the claims of creditors of both the settlor and the settlor's spouse; and 3) control of the ultimate disposition of the trust assets by the settlor. If desired, the settlor can assure that the trust assets will be continued in trust for his or her benefit after the death of the beneficiary spouse in a creditor-protected trust not subject to estate taxes at the subsequent death of the settlor.

In light of the recent statutory change, inter vivos QTIP trusts can now be considered by anyone desiring both to take full advantage of his or her estate tax exemption and to maintain asset protection for their assets.❑

[1] FLA. STAT. §736.0505 (3).

[2] Barry A. Nelson, Asset Protection for Estate Planners, Address at the 43rd Annual Heckerling Institute on Estate Planning (Jan. 2009), *in* 43rd Annual Heckerling Institute on Estate Planning at 18-15-18-20 (Matthew Bender, Pub., 2009); Mitchell M. Gans, Jonathan G. Blattmachr & Diana S.C. Zeydel, *Supercharged Credit Shelter Trust*, 21 PROBATE & PROP. 52 (July/August 2007); Dana R. Irwin, *Removing the Scaffolding: The QTIP Provisions and the Ownership Fiction*, 84 NEB. L. REV. 571 (2005).

[3] *See* Gans, Blattmachr, and Zeydel, *Supercharged Credit* at 58-59.

[4] FLA. STAT. §736.0505(1)(a) ("The property of a revocable trust is subject to the claims of the settlor's creditors during the settlor's lifetime to the extent the property would not otherwise be exempt by law if owned directly by the settlor").

[5] FLA. STAT. §736.0505 (3).

[6] This should only be done if Bob and Judy do not have existing debt because once assets held as tenants by the entirety are divided and retitled in their respective names, assets that previously were protected from creditors as tenants by the entirety (assuming no joint debt) would be subject to creditor's claims of Bob and Judy since they will have outright ownership of $5 million each prior to contributing such assets to the new QTIP trusts. Reciprocal trusts must be avoided. *See* endnote 2 for articles addressing the reciprocal trust issue in great detail.

[7] A special power of appointment provides the power holder with the right to distribute property, subject to the power, to a limited class of beneficiaries or alternatively to a broad class that excludes the power holder, the power holder's estate, the power holder's creditors, or the creditors of the power holder's estate. *See* I.R.C. §2041.

[8] The mandatory reversion in favor of Bob would be even more critical if he had his four children from a prior marriage and he wanted to be certain that upon his death the assets would a) pass for his benefit if he survives Judy or b) to his children if he predeceases Judy or disclaims the interest otherwise passing to him upon Judy's death.

[9] This article assumes assets in a spendthrift trust are protected from general creditors. Exception creditors, such as the IRS or child support, may circumvent spendthrift protection. *See* FLA. STAT. §736.0503(2): "To the extent provided in subsection (3), a spendthrift provision is unenforceable against: (a) A beneficiary's child, spouse, or former spouse who has a judgment or court order against the beneficiary for support or maintenance. (b) A judgment creditor who has provided services for the protection of a beneficiary's interest in the trust. (c) A claim of this state or the United States to the extent a law of this state or a federal law so provides."

[10] *See* FLA. STAT. §736.0505(1)(b) ("With respect to an irrevocable trust, a creditor or assignee of the settlor may reach the maximum amount that can be distributed to or for the settlor's benefit"). If the original settlor of an inter vivos QTIP trust is also treated as the settlor of the trust for his or her benefit after the death of the initial beneficiary spouse, under Florida law prior to §736.0505(3), the settlor's creditors could reach the trust assets in satisfaction of their claims.

[11] 26 C.F.R. §25.2523 (f)(1)(f), Ex. 11.

[12] *See* Gans, Blattmachr, and Zeydel, *Supercharged Credit*, for a thorough analysis of reciprocal trusts.

[13] A.R.S. §14-10505(E).

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This column is submitted on behalf of the Real Property, Probate and Trust Law Section, Brian J. Felcoski, chair, and William P. Sklar and Kristen Lynch, editors.

Exhibit 1
Bob and Judy – Tenancy by the Entireties Plan

	Bob	Judy	T by E
House – Protected Homestead			$3.5 M
Brokerage			$10 M
TOTAL			$13.5 M
Bob's Gross Estate Assuming He Dies First			$6.75 M
MARITAL DEDUCTION			$6.75 M
Bob's Taxable Estate			$0
Bob's Tax			$0

	Bob	Judy	T by E
UPON JUDY'S DEATH			
Judy's Gross Estate			$13.5 M
Less Unified Credit Equivalent Amount			($3.5 M)
Judy's Taxable Estate			$10 M
Judy's Tax			$4.5 M
Assets subject to creditors while both married and living			$0
Assets subject to creditors upon death of 1st spouse or divorce			$10 M

Exhibit 2
Bob and Judy – CPA's Tax Savings Plan

	Bob's Revocable Trust	Judy's Revocable Trust	T by E
House – Protected Homestead			$3.5 M
Brokerage	$5 M	$5 M	
TOTAL	$5 M	$5 M	$3.5 M
Bob's Gross Estate Assuming He Dies First	$6.75 M		
Bob's Share of Homestead to Judy Outright	($1.75 M)		
Marital Trust	($1.5 M)		
MARITAL DEDUCTION	$3.25 M		
Bob's Taxable Estate	$3.5 M		
Less Unified Credit Equivalent Amount	($3.5 M)		
Bob's Tax	$0		

	Bob's Revocable Trust	Judy's Revocable Trust	T by E
UPON JUDY'S DEATH			
Judy's Gross Estate	$10 M		
Less Unified Credit Equivalent Amount	($3.5 M)		
Judy's Taxable Estate	$6.5 M		
Judy's Tax	$2.925 M		
Savings Compared to Tenancy by the Entireties	$1.575 M		
Assets subject to creditors while both married and living			$10 M
Assets subject to creditors upon death of 1st spouse or divorce Assuming assets pass into spendthrift trust for surviving spouse upon death of 1st spouse			$5 M

Homestead	$3.5 M
Judy's Rev Trust	$ 5 M
Marital Trust	$1.5 M

Exhibit 3
Bob and Judy – Inter Vivos QTIP

	Bob's QTIP	Judy's QTIP	T by E
House – Protected Homestead			$3.5 M
Brokerage	$5 M	$5 M	
TOTAL	$5 M	$5 M	$3.5 M
Bob's Gross Estate Assuming He Dies First	$6.75 M		
Bob's Share of Homestead to Judy's Marital Deduction	($1.75 M)		
QTIP Marital Gift to Judy	($1.5 M)		
MARITAL DEDUCTION	$3.25 M		
Bob's Taxable Estate	$3.5 M		
Less Unified Credit Equivalent Amount	($3.5 M)		
Bob's Tax	$0		

	Bob's QTIP	Judy's QTIP	T by E
UPON JUDY'S DEATH			
Homestead	$3.5 M		
Marital Trust	$1.5 M		
QTIP Trust from Bob	$5 M		
Judy's Gross Estate	$10 M		
Less Unified Credit Equivalent Amount	($3.5 M)		
Judy's Taxable Estate	$6.5 M		
Judy's Tax	$2.925 M		
Savings Compared to Tenancy by the Entireties	$1.575 M		
Assets subject to creditors while both married and living			$0
Assets subject to creditors upon death of first spouse or divorce			$0 M

Exhibit 4
Comparison of Benefits of Inter Vivos QTIP

	Tenancy by the Entirety Plan	Tax Plan	Winner & New Champion (QTIP Plan)
Technique	T by E	Tax Savings Plan	Funded Inter Vivos QTIP
Securities Protected While Both Living	$10 M	$0	$10 M
Securities Protected Upon Death of 1st Spouse	$0	$5 M	$10 M
Tax Paid Upon Death of Spouse	$4.5 M	$2.925 M	$2.925 M*