Mary Vandenack provides the transcript from Legal Visionaries podcast on Alaska Trusts.

TRANSCRIPT:

Mary: On today's episode, my guest is Abby O'Connor. Abby practices in estate planning, trusts and estates in Alaska, representing both Alaskans and non-Alaskans. She also engages in mathematical modeling to support the analysis for estate planning strategies or other things as well, I think litigation support and various, but she's good at math. She's also a frequent writer and presenter on estate planning topics. She's joined me on a previous episode to talk about building our practice in Alaska. Today I asked her to come back on the podcast and talk about Alaska trusts. Thanks for coming back, Abby.

Abigail: Thank you for having me, Mary. Great to be back.

Mary: So, I think the really important thing is that just before we started this podcast, you were mentioning that you're in salmon season in Alaska. Is it because they have great salmon that they also have great trusts in Alaska?

Abigail: I wish I could connect the two because I would connect great fishing with everything in Alaska, but I think they're mutually exclusive.

Mary: So, I'm looking forward to seeing some pictures of you fishing salmon while I am at ACTEC in DC. But can you start by just talking about why is Alaska a popular state for creating trusts?

Abigail: Sure Mary. Alaska back in the 90s adopted the first statutory structure for domestic self-settled asset protection trusts, and Alaska was really the pioneer in the US for those types of trusts. And other states have now followed suit, so there's numerous places to go, but Alaska remains among the strongest jurisdictions for self-settled asset protection trusts. That's probably why Alaska's the most popular for non-Alaskans. Another offering of Alaska that is not as popular because I think it's simply just not as well known, is that non-Alaskans can come to Alaska and create Alaska community property trusts, which can be incorporated into their overall estate plan and may provide for some positive income tax planning in the long term.

Mary: And so as long as you brought that up, I'm going to just break those down into a couple of categories. At the end of the day, Alaska's a great jurisdiction for trust because it's a state that's been proactive in passing legislation and creating tools that you can use in Alaska that are not necessarily available in other states.

The first example of that is that they were the pioneer. And I guess as I was listening to you talk about them being a pioneer for domestic asset protection trust, I was just curious whether you know who's the driver of that or why? Who came up with that idea or what drove the concept?

Abigail: That would be Jonathan Blattmachr. He was the head of the pioneering idea behind the asset protection trust planning in Alaska. And he and his brother, Doug Blattmachr, and a team of Alaskan lawyers worked very hard to get that legislation through. I can't give you a lot more detail, as I was in college at the time. But from what I heard, it was quite the feat and terrific legislation and other states have followed in those footsteps.

The other thing I want to mention about our state is that we're very approachable for non-Alaskans. Meaning our core system is not overwhelming. I wouldn't call it simple, but it's not overly complicated. We can get into the courts. We can have trust proceedings. I think my clients find it to be an approachable state. We have good counsel. We've got a terrific trust company here that works with people out of state. So, it's not an overwhelming task to create an Alaska trust.

Mary: Usually when I've done trust in other states that have some of these special rules, there's people who specialize in helping somebody like me bring clients to their state. I could readily call you and say, "Hey, help me with this Alaska trust." Or I could call Jonathan. I'm thinking, "Oh, we should have had him on for this conversation as well today." Because I'm thinking, "Okay, he's from New York and was at a New York law firm for a long time." How did he end up deciding to drive legislation in Alaska? Do you know? Or do I have to ask him?

Abigail: I think you'll have to ask him, but I think he fell in love with Alaska for the same reason I did. But I'm not sure you would be able to get him today because I am pretty confident he's fishing.

Mary: He's fishing. Oh, no.

Abigail: Yeah.

Mary: So we'll ask him for some pictures of the fish to go with this podcast as well. We can ask him to talk about that.

Abigail: He and I were supposed to go fishing last weekend, and the weather didn't cooperate. We may try again for this weekend, but I think it will be okay.

Mary: June is pretty solid there, correct?

Abigail: Correct.

Mary: I got there in late May one year, and it was still a little not great, but I think it depends on the day.

Well, let's talk about what the domestic asset protection trust is. That's one of the things you mentioned. Alaska was a pioneer in allowing people to set up the Alaska asset protection trust. Can you just explain what one is?

Abigail: Sure. The theory behind it and the general concept is that an individual creates an irrevocable trust in Alaska, transfers assets to that trust. And that individual, the grantor, remains a beneficiary, usually one of a number of beneficiaries, a discretionary beneficiary. And in the future, if a creditor comes after and gets a judgment against that individual, then the idea is that if the trust works, the creditor would not be able to attack the assets in the trust.

Mary: So what type of client would be the client that I would say you should consider an Alaska asset protection trust?

Abigail: A wealthy client in a high-risk field who can part with some assets and essentially siphon off some degree of wealth that they don't need on a regular basis. So, for example, if you have a client with $5 million and what they want to do is take $4 million of it and put into an asset protection trust, I would not recommend that. But if you've got a client, and it's hard to pin down a number, but just for discussion purposes, if you have a client with north of $20 or $30 million who wants to take an account with maybe $3 or $4 million and put that into an asset protection trust that they're not going to need to draw from, it's not really a rainy day fund, but part of an overall savings strategy and they don't think they'll need it and they're not involved in litigation at the moment, this is for a someday potential creditor, then this could be a good part of their overall estate plan.

Mary: When I first started doing asset protection planning, I remember one of the early calls that I got, and it was somebody who owned a lot of real estate. I can't remember which state they were in, but they're somewhere on the West Coast or the Great Northwest. They had 20 lawsuits pending against them and were hoping that we could go take everything and put it into an Alaska asset protection trust and save them. That's the client that's too late, right? It's the complete opposite of what you just shared.

Abigail: Right. Right. Yeah. This needs to be planned in advance.

Mary: For it to work. You can go try it. You can probably find somebody who'll let you pay you to do an asset protection trust, but make sure you're covered.

Abigail: Right. We had a case a number of years ago. If I recall, it was a particular case or the Wacker case where that was the situation. It was too late. They already had a judgment against them. They were already embroiled in litigation and tried an asset protection trust in Alaska, and it didn't work for some very technical reasons. The short story is it didn't work. I consider myself a conservative planner, so if somebody is already in litigation in my book, that's too late.

Mary: Another call that I got early on was a client who was in, I can't remember the term that was used, but a high-risk industry. They had an industry. They got sued a lot. The client had gotten into this particular industry. It was early, so he'd be the one who only had $5 million at the time. Only $5 million. That sounds ridiculous. So he had $5 million at the time. But when we're talking asset protection trust, what we're saying is we don't want them to put their entire wealth at that level into a trust that they have potentially some limited access to. But this guy called them and said, "Well, this is how much I'm making a year. And what I want to do now is I've heard about these asset protection trusts and I think I'm going to do pretty well in my business, but it's a high-risk business, so I'm likely to get sued, but I don't want to put everything I have in it." So he started at that time. The first year he set it up, he put a hundred thousand in and that's what he was able to put away for the first few years. And then as he made more, he increased that amount and continued to increase it until he did have a really nice backup fund many years later, and that still exists. Would that be another potential client that could consider that strategy?

Abigail: It would. Just keep in mind every time the grantor funds the trust again, we have to go through the same exercise to evaluate whether or not it's a good fit. You're not creating a new trust, but we're going through the same thing. What's the portion of overall wealth? Making sure there's solvent afterwards. There's an affidavit of solvency that's required at the time. So, it's not something where you can just keep feeding it without any further work. You need to go through the exercise each time of deciding whether or not it's a good idea.

Mary: So there's some expenses and some considerations. Again, if you are doing that gradually and then you've been sued, that probably creates some risk that you wouldn't want to at that point continue. But it's not that you would throw that strategy under the bus. It's something that could be considered by somebody who isn't at the $20 or $30 million but has concerns with asset protection, just knowing that there's some compliance and it's an ongoing maintenance process, so to speak.

Abigail: Sure. The other thing to consider is if you're funding it to start with low value assets, there still will be expenses. One of the expenses is you have to have an Alaskan trustee. Now that trustee can have limited duties, but the grantor cannot be the trustee in charge of distributions. So there has to be a trustee in charge of distributions who's different, and there has to be an Alaskan trustee. So, there will be some trustee fees. That has to be considered as to whether or not it's worth it depending on how much you're putting in it. It's a cost benefit analysis no matter what you do.

Mary: There's a lot of jurisdictions these days. Alaska was the pioneer and we're talking about Alaska, but my next question is, so what are the most important considerations in choosing a jurisdiction? There's a lot of competitors out there. At one point Alaska was pretty much the game in town, and then that started to expand. Other states said, "Hey, that's a great idea. I've tried to sell it in my home state to no avail. So, we're behind the curve at this point. But there's competitors out there and they all have different strengths and weaknesses." What would you say are some of the important considerations in deciding where to go?

Abigail: Well, the first one is the statutory structure, making sure the state statute supports asset protection planning. What you're talking about is choosing between all states who do. Other aspects are if this is a trust that you need to decant, if you have notice concerns, take a look at the notice statutes. Take a look at the specific statutes that you think you might need. The other factor in my book is just being able to work with people in that state. Making sure there's a trust company in that state that you want to work with. Making sure you have local counsel that you want to work with. Making sure that the courts are accessible, which ours are. I think that's a very important factor. Especially when you have trusts that have been going on for a long time, they need to be modified. Take a look at what the modification statutes are. Can the trust be decanted? Is judicial modification a possibility so that we can create flexibility in the long run? What is that like and what are the experiences in that state for people to be able to work within the trusts so that they don't become a hindrance but become something that's really positive for the family?

Mary: Let's say that in my home state, and I'm surrounded by a few states that offer the domestic asset protection trust, and actually I think South Dakota has the community property trust as well. So let's say in my home state that a lot of people will own hunting land. So they go hunting in South Dakota, that's really common. They have a cabin or they have some hunting land. In Alaska, you own a water plane and you go salmon fishing. So that might be the connection. Does it matter when I'm talking to a client about where they should set up this type of trust if they have any relationships with Alaska or South Dakota or whatever jurisdiction they might be looking at?

Abigail: Well, connections certainly don't hurt. We create the connection here by having an Alaska trustee and some of the trust assets have to be held and deposited in Alaska. So, there's always at least an Alaskan bank account. One of the other strategies, and nothing is guaranteed, but one of the things that I'll use is if a client does have assets in a different state, we might create an Alaskan LLC, transfer those assets to the Alaskan LLC, and now we have another Alaska asset. So, it is certainly helpful to have more connection to the state, but I don't know that that's determinative.

Mary: I'm going to go back to the other trust type that you mentioned because I think that's worthy of a mention because it's not possible in every state, and that's the community property trust. Can you briefly describe what that is and why somebody would consider that? Because I think you're right, that is less well known, but it has some great benefits.

Abigail: Sure. Well, the benefit of community property is the double step up in basis on death. And not all states have community property. Alaska has an opt-in community property system. So, for Alaska residents, you opt in either by agreement or with a community property trust. For non-residents, under our statutes, you can create an Alaska community property trust, put the assets in the trust and designate them as Alaska community property. Now whether the IRS will respect it or not, I can't guarantee that. However, if done correctly as part of the overall planning, it's in my view, one of those situations of if it works great, and if it doesn't, you really haven't lost anything. So, you have to take a look at what the property was before you made a community property and spousal rights and all of that. So, there's definitely some analysis involved. But it is a potential avenue for, let's say, a couple in a non-community property jurisdiction who has low basis assets or maybe depreciated commercial property or something where they really could benefit from the double step up in basis. They create the Alaska community property trust, convey those assets into the Alaska community property trust, and then there's the potential for the double step up in basis on the first death. So, a significant potential upside. And if you structure it correctly and the analysis is right, you would have a limited potential downside.

Mary: So I'm in a non-community property jurisdiction, but a client that's located here, a resident in the state of Nebraska, domiciled here, whatever the case might be, could set up an Alaskan community property trust and have some benefits. So are the rules similar to the domestic asset protection trust, I name an Alaskan trustee? What do I have to do to get that done?

Abigail: Yeah, similar jurisdictional issues. You have to have an Alaskan trustee. There are some basic duties that Alaska trustee has to have. So, for example, keeping the books and records of the trust, do some of the administration in Alaska, making sure any tax returns are filed for the trusts, and as I said, hold some of the assets here. I certainly, with tax counsel, would want to consider whether or not to create an Alaskan LLC and have the assets conveyed into the Alaskan LLC. I think a lot of analysis has to be done depending on the assets, but generally that's what's required to have the Alaska trust is the trustee, some assets here. And those are the two real connections.

Mary: And if we were to talk about requirements versus best practices, is there anything that you would say this is what's required, it's always going to help if these things happen?

Abigail: Well, for the asset protection trust, in my view, the best practices has to do with the percentage of assets that you're transferring into the trust. I'm a conservative planner. I feel like a quarter or a third is the most that I would be comfortable doing. I don't have any hard data to back that up. I'm just very conservative. However, I know there are practitioners who'd be comfortable with a lot more of a percentage of wealth being put into the trust and they would stand by it. And I can't criticize that at all. It's just not my comfort level. So, in terms of best practices, that's something to consider as to the percentage of the overall wealth that is transferred into the trust. There's an affidavit required for self-settled trusts that's required by statute. However, I don't think it would hurt to go above and beyond that. And then also, just from a practitioner standpoint, know your client, know who's coming to this state, why they're coming to this state. It's something where I like to know if an attorney's calling me and they have clients who want to come and create an Alaska trust; I will ask for the backstory. And why are they coming? If I think it's a bad idea, I certainly will say so and will want to be very candid about that. So in terms of best practices, I would say those are my two top concerns.

Mary: With respect to the asset protection trust, can you get protection from any and every type of potential creditor, or are there any limitations?

Abigail: I would think that there are super creditors like the IRS. I don't know that it would stand up. I can't tell you one way or the other from experience. I would think there's a super creditor. We don't have a carve out for divorce. There are some requirements when you're creating it, if you're married about notice to a spouse. But generally speaking, for our Alaska trusts through our spendthrift rules, we don't have a carve out for divorce. Meaning if someone's getting divorced, they can't attack the assets in the trust merely because it's a divorce. So it's another aspect I'll talk about with clients. Even my Alaska clients, if they're creating their trust for their children after their death, say, "Why is it important to keep the Alaska trust or keep the trust in Alaska?" It's one of the things I'll say is, "I think we're stronger in terms of divorce and keeping the assets protected." But if it's an asset protection trust, then it depends on notice requirements when you created the trust if you were married at the time.

Mary: And with that, isn't this type of trust, the asset protection trust, held out sometimes as an alternate to a premarital agreement?

Abigail: I think it could be used in conjunction with a premarital agreement, for sure. As long as it's done again, far enough in advance, creating the Alaska asset protection trust, it would be a good counterpart to a prenuptial agreement. I can't say I would use it solely instead of it, but I think it would be very helpful. And if you can't get a prenuptial agreement, but you've already had the Alaska asset protection trust, I think that's certainly better than not having anything in place.

Mary: So what are the estate tax consequences if you pass away and you have assets in the Alaska self-settled spendthrift trust?

Abigail: I think it depends on how you set up the trust. More common than not, I see the asset protection trust set up as incomplete gift trusts. So, the grantor has either retained a veto power or maybe a testamentary power of appointment. It's an incomplete gift trust, so the assets are included in the estate. As far as the completed gift, I do know of practitioners who take the position that the assets are excluded from the estate. Personally, I think I have some questions about 2036 and reserved retained interests, but I think that's a debatable discussion and beyond the scope of today. But I think it depends on what the goal is. If it's pure asset protection planning, then an incomplete gift trust might be the best option, because all because you're trying to do is get the asset protection.

Mary: This might be an unfair question to ask you off the top of my head because I didn't warn you I was going to ask it, but that's only because I just thought of it as we're talking about that. Let's say I have clients who live in one of the states that still has state estate taxes, and they're a resident of that state at the time of their death. And maybe that makes the last question even more complicated. But the fact that that's in Alaska... going to get it outside of their state's estate tax, or is it still going to be subject to estate tax, or is that going to depend on what the laws of that state say?

Abigail: I think it would depend on what the laws of that state would say, because if the state is going to tax them on their overall gross estate wherever located because they're a resident there, I don't know that it would matter. So I think that's a state specific question. Alaska does not have a state estate tax. So at least we don't have anything here.

Mary: We still have an inheritance tax in Nebraska. And I was just reading through the states that still have estate taxes, and I was actually surprised by the number that do. Do you have any last thoughts on today's topic?

Abigail: I really don't. We certainly enjoy working with attorneys from out of state who call and want to create a trust in Alaska. I always recommend working with local counsel to at least review a draft trust and make sure that it complies with Alaska law and to just give insight as to how the trust might be run in the state of Alaska. But other than that, I don't. I think this is a strong area and I appreciate the opportunity to talk to you about it.

Mary: I think that point you made about using, even if you're familiar with the state laws, so to speak, I always contact somebody who's in that state dealing with that issue on a regular basis. And I use my weird analogy; when I visited Alaska and you took me around the airport and I'm thinking, "It's an airport, and yet there's tons of these little planes." And going, "Oh, wow." That is just how different the culture is in different states. And if you are dealing with the law, you're going to have a little nuances of differences that you don't know. I didn't know until we were talking today that it's easier to get in the court system. And I might've thought differently just because of the population of the state and thinking some states have specialized courts, and I actually don't know what Alaska has. But that's kind of a nice thing to hear because there's a lot of states that can't say that.

Well, I appreciate you joining me again today, Abby. And as we reach the end of our episode, I want to thank our sponsors; InterActive Legal, Foster Group, Veterans Victory Housing & Business Centers, and Carson Private Client. That's all for now. Thanks for listening to today's episode and stay tuned for our weekly releases.