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Domestic Asset Protection Trusts in Divorce Litigation

by  
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## I. Introduction

Domestic Asset Protection Trusts (“DAPTs”) are a relatively new estate planning tool to protect assets and obtain tax benefits. As such, only a small number of reported cases exist on handling DAPT in divorce matters.<sup>1</sup> Yet from the resolution of even these few cases, the ability of the DAPT to undermine vital public policies such as the fulfillment of contractual obligations<sup>2</sup> has become all too clear. Where the state has not carefully constructed (or perhaps too carefully constructed) its legislative scheme for the establishment of a DAPT, the indebted settlor might hide away his assets in the face of creditors seeking lawful repayment. Where legislative approval has been given, it understandably was with the aim of attracting further business and revenue to the state.<sup>3</sup> Thus, the concern of debtors at least attempting to avoid their creditors, if not successfully doing so, was reasonably apparent at the inception of the DAPT statutes and is likely a feature rather than a bug of the legislation.<sup>4</sup> The

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<sup>1</sup> See Steven J. Oshins, *The Domestic Asset Protection Trust: Combining It With the Double LLC Strategy*, 27 PROB. & PROP. 22, 23 (2013) (“So far, not a single DAPT has been tested all the way through the court system.”).

<sup>2</sup> See U.S. CONST. art I, § 10, cl. 1 (“No State shall . . . pass any . . . Law impairing the Obligation of Contracts . . . .”)

<sup>3</sup> Kevin R. McKinnis, Note, *The Good, the Bad, and a New Kind of Prenup: An Analysis of the Ohio Legacy Trust Act and What Asset Protection Trusts Will Mean for Ohio*, 61 CLEV. ST. L. REV. 1105, 1106–07 (2013) (citing Timothy Lee, Note, *Alaska on the Asset Protection Trust Map: Not Far Enough for a Regulatory Advantage, but Too Far for Convenience?*, 29 ALASKA L. REV. 149, 155–60 (2012); Amy Lynn Wagenfield, Note, *Law for Sale: Alaska and Delaware Compete for the Asset Protection Trust Market and the Wealth that Follows*, 32 VAND. J. TRANSNAT’L L. 831, 847 (1999); William J. McGraw, *Report of the Estate Planning, Trust and Probate Law Section*, OHIO BAR ASS’N, [https://www.ohiobar.org/General%20Resources/pubs/councilfiles/Report\\_of\\_the\\_Estate\\_Planning\\_Trust\\_and\\_Probate\\_Law\\_Section\\_11\\_10.pdf](https://www.ohiobar.org/General%20Resources/pubs/councilfiles/Report_of_the_Estate_Planning_Trust_and_Probate_Law_Section_11_10.pdf) (last visited Nov. 28, 2012)) (“The Ohio Legacy Trust Act is an attempt to modernize Ohio’s wealth management laws to make Ohio competitive with other states . . . [and] . . . was modeled after the ‘successful plans used in other states,’ such as Alaska, Delaware, and Nevada.”).

<sup>4</sup> Cf. Joseph E. Hershewe, Note, *Missouri Asset Protection Trusts: Debunking the Vulnerability Myth and a Call for Uniformity*, 79 UMKC L. REV. 211, 211–213, 233–35 (2010) (suggesting that a (presumably hypothetical) man who negligently caused the paralysis of a young girl, subsequently had a \$5M judgment issued, and filed for bankruptcy could have avoided paying substan-

marital DAPT, however, cannot be considered in the same light. The equitable division of such property is another important public policy,<sup>5</sup> and in the context of family law, the DAPT may become a tool utilized by one spouse, whether initially coldly calculating or well-intentioned and now spiteful, to deprive the other of his or her right to quantities of marital property—often at the expense of their children.<sup>6</sup>

Legislative action is necessary because DAPTs containing marital property may be used to violate not only public policy but also simple fairness in a dissolution of marriage. The state legislatures must ensure that a vehicle of economic development does not also deliver mass injustice to unsuspecting spouses and their children. In Part II, this article first generally describes the DAPT. Then Part III places the DAPT in the context of marital property, discussing when courts have validated DAPTs, ways in which courts have invalidated DAPTs, and what remedies exist if a valid DAPT has been created with marital property. If the DAPT is validated, Part IV discusses what few remedies remain. Part V examines some of the ethical problems that exist when transferring assets into DAPTs. Finally, Part VI argues for necessary changes in DAPT statutes to provide protection for spouses and their children when marital assets are placed in DAPTs.

## II. Brief Description of Domestic Asset Protection Trusts

DAPTs are trusts created by the settlor who can designate himself (called “self-settled trusts”) or others, as beneficiaries. Most states that allow DAPTs require that a qualified trustee be a resident of that state and the settlor be solvent upon creation of

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tial portions of what he did pay to the paralyzed by placing his assets in a DAPT).

<sup>5</sup> Young v. Kelly, 334 P.3d 153, 161 (Alaska 2014); Case v. Case, 325 S.E.2d 661, 665 (N.C. 1985); Martin v. Martin, 480 N.E.2d 1112, 1115 (Ohio 1985) (Douglas, J., dissenting); Dahl v. Dahl, 345 P.3d 566, 579 (Utah 2015).

<sup>6</sup> See generally Trent Maxwell, Comment, *Domestic Asset Protection Trusts: A Threat to Child Support?*, 2014 BYU L. Rev. 477 (arguing that “shielding of child support debts is immoral, and the economic cost to society of not having an exception for child-support claimants likely outweighs the economic benefits to the states”).

the DAPT. People generally use DAPTs to protect their assets from potential creditors and taxation. They are created prior to marriages to protect one spouse from another in the event of a divorce as a spouse in that instance would be a future creditor. However most concerning of all, DAPTs are sometimes created during the marriage with marital property, and without proper protections, such a DAPT would allow the self-settling spouse to effectively pillage the rightful property of the other on his or her way out of the marriage.

Although Colorado has a statute that allows for asset protection dating from 1861,<sup>7</sup> Alaska was the first state to enact legislation allowing the creation of DAPTs in 1997.<sup>8</sup> Currently, there are sixteen states that have their own recognized versions of a DAPT statute.<sup>9</sup> Most people create DAPTs to protect themselves from creditors, but courts scrutinize such transfers for fraud. DAPTs have many features, but this Article will discuss the states that provide protection for people who participate in the creation of the trust, due diligence procedures, exceptions for alimony, property division, and child support, and which type of interest insulates the beneficiary from creditors when the trustee makes distributions.

#### A. *States That Provide Protection for Attorneys, Trustees, and Others*

Most of the DAPT states provide protection for attorneys, trustees, and others who contribute to the creation and administration of the DAPTs. Alaska,<sup>10</sup> Delaware,<sup>11</sup> Hawaii,<sup>12</sup> Missis-

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<sup>7</sup> DAVID H. BRANTZ & CARL G. STEVENS, *COLORADO ESTATE PLANNING HANDBOOK* § 33.3.1 (2014) (“Colorado is frequently cited in national publications as a self-settled domestic asset protection trust jurisdiction based on an 1861 statute, C.R.S. § 38-10-111.”).

<sup>8</sup> ALASKA STAT. §§ 13.36.310, 34.40.110 (LEXIS through the 2015 First Regular Session and the First, Second, and Third Special Sessions of the Twenty-Ninth State Legislature); *Comparison of the Domestic Asset Protection Trust Statutes*, AM. COLL. TR. & ESTATE COUNSEL 1 (David G. Schaftel ed., Sept. 2015), <http://www.actec.org/assets/1/6/Shaftel-Comparison-of-the-Domestic-Asset-Protection-Trust-Statutes.pdf>.

<sup>9</sup> AM. COLL. TR. & ESTATE COUNSEL, *supra* note 8, at 43.

<sup>10</sup> ALASKA STAT § 34.40.110(e) (“[A] creditor [is prevented] from asserting any cause of action . . . against a trustee of the trust or against others involved in the preparation or funding of the trust for conspiracy to commit

Mississippi,<sup>13</sup> Nevada,<sup>14</sup> New Hampshire,<sup>15</sup> Ohio,<sup>16</sup> Rhode Island,<sup>17</sup> South Dakota,<sup>18</sup> Tennessee,<sup>19</sup> Utah,<sup>20</sup> Virginia,<sup>21</sup> and Wyoming<sup>22</sup>

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fraudulent conveyance, aiding and abetting a fraudulent conveyance, or participation in the trust transaction.”).

<sup>11</sup> DEL. CODE ANN. tit. 12, § 3572(d) (2015) (“[N]o . . . creditor . . . shall have any claim or cause of action against the trustee, or advisor . . . , of this title, of a trust that is the subject of a qualified disposition, or against any person involved in the counseling, drafting, preparation, execution or funding of a trust that is the subject of a qualified disposition.”).

<sup>12</sup> HAW. REV. STAT. ANN. § 554G-8(f) (LexisNexis 2015) (“No creditor . . . shall have any claim or cause of action, including an action to enforce a judgment entered by a court or other body having adjudicative authority, against a trustee or advisor . . . or against any person involved in drafting, preparing, executing, or funding a trust or in counseling the parties to a trust that is the subject of a permitted transfer.”).

<sup>13</sup> MISS. CODE ANN. § 91-9-707(d) (2015) (“[N]either a creditor nor any other person shall have any claim or cause of action against the trustee, an advisor of a trust that is the subject of a qualified disposition, or against any person involved in the counseling, drafting, preparation, execution, or funding of a trust that is the subject of a qualified disposition.”).

<sup>14</sup> NEV. REV. STAT. ANN. § 166.170(5) (2015) (“A person may not bring a claim against an adviser to the settlor or trustee of a spendthrift trust unless the person can show by clear and convincing evidence that the adviser acted in violation of the laws of this State, knowingly and in bad faith, and the adviser’s actions directly caused the damages suffered by the person.”).

<sup>15</sup> N.H. REV. STAT. ANN. § 564-D:12 (LexisNexis 2015) (“[N]o . . . creditor nor any other person has any claim or cause of action against the trustee, or an advisor . . . , of a trust that is the subject of a qualified disposition, or against any person involved in the counseling, drafting, preparation, execution, or funding of a trust that is the subject of a qualified disposition.”).

<sup>16</sup> OHIO REV. CODE ANN. § 5816.07(D) (LEXIS through file 60 (SB 264) (excluding file 57 (SB 182) and file 58 (HB 233))) (“[C]reditor[s] . . . shall have no claim or cause of action against any trustee or advisor of a legacy trust or against any person involved in the counseling in connection with, or the drafting, preparation, execution, administration, or funding of, a legacy trust.”).

<sup>17</sup> 18 R.I. GEN. LAWS § 18-9.2-4(d) (LEXIS through January 2016 Ch. 22 (excluding corrections and changes made by the Director of Law Revision)) (“[N]o . . . creditor nor any other person shall have any claim or cause of action against the trustee, or advisor . . . of a trust that is the subject of a qualified disposition, or against any person involved in the counseling, drafting, preparation, execution or funding of a trust that is the subject of a qualified disposition.”).

<sup>18</sup> S.D. CODIFIED LAWS § 55-16-12 (LEXIS through all legislation signed during the 2016 Regular Session of the 91st Legislative Assembly and Supreme Court Rule 16-67) (“[N]o . . . creditor nor any other person has any claim or cause of action against the trustee, or advisor . . . of a trust that is the subject of

all provide such protections. However, differences exist among states with DAPTs. Alaska, Mississippi, Ohio, Tennessee, and Utah provide protection for funding of limited partnerships and limited liability companies that are transferred to the trust.<sup>23</sup> In Nevada, a trustee, an advisor of the trustee, or an advisor of the settlor may be found liable only if a plaintiff establishes by clear and convincing evidence that the damages directly resulted from

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a qualified disposition, or against any person involved in the counseling, drafting, preparation, execution, or funding of a trust that is the subject of a qualified disposition.”).

<sup>19</sup> TENN. CODE ANN. § 35-16-104(d) (LEXIS through the 2015 Regular Session) (“[N]either a creditor nor any other person shall have any claim or cause of action against the trustee, or an advisor of an investment services trust, or against any person involved in the counseling, drafting, preparation, execution or funding of an investment services trust.”).

<sup>20</sup> UTAH CODE ANN. § 25-6-14(8) (LexisNexis 2015) (“[A] creditor [is prevented] from asserting any cause of action or claim for relief against a trustee of the trust or against others involved in the counseling, drafting, preparation, execution, or funding of the trust for conspiracy to commit fraudulent conveyance, aiding and abetting a fraudulent conveyance, participation in the trust transaction, or similar cause of action or claim for relief.”).

<sup>21</sup> VA. CODE ANN. § 64.2-745.1(E) (2015) (“No creditor and no other person shall have any claim or cause of action against any trustee, trust adviser, trust director, or any person involved in the counseling, drafting, preparation, or execution of, or transfers to a qualified self-settled spendthrift trust.”).

<sup>22</sup> WYO. STAT. ANN. § 4-10-517 (2015) (“[N]o creditor, assignee or agent may have any claim or cause of action against the trustee, trust protector, trust advisor or other fiduciary of the trust, or against any person involved in the counseling, drafting, administration, preparation, execution or funding of the trust unless the creditor, assignee or agent can prove by clear and convincing evidence that the transfer of property to the trust was a fraudulent transfer pursuant to the provisions of the Uniform Fraudulent Transfers Act.”).

<sup>23</sup> ALASKA STAT. § 34.40.110(e) (LEXIS through the 2015 First Regular Session and the First, Second, and Third Special Sessions of the Twenty-Ninth State Legislature); MISS. CODE ANN. § 91-9-707(d) (2015); OHIO REV. CODE ANN. § 5816.07(G) (LEXIS through file 60 (SB 264) (excluding file 57 (SB 182) and file 58 (HB 233))); TENN. CODE ANN. § 35-16-104(d); UTAH CODE ANN. § 25-6-14(8). Ohio and Utah have broader definitions. Ohio includes protections for the funding of “limited partnership[s], limited liability compan[ies], corporation[s], or similar or comparable entit[ies].” OHIO REV. CODE ANN. § 5816.07(G). Utah includes protections for the funding of “limited partnership[s], . . . limited liability compan[ies], or other entit[ies].” UTAH CODE ANN. § 25-6-14(8).

the defendant's knowing and bad-faith violation of the law.<sup>24</sup> Similarly in Wyoming, creditors need to prove by clear and convincing evidence that the property transfer to the DAPT was fraudulent under the UFTA.<sup>25</sup>

### B. Due Diligence Procedures

Alaska,<sup>26</sup> Mississippi,<sup>27</sup> Ohio,<sup>28</sup> Tennessee,<sup>29</sup> Utah,<sup>30</sup> and Wyoming<sup>31</sup> require sworn affidavits for the creation of a valid DAPT. Generally to satisfy the requirements for an affidavit, the settlor declares that (1) he has rights, title, and authority to create the DAPT, (2) he would not be made insolvent after his assets are transferred to the DAPT, (3) the purpose of the transfer is not to defraud creditors, (4) there are no pending or threatened suits against the settlor or administrative proceedings except the ones disclosed by the settlor on the affidavit, (5) he does not intend to file for bankruptcy, and (6) the assets being transferred were not obtained through illegal means.<sup>32</sup>

There are some variations in due diligence requirements among these states. Alaska, Utah, and Wyoming require the settlor to state that he is not in default of child support payments,<sup>33</sup> but Alaska and Wyoming only impose this requirement if the settlor is in default by more than thirty days.<sup>34</sup> Mississippi and Wy-

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<sup>24</sup> NEV. REV. STAT. ANN. § 166.170(5)–(6) (LEXIS through legislation from the Seventy-Eighth Regular Session (2015) and the Twenty-Ninth Special Session (2015), subject to revision by the Legislative Counsel Bureau).

<sup>25</sup> WYO. STAT. ANN. § 4-10-517.

<sup>26</sup> ALASKA STAT. § 34.40.110(j).

<sup>27</sup> MISS. CODE ANN. § 91-9-705 (2015).

<sup>28</sup> OHIO REV. CODE ANN. § 5816.06 (LEXIS through file 60 (SB 264) (excluding file 57 (SB 182) and file 58 (HB 233))).

<sup>29</sup> TENN. CODE ANN. § 35-16-103 (LEXIS through the 2015 Regular Session).

<sup>30</sup> UTAH CODE ANN. § 25-6-14(5)(m) (LEXIS through the 2016 Second Special Session).

<sup>31</sup> WYO. STAT. ANN. § 4-10-523 (2015).

<sup>32</sup> See *supra* notes 26–31 (setting forth the affidavit requirements in these states).

<sup>33</sup> ALASKA STAT. § 34.40.110(j)(6) (LEXIS through the 2015 First Regular Session and the First, Second, and Third Special Sessions of the Twenty-Ninth State Legislature); UTAH CODE ANN. § 25-6-14(5)(m)(vi); WYO. STAT. ANN. § 4-10-523(a)(vi).

<sup>34</sup> ALASKA STAT. § 34.40.110(j)(6); WYO. STAT. ANN. § 4-10-523(a)(vi).



oming further require the settlor to be a named insured of a general liability insurance policy with a one million dollar (\$1,000,000) policy limit for each policy;<sup>35</sup> Wyoming allows the settlor to do the lesser of the one million dollar (\$1,000,000) policy limit or provide coverage equal to the fair market value of the settlor's transfer total to the DAPT.<sup>36</sup> Utah includes the language in addition to not defrauding a creditor that a settlor does not "intend to hinder, delay, or defraud a known creditor."<sup>37</sup>

### *C. Exceptions for Family Law Judgments*

#### *1. Child Support, Alimony and Property Distribution*

Some states have built protections for judgments in the family law arena into their DAPT legislative schemes. Alaska,<sup>38</sup> Delaware,<sup>39</sup> Hawaii,<sup>40</sup> Mississippi,<sup>41</sup> Missouri,<sup>42</sup> New Hampshire,<sup>43</sup> Ohio,<sup>44</sup> Oklahoma,<sup>45</sup> Rhode Island,<sup>46</sup> South Dakota,<sup>47</sup> Tennes-

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<sup>35</sup> MISS. CODE ANN. § 91-9-705(h) (2015); WYO. STAT. ANN. § 4-10-523(a)(ix).

<sup>36</sup> WYO. STAT. ANN. § 4-10-523(a)(ix).

<sup>37</sup> UTAH CODE ANN. § 25-6-14(5)(m)(iii).

<sup>38</sup> ALASKA STAT. § 34.40.110(b)(4).

<sup>39</sup> DEL. CODE ANN. tit. 12, § 3573(1) ((LEXIS through 80 Del. Laws, ch. 243).

<sup>40</sup> HAW. REV. STAT. ANN. § 554G-9(1) (LEXIS through Ch. 51 of the 2016 Legislative Session).

<sup>41</sup> MISS. CODE ANN. § 91-9-707(i)(1)(A) (LEXIS through HB 1, 2016 1st Extraordinary Session and House Bills 447, 461, 496, 968, 1369, 1380 and 1413, and Senate Bills 2209, 2211, 2300, 2342, 2372, 2398, 2508, 2520, 2660, 2704 and 2808, 2016 Regular Session, not including changes and corrections made by the Joint Legislative Committee on Compilation, Revision and Publication of Legislation).

<sup>42</sup> MO. REV. STAT. § 456.5-503(1) (2) (2015).

<sup>43</sup> N.H. REV. STAT. ANN. § 564-D:15(I)(a) (LEXIS through Chapter 128 of the 2016 Regular Session).

<sup>44</sup> OHIO REV. CODE ANN. § 5816.03(C)(1) (LEXIS through file 60 (SB 264) (excluding file 57 (SB 182) and file 58 (HB 233))).

<sup>45</sup> OKLA. STAT. tit. 31, § 12 (LEXIS through Acts 1-12, 14-63, 65, 67-70, 72-87, 89-92, 94-163, 165-189, 191-196, 198-201, 203, 205-209, 211-221, 223-233, 235-238, 240-243, 245-253, 255, 257-259, 261, 264-269, 272, 274, 277-291, 294-296, 299-300, 302-309, 311-316, 319-320, 325-326, 328, 330-334 of the Second Regular Session of the 55th Legislature (2016)).

<sup>46</sup> 18 R.I. GEN. LAWS § 18-9.2-5(1) (LEXIS through Jan. 2016 Ch. 22 (excluding corrections and changes made by the Director of Law Revision)).

see,<sup>48</sup> Virginia,<sup>49</sup> and Wyoming<sup>50</sup> do not provide asset protection from child support claims, but some of these states have additional requirements that must be met in order for the exception to be effective. For example, Alaska, Hawaii, and Wyoming only withhold DAPT protection if the settlor was thirty days or more in default of making child support payments at the time of the transfer of assets to the trust.<sup>51</sup> Hawaii only provides protection if at the time of transfer a child support order existed. Rhode Island will provide the DAPT protection unless the court order for child support existed at the time the settlor established the DAPT.<sup>52</sup> South Dakota only permits recovery to the extent of the debt that existed upon the establishment of the DAPT.<sup>53</sup> While Utah does not provide for a child support exemption, the trustee must give the child support creditor thirty days advance notice of any distribution to the settlor, but the child support

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<sup>47</sup> S.D. CODIFIED LAWS § 55-16-15(1) (LEXIS through all legislation signed during the 2016 Regular Session of the 91st Legislative Assembly and Supreme Court Rule 16-67).

<sup>48</sup> TENN. CODE ANN. § 35-16-104(i)(1)(A) (LEXIS through the 2015 Regular Session).

<sup>49</sup> VA. CODE ANN. § 64.2-744 (LEXIS through Chapter 1-4, 19, 55, and 71 of the 2016 Regular Session of the General Assembly).

<sup>50</sup> WYO. STAT. ANN. § 4-10-520(a)(i) (LEXIS through 2016 Legislative Session). This provision only applies to the “Qualified Spendthrift Trust” provisions; the Wyoming statutes distinguish between that trust and the “Discretionary Asset Protection Trust,” for which the state has provided no child support exception. See AM. COLL. TR. & ESTATE COUNSEL, *supra* note 8, at 32, 37 (citing WYO. STAT. ANN. §§ 4-10-502, -504, 506(c), -510-523).

<sup>51</sup> ALASKA STAT. § 34.40.110(b)(4) (LEXIS through the 2015 First Regular Session and the First, Second, and Third Special Sessions of the Twenty-Ninth State Legislature); HAW. REV. STAT. ANN. § 554G-9(1) (LEXIS through Ch. 51 of the 2016 Legislative Session); WYO. STAT. ANN. § 4-10-520(a)(i).

<sup>52</sup> 18 R.I. GEN. LAWS § 18-9.2-5(1) (LEXIS through Jan. 2016 Ch. 22 (excluding corrections and changes made by the Director of Law Revision)).

<sup>53</sup> S.D. CODIFIED LAWS § 55-16-15(1) (LEXIS through all legislation signed during the 2016 Regular Session of the 91st Legislative Assembly and Supreme Court Rule 16-67). The exact or similar language “but only to the extent of such debt” appears in nearly every DAPT statute, and it is meant to confirm that a family-related claim does not open up the rest of the DAPT to attack once the claim has been satisfied; however, South Dakota specifically refers to the debt of the transferor “at the time of the transfer.” *Id.*

creditor cannot force or require the trustee to make a distribution to the settlor, as beneficiary.<sup>54</sup>

Several states provide a similar exception for alimony. Delaware,<sup>55</sup> Hawaii,<sup>56</sup> Mississippi,<sup>57</sup> Missouri,<sup>58</sup> New Hampshire,<sup>59</sup> Ohio,<sup>60</sup> Rhode Island,<sup>61</sup> South Dakota,<sup>62</sup> and Tennessee<sup>63</sup> do not protect a trust's assets from claims for alimony against the settlor. However, Delaware, Hawaii, Mississippi, New Hampshire, Ohio, Rhode Island, South Dakota, and Tennessee all specify that the settlor must have been married to the ex-spouse in question when the DAPT was created.<sup>64</sup> Similar to its provisions on child

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<sup>54</sup> UTAH CODE ANN. § 25-6-14(6)(b) (LEXIS through the 2016 Second Special Session).

<sup>55</sup> DEL. CODE ANN. tit. 12, § 3573(1) (LEXIS through 80 Del. Laws, ch. 243).

<sup>56</sup> HAW. REV. STAT. ANN. § 554G-9(1).

<sup>57</sup> MISS. CODE ANN. § 91-9-707(i)(1)(A) (LEXIS through HB 1, 2016 1st Extraordinary Session and House Bills 447, 461, 496, 968, 1369, 1380 and 1413, and Senate Bills 2209, 2211, 2300, 2342, 2372, 2398, 2508, 2520, 2660, 2704 and 2808, 2016 Regular Session, not including changes and corrections made by the Joint Legislative Committee on Compilation, Revision and Publication of Legislation).

<sup>58</sup> MO. REV. STAT. § 456.5-503.2 (LEXIS through all legislation approved as of May 6, 2016, during the 98th General Assembly, Second Regular Session).

<sup>59</sup> N.H. REV. STAT. ANN. § 564-D:15(I)(a) (LEXIS through Chapter 128 of the 2016 Regular Session).

<sup>60</sup> OHIO REV. CODE ANN. § 5816.03(C)(1) (LEXIS through file 60 (SB 264) (excluding file 57 (SB 182) and file 58 (HB 233))).

<sup>61</sup> 18 R.I. GEN. LAWS § 18-9.2-5(1) (LEXIS through Jan. 2016 Ch. 22 (excluding corrections and changes made by the Director of Law Revision)).

<sup>62</sup> S.D. CODIFIED LAWS § 55-16-15(1) (LEXIS through all legislation signed during the 2016 Regular Session of the 91st Legislative Assembly and Supreme Court Rule 16-67).

<sup>63</sup> TENN. CODE ANN. § 35-16-104(i)(1)(B)-(C) (LEXIS through the 2015 Regular Session).

<sup>64</sup> DEL. CODE ANN. tit. 12, §§ 3570(9), 3573(1) (LEXIS through 80 Del. Laws, ch. 243); HAW. REV. STAT. ANN. §§ 554G-2, -9(1) (LEXIS through Chapter 51 of the 2016 Legislative Session); MISS. CODE ANN. §§ 91-9-703(l), -707(i)(1)(A) (LEXIS through HB 1, 2016 1st Extraordinary Session and House Bills 447, 461, 496, 968, 1369, 1380 and 1413, and Senate Bills 2209, 2211, 2300, 2342, 2372, 2398, 2508, 2520, 2660, 2704 and 2808, 2016 Regular Session, not including changes and corrections made by the Joint Legislative Committee on Compilation, Revision and Publication of Legislation); N.H. REV. STAT. ANN. §§ 564-D:1(VIII), 15(I)(a); OHIO REV. CODE ANN. §§ 5816.02(U), 5816.03(C)(1); 18 R.I. GEN. LAWS §§ 18-9.2-2(7), -5(1); S.D. CODIFIED LAWS §§ 55-16-1(7), -15(1); TENN. CODE ANN. § 35-16-102(13), -104(i)(1)(B)-(C).

support, South Dakota only allows such claims to reach the extent of the debt that existed at the time of the transfer<sup>65</sup> and Hawaii requires a family court supervised agreement or order for the alimony.<sup>66</sup>

Alaska,<sup>67</sup> Delaware,<sup>68</sup> Hawaii,<sup>69</sup> Mississippi,<sup>70</sup> New Hampshire,<sup>71</sup> Ohio,<sup>72</sup> Rhode Island,<sup>73</sup> South Dakota,<sup>74</sup> and Tennessee<sup>75</sup> generally do not provide asset protection for property division upon divorce. In Alaska, if the settlor transfers assets to the DAPT thirty days or less before marriage, assets are not protected unless written notice is provided to the to-be spouse; if the settlor transfers assets during marriage or thirty days or less before marriage without written notice to the to-be spouse, then assets are not protected unless the parties to the marriage agree in writing that the property is not subject to division.<sup>76</sup> In Hawaii, DAPT assets are not protected if the transfer to the DAPT is made after the settlor's marriage or within thirty days prior to

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<sup>65</sup> S.D. CODIFIED LAWS § 55-16-15(1).

<sup>66</sup> HAW. REV. STAT. ANN. § 554G-9(1).

<sup>67</sup> ALASKA STAT. § 34.40.110(l) (LEXIS through the 2015 First Regular Session and the First, Second, and Third Special Sessions of the Twenty-Ninth State Legislature).

<sup>68</sup> DEL. CODE ANN. tit. 12, § 3573(1).

<sup>69</sup> HAW. REV. STAT. ANN. §§ 554G-9(1).

<sup>70</sup> MISS. CODE ANN. § 91-9-707(i)(1)(A) (LEXIS through HB 1, 2016 1st Extraordinary Session and House Bills 447, 461, 496, 968, 1369, 1380 and 1413, and Senate Bills 2209, 2211, 2300, 2342, 2372, 2398, 2508, 2520, 2660, 2704 and 2808, 2016 Regular Session, not including changes and corrections made by the Joint Legislative Committee on Compilation, Revision and Publication of Legislation).

<sup>71</sup> N.H. REV. STAT. ANN. § 564-D:15(I)(a) (LEXIS through Chapter 128 of the 2016 Regular Session).

<sup>72</sup> OHIO REV. CODE ANN. § 5816.03(C)(2) (LEXIS through file 60 (SB 264) (excluding file 57 (SB 182) and file 58 (HB 233))).

<sup>73</sup> 18 R.I. GEN. LAWS § 18-9.2-5(1) (LEXIS through Jan. 2016 Ch. 22 (excluding corrections and changes made by the Director of Law Revision)).

<sup>74</sup> S.D. CODIFIED LAWS § 55-16-15(1) (LEXIS through all legislation signed during the 2016 Regular Session of the 91st Legislative Assembly and Supreme Court Rule 16-67).

<sup>75</sup> TENN. CODE ANN. § 35-16-104(i)(1)(D) (LEXIS through the 2015 Regular Session).

<sup>76</sup> ALASKA STAT. § 34.40.110(l) (LEXIS through the 2015 First Regular Session and the First, Second, and Third Special Sessions of the Twenty-Ninth State Legislature).

the marriage; however, the assets are protected if written notice is provided to the other party to the marriage.<sup>77</sup> In addition, when there is a family court-supervised agreement or order for a division or distribution of property to the transferor's spouse or former spouse and if the transferor is in default by thirty days or more, the DAPT assets are only protected to the extent of the debt.<sup>78</sup> In Delaware, Mississippi, New Hampshire, Ohio, Rhode Island, South Dakota, and Tennessee, DAPTs are not protected if the ex-spouse was married to the settlor before or on the date of transfer to the DAPT.<sup>79</sup> In South Dakota, the DAPT assets are not protected only "to the extent of the debt" existing at the time the transfer was made.<sup>80</sup> The settlor's separate property in the DAPT is protected regardless of the date of the marriage,<sup>81</sup> and any marital property transferred into the DAPT is also protected if the spouse received a statutory notice or provides written consent after having received the notice.<sup>82</sup> The notice must contain the following language:

YOUR SPOUSE IS CREATING A PERMANENT TRUST INTO WHICH PROPERTY IS BEING TRANSFERRED.

YOUR RIGHTS TO THIS PROPERTY MAY BE AFFECTED DURING YOUR MARRIAGE, UPON DIVORCE (INCLUDING THE PAYMENT OF CHILD SUPPORT OR ALIMONY OR A DIVISION OR DISTRIBUTION OF

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<sup>77</sup> HAW. REV. STAT. ANN. § 554G-9(5) (LEXIS through Chapter 51 of the 2016 Legislative Session).

<sup>78</sup> *Id.* § 554G-9(1).

<sup>79</sup> DEL. CODE ANN. tit. 12, §§ 3570(9), 3573(1) (LEXIS through 80 Del. Laws, ch. 243); MISS. CODE ANN. §§ 91-9-703(1), -707(i)(1)(A) (LEXIS through HB 1, 2016 1st Extraordinary Session and House Bills 447, 461, 496, 968, 1369, 1380 and 1413, and Senate Bills 2209, 2211, 2300, 2342, 2372, 2398, 2508, 2520, 2660, 2704 and 2808, 2016 Regular Session, not including changes and corrections made by the Joint Legislative Committee on Compilation, Revision and Publication of Legislation); N.H. REV. STAT. ANN. §§ 564-D:1(VIII), 15(I)(a); OHIO REV. CODE ANN. §§ 5816.02(U), 5816.03(C)(2) (LEXIS through file 60 (SB 264) (excluding file 57 (SB 182) and file 58 (HB 233))); 18 R.I. GEN. LAWS §§ 18-9.2-2(7), -5(1); S.D. CODIFIED LAWS §§ 55-16-1(7), -15(1); TENN. CODE ANN. § 35-16-102(13), -104(i)(1)(D).

<sup>80</sup> S.D. CODIFIED LAWS § 55-16-15(1); *see supra* note 53.

<sup>81</sup> *Id.* § 55-16-15(2)(a).

<sup>82</sup> *Id.* § 55-16-15(2)(b).

PROPERTY IN A DIVORCE), OR AT THE DEATH OF YOUR SPOUSE.

YOU HAVE A VERY LIMITED PERIOD OF TIME TO OBJECT TO THE TRANSFER OF PROPERTY INTO THIS TRUST.

YOU MAY, UPON REQUEST TO THE TRUSTEE AT THE ADDRESS BELOW, BE FURNISHED A COPY OF THE TRUST DOCUMENT.

IF YOU HAVE ANY QUESTIONS, YOU SHOULD IMMEDIATELY SEEK INDEPENDENT LEGAL ADVICE.

IF YOU FAIL TO OBJECT WITHIN THE REQUIRED TIME PERIOD, YOU WILL HAVE CONSENTED TO THE TRANSFER OF PROPERTY INTO THIS TRUST.<sup>83</sup>

Further, the notice must describe the property to be transferred,<sup>84</sup> and the statute additionally dictates that the responsibility of providing notice rests with either “the transferor, the transferor’s agent, the trustee, or other fiduciary of the trust.”<sup>85</sup>

## 2. *Non-Settlor Beneficiary’s Interest upon Distributions*

In the case of a non-settlor beneficiary’s (“NSB”) interest in property division, Alaska,<sup>86</sup> Colorado,<sup>87</sup> Delaware,<sup>88</sup> Hawaii,<sup>89</sup>

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<sup>83</sup> *Id.* § 55-16-15(3)(a). The statute further provides that such notice must include the above language, “in capital letters, at or near the top of the notice.” *Id.*

<sup>84</sup> *Id.* § 55-16-15(3)(b).

<sup>85</sup> *Id.* § 55-16-15(3)(d).

<sup>86</sup> ALASKA STAT. § 34.40.110(1) (LEXIS through the 2015 First Regular Session and the First, Second, and Third Special Sessions of the Twenty-Ninth State Legislature).

<sup>87</sup> See AM. COLL. TR. & ESTATE COUNSEL, *supra* note 8, at 7 (citing *In re Marriage of Balanson*, 25 P.3d 28 (Colo. 2001)) (“Increases in value of and income from separate property after marriage are marital property. Some interests in trusts are considered to be the separate property of a non-settlor beneficiary.”).

<sup>88</sup> DEL. CODE ANN. tit. 12, § 3573(1) (LEXIS through 80 Del. Laws, ch. 243). The statute provides that the listed exceptions are only applicable “[t]o any person to whom the *transferor* is indebted.” *Id.* (emphasis added).

<sup>89</sup> HAW. REV. STAT. ANN. § 554G-9(5) (LEXIS through Chapter 51 of the 2016 Legislative Session).

Mississippi,<sup>90</sup> Missouri,<sup>91</sup> Nevada,<sup>92</sup> New Hampshire,<sup>93</sup> Ohio,<sup>94</sup> Oklahoma,<sup>95</sup> Rhode Island,<sup>96</sup> South Dakota,<sup>97</sup> Tennessee,<sup>98</sup> Utah,<sup>99</sup> Virginia,<sup>100</sup> and Wyoming<sup>101</sup> protect a non-settlor beneficiary's interest from property division at divorce. In Delaware, Hawaii, Missouri, Rhode Island, and Wyoming, although the NSB's interest is protected from property division at divorce, that interest may be considered in property division.<sup>102</sup> In Colorado, some interests in trusts held by a beneficiary are considered separate property and are thus protected in the property division following a dissolution of marriage; however, the appreciation of

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<sup>90</sup> *Sligh v. First Nat'l Bank*, 704 So. 2d 1020, 1025-26 (Miss. 1997) (citing *Deposit Guaranty Nat'l Bank v. Walter E. Heller & Co.*, 204 So. 2d 856, 859 (Miss. 1967)).

<sup>91</sup> See MO. REV. STAT. § 456.5-502.3 (LEXIS through all legislation approved as of May 6, 2016, during the 98th General Assembly, Second Regular Session) (stating that a creditor or assignee of the beneficiary may not reach the interest or a distribution by the trustee before its receipt by the beneficiary); MO. REV. STAT. § 456.5-503 (providing no exception to the spendthrift provision for property division).

<sup>92</sup> NEV. REV. STAT. ANN. § 166.120.3 (LEXIS through legislation from the Seventy-Eighth Regular Session (2015) and the Twenty-Ninth Special Session (2015), subject to revision by the Legislative Counsel Bureau).

<sup>93</sup> N.H. REV. STAT. ANN. § 564-B:8-814(b) (LEXIS through Chapter 128 of the 2016 Regular Session).

<sup>94</sup> OHIO REV. CODE ANN. § 5816.13 (LEXIS through file 60 (SB 264) (excluding file 57 (SB 182) and file 58 (HB 233))).

<sup>95</sup> OKLA. STAT. tit. 31, § 12 (LEXIS through Acts 1-12, 14-63, 65, 67-70, 72-87, 89-92, 94-163, 165-189, 191-196, 198-201, 203, 205-209, 211-221, 223-233, 235-238, 240-243, 245-253, 255, 257-259, 261, 264-269, 272, 274, 277-291, 294-296, 299-300, 302-309, 311-316, 319-320, 325-326, 328, 330-334 of the Second Regular Session of the 55th Legislature (2016)).

<sup>96</sup> AM. COLL. TR. & ESTATE COUNSEL, *supra* note 8, at 29; see 15 R.I. GEN. LAWS § 15-5-16.1(b) (LEXIS through January 2016 Ch. 22 (excluding corrections and changes made by the Director of Law Revision)).

<sup>97</sup> AM. COLL. TR. & ESTATE COUNSEL, *supra* note 8, at 29.

<sup>98</sup> *Id.* at 40.

<sup>99</sup> UTAH CODE ANN. § 75-7-502(3) (LEXIS through the 2016 Second Special Session).

<sup>100</sup> VA. CODE ANN. § 64.2-743(C) (LEXIS through Chapter 1-4, 19, 55, and 71 of the 2016 Regular Session of the General Assembly).

<sup>101</sup> AM. COLL. TR. & ESTATE COUNSEL, *supra* note 8, at 40.

<sup>102</sup> *Id.* at 7, 17, 29, 40.

a trust constitutes marital property.<sup>103</sup> In Mississippi, Nevada, and Oklahoma, the NSB's interest is protected if property is retained in a spendthrift trust for the beneficiary, but the court may consider trust income as resources when determining alimony and child support.<sup>104</sup> In New Hampshire, the NSB's interest "is neither a property interest nor an enforceable right, but a mere expectancy."<sup>105</sup> In South Dakota, this issue is not addressed by the DAPT statute, but some statutory sections suggest that the NSB's interest is protected.<sup>106</sup>

In Tennessee, the statute on distributions by the trustee provides for three types of interests: mandatory, support, and discretionary.<sup>107</sup> When the trustee is mandated to distribute property to the beneficiary, that distribution is a property interest and thus is considered in making an award for child support or alimony.<sup>108</sup> If the trustee is given discretionary powers to dis-

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<sup>103</sup> *In re Marriage of Balanson*, 25 P.3d 28, 41–42 (Colo. 2001); AM. COLL. TR. & ESTATE COUNSEL, *supra* note 8, at 7. The distinction, as the *Balanson* court explained, lies in the statutory language exempting "property acquired by gift, bequest, devise, or descent" from division. *Balanson*, 25 P.3d at 42 (citing COLO. REV. STAT. § 14-10-113(2) (LEXIS through all laws passed at the First Regular Session of the Seventieth General Assembly of the State of Colorado (2015))). The subsequent increase in the value of the trust does not constitute such a gift. *See id.*

<sup>104</sup> AM. COLL. TR. & ESTATE COUNSEL, *supra* note 8, at 17, 29.

<sup>105</sup> *In the Matter of Goodlander & Tamposi*, 20 A.3d 199, 205 (N.H. 2011) (quoting N.H. REV. STAT. ANN. § 564-B:8-814(b) (2007 & Supp. 2010)).

<sup>106</sup> AM. COLL. TR. & ESTATE COUNSEL, *supra* note 8, at 29 (stating that under South Dakota law, "discretionary interests are not property," "powers of appointment are not property," "certain remainders are not property," and "distribution and remainder interests [are] irrelevant to divorce"); *see* S.D. CODIFIED LAWS §§ 55-1-26, -27, -30, -43 (LEXIS through all legislation signed during the 2016 Regular Session of the 91st Legislative Assembly and Supreme Court Rule 16-67).

<sup>107</sup> *See* TENN. CODE ANN. § 35-15-103(10)(C) ("A distribution interest is classified as either a mandatory interest, a support interest or a discretionary interest.") (LEXIS through the 2015 Regular Session); § TENN. CODE ANN. § 35-15-814(b)–(c).

<sup>108</sup> *See id.* § 103(23) ("Property" means anything that may be the subject of ownership, whether real or personal, legal or equitable, or any interest therein"); § 814(b)(1), (c)(3) (stating that neither a discretionary interest nor a support interest constitutes a property interest); *see also* § 814(c)(1) ("A beneficiary of a mandatory or a support interest has an enforceable right to a distribution.").



tribute the income and/or property, the beneficiary has a “mere expectancy,” and thus, the income and/or property is not considered when the beneficiary divorces.<sup>109</sup> The support interest is not a property interest until the trustee makes the distribution.<sup>110</sup> The creditors may not reach the interest until the trustee distributes.<sup>111</sup>

### III. DAPTs Containing Marital Property

#### A. Cases in Which Courts Have Validated DAPTs

In *TrustCo Bank v. Mathews*,<sup>112</sup> Susan Mathews signed a personal guaranty in 2006 of a loan for a Florida limited liability company that she was a member of and managed.<sup>113</sup> A few months later she established three Delaware asset protection trusts.<sup>114</sup> The bank that provided the loan to the LLC and the assignee of the bank’s “rights, title, and interest in the . . . loan” brought a fraudulent transfer claim against Mathews, the trusts, the beneficiaries of those trusts, and ten unknown defendants following a default on the loan and the entry of foreclosure and deficiency judgments.<sup>115</sup> The court ultimately ruled that the claim was barred because either the four year or one-year-from-notice statute of limitations on fraudulent transfers had run.<sup>116</sup> This case is interesting because Mathews transferred assets to the trust after she incurred the obligation, which would have been voidable as a fraudulent transfer if not for the statute of limitations.

Although Colorado does not have a formal and universally recognized DAPT statute, it does have asset protection.<sup>117</sup> In *In re Marriage of Pooley*,<sup>118</sup> the wife placed personal injury proceeds acquired during the marriage into an irrevocable trust with

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<sup>109</sup> See TENN. CODE ANN. § 35-15-814(b)(1).

<sup>110</sup> See *id.* § 506(a)(1); TENN. CODE ANN. § 35-15-814(b)(1), (c)(3).

<sup>111</sup> TENN. CODE ANN. § 35-15-506(a)(2).

<sup>112</sup> 2015 Del. Ch. LEXIS 18 (Del. Ch. Jan. 22, 2015).

<sup>113</sup> *Id.* at \*4

<sup>114</sup> *Id.* at \*3-4.

<sup>115</sup> *Id.* at \*2-5.

<sup>116</sup> *Id.* at \*38.

<sup>117</sup> See *supra* notes 7, 87 and accompanying text.

<sup>118</sup> 996 P.2d 230 (Colo. App. 1999).

her parents as trustee and herself as the beneficiary.<sup>119</sup> When she and her husband divorced, the trial court held that the assets in the trust were not marital property “because the proceeds here were in an irrevocable trust over which wife had no control.”<sup>120</sup> Instead, the creation of the trust and transferring of marital assets to the trust were merely “an economic circumstance” for the court to consider.<sup>121</sup> In dispensing with the husband’s argument to the contrary, the appellate court explained that it considered only the “the extent of the beneficiary’s right to or interest in the trust”—the source of the funds was irrelevant.<sup>122</sup> The appellate court recognized that “placing marital property into a trust would amount to dissipation of that property” in some instances, suggesting that the case before it might reasonably be perceived as such an instance.<sup>123</sup> However, the appellate court concluded that *Pooley* did not amount to a dissipation of marital property because the evidence before it did not establish that the transfer of settlement proceeds into a trust for the wife was created for an improper purpose, and the trial court expressly did not make that finding.<sup>124</sup>

Thus, impropriety is generally necessary to set aside the creation of a DAPT, and even then, the most unscrupulous of motivations may be barred by a statute of limitations.

## B. Ways Courts Have Invalidated DAPTs

### 1. Bankruptcy Proceedings

Bankruptcy courts have power to invalidate DAPTs that have been created within ten years of the filing for bankruptcy under 11 U.S.C. § 548(e)(1). A bankruptcy trustee may void<sup>125</sup> any transfer

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<sup>119</sup> *Id.* at 231.

<sup>120</sup> *Id.*

<sup>121</sup> *Id.*

<sup>122</sup> *Id.* at 232.

<sup>123</sup> *See id.* (citing *In re Marriage of Huston*, 967 P.2d 181 (Colo. App. 1998)).

<sup>124</sup> *Id.*

<sup>125</sup> The language of the statute uses “avoid.” 11 U.S.C. § 548(e)(1) (LEXIS through PL 114-165). However, there is no difference in meaning with “void.” *Avoid*, BLACK’S LAW DICTIONARY (10th ed. 2014) (defining avoid as “[t]o render void; void” and stating “[b]ecause this legal use of *avoid* can be

made on or within 10 years before the date of the filing of the petition, if—

- (A) such transfer was made to a self-settled trust or similar device;
- (B) such transfer was by the debtor;
- (C) the debtor is a beneficiary of such trust or similar device; and
- (D) the debtor made such transfer with actual intent to hinder, delay, or defraud any entity to which the debtor was or became, on or after the date that such transfer was made, indebted.<sup>126</sup>

Two federal bankruptcy cases have used this provision to invalidate DAPT transfers based on the finding that the debtor created the DAPT with “actual intent to hinder, delay, or defraud” creditors.

The first case, *Battley v. Mortensen*,<sup>127</sup> involved an Alaskan resident who transferred property to a DAPT, the “Mortensen Seldovia Trust,” which he attempted to establish under the laws of that state.<sup>128</sup> The debtor then filed for bankruptcy.<sup>129</sup> The bankruptcy trustee argued that the debtor was insolvent at the time of the creation of the trust.<sup>130</sup> Although the court found that the trust was correctly established under Alaska law, i.e., that the debtor’s assets exceeded his liabilities when the DAPT was created,<sup>131</sup> the court determined that he made the transfer to the DAPT with actual intent to defraud current and future creditors and voided the property transfer pursuant to section 548(e).<sup>132</sup> The court pointed to facts such as Mortenson was “coming off some very lean years,” accumulated credit card debt, and experienced “financial carnage” from his divorce to reach the conclusion that the transfer of property was evidence of his intent.<sup>133</sup> Despite the fact that the debtor alleged the DAPT was created to preserve property for his children, his actions of investing in the stock market using the trust and loaning to his acquaintances convinced the court otherwise.

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easily confused with the ordinary sense of the word, the verb *void* is preferable”).

<sup>126</sup> 11 U.S.C. § 548(e)(1).

<sup>127</sup> No. A09-00565-DMD, 2011 Bankr. LEXIS 5560 (Bankr. D. Alaska Jan. 14, 2011).

<sup>128</sup> *Id.* at \*5–6.

<sup>129</sup> *Id.* at \*10–11.

<sup>130</sup> *Id.* at \*12.

<sup>131</sup> *Id.* at \*16.

<sup>132</sup> *Id.* at \*21–23.

<sup>133</sup> *Id.* at \*20–21.

In a 2013 case, *Waldron v. Huber (In re Huber)*,<sup>134</sup> a bankruptcy trustee brought an action against the defendant bankruptcy debtor for a determination that the debtor's transfers to a DAPT were fraudulent.<sup>135</sup> The element at issue under the Bankruptcy Code was whether the transfers were made with "actual intent to hinder, delay, or defraud" creditors.<sup>136</sup> Quoting the Court of Appeals for the Ninth Circuit, the bankruptcy court explained that while "[t]he presence of a single badge of fraud may spur mere suspicion[,] the confluence of several can constitute conclusive evidence of actual intent to defraud."<sup>137</sup> The bankruptcy court acknowledged the following as the "badges of fraud" in this case: (1) creditors were already threatening litigation at the time of the transfers,<sup>138</sup> (2) those transfers included "all or substantially all" of Mr. Huber's property,<sup>139</sup> (3) Mr. Huber was significantly indebted at the time of the transfers,<sup>140</sup> (4) Mr. Huber was both the grantor and beneficiary of the trust,<sup>141</sup> and (5) Mr. Huber virtually retained the trust corpus.<sup>142</sup> Having been presented with no "significantly clear" evidence of a legitimate supervening purpose," the bankruptcy court found "actual fraudulent intent by the Debtor to hinder, delay, or defraud" necessary to void the transfers.<sup>143</sup>

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<sup>134</sup> 493 B.R. 798 (Bankr. W.D. Wash. 2013).

<sup>135</sup> *Id.* at 804-05.

<sup>136</sup> *Id.* at 810-11.

<sup>137</sup> *Id.* at 812 (quoting *Acequia, Inc. v. Clinton (In re Acequia, Inc.)*, 34 F.3d 800, 806 (9th Cir. 1994)). The "five badges of fraud" are

(1) actual or threatened litigation against the debtor; (2) a purported transfer of all or substantially all of the debtor's property; (3) insolvency or other unmanageable indebtedness on the part of the debtor; (4) a special relationship between the debtor and the transferee; and, after the transfer, (5) retention by the debtor of the property involved in the putative transfer.

*Id.* at 811-12.

<sup>138</sup> *Id.* at 812.

<sup>139</sup> *Id.* at 812-13.

<sup>140</sup> *Id.* at 813.

<sup>141</sup> *Id.*

<sup>142</sup> *Id.*

<sup>143</sup> *Id.* at 812, 814.

## 2. *Conflict of Laws Used to Invalidate DAPT*

*In re Huber* was decided under a conflicts of law analysis. Huber, a Washington resident, created a DAPT in Alaska and designated Alaska as the governing law.<sup>144</sup> Washington is a non-DAPT state, so the court did a conflict of laws analysis.<sup>145</sup> In the Ninth Circuit, federal courts follow a federal choice-of-law approach when jurisdiction is premised upon an exclusively federal question.<sup>146</sup> The Ninth Circuit's federal approach constitutes the *Restatement (Second) of Conflicts* approach.<sup>147</sup> Under this approach, a choice-of-law provision in the trust agreement is generally upheld if the designated state has a significant relationship to the trust.<sup>148</sup> Recognizing that all of the property in the DAPT was in Washington, except for a small certificate of deposit, and that the only relation to Alaska was that it was the location of the administration of the trust and the location of one of the trustees, the court found that Washington had the most significant relationship with the trust.<sup>149</sup> Washington also has a strong public policy against self-settled trusts and Washington's UFTA law voided the transfers to the DAPT.<sup>150</sup>

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<sup>144</sup> *Id.* at 805, 807.

<sup>145</sup> *Id.* at 807.

<sup>146</sup> *Id.* (quoting *Lindsay v. Beneficial Reinsurance Co.* (*In re Lindsay*), 59 F.3d 942, 948 (9th Cir. 1995)); *SEC v. Elmas Trading Corp.*, 683 F. Supp. 743, 747 (D. Nev. 1987). However, this view is not uniform. Compare *In re Lindsay*, 59 F. Supp. at 948 ("In federal question cases with exclusive jurisdiction in federal court, such as bankruptcy, the court should apply federal, not forum state, choice of law rules.") (citations omitted), and *Elmas Trading Corp.*, 683 F. Supp. at 747-748 (D. Nev. 1987) ("[T]his Court's jurisdiction derives from the interpretation of federal law. This conclusion would normally tend to indicate that some federal choice of law principle should apply . . .") with *Campbell v. Fawber*, 975 F. Supp. 2d 485, 506 (M.D. Pa. 2013) (applying Pennsylvania choice-of-law rules) and *In re Merritt Dredging Co.*, 839 F.2d 203, 205-06 (4th Cir. 1988) (citing *Klaxon Co. v. Stentor Elec. Mfg. Co.*, 313 U.S. 487, 496 (1941)) (holding that "in the absence of a compelling federal interest which dictates otherwise, the *Klaxon* rule should prevail where a federal bankruptcy court seeks to determine the extent of a debtor's property interest").

<sup>147</sup> *Huber*, 493 B.R. at 807 (citing *Liberty Tool & Mfg. v. Vortex Fishing Sys., Inc.* (*In re Vortex Fishing Sys., Inc.*), 277 F.3d 1057, 1069 (9th Cir. 2002)).

<sup>148</sup> *Id.* (quoting RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 270 (AM. LAW INST. 1971)).

<sup>149</sup> *Id.* at 808.

<sup>150</sup> *Id.*

In *Dahl v. Dahl*,<sup>151</sup> the wife challenged a DAPT in connection with a divorce proceeding before the Utah courts. The husband executed during the marriage The Dahl Family Irrevocable Trust naming himself as settlor and his brother as investment trustee.<sup>152</sup> The trust named the husband, his wife (as long as she remained his wife), and his issues as beneficiaries.<sup>153</sup> The trust also had a choice-of-law provision designating Nevada's law.<sup>154</sup> The husband and wife jointly deeded their primary residence to the trust, and the wife also contributed other marital property, including her interest in the husband's real estate company.<sup>155</sup> When the parties divorced, the wife argued that the trust assets were marital property.<sup>156</sup> The trial court applied Nevada law, ruling that the trust was irrevocable.<sup>157</sup> The Supreme Court of Utah applied Utah law to interpret the trust and invalidated it, saying that it was revocable because by the terms of the trust, the husband still could alter and amend the terms of the trust.<sup>158</sup> Because by the trust terms the wife was a beneficiary as long as she remained his spouse, the husband argued that the wife had no interest in the trust property due to the fact that the parties were divorced.<sup>159</sup> Under Utah law, a settlor is anyone who creates a trust or contributes property into the trust, so the wife was a settlor under Utah law because she contributed property and no facts suggest that she gave up this right.<sup>160</sup> Thus she could revoke any of her separate property or marital property in the trust. According to the court:

Were we to decide that Ms. Dahl had no enforceable interest in the Trust, despite having contributed marital property to it, the result would be to allow a spouse to shield marital property from equitable division in the event of divorce. And that is exactly what Dr. Dahl attempted to do in this case. He crafted a trust agreement purporting

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<sup>151</sup> 345 P.3d 566 (Nev. 2015).

<sup>152</sup> See *id.* at 575–76.

<sup>153</sup> *Id.* at 581.

<sup>154</sup> *Id.* at 578–79.

<sup>155</sup> *Id.* at 579.

<sup>156</sup> *Id.* at 576.

<sup>157</sup> *Id.* at 577; *Dahl v. Dahl*, No. 090402989 (Utah Dist. Ct. Nov. 1, 2011), [http://www.assetprotectionbook.com/casedocs/dahl/dahl\\_sj\\_01nov11.pdf](http://www.assetprotectionbook.com/casedocs/dahl/dahl_sj_01nov11.pdf).

<sup>158</sup> *Dahl*, 345 P.3d at 579–81.

<sup>159</sup> *Id.* at 581.

<sup>160</sup> *Id.* at 581–82.

to eliminate any interest Ms. Dahl had in the Trust property upon the couple's divorce. But Utah law does not allow spouses to place marital assets in revocable trusts and then shield those assets from equitable property division in the event of a divorce.<sup>161</sup>

The Utah court resolved whether this trust was revocable or irrevocable, but unfortunately, the court did not decide whether a spouse could validly create an irrevocable trust of marital property because the issue was not before the court.<sup>162</sup>

Although not expressly an invalidation of a DAPT, a Delaware court declined to exercise jurisdiction when a Kentucky court issued a status quo order on a Delaware trust. In *In re Kloiber*,<sup>163</sup> the husband's father created a trust under Delaware law for the husband, who would act as special trustee who could tell the trustee what to do, and designated a Delaware bank as trustee.<sup>164</sup> The husband and others were named as beneficiaries but the wife was not named; she was only referred to as "wife of Grantor's son" for the purpose of cutting her off as a beneficiary if they divorced.<sup>165</sup> When the parties divorced in Kentucky, the Kentucky court entered a status quo order pending the divorce proceedings so that neither side would dissipate marital property and identified the trust as an asset subject to the order.<sup>166</sup> The husband transferred his special trustee powers to his son.<sup>167</sup> The son made transfers in potential violation of the Kentucky court's order, but he claimed he was not a party to the divorce proceedings and therefore Kentucky had no jurisdiction over the administration of the trust.<sup>168</sup> The son also asked Delaware for a temporary restraining order to prevent having to follow the Kentucky court's orders and argued that Delaware had "exclusive jurisdiction" under the DAPT statute.<sup>169</sup> Having learned of the husband's resignation, the Kentucky court ordered the husband

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<sup>161</sup> *Id.* at 583.

<sup>162</sup> *Id.* at 583 n.13.

<sup>163</sup> 98 A.3d 924 (Del. Ch. 2014), *vacated*, No. 9685-VCL, 2014 Del. Ch. LEXIS 190 (Sep. 3, 2014).

<sup>164</sup> *Id.* at 928-31.

<sup>165</sup> *Id.* at 929.

<sup>166</sup> *Id.* at 928.

<sup>167</sup> *See id.* at 927 n.1, 928.

<sup>168</sup> *Id.* at 935.

<sup>169</sup> *Id.* at 937-38. The court noted that it was not technically the son that asserted the "exclusive jurisdiction" of Delaware but the trustee bank, which

to immediately revoke his previous resignation as Special Trustee and immediately reconstitute himself.<sup>170</sup> The Delaware Chancery Court declined to exercise jurisdiction to the exclusion of any rulings emanating from a Kentucky divorce proceeding concerning a Delaware APT, citing both Delaware statutory law as well as the federal pre-emption doctrine and the Full Faith and Credit Clause.<sup>171</sup> The court reasoned that “exclusive jurisdiction” in the Delaware statute did not mean jurisdiction among other states, only within courts of Delaware.<sup>172</sup> However, the Delaware court suggested that a fraudulent transfer judgment issued by the Kentucky court might be treated differently, i.e., that it may not be upheld by Delaware, from a judgment concerning the division of marital assets or claims for spousal support, i.e., that this is something the Kentucky court could do.<sup>173</sup>

### 3. Control Might Invalidate DAPT

In the Tennessee case of *Barnett v. Barnett*,<sup>174</sup> the court of appeals affirmed the decision of the trial court and found the self-settled spendthrift trust to be void *ab initio*, since the beneficiary husband was directing the trustee how to spend the money, and thus, the trust was not effective to insulate the property from marital claims of the wife.<sup>175</sup> During the marriage, the husband told the wife that he was transferring four pieces of real estate into a trust to “protect their assets from creditors” and made her trustee of the trust.<sup>176</sup> The trust gave the husband the power to relieve the trustee and appoint a substitute with ten days’ notice, and it gave the trustee sole discretion to pay to the grantor such amounts of net income and principal from the trust estate as the

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made the assertion in its own petitions and in support of the son’s temporary restraining order. *Id.* at 938.

<sup>170</sup> *Id.* at 936.

<sup>171</sup> *Id.* at 938–40.

<sup>172</sup> *Id.* at 939 (“When a Delaware state statute assigns exclusive jurisdiction to a particular Delaware court, the statute is allocating jurisdiction among the Delaware courts. The state is not making a claim against the world that no court outside of Delaware can exercise jurisdiction over that type of case.”).

<sup>173</sup> *Id.* at 941.

<sup>174</sup> No. E2008-02679-COA-R3-CV, 2010 Tenn. App. LEXIS 170 (Tenn. Ct. App. Feb. 26, 2010).

<sup>175</sup> *Id.* at 2, 17–19.

<sup>176</sup> *Id.* at 10–11.



trustee deemed “necessary for the health, support, and maintenance of the [g]rantor.”<sup>177</sup> After the divorce was filed against the husband, the husband relieved his wife as the trustee, and named his niece as the next trustee.<sup>178</sup> Due to the collective actions of the husband in controlling the assets, the court invalidated the trust and allowed the four pieces of marital property to be sold as part of the divorce.<sup>179</sup>

#### 4. *The Contract Clause of the U.S. Constitution Might Invalidate DAPTs*

Randall B. Wilhite explained that a potential challenge of existing creditors to DAPTs might be the contract clause of the U.S. Constitution which prohibits states from passing legislation that “substantially impair the obligations of parties to existing contracts or make them unreasonably difficult to enforce.”<sup>180</sup> Yet, Wilhite notes the counter argument is that “the contractual rights of existing creditors have not been impaired; rather, merely the remedies available to these creditors to enforce these rights have been affected.”<sup>181</sup>

### **IV. Limited Remedies if DAPTs With Marital Property Are Validated**

In the event that the court does validate a DAPT created with marital property, there are limited remedies for the non-beneficiary spouse.

#### A. *Avoid the Transfer by Using UFTA/UVTA or Bankruptcy Code*

A spouse can attack the transfer under either state law or federal law. Under state law, the spouse can use the state’s

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<sup>177</sup> *Id.*

<sup>178</sup> *Id.* at 10.

<sup>179</sup> *Id.* at 17–19.

<sup>180</sup> Randall B. Wilhite, Fullenweider Wilhite, P.C., *Attacks on Domestic Asset Protection Trusts*, American Academy of Matrimonial Lawyers Mid-Year Meeting in Nassau, Bahamas (Mar. 14–18, 2016) (citing Duncan E. Osborne et al., *Asset Protection: Trust Planning*, SJ036 ALI-ABA 1419, 1446 (ALI-ABA C.L.E. Annual Advanced Course of Study (Nov. 17–21, 2003))).

<sup>181</sup> *Id.* (citing Richard W. Nenno, *Planning With Domestic Asset-Protection Trusts: Part I*, 40 REAL PROP. PROB. & TR. J. 263, 331 (2005)).

fraudulent transfer or voidable transaction statute as long as the spouse resides in a non-DAPT state. Under federal law, the spouse can use the Uniform Fraudulent Transfer Act (“UFTA”) and Section 548 of the Bankruptcy Code to void property transfers made with “intent to hinder, delay, or defraud” creditors.<sup>182</sup> Although amendments in 2014 renamed the UFTA as the Uniform Voidable Transactions Act (“UVTA”)<sup>183</sup> and the amended UVTA featured several changes from UFTA, this language remained the same. The change in the title is intended to make clear that proof of fraud is not needed to establish a voidable transfer.<sup>184</sup> Nine states enacted the UVTA and seven states have introduced the legislation; none of the states that have enacted UVTA is a DAPT state, and of those where a bill has been introduced, only Rhode Island is a DAPT state.<sup>185</sup>

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<sup>182</sup> 11 U.S.C. § 548(a)(1)(A) (LEXIS through PL 114-165); UNIF. FRAUDULENT TRANSFER ACT § 4(a)(1) (amended 2014) (UNIF. LAW COMM’N 1984). Another way to void the transfer is if the debtor did not receive reasonable equivalent value in a transaction and was either insolvent, about to enter into a business transaction for which they have unreasonably small capital, or is expected to incur debts beyond the ability to pay. 11 U.S.C. § 548(a)(1)(B); UNIF. VOIDABLE TRANSFER ACT §§ 4(a)(2), 5(a).

<sup>183</sup> See UNIF. VOIDABLE TRANSACTIONS ACT § 4(a)(1).

<sup>184</sup> *Id.* §§ 15 cmt. 1; Gary A. Forster & Eric C. Boughman, *The Uniform Voidable Transactions Act: An Overview of Refinements to the Uniform Fraudulent Transfer Act*, 29 PROB. & PROP. 51, 51–52 (2015).

<sup>185</sup> See CAL. CIV. CODE § 3439 (Deering 2015); GA. CODE ANN. §§ 18-2-70 to -85 (LEXIS through the 2015 Regular Session); IDAHO CODE § 55-910; IOWA CODE §§ 684 (LEXIS through all legislation signed as of May 27, 2016 from the 2016 Second Regular Session of the 86th General Assembly); KY. REV. STAT. ANN. §§ 378A.005–378A.140 (LEXIS through the 2016 Legislative Session, not including changes and corrections made by the Kentucky Reviser of Statutes); MINN. STAT. §§ 513.41–513.51 (LEXIS through Act chapter 138, except for ch’s 99, 125, and 135 of the 2016 Regular Session); N.M. STAT. ANN. §§ 56-10-14 to -29 (LEXIS through the end of the 2d Regular session (2016) of the 52d Legislature); N.C. GEN. STAT. §§ 39-23.1 to -23.12 (LEXIS through Session Laws 2016-3, 2016 2nd Extra Session); N.D. CENT. CODE § 13-02.1-01 to -13 (LEXIS through all acts signed by the governor through the end of 2015 Regular Legislative Session including changes and corrections made by the North Dakota Code Revisor). States that have introduced the legislation include: Indiana, SB 68; Massachusetts, HB 35; Michigan, SB 982; New Jersey, AB 3742; New York, SB 7687; Rhode Island, HB 7960; South Carolina, HB 5234. *Voidable Transactions Act Amendments (2014) - Formerly Fraudulent Transfer Act*, UNIF. LAW COMM’N, <http://www.uniformlaws.org/Act.aspx?ti>

The UVTA, unlike the UFTA, includes a choice of law provision designating the law of the jurisdiction where the settlor lived at the time of the transfer.<sup>186</sup> If a debtor lives in a jurisdiction with a DAPT statute and sets up a trust that complies with the requirement under that state's law, then under the UVTA, the trust will be insulated from attack except to the extent provided by the DAPT statute.<sup>187</sup> However, if a debtor lives in a jurisdiction without a DAPT statute and sets up a trust in a jurisdiction with a DAPT statute, states will take one of three approaches when determining the validity of a transfer depending on where the DAPT is attacked. If the DAPT transfer is attacked in a jurisdiction that has enacted UVTA, the validity of the transfer is governed by the law of the jurisdiction where the settlor lived at the time of the transfer.<sup>188</sup> The common law rule can void the transfer because there is a conclusive presumption that transfers to a self-settled spendthrift trust were to hinder, delay, or defraud creditors.<sup>189</sup> If the DAPT transfer is attacked in a

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tle=voidable%20Transactions%20Act%20Amendments%20(2014)%20-%20Formerly%20Fraudulent%20Transfer%20Act.

<sup>186</sup> UNIF. VOIDABLE TRANSACTIONS ACT § 10.

<sup>187</sup> *See id.* § 10(b).

<sup>188</sup> *See id.*

<sup>189</sup> *See, e.g.,* Rush Univ. Med. Ctr. v. Sessions, 980 N.E.2d 45, 50 (Ill. 2012) (referring to “the common law rule that a person cannot settle his estate in trust for his own benefit so as to be free from liability for his debts”); *Cohen v. Comm’r of the Div. of Med. Assistance*, 668 N.E.2d 769, 777–78 (Mass. 1996) (“Not only the courts of this State, but those of many other jurisdictions have long followed this Restatement principle.”) (citing *Ware v. Gulda*, 331 Mass. 68, 70, 117 N.E.2d 137 (1954); *Merchants Nat’l Bank v. Morrissey*, 109 N.E.2d 821 (Mass. 1953); RESTATEMENT (SECOND) OF TRUSTS § 156 n.1 (AM. LAW INST. 3d ed. 1967 & Supp. 1985)); *Aronsohn & Springstead v. Weissman*, 552 A.2d 649, 651–53 (N.J. Super. Ct. App. Div. 1989) (“Statutes and cases in the law of trusts have repeatedly held that a spendthrift trust created by the settlor and which names him or her as sole beneficiary of the trust res is void as against present and future creditors . . . the strong common law policy of spendthrift trusts . . . would be subverted. . . . [if d]ebtors could shelter funds . . . immediately before declaring bankruptcy . . .”) (citing *Hebert v. Fliegel*, 813 F.2d 999, 1002 n.3 (9th Cir. 1987); *Matter of Goff*, 706 F.2d 574 (5th Cir. 1983)). The Fraudulent Conveyances Act of 1571 declared that “[f]eigned, covinous, and fraudulent’ transfers were declared ‘to be clearly and utterly void, frustrate, and of none effect, any pretence, color feigned consideration, expressing of use or any other matter or thing to the contrary notwithstanding.’” Earl D. Tanner Jr., *Rethinking Asset Protection Trusts*, 28 UTAH B.J. 42, 42–43 (2015) (citing Fraudulent Convey-

jurisdiction without the UVTA, the court may apply the *Restatement (Second) of Conflict of Laws* and thereby the law of the jurisdiction with the most significant relationship to the transaction: which could be where the debtor lives, where the property is located, or where the trust is administered; however, the policies of the state—particularly, a strong policy in favor of the equitable distribution of property in a divorce—could also dictate the result.<sup>190</sup> If the DAPT transfer is attacked in the bankruptcy court, it is not clear which state's law will be applied.<sup>191</sup>

### B. Other Assets

In *In re Marriage of Pooley*,<sup>192</sup> the court stated that the validly created irrevocable trust the wife created with marital property was an “economic circumstance” the court could consider when equitably distributing other property deemed marital.<sup>193</sup> This suggests that the court can award the non-beneficiary spouse more marital property because the beneficiary spouse has the benefit of the trust assets. In effect, the DAPT would be substantially defeated where that additional award is comparable to what would have been given if the DAPT was invalid.

In *Dahl v. Dahl*,<sup>194</sup> the Utah Supreme Court explained that Utah's DAPT formulation permitted a spouse to revoke the property that he or she contributed to the trust.<sup>195</sup> Using the facts of *Dahl* as an example, the court stated that the wife could revoke the trust as pertaining to the marital home.<sup>196</sup> The home would be completely withdrawn from the trust and its worth would be split between the husband and wife.<sup>197</sup> However, if the husband wanted to retain the home as part of the trust, the court

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ances Act 1571, 13 Eliz c. 5 (Eng.)). The Anglo-American common law applied this notion “to facts in which a debtor transferred assets to a trust but retained some beneficial interest in the trust.” *Id.* at 43. In effect, the “self-settled trusts were ignored, and creditors of the settlor were permitted to reach all transferred assets.” *Id.*

<sup>190</sup> See *supra* Section III(B)(2).

<sup>191</sup> See *supra* note 146.

<sup>192</sup> 996 P.2d 230 (Colo. App. 1999).

<sup>193</sup> *Id.* at 232.

<sup>194</sup> 345 P.3d 566 (Utah 2015).

<sup>195</sup> *Id.* at 582 n.11.

<sup>196</sup> *Id.*

<sup>197</sup> *Id.*

could award additional money to wife as “an equitable offset of half the property’s value” to the wife.<sup>198</sup>

### C. *Trustee as a Party/Writ of Attachment*

The parties may also attempt to add the trustee as a party and have the court issue a writ of attachment over the DAPT as long as there is personal jurisdiction over the trustee. However, in the case of *Hanson v. Denckla*,<sup>199</sup> the U.S. Supreme Court held that a Florida court did not have jurisdiction over the Delaware trustee or its assets,<sup>200</sup> and thus the Delaware court need not give full faith and credit to the Florida court’s decision regarding the trust’s validity.<sup>201</sup>

## V. Ethical Problems With Transfers of Assets to DAPTs

In DAPT states, attorneys who prepare the trust property and place the assets into the trust are typically at low risk for violations of professional responsibility rules, especially when they state the purpose of the trust in the trust instrument, e.g., for estate planning purpose.<sup>202</sup> However, an attorney who represents both the husband and the wife when DAPTs are created may be at risk of legal and ethical problems for failure to disclose the consequences to the spouses.<sup>203</sup> Take the example of the couple who want to transfer both separate and marital assets into a DAPT. If the spouse who had separate property in that trust did not know that placing separate assets into this DAPT commingles the assets, the attorney who failed to disclose this may have exposure to that spouse.

In a non-DAPT state, attorneys are most at risk if they assist in transferring assets into a DAPT.<sup>204</sup> If a given state still follows the UFTA, the transfer is fraudulent if a party and/or that party’s

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<sup>198</sup> *Id.*

<sup>199</sup> 357 U.S. 235 (1958).

<sup>200</sup> *Id.* at 248.

<sup>201</sup> *Id.* at 255.

<sup>202</sup> See Henry J. Lischer, Jr., *Professional Responsibility Issues Associated with Asset Protection Trusts*, 39 REAL PROP. PROB. & TRUST J. 592, 611 (2004).

<sup>203</sup> See MODEL RULES OF PROF’L CONDUCT r. 1.7 (AM. BAR ASS’N 2016).

<sup>204</sup> Lischer, *supra* note 202, at 611–25.

attorney defrauds, hinders, or delays the other spouse. Because not all of the states with DAPTs have adopted the UVTA or UFTA, then the transfer of assets into the trust is not necessarily a violation of UFTA or UVTA. The lawyer in the non-DAPT state also runs the risk of violating the disciplinary rules and the Model Rules of Professional Responsibility, as well as aiding and abetting a tort, and committing the tort of civil conspiracy to defraud creditors.<sup>205</sup> Moreover, the “communications about an APT transfer might provide evidence of an intent to frustrate courts or creditors,” so the court might apply the crime-fraud exception to pierce the attorney-client privilege.<sup>206</sup>

## VI. Need for Statutory Change With Respect to Marital Property

The *Dahl* case left open the question whether an irrevocable trust could ever be created with marital property by a spouse.<sup>207</sup> The *Pooley* case seemed to allow it.<sup>208</sup> Although the statutes themselves do not prohibit the transfer of marital property into a DAPT, the statutes are also silent on whether a valid transfer of marital property into a DAPT by one spouse is permitted. Arguably transferring marital assets into a DAPT by a spouse could be deemed dissipation of marital assets, so spouses who wish to create these trusts should have some statutory protection. Courts have interpreted transfers of assets into irrevocable trusts to be either separate property or marital property subject to equitable division, but there needs to be clear statutory guidance to the spouse of the consequences. Indeed, there should be some statutory protections in place so that one spouse does not take advantage of the other spouse and that the parties' intent should be respected. Recognizing that non-DAPT states could invalidate a DAPT and refuse to enforce a valid DAPT created in a DAPT state based on conflict of laws and public policy, this article seeks only to clarify the statutes in DAPT states that provide protections for DAPT residents to create more certainty for couples wishing to create DAPTs during marriage.

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<sup>205</sup> *Id.* at 620–23.

<sup>206</sup> *Id.* at 619–20.

<sup>207</sup> *See supra* note 162 and accompanying text.

<sup>208</sup> *See supra* notes 122–24 and accompanying text.

### A. Presumptions

If a DAPT is executed during the marriage, the assets in the DAPT are marital unless the other spouse signs a waiver. This is similar to ERISA rules when waiving a spouse's rights to the retirement benefits.<sup>209</sup>

### B. Prenuptial/Postnuptial Language

To make a valid prenuptial agreement, generally, the parties have to knowingly enter into the agreement. The parties have to know the consequences of their actions. Parties wishing to create DAPTs during marriage with marital property should likewise have the same statutory safeguards.

Although Tennessee is not a community property state, spouses can opt into a community property status via the Tennessee Community Property Trust Act of 2010 ("CPT").<sup>210</sup> This law allows married couples to create a joint revocable trust and convert assets into community property to receive the step-up basis for tax benefits. The requirements for a CPT creation are that the trust agreement states that it is a Tennessee Community Property Trust, at least one trustee is a resident of Tennessee, it is signed by both spouses, and it contains a notice provision at the beginning of the trust in capital letters spelling out the consequences of the trust.<sup>211</sup> However, there is no warning to the un-

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<sup>209</sup> 29 U.S.C. § 1055(c)(2) (LEXIS through PL 114-165); *Boggs v. Boggs*, 520 U.S. 833, 869 (1997) (citing 29 U.S.C. § 1055(c)) (acknowledging that a waiver is required for a spouse to not receive the provided benefits); *IBEW Pac. Coast Pension Fund v. Lee*, 462 F. App'x 546, 549-50 (6th Cir. 2012) (quoting *Hagwood v. Newton*, 282 F.3d 285, 288-89 (4th Cir. 2002) ("[T]he formalities required in § 1055(c) are included to protect against the risks of a spouse's unwitting waiver of [the spousal rights conferred by § 1055(a)].")); *Ponsetti v. GE Pension Plan*, 614 F.3d 684, 687 (7th Cir. 2010) (citing 29 U.S.C. § 1055(c)(2)(A)(iii)) (referring to the specific requirements for spousal waiver under ERISA); *Nat'l Auto. Dealers & Assocs. Ret. Tr. v. Arbeitman*, 89 F.3d 496, 502 (8th Cir. 1996) ("ERISA[ ] . . . requires the participant's spouse to consent in writing to the election, the election to designate a specific beneficiary, the spouse's consent to acknowledge the effect of the election, and the consent to be witnessed by a plan representative or notary public.") (citing 29 U.S.C. § 1055(c)).

<sup>210</sup> TENN. CODE ANN. §§ 35-17-101 to -108 (LEXIS through the 2015 Regular Session).

<sup>211</sup> *Id.* § 35-17-103. The required language that must be included at the beginning of the trust document is the following:

sophisticated that placing separate property into a Community Property Trust loses its characteristic of separateness. There should be legislation in the DAPT states that require the same scrutiny of DAPTs as antenuptial agreements.<sup>212</sup>

### C. Need for Uniformity

#### 1. In Equitable Distribution Jurisdiction

J. Thomas Oldham has advocated for a new Uniform Equitable Distribution Jurisdiction Act to guide courts and to reduce forum shopping in divorce proceedings.<sup>213</sup> Child support and child custody issues are guided by the Uniform Interstate Family Support Act (“UIFSA”) and the Uniform Child Custody Jurisdiction and Enforcement Act (“UCCJEA”), respectively, which provide clarity for courts when deciding which state has jurisdiction to decide these issues.<sup>214</sup> All states have adopted the UIFSA, and all but Massachusetts have adopted the UCCJEA.<sup>215</sup> Thus, there is uniformity and certainty among the

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THE CONSEQUENCES OF THIS TRUST MAY BE VERY EXTENSIVE, INCLUDING, BUT NOT LIMITED TO, YOUR RIGHTS WITH YOUR SPOUSE BOTH DURING THE COURSE OF YOUR MARRIAGE AND AT THE TIME OF A DIVORCE. ACCORDINGLY, THIS AGREEMENT SHOULD ONLY BE SIGNED AFTER CAREFUL CONSIDERATION. IF YOU HAVE ANY QUESTIONS ABOUT THIS AGREEMENT, YOU SHOULD SEEK COMPETENT ADVICE.

*Id.* § 35-17-103(4).

<sup>212</sup> Cf. David A. Warren, *Use of Asset Protection Trusts in Lieu of or in Conjunction With Prenuptial Agreements*, Bridgeford Trust Company, at 5 (last visited Apr. 5, 2016), available at <http://bridgefordtrust.com/wp-content/uploads/2013/11/11.18.13-Use-of-Asset-Protection-Trust-in-Lieu-of-or-Conjunction-with-Pre-2.pdf>. Mr. Warren finds the advantages of DAPTs to prenuptial agreements are that DAPTs have no disclosure requirement and the trust can be established, signed and funded moments before the wedding.

<sup>213</sup> J. Thomas Oldham, *Why a New Uniform Equitable Distribution Jurisdiction Act Is Needed to Reduce Forum Shopping in Divorce Litigation*, 49 FAM. L.Q. 359 (2015).

<sup>214</sup> UNIF. INTERSTATE FAMILY SUPPORT ACT (amended 2008) (UNIF. LAW COMM’N 2008); UNIF. CHILD CUSTODY JURISDICTION & ENF’T ACT (UNIF. LAW COMM’N 1997).

<sup>215</sup> *Interstate Family Support Act Amendments (2008)*, UNIF. LAW COMM’N, [http://www.uniformlaws.org/Act.aspx?title=interstate%20Family%20Support%20Act%20Amendments%20\(2008\)](http://www.uniformlaws.org/Act.aspx?title=interstate%20Family%20Support%20Act%20Amendments%20(2008)); *Child Custody Jurisdiction and*



states regarding which state has jurisdiction to decide child support and custody issues, the uniformity and certainty of which do not exist when courts are faced with equitable division of property in divorce proceedings. Each state has its own rules regarding what marital property is, so equitable distribution can vary substantially among states. Courts that assume jurisdiction over equitable distribution issues apply the local law of the state in which the court sits. Thus, without guidance, litigants are encouraged to forum shop for whichever state has more favorable laws. As long as the court has personal jurisdiction over the parties and one of the parties satisfies the divorce residency requirement, the court may issue an equitable distribution award. As it relates to DAPTs, a party may choose a forum that has more favorable DAPT laws. Uniformity is needed to reduce the settlor's ability to gain an advantage on an unsuspecting spouse or other creditor.

## 2. *In a Child Support Exception*

Yet at the same time, uniformity is needed for more than a reduction of forum shopping. The DAPT settlors' children remain an unintended victim of the state legislatures' attempts to bring additional revenue into their respective states through DAPTs as the states that do not permit an exception for child support claims allow the settlor to shield his assets where such claims are asserted. Considerations of public policy and morality demand that children, blameless for the affairs of their parents, not be left out in the cold by DAPTs.<sup>216</sup> Protections that apply only if the settlor is in default of child support payment by thirty days or more do nothing if the settlor subsequently defaults, which includes the children of a marriage not yet dissolved or even children not yet born, and therefore are not enough.<sup>217</sup>

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*Enforcement Act*, UNIF. LAW COMM'N, <http://www.uniformlaws.org/Act.aspx?title=child%20Custody%20Jurisdiction%20and%20Enforcement%20Act>.

<sup>216</sup> Maxwell, *supra* note 6, at 500–05. Maxwell further suggests an economic upside to legislating a child support exemption to DAPTs in every state as children in need of support receive it from the taxpayers if not their parents. *Id.* at 505–06 (citing Steve Hargreaves, *Deadbeat Parents Cost Taxpayers \$ 53 Billion*, CNN MONEY (Nov. 5, 2012, 5:42 AM), <http://money.cnn.com/2012/11/05/news/economy/unpaid-child-support>).

<sup>217</sup> *Id.* at 497–98.

Several states do not even provide this feeble protection.<sup>218</sup> All that is needed is the simple language of a state such as Delaware: “With respect to the limitations imposed by [the DAPT statute], those limitations on actions by creditors to avoid a qualified disposition shall not apply [t]o any person to whom the transferor is indebted on account of an agreement or order of court for the payment of support . . . in favor of such transferor’s . . . children.”<sup>219</sup>

#### D. *The Effectiveness of DAPTs*

DAPTs may not even be the best method of achieving the settlor’s goals. Tennessee attorney Steve McDaniel believes that DAPTs<sup>220</sup> are working well in Tennessee but are relatively uncommon.<sup>221</sup> He is not a fan of DAPTs, however, believing them to be the product of good legislation but hardly the best option available.<sup>222</sup> Mr. McDaniel suggests that a tenancy by the entirety trust<sup>223</sup> or a spousal gift trust would function with similar

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<sup>218</sup> See *infra* notes 38–50 and accompanying text.

<sup>219</sup> DEL. CODE ANN. tit. 12, § 3573(1) ((LEXIS through 80 Del. Laws, ch. 261).

<sup>220</sup> DAPTs are known as Tennessee Investment Service Trusts in Tennessee. See TENN. CODE ANN. § 35-16-101 (LEXIS through the 2015 Regular Session).

<sup>221</sup> E-mail from A. Stephen McDaniel, Williams McDaniel, to author (May 27, 2016) (on file with author).

<sup>222</sup> *Id.* (“Clients don’t like creating an irrevocable trust and losing control!”). Mr. McDaniel has previously acknowledged the difficulties of the Tennessee version of the DAPT, noting that it is not for those with large debt obligations, knowledge of any possible claims against them, a desire to hide assets, or, most importantly, need frequent access to the protected assets. A. Stephen McDaniel, Wyatt, Tarrant & Combs, LLP, *Asset Protection: More to Think About Than Ever Before* (Sept. 2009)

<sup>223</sup> The Tennessee legislature has provided for the use of Tenancy by the Entirety Joint Revocable Trusts in Tennessee Code Annotated § 35-15-510. C. MICHAEL ADAMS, JR., TRUST LAW UPDATE: TWO NEW TRUSTS IN TENNESSEE AND HOW TO “FIX” OLD TRUSTS 6. This statutory creation largely resembles its common law counterpart in notably that should the debtor spouse die before the creditors execute on his or her debts, all assets held in the trust will pass to the non-debtor spouse free and clear. *Id.* at 6–8. However, a different result is obtained with the new trust if the non-debtor spouse dies first. In that case, at least one-half of the trust should remain exempt from the surviving debtor spouse, which is in contrast to the common law tenancy by the entirety, where

success yet also permit the family to retain control.<sup>224</sup> He acknowledges a trend toward the utilization of DAPTs but also cites the slow pace of this trend as evidence that Tennessee is no outlier in the use of DAPTs.<sup>225</sup> Mr. McDaniel believes that “more states would have adopted [DAPT] legislation” if the demand for DAPTs was high.<sup>226</sup>

Yet in Tennessee, the spendthrift provision of the DAPT remains a strong protection from all creditors, including spouses.<sup>227</sup> Notably, a trustee may simply pay a beneficiary’s expenses rather than the beneficiary directly, cannot be garnished, and may not be liable to the beneficiary’s creditors.<sup>228</sup> Further, a creditor cannot force the trustee to distribute to the beneficiary, even if the beneficiary has such power.<sup>229</sup> The DAPT still provides a tantalizing and effective vehicle to achieve a settlor’s unscrupulous goals.

## CONCLUSION

DAPTs are complex trusts that are under scrutiny by the courts. It is imperative that when a party wishes to place marital assets into a self-settled trust that the other spouse is aware and knows of the consequences in the event there is a divorce. It appears that these DAPTs were created to minimize taxes, but little if any thought was given to situations involving a divorce. Thus, estate planning attorneys need to consult with the domestic bar to ensure full disclosure of the consequences of their actions in setting up these DAPTs and to properly advise their clients of all of their repercussions.

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none of the assets would be exempt from the surviving debtor spouse’s creditors. *Id.*

<sup>224</sup> E-mail from A. Stephen McDaniel, *supra* note 221.

<sup>225</sup> *Id.* (“I think the fact that so few states have created them is indicative of how few have actually been implemented around the country.”).

<sup>226</sup> *Id.*

<sup>227</sup> See Robert D. Malin, Tennessee “Uniform Trust Code”: The 2013 Amendments (Feb. 11, 2016).

<sup>228</sup> *Id.*

<sup>229</sup> *Id.*