THE REVOCABLE ASSET PRESERVATION TRUST

New Planning Horizons from Oklahoma

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DRAFTING AND ADMINISTRATION ISSUES
FOR THE
NON-OKLAHOMA U.S. CITIZEN SETTLOR
OF AN
OKLAHOMA PRESERVATION TRUST

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I. The Perspective of My Analysis

I am going to consider the efficacy of the new Oklahoma Family Wealth Preservation Trust Act ("OKFWPTA") for either a Virginia or District of Columbia ("DC") domiciliary. Somewhat different considerations apply because Virginia is one of the 15 states which have sanctioned self-settled spendthrift trusts – Domestic Asset Protection Trusts ("DAPTs") – and DC has not adopted a DAPT statute.

In considering whether and how a trust established under the OKFWPTA may be useful to a Virginia or District of Columbia domiciliary, I will focus particularly on drafting and administration issues.

I will consider three unique features of the new Oklahoma law and speculate on how courts may react to them.

I will take as a framework for analysis the considerable body of applicable case law which has developed in the past few years as various state and federal bankruptcy courts in jurisdictions which do and do not have DAPTs have considered the extent to which domiciliaries of such states may protect themselves from creditors by using DAPTs in other states authorizing them.

I will also briefly discuss possibly relevant issues under the U.S. Constitution and otherwise that remain largely unexplored by the courts.

II. Cases Considering DAPTs to Date

A number of cases over the last three years have considered trusts created under the laws of states that recognize DAPTs, and NONE has recognized the effectiveness of the transfer against creditor claims. Notable among these are Battley v. Mortensen, 2011 Bankr. LEXIS 5004, 2011 WL 5025288 (Bankr. D. Alaska Jan. 14, 2011) and In re Huber, 493 B.R. 798, 2013 Bankr. LEXIS 2038, 2013 WL 2154218 (Bankr. W.D. Wash. 2013).

In re Huber involved an attack by creditors of a Washington State domiciliary against assets he had contributed to an Alaska DAPT. The facts were bad: a Washington real estate developer established an Alaska DAPT after the 2008 Wall Street Crash foreseeing that his ability to repay loans would be problematic. The Washington State Bankruptcy court applied Washington's law of fraudulent conveyance and found the funding of the Alaska trust to be a voidable fraudulent conveyance under Bankruptcy Code Section 544(b)(1), which recognizes applicable state law of fraudulent conveyance, and under Bankruptcy Code Section 548(e), which permits voiding of a transfer to a DAPT made within 10 years before filing a bankruptcy petition if made with actual intent to defraud creditors.

The court also looked at the conflict-of-laws issues, and found that Washington State had the most significant contacts with the trust, citing section

270 of the Restatement (Second) of Conflict of Laws and Washington's strong public policy against DAPTs.

Similarly, in Battley v. Mortensen, an Alaska Bankruptcy Court allowed a bankruptcy trustee to recover assets transferred to a Alaska DAPT under the same 10-year clawback provision of Bankruptcy Code Section 548(e). Very bad language for DAPT planners is found in the Battley v. Mortensen opinion, arguably in dicta:

> "I conclude that a Settlor's expressed intention to protect assets placed in a self-settled trust from a beneficiary's 'potential future creditors' (emphasis added) can be evidence of an intent to defraud. The express purpose of the trust was 'to maximize the protection of the trust estate... from creditor's claims of the Grantor...'"

It is conventional wisdom under traditional common law that it is perfectly proper to establish a DAPT to protect from "potential future creditors."

It merits our attention that in Matter of Morris, 2013 WL 6598701 (Calif.Bar.Ct., unpublished, December 4, 2013) an attorney was suspended from practice for two years for aiding and abetting in a fraudulent transfer.

Other recent "bad" cases for DAPTs cited by Professor Jonathan Pennell of Emory Law in an outline he presented at the Heckerling Institute on Estate Planning in 2014 include the following:

U.S. v. Eversoff 528 Fed. Appx. 75 (2d Cir. N.Y. 2013)

Kilker v. Stillman 2012 Cal. App. Unpub. LEXIS 8542, 2012 WL 5902348 (Cal. App. 4th Dist. Nov. 26, 2012)

U.S. v. Spencer 2012 U.S. Dist. LEXIS 142195, 2012-2 U.S. Tax Cas. (CCH) P50,610, 110 A.F.T.R.2d (RIA) 6224, 2012 WL 4577927 (N.D. Okla. 2012)

Rush University Medical Center v. Sessions, 956 N.E.2d 490 (Ill. App. Ct. 1st Dist. 2011)

Watterson v. Burnard 986 N.E.2d 604 (Ohio Ct. App., Lucas County 2013)

Other "bad" DAPT court decisions include:

Dahl. v. Dahl 2015 UT 23, 2015 Utah LEXIS 51, 779 Utah Adv. Rep. 13 (Utah 2015)

Kloiber v. Daniel Kloiber Dynasty Trust 2014 Ky. App. Unpub. LEXIS 929 (Ky. Ct. App. Dec. 5, 2014)

IMO Daniel Kloiber Dynasty Trust 98 A.3d 924, 2014 Del. Ch. LEXIS 140 (Del. Ch. 2014)

In summary, US have courts have uniformly ruled against the efficacy of DAPTs, and that is true even of courts of states with DAPT statutes and federal courts within states with DAPT statues.

III. The Full Faith and Credit Issue Under the U.S. Constitution

(a) The issue: If a non-DAPT forum court, which has jurisdiction over a DAPT trust created under one of the DAPT statutes, applies the forum state's own law and finds the spendthrift provisions invalid, must the DAPT court recognize that judgment?

(b) The Authority:

1. The full faith and credit clause of Article IV of the U.S. Constitution requires that each state give full faith and credit to the judicial proceedings of every other state.

2. However, whether assets are exempt from the claims of creditors is determined by the law of the state where the assets are located. See Restatement (Second) of Conflict of Laws §132 (1971). Therefore, when a creditor asks a DAPT court to enforce a sister state's judgment against the trust assets, the DAPT court would use it's own state's exemption laws.

3. Note that in theory a DAPT jurisdiction's court could, under general conflicts of laws principles, decide that a sister state has a greater interest in the trust and apply that state's law, but query how likely this is given the clear legislative purpose of these statues. Surprisingly, in IMO Daniel Kloiber Dynasty Trust (supra.), that is exactly what happened.

4. There is no case law on point.

IV. The "Supremacy Clause" of the U.S. Constitution

Under the U.S. Constitution's Supremacy Clause, in Article VI, Section 2, federal courts are not bound by state laws. Accordingly there is a risk that if a judgment creditor is able to obtain jurisdiction over a judgment debtor or the debtor's assets held in a DAPT by virtue of federal question jurisdiction or diversity jurisdiction, the creditor will have the opportunity to avoid the debtor-friendly provisions of the DAPT jurisdiction's laws. The harsh provisions of the federal bankruptcy laws – e.g., the 10-year clawback provision of Section 548(e) of the Bankruptcy Code – are a particular threat to DAPTs.

There is no case law on point.

V. "Contract Clause" Concerns

The Constitution prohibits states from enacting any law that impairs the obligation of contracts (in Article I, Section 10), and this clause was particularly intended to prevent states from enacting extensive debtor relief laws.

There is no case law on point.

VI. Sham or Alter Ego Attacks

A court outside the DAPT venue could invalidate the DAPT on the grounds that it is a "sham" or the "alter ego" of the settlor, under legal precedents for such attacks.

VII. Conflicts of Laws Issues

The issue: can a non-DAPT forum court which has jurisdiction over the setttlor of a DAPT self-settled spendthrift trust created under one of these statutes apply the law of the forum state rather than that of the DAPT jurisdiction? Consider In re Brooks, 217 B.R. 98, 1998 Bankr. LEXIS 60, 32 Bankr. Ct. Dec. 23 (Bankr. D. Conn. 1998). See the 2013 Washington State Bankruptcy court decision In re Huber, cited above.

As a general rule, a settlor of an inter vivos trust may create a spendthrift trust in another state and take advantage of that state's spendthrift trust laws. See Fratcher, Scott on Trusts §626(1989) and Restatement (Second) of Conflict of Laws §273(b) (1971).

Generally the choice of governing law expressed in a trust agreement will be respected and enforced unless doing so would undermine a strong public policy of the forum state where the challenge to the trust is being heard. For example, in Dahl v. Dahl (supra.) a Utah court refused to enforce Nevada law governing a Nevada trust which held marital property of a Utah married couple. In IMO Daniel Kloiber Dynasty Trust (supra.) a Delaware court refused to enforce the governing Delaware law of a Delaware trust, deferring to a Kentucky court's application of Kentucky law where the marital domicile of the claimant was Kentucky and the issue related to the definition of marital property.

Note that the common law underlying the Scott and Restatement authority likely dealt with non-self-settled spendthrift trusts, as most states traditionally did not permit self-settled spendthrift trusts.

In at least one case, In re Portnoy, 201 B.R. 685, 1996 Bankr. LEXIS 1392 (Bankr. S.D.N.Y. 1996), a U.S. court has ignored the foreign law (Jersey) incorporated into an offshore self-settled asset protection trust and instead applied New York law.

VIII. The Enforceability of Foreign Judgments

(1) Jurisdiction of Out-of-State Courts

(a) The Issue. Despite the statutory announcement of exclusive jurisdiction over self-settled spendthrift trusts created under its statute in many DAPT jurisdictions, and despite their statutory prohibition against actions attaching assets in self-settled spendthrift trusts created under its statute, can a non-DAPT jurisdiction's court obtain jurisdiction over the trust and decide the validity of the spendthrift provisions? For a thorough analysis of this and related jurisdictional issues, see Cannon, *The New Self-Settled Trust Statutes*, California Trusts and Estates Quarterly, Vol. 3, Number 4 (Winter 1997) and Giordani and Osborne, *Will the Alaska Trusts Work*? Journal of Asset Protection (September/October 1997). See In re Huber and Kloiber cited above. See "Find the Best Situs for Domestic Asset Protection Trusts" published by Mark Merric and Daniel G. Worthington in the January 2015 issue of Trusts and Estates, even though their analysis does not consider the 2014 OKFWPTA.

(b) The Authorities.

1. Statutory extra-territorial Impact. A state statute that purports to have extra-territorial impact outside of that state may not be effective to prevent another state from deciding a matter in which that state has an interest. See generally Thomas v. Washington Gas Light Co., 448 U.S. 261, 100 S. Ct. 2647, 65 L. Ed. 2d 757, 1980 U.S. LEXIS 54 (U.S. 1980); Alaska Packers Association v. Industrial Accident Commissioner of California, 294 U.S. 532, 55 S. Ct. 518, 79 L. Ed. 1044, 1935 U.S. LEXIS 56 (U.S. 1935); Tennessee Coal, Iron & Railroad Co. v. George, 233 U.S. 354, 34 S. Ct. 587, 58 L. Ed. 997, 1914 U.S. LEXIS 1255 (U.S. 1914). Hence, it is unclear that either the Alaska statute, which purports to give Alaska exclusive jurisdiction over trusts created under its statute, or the Delaware statute, which prohibits actions to attach or otherwise reach the property of a trust created under its statute (or comparable laws of other DAPT jurisdictions), is effective to prevent another state from ruling on the validity of the trust's spendthrift provisions when that other state has an interest in the trust and a basis for jurisdiction over the trust.

2. Jurisdictional bases for non-DAPT forum courts over DAPTs:

(i) The due process clause of the 14th Amendment to the U.S. Constitution in general requires a forum court to have either personal jurisdiction over the trustee of the trust or *in rem* jurisdiction over the trust assets. See Hanson v. Denkla, 357 U.S. 235, 78 S. Ct. 1228, 2 L. Ed. 2d 1283, 1958 U.S. LEXIS 752 (U.S. 1958).

(ii) Presumably, so long as a trust has exclusively DAPT jurisdiction-sitused trustees, those trustees have no contacts in the forum state, and all of the trust assets are held in the DAPT jurisdiction, a non-DAPT forum

state would fail to have jurisdiction over the trust. A national corporate trustee with offices in many states may effectively be subject to the jurisdiction of the courts of each of those sates.

(iii) Note that a forum court that could legitimately exercise jurisdiction may decline to do so, either because the forum is not convenient or because the court does not want to interfere with courts of another state.

IX. Three Unique Features of Oklahoma DAPT: Revocability, Exemption (not Spendthrift) Protection, and the Settlor May NOT Be A Beneficiary.

Exempt Status of Trust

The Oklahoma Family Wealth Preservation Trust Act ("OKFWPTA") provides for a "preservation" trust which is exempt from claims of creditors. (Section 12). This exemption is found in Title 31 of the Oklahoma Code, "Homestead and Exemptions".

> *"The corpus and income of a preservation trust shall be exempt (emphasis added) from attachment or execution and every other species of forced sale, and no judgment, decree, or execution can be a lien on the trust for payment of debts of a grantor, except a child support judgment."*

All of the other 14 DAPT statutes protect spendthrift trusts.

Why did the drafters go to such lengths to characterize the trust assets as exempt from attachment or execution? Presumably because federal bankruptcy law - covered in detail by another presenter on this program - expressly respects exemptions from creditor claims under state law, for example IRAs in states where protected (like Oklahoma) and presumably would have to respect as protected assets held in Oklahoma preservation trusts.

Oklahoma's statutory exemption from creditor claims is a new approach among DAPT states, clearly intended to be effective in federal bankruptcy proceedings as well as in civil creditor's suits. This is perceived to add protection beyond that generally accorded to discretionary and spendthrift trusts. It is impossible to predict how effective this will be in bankruptcy and civil cases, but it may have a better chance to survive in a bankruptcy proceeding.

Revocability

The OKFWPTA provides that a preservation trust may be revocable or irrevocable. (Section 13).

> *"A preservation trust maybe established as a revocable*

> *and amendable trust or as an irrevocable trust. If a Grantor of a preservation trust revokes or partially revokes the preservation trust, the exemption provisions of Section 12 shall not be applicable to any property received by the grantor as a result of such revocation.."*

All of the other 14 DAPT statutes protect irrevocable spendthrift trusts only.

Under Oklahoma law a preservation trust is not the only revocable asset protection trust arrangement in Oklahoma. An IRA is also a so-called self-settled revocable trust protected by statute.

Why did the drafters use this approach to permit protected revocable trusts? I would speculate that they were trying to avoid some of the bad court precedents on self-settled spendthrift trusts in which the settlor was a beneficiary, while still leaving the settlor with the ability to revest ownership of trust assets in himself by revoking the trust.

Under Section 16 of the Oklahoma Law no court shall have the authority to compel a person holding a power of revocation or amendment to exercise such power. This provision shall be considered a "restriction on the transferability of the grantor's beneficial interest in the trust that is enforceable under applicable non-bankruptcy law within the meaning of section 541(c)(2) of the Bankruptcy Code."

Ever though a trust may be revocable, caution may dictate that it should be irrevocable because of the prevalent common law view that revocable trusts may not be protected, and the prevalent approach of other DAPT statutes that such an asset protection trust must be irrevocable.

Quoting from Phil Feist's article in the Oklahoma Journal:

> "The case of a non-Oklahoma grantor of a *revocable* Preservation Trust poses a particular challenge. Under the Act, the creditor of a debtor grantor cannot step into the shoes of the grantor to exercise the revocation power under the authority of a judgment rendered by a "court or other judicial body". Therefore, assuming that the non-resident grantor's Preservation Trust holds no assets in the grantor's state, and that the courts of that state cannot obtain *in personam* jurisdiction over the Preservation Trust trustee, the foreign judgment against the non-resident grantor will need to be domesticated in Oklahoma before it can be asserted against Preservation Trust assets. In such a case, Oklahoma public policy should govern.
>
> But while the creditor's judgement may not fare well against the Preservation Trust trustee in Oklahoma, could the grantor who resides in a non-DAPT state and who holds the power to revoke her Oklahoma

Preservation Trust be held in contempt by the courts of her state for not exercising the revocation power in favor of her creditors, as has been done by the federal courts with regard to grantors of non-U.S. asset protection trusts? Or would the Full Faith and Credit Clause require the courts of grantor's non-DAPT jurisdiction to analyze the enforceability of its judgment against the grantor on the basis of conflict of laws principles?

The follow-on question is this: Does the Oklahoma corporate trustee of this grantor's Preservation Trust have a duty not to recognize any forced exercise of the revocation power, not only on the basis of the explicit prohibition in the Act against judicial coercion in this matter, but also because of the fact that the grantor would be exercising the revocation power under duress? And if the Oklahoma trustee were to acquiesce in an exercise of the revocation by a grantor under duress, would the beneficiaries have a claim against the trustee for failing to enforce the protections afforded by the Act? In light of this, a corporate trustee may require provisions in the grantor's Preservation Trust indenture that address this eventuality, especially in the case of a grantor residing in a non-DAPT jurisdiction. *Revocability Has Its Benefits.* The provisions of the Act are consistent with the established common law of trusts, inasmuch as a Preservation Trust, by law, cannot be settled for the benefit of its grantor. However, a grantor can reserve the power to revoke her Preservation Trust, in part or in whole. This is another unique feature of the Act that sets it apart from other states' DAPT statutes.

A revocation power is not an interest in trust property but a power over property, and a reversionary interest in trust property does not constitute a beneficial interest in trust property. Therefore, that a Preservation Trust cannot have its grantor as a beneficiary, and with the involvement of a corporate trustee having a duty to vet asset transfers in light of the UFTA, is the basis for a robust argument that the 10-year clawback provision of 11 U.S.C. §548(e), Para.(1), does not apply to Preservation Trusts. In addition to not falling within the provisions of §548(e)(1)(A),(C)and(D), the clear *exemption* language of Sec. 12 of the Act parallels the *exemption* language that applies to an Individual Retirement Account (also a self-settled trust arrangement) under Oklahoma law, which has been respected in bankruptcy.

A cautionary comment is appropriate here. To avoid a "pierce the veil" attack by a creditor, the grantor, in her Preservation Trust indenture, would be well advised to consider including some restrictions on (a) the timing and extent of her exercise of her revocation power, and (b) her ability to be involved in control over Preservation Trust assets. Again, the presence of a corporate trustee, with the duty to enforce those restrictions, lends strength to the Kevlar protection fabric of the Preservation Trust."

Jay D. Adkisson has made the point in an Oklahoma Bar Association Journal article that "for Oklahoma's protection of revocable trusts to be effective, it may be that the settlor/beneficiary will need to avoid bankruptcy or having a receiver appointed by the courts of another state" because "there is a concern that a court-appointed receiver or a bankruptcy trustee may be able to enforce revocation of the trust."

Settlor May NOT Be A Beneficiary

The OKWPTA duties "qualified beneficiaries" of a defined trust as excluding the settlor, including any lineal ancestors and descendants of settlor and spouse, the spouse of settlor, and charities under IRS Section 501(c)(3), or other trusts for same.

Why did the drafters of the Oklahoma statute preclude the settlor from the class of beneficiaries? See my comments under revocability. A factor was probably a series of "bad" court cases concerning self-settled spendthrift trusts in which the settlor was in the class of discretionary beneficiaries. So, to speculate, the drafters got the idea that they could achieve a substantially similar result but outside of the bad precedents by providing that, on the one hand, the settlor could not be beneficiary but, on the other hand, he could revoke the trust. From theoretical and practical points of view, both approaches would be equally effective to protect trust assets from settlor's creditors while keeping the assets available to settlor. Based on the case law the first approach – irrevocable self-settled discretionary trusts – has not worked, so Oklahoma is testing an alternative comparable approach.

Will this approach experience more favorable treatment for the settlor from state civil courts and federal bankruptcy courts? This remains to be seen, but it will not be difficult for courts to determine that in substance this new approach is virtually identical as for as the settlor is concerned.

An obvious advantage in a bankruptcy proceeding is that if the settlor is not a beneficiary, the 10-year clawback rule cannot apply.

Can a settlor be a remainderman under the statute? Should the settlor be a remainderman even if he can be?

X. Trust Drafting Suggestions

1. Comply carefully with OKWPTA and other Oklahoma statutes, working with local counsel to draft or review the trust.
2. Designate Oklahoma law as governing law for the administration of the trust.
3. Designate Oklahoma law as governing law for validity and construction of the trust.
4. Designate Oklahoma clearly as the place where the trust is to be exclusively administered.

5. Do NOT provide for actual control of any aspect of the trust by the settlor or by directed or special or co-trustee or trust advisors or trust protectors or power of appointment holders who are outside of Oklahoma.
6. The Oklahoma bank or trust company trustee should be the sole trustee.
7. Recite expressly that the income of the trust is subject to Oklahoma income tax.
8. The grantor may not be a current beneficiary. Ideally he should not be a remainderman.
9. Can husband and wife establish reciprocal trusts for one another? Perhaps, but taking into account the reciprocal trust doctrine applicable for transfer tax purposes.
10. Require that the trust assets be periodically revalued and describe how and when to assure that the "majority in value" requirement (at least 50% Oklahoma assets) continues to be met. The trust should require that the test should always be met.
11. Permit or require the trust to accept additional future contributions.
12. Avoid giving any non-Oklahoma court an opportunity to have *in personam* jurisdiction over any trustee (or maybe over any fiduciary or other power holder) or *in rem* jurisdiction over any trust asset. Particularly avoid possible jurisdiction in a state without DAPT legislation.
13. Avoid revocability, as it may provide an opening for attachment, particularly if the settlor lives outside of Oklahoma, and especially if the settlor lives in a non-DAPT jurisdiction, or if assets are held outside of Oklahoma, particularly if the assets are not held in an Oklahoma LLC or are sitused in a non-DAPT jurisdiction.
14. If revocability is used, include restrictions on the timing and extent of the revocation power, and expressly forbid the Oklahoma trustee from honoring a revocation under duress, with appropriate indemnification to the bank trustee.
15. The trust should be a purely discretionary trust with a "spendthrift" restriction.

XI. Trust Administration Suggestions

1. Make this "rainy day" asset protection. Do not put in an Oklahoma Preservation Trust more than 1/3 to 50% of settlor's net worth.
2. The drafting lawyer should obtain a notarized Affidavit of Solvency under penalty of perjury from prospective settlor disclosing no material present creditors or creditor concerns.
3. Transfers to the Trust should reflect thoughtful non-asset protection planning, i.e., estate and gift tax planning, probate avoidance planning, financial planning, so that the transfer may be justified, at lease partly, by "other business (non- asset protection) purposes."
4. Hold and administer as much of trust corpus as possible in

Oklahoma. If out-of-Oklahoma assets are to be held in the trust, put them in an Oklahoma LLC owned by the trust.

5. Make no distributions to any beneficiaries without written requests for same explaining why the request is being made.
6. In all respects make the trust as "Oklahoman" as possible.
7. Beware of dishonest or desperate settlors.
8. Use local counsel for advice on drafting and administering the trust in order to comply with Oklahoma statutory and case law.
9. Have the trustee maintain meticulous books and records.
10. Avoid any possible application of the 10-year clawback provision of the Bankruptcy Code by having the settlor avoid going bankrupt. Keep court jurisdiction in state courts.
11. If the creditor is the IRS or any other federal agency, the settlor and trustee should negotiate the best settlement they can.
12. If the creditor is a spouse, the settlor better have very good facts.
13. Transfers to the trust should be reported as completed gifts if so characterized by gift tax law. Appropriate gift tax returns should be filed.
14. If the trust is not a grantor trust (e.g., if it is irrevocable and not "defective"), file Oklahoma (and federal) trust income tax returns.

XII. Potential Attack on Oklahoma DAPT Established by Virginia Domiciliary Settlor by Creditors of Settlor in Virginia Courts

First of all, Virginia adopted effective July 1, 2012 what I would characterize as a "conservative" DAPT statute. So it may not be said that Virginia has a public policy against DAPTs. Prior to 2012 self-settled spendthrift trusts in Virginia were expressly against public policy and ineffective against settlor's creditors. The Virginia statute relies on the spendthrift provision of the trust (rather than an exemption) as Oklahoma's does. No revocable trust has creditor protection in Virginia.

Like Oklahoma's Preservation Trust statute, Virginia's DAPT statute does not protect against child support claims. Virginia's DAPT statutes also does not protect against claims from (a) federal, state or local government, or (b) a judgment creditor who has provided services "for the protection of a beneficiary's interest in the trust."

So a government creditor or service provider creditor might find more sympathy from a Virginia court.

Because Virginia's law does not recognize asset protection for a revocable trust, an Oklahoma trust which is revocable might be more likely to be successfully challenged on public policy grounds in Virginia than an irrevocable trust.

XIII. Potential Attack on Oklahoma DAPT Established by District of Columbia Domiciliary Settlor by Creditors of Settlor in D.C. Courts

The District of Columbia ("D.C.") has not adopted a DAPT statute. The law and public policy of D.C. precludes a D.C. resident from protecting himself from his creditors by establishing a self-settled spendthrift trust of which he is in the class of beneficiaries, as he might be if he established a DAPT in any DAPT jurisdiction other than Oklahoma. But, of course, on Oklahoma DAPT cannot and would not include the settlor among the beneficiaries. Accordingly any transfer to an irrevocable DAPT for the benefit of family members would be tested under DC's law of fraudulent conveyance, which is materially similar to Oklahoma's, and for purposes of this program we are only discussing "clean" transfers which are not fraudulent conveyances under Oklahoma law.

So the only area of vulnerability would be if a D.C. domiciliary established a revocable DAPT in Oklahoma. As noted above in the discussion of this unique characteristic of Oklahoma law, Oklahoma law prohibits the exercise of a revocation or amendment right under duress. Would a D.C. court honor Oklahoma law in that regard or possibly order a D.C. domiciliary to revoke or amend? And if it did, would not the Oklahoma bank trustee refuse to honor such a compulsory revocation or amendment under duress, assuming this came to its attention which presumably it would? And presumably an Oklahoma court would not respect or enforce a D.C. court order in violation of its own statutes.

So perhaps even a revocable trust would survive a D.C. court challenge. But the Kloiber case, in which a Delaware court deferred to a Kentucky court in the determination of a claim against a Delaware trust by a Kentucky claimant may be cause for concern that under certain circumstances, e.g., a marital claim where the martial domicile is D.C., an Oklahoma court might defer to a D.C. court based on a conflicts of law analysis, as the Delaware court did in Kloiber. To take another example, generally the governing law of a contract is the law of the jurisdiction in which the contract was signed, and if the D.C. court claim was based on a D.C. contract, might an Oklahoma court defer to a D.C. court's view of the enforceability of contract?. In the practical world, the "sympathy factor" as to the facts might be determinative for both the D.C. court and the Oklahoma court.

XIV. Conclusions/Suggestions

- Beware of bad (desperate) clients/settlors and bad facts! Both lead to bad law.

- If the creditor sought to be avoided is the IRS or other organ of the federal government, an Oklahoma DAPT is unlikely to effectively protect the assets.
  - Ditto if the claimant is a state government other than Oklahoma.
  - Ditto if the claimant is a spouse or ex-spouse and the facts are at all tainted. Marital claims consistently excite judges to rule on

"fairness" and "equity" and to look hard for fraud.

- The <u>Kloiber</u> case from Delaware, a DAPT state, in which the court defers to a Kentucky court and Kentucky law (which does not recognize the DAPT concept) on the susceptibility of a Delaware DAPT to a matrimonial claim, is both shocking and disturbing.

- An Oklahoma Preservation Trust is more vulnerable to claims of Settlor's creditors.
  - If the Settlor lives outside of Oklahoma
  - especially if the Settlor lives in a jurisdiction with no DAPT statute
  - If the trust hold assets outside of Oklahoma, especially if they are not held in an Oklahoma LLC
  - If the trust is revocable
  - If the Settlor maintains directly or indirectly any control over the administration or disposition of trust assets
  - If the Settlor is even a contingent remainderman
  - If the gift tax treatment and income tax treatment of the trust is not appropriate

- There are very great differences of opinion among sophisticated estate planning attorneys about the effectiveness and future prospects of DAPTs

- The case law on the effectiveness of DAPTs could hardly be worse

- Some sophisticated asset protection attorneys believe passionately that offshore asset protection trusts are much more likely to be effective. But, the burdens of FACTA and the history of tax fraud, money laundering and crude creditor fraud have made many offshore banks wary or working with Americans to establish asset protection trusts unless the assets to be placed offshore are very substantial, preferably cash or liquid, unless the client is very "clean" and unless the fees to the bank are very substantial. As a result, for many Americans DAPTs are "the only game in town."

- The good news for DAPTs: as more and more states each year adopt DAPTs, the number of states from which public policy attacks are possible is shrinking.

The "expert" panelists participating in a recent online ABA CLE program on asset protection trusts had radically divergent views on the efficacy of domestic vs. offshore asset protection trusts, but all agreed that the safest way to draft a domestic asset protection trust is to avoid making the settlor a beneficiary or giving him any direct or indirect control. So from that point of view, an irrevocable Oklahoma preservation trust is ideal.

On the other hand, if the transfer is clean (not a fraudulent conveyance) and the settlor is not a beneficiary, why not use in the settlor's home state a traditional irrevocable spendthrift trust for the benefit of family members which is sanctioned by public policy in all states?

- Perhaps the reasons to use an Oklahoma DAPT for an irrevocable discretionary spendthrift trust for the benefit of settlor's family are these:
  -Oklahoma law has adopted by statute the law of the Restatement (2nd) of Trusts which is crystal clear – as the 3rd Restatement which has been indirectly adopted in a number of jurisdictions as part of the Uniform Trust Code is not – that purely discretionary trusts are not susceptible to creditor's claims.
  - Because Oklahoma courts may defer to the determination of Oklahoma banks as to fraudulent conveyance issues, and Oklahoma banks may be somewhat indulgent.
  - Oklahoma courts would be unlikely to countenance a claim from future creditors who could not reasonably be anticipated at the time of a transfer, as other courts might. (See Battley v. Mortensen, supra).

- On the face of it Bankruptcy Code Section 548(e) – the 10-year clawback provision – cannot apply to assets transferred to an Oklahoma Family Preservation Trust because such a trust may not be "self-settled" – i.e. for the benefit, inter alia, of the Settlor – and Section 548(e)(I)(c) requires the settlor to be a beneficiary of the transferee trust to invoke the 10-year rule. Caution: is it possible that a bankruptcy court could construe the right to revoke as equivalent to being a beneficiary?

- There is a "game" going on between the banks and asset protection bar and the creditors' rights bar. Every year states update and "improve" their DAPT statutes to avoid the implications of the most recent court cases. And every year the creditors creatively challenge the new approach in court. To date the creditors have been winning the "game."