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## INTERNATIONAL TRUST DOMESTICATION: MIGRATING AN OFFSHORE TRUST TO A U.S. JURISDICTION

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### Introduction

International families face a dizzying array of options when deciding where to locate a trust to safeguard wealth from income and transfer taxes and the threat of future creditor liability. Modern trust situs options do not simply include the traditional fifty U.S. states and the District of Columbia. We live in the midst of a truly global economy<sup>1</sup> and settlors may create trusts in a number of international jurisdictions, ranging from the remote shores of the Cook Islands in the South Pacific Ocean, to the Principality of Liechtenstein in the heart of central Europe. Choice of law rules typically permit settlors to have their assets held in a trust (or some analogous financial structure) in a jurisdiction other than the one in which they permanently reside. This practice has given rise to international competition

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<sup>1</sup> See DAVID HELD & ANTHONY MCGREW, GLOBALIZATION/ANTI-GLOBALIZATION: BEYOND THE GREAT DIVIDE 109 (2d ed. 2007).

among jurisdictions for trust business, as well as a steady stream of articles and web sites identifying the advantages and disadvantages posed by placing assets in different jurisdictions.

Offshore trusts<sup>2</sup> have sparked the interest of lawyers, investment advisers, and clients for decades. The opportunity for unparalleled asset protection may have been the foremost impetus for moving assets to such trusts.<sup>3</sup> In addition, offshore jurisdictions have offered a number of substantive laws that were once unavailable to settlors of U.S. trusts. However, the international trust market is not static. Legislatures in the U.S. have been cognizant of the innovations in modern trust law, and many U.S. states have updated their laws. For example, the State of Wyoming now permits domestic trust strategies that were once unthinkable, including near perpetual 1,000-year dynasty trusts, asset protection trusts, directed trusts, trust protectors, purpose trusts, unregulated private trust companies, and extremely flexible trust modification procedures.<sup>4</sup> Wyoming also has an innovative and highly protective limited liability company (LLC) act.<sup>5</sup> When viewed in combination with the disadvantages of offshore trusts (including burdensome tax and reporting requirements and potential blacklist treatment of offshore tax havens), Wyoming and other domestic jurisdictions may have closed the international trust law gap. Offshore trust structures that may have once been ideal for certain kinds of high-net-worth clients may have lost their comparative advantage to onshore trusts. Settlers and beneficiaries, whether U.S. residents or not, may obtain new advantages by migrating their offshore trusts to a U.S. jurisdiction such as Wyoming.

This article discusses important considerations facing individuals who seek to change the governing law applicable to an offshore trust. First, this article explores considerations that may motivate an initial choice of governing law, as well as later changes in governing law. Next, this article examines some of the primary methods of moving a trust. This article then looks at the extent to which an original choice of law may inhibit a subsequent change of governing law, and specific provisions of Wyoming law that facilitate trust migration. Finally, this article reviews some important problems in trust migration, including the ability to change the applicability of the Rule Against Perpetuities (RAP) to a preexisting trust, statutory and com-

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<sup>2</sup> For the purpose of this article, “onshore trusts” are created under or governed by the law of a U.S. jurisdiction and “offshore trusts” (also known as “foreign-situs trusts”) are created under or governed by the law of a non-U.S. jurisdiction.

<sup>3</sup> See discussion *infra* Section I.B.

<sup>4</sup> Christopher M. Reimer, *The Undiscovered Country: Wyoming’s Emergence as a Leading Trust Situs Jurisdiction*, 11 WYO. L. REV. 165, 176 (2011).

<sup>5</sup> Dale W. Cottam et al., *The 2010 Wyoming Limited Liability Company Act: A Uniform Recipe with Wyoming “Home Cooking,”* 11 WYO. L. REV. 49, 76-81 (2011).

mon law decanting, the problem of the Delaware tax trap, problems in migrating non-charitable purpose trusts, and the use of automatic migration clauses. This article focuses on the transnational trust migration and decantings from a trust settled in one sovereign jurisdiction to a separate trust created or administered under the law of another sovereign jurisdiction, with particular emphasis on relocating a trust to the State of Wyoming.

### **I. Why Move a Trust?**

Different types of settlors, beneficiaries, and trustees may have different motivations for seeking to change a trust's place of administration, its governing law, or the forum for resolving trust disputes (often referred to as a "change in governing law"). The relative weight of different considerations depends on a variety of factors, including the current situs of the trust and its assets, the current law applicable to the trust, the domicile of the settlors and beneficiaries, and the immigration and travel plans of the settlors and beneficiaries. Possible reasons for changing a trust's governing law include tax considerations, asset protection, a jurisdiction's structural characteristics, and features of a jurisdiction's substantive law.

#### **A. Tax Considerations**

##### **1. Trusts Whose Beneficiaries Include U.S. Persons**

In the U.S., federal law imposes two tax regimes relevant to inbound trusts: federal income tax and federal transfer tax (including estate, gift, and Generation Skipping Transfer (GST) taxes). U.S. persons are subject to federal income tax on all income, regardless of its source, and to federal transfer tax on all transfers, regardless of the situs of the property transferred. Non-U.S. persons are subject to federal income tax on U.S. source income and federal transfer tax on U.S. situs property. A trust is considered a "U.S. person" for federal tax purposes if "(i) a court within the United States is able to exercise primary supervision over the administration of the trust, and (ii) one or more United States persons have the authority to control all substantial decisions of the trust."<sup>6</sup>

The Treasury Regulations define a "substantial decision" as any non-ministerial decision that a trust instrument or applicable law requires or allows a person to make.<sup>7</sup> Examples of substantial decisions include "whether and when to distribute trust income or corpus," the amount of such distributions, beneficiary selection, invest-

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<sup>6</sup> See I.R.C. § 7701(a)(30)(E) (2011).

<sup>7</sup> Treas. Reg. § 301.7701-7(d)(ii) (2011).

ment decisions, and the appointment and removal of trustees.<sup>8</sup> A trust must meet both tests—the “court” and “control” tests, respectively—to be classified as a U.S. person subject to federal income tax on its worldwide income and federal transfer tax on all transfers.<sup>9</sup> A trust that does not meet both requirements is considered a “foreign trust.”<sup>10</sup>

Since the mid-1970s, the creation or funding of offshore trusts by U.S. persons for the benefit of other U.S. persons has been uncommon due to unfavorable tax consequences attributable to such action and has become even more uncommon as the provisions of Internal Revenue Code (IRC) section 679 have been increasingly tightened to discourage U.S. persons from funding foreign trusts. Other difficulties associated with offshore trusts included the heavy compliance burden placed upon U.S. persons who derive benefits from foreign trusts, the comparatively higher costs associated with administration in a jurisdiction remote from the beneficiaries (often stemming from the trust investment advisor and persons having direction powers), and uncertainty about the political stability of certain offshore jurisdictions. But many U.S. settlors and investment advisers have perceived foreign trust benefits, which can override the possible disadvantages, including asset protection,<sup>11</sup> secrecy,<sup>12</sup> the lack of U.S. tax jurisdiction,<sup>13</sup> and the inability of U.S. authorities to pressure a foreign trustee to produce information regarding foreign operating companies controlled by a foreign trust pursuant to the International Emergency Economic Powers Act.<sup>14</sup> As such, the creation of foreign trusts by foreign persons for the benefit of a class of persons, some or all of whom may be citizens or tax residents of the U.S., remains a popular planning technique.<sup>15</sup>

#### The recent enactment of the Foreign Account Tax Compliance

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<sup>8</sup> *Id.*

<sup>9</sup> See *infra* notes 25-31 and accompanying text.

<sup>10</sup> I.R.C. § 7701(a)(31)(B) (2011).

<sup>11</sup> Gideon Rothschild, *Establishing and Drafting Offshore Asset Protection Trusts*, in ASSET PROTECTION STRATEGIES: PLANNING WITH DOMESTIC AND OFFSHORE ENTITIES 47, 47 (Alexander A. Bove, Jr. ed., 2002).

<sup>12</sup> Maria Tihin, Note, *The Trouble with Tax Havens: The Need for New Legislation in Combating the Use of Trusts in Abusive Tax Shelters*, 41 COLUM. J.L. & SOC. PROBS. 417, 424 (2008).

<sup>13</sup> See Stewart E. Sterk, *Asset Protection Trusts: Trust Law's Race to the Bottom?*, 85 CORNELL L. REV. 1035, 1048-49 (2000) (noting the tax advantages for U.S. settlors of offshore trusts prior to the enactment of the Tax Reform Act of 1976).

<sup>14</sup> Act with Respect to the Powers of the President in Time of War or National Emergency, Pub. L. No. 95-223, 91 Stat. 1625 (1977).

<sup>15</sup> Evan Metaxatos, Comment, *Thunder in Paradise: The Interplay of Broadening United States Anti-Money Laundering Legislation and Jurisprudence with the Caribbean Law Governing Offshore Asset Preservation Trusts*, 40 U. MIAMI INTER-AM. L. REV. 169, 171-72 (2008).

Act (FATCA) as a component of the Hiring Incentives to Restore Employment (HIRE) Act raises the possibility that an offshore trust may be considered a “foreign financial institution” with the result that remittances to it of fixed or determinable, annual or periodic income from a U.S. source may be subjected to federal withholding tax.<sup>16</sup> FATCA materially increases the amount of reporting that may be required by persons who are beneficiaries of foreign trusts (in many cases duplicating already existing obligations) and expands the scope of persons who might be deemed to have a reportable interest without providing a clear definition of who is within the expanded scope of required reporting.<sup>17</sup> FATCA clarifies and introduces certain presumptions for the determination of when a foreign trust to which a U.S. person has contributed has a U.S. beneficiary.<sup>18</sup> Finally, FATCA requires any U.S. person considered an owner of a foreign trust under grantor trust rules to comply with new reporting requirements.<sup>19</sup> Substantial penalties may result from failing to report as required by law.<sup>20</sup>

U.S. persons may avoid such onerous tax and reporting requirements if the foreign trust of which they are a grantor or a beneficiary is brought into the U.S. and rendered “domestic” through either decanting or migration. A conversion of a trust from foreign to domestic should take into account the fact that each U.S. jurisdiction will impose a different tax burden on assets held by the repatriating trust. Before a foreign trust is converted to a domestic trust, the trustee, the protector (if any), and the beneficiaries, both U.S. and non-U.S., should investigate what additional tax burdens will be imposed in exchange for avoiding the burdens associated with enjoyment by a

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<sup>16</sup> I.R.C. § 1471(d)(5) (2011) (enacted as part of the Hiring Incentives to Restore Employment (HIRE) Act, Pub. L. No. 111-147, 124 Stat. 71, § 501 (2010)). A strong argument exists that family trusts, particularly those that include a spendthrift clause or an English-style lapse clause, should not be treated as foreign financial institutions because they are not entities engaged in business through associates who have transferrable interests. See I.R.C. § 641(b) (2011) (expressly providing that a foreign trust should be treated “as a nonresident alien individual who is not present in the United States at any time.”).

<sup>17</sup> See I.R.C. § 6038D (2011) (enacted as part of HIRE Act § 511, 124 Stat. at 71). Generally, an individual who holds an interest in requisite foreign financial assets with an aggregate value greater than \$50,000 (or a greater amount determined by the Secretary of the Treasury) must file an information return. *Id.* § 6038D(a). It remains unclear what obligations to report are owed by beneficiaries of discretionary trusts. N.Y. City Bar Ass’n, Comm. on Estate & Gift Tax, Comments on Notice 2010-22, Foreign Account Tax Compliance Act (July 12, 2011) (suggesting that the Department of Treasury apply guidance provided by the Financial Crimes Enforcement Network rules regarding Foreign Bank and Financial Account Reports rules and not require a discretionary beneficiary to make a § 6038D filing unless the beneficiary receives trust distributions during the year).

<sup>18</sup> See generally HIRE Act §§ 531, 532, 124 Stat. at 71 (codified as amended at I.R.C. § 679 (1998)).

<sup>19</sup> *Id.* §§ 534, 535 (codified as amended at I.R.C. §§ 6048(b), 6677(a) (2010)).

<sup>20</sup> *Id.* § 535 (codified as amended at I.R.C. § 6677(a)).

U.S. person of a beneficial interest in a foreign trust.

Some U.S. states impose substantial tax burdens on domestic trusts.<sup>21</sup> However, the State of Wyoming presents an ideal situs for repatriating trusts because it presently imposes no state tax on trust income or capital gains, individual or corporate income, gifts, out-of-state retirement income, mineral ownership, intangibles, and imposes a very low property tax.<sup>22</sup> While all tax laws are subject to change, future imposition of Wyoming income tax remains unlikely because of the state's substantial mineral wealth and the fact that the Wyoming Constitution requires that any income tax liability be offset by sales, use, and property taxes.<sup>23</sup>

## 2. Trusts for Non-U.S. Persons

Some foreign trusts without U.S. settlors or beneficiaries might obtain tax advantages similar to those offered by certain offshore jurisdictions by relocating to a U.S. jurisdiction, particularly one that imposes few or no state or local taxes that might adversely affect the trust or its beneficiaries. While many offshore clients have relied on traditional offshore jurisdictions, such as the Channel Islands and the Cayman Islands, some commentators now see U.S. jurisdictions as potentially favorable tax situs for non-U.S. individuals.<sup>24</sup>

At one time, federal tax law was vague about whether a trust settled in a U.S. jurisdiction by a non-U.S. person could become subject to U.S. taxes.<sup>25</sup> It was thought that settling a U.S. trust created the risk of subjecting the trust to U.S. taxes, and it was better to avoid that possibility by locating the trust in a more traditional offshore jurisdiction, like Jersey or Guernsey. The Small Business Job Protection Act of 1996<sup>26</sup> changed this by requiring that a U.S. trust satisfy both the court test and control test. Congress's primary impetus for the legislation's bias in favor of finding that a trust is foreign was to

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<sup>21</sup> See Max Gutierrez, Jr. & Frederick R. Keydel, *State Taxation on Income of Trusts with Multi-State Contacts*, in ACTEC STUDIES 6-1, 6-26, 6-58 (2001) (discussing how states tax trust income).

<sup>22</sup> Reimer, *supra* note 4.

<sup>23</sup> See WYO. CONST. art. 15, § 18 (requiring a full tax credit).

<sup>24</sup> See generally Alexander A. Bove, Jr., *The United States as an Offshore Asset Protection Trust Jurisdiction – The World's Best Kept Secret*, 14 TR. & TRUSTEES 12, 12 (2008); G. Warren Whitaker, *The U.S. May be a Good Trust Jurisdiction for Foreign Persons*, 33 EST. PLAN. 36, 36 (2006); Henry Steinway Ziegler, *Come to America*, TR. & EST., Jun. 2005, at 22, 22; Mark G. Holden, *Surprise: The U.S. is the New Tax Haven*, TR. & EST., Dec. 2003, at 64, 64.

<sup>25</sup> Whitaker, *supra* note 24.

<sup>26</sup> 104 Pub. L. No. 188 § 1907(a)(1)(E), 110 Stat. 1755 (codified as amended at I.R.C. § 7701 (2011)).

diminish the incentive to create offshore asset protection trusts.<sup>27</sup> Under the ambiguous pre-1996 trust situs rules, such offshore trusts could be construed as domestic, and therefore exempt, from reporting provisions pertinent to foreign trusts funded by U.S. persons.<sup>28</sup> Additionally, legislators believed that the bias in favor of finding a trust foreign would encourage foreign persons to employ U.S. trust companies.<sup>29</sup>

The creation of the court and control tests provided more certainty in determining whether a trust is a U.S. or foreign person for federal tax purposes.<sup>30</sup> Federal law is now heavily weighted in favor of finding a trust to be foreign rather than domestic. It also provides clear guidelines on how to create a trust in a U.S. jurisdiction that will be considered a foreign trust for federal tax purposes and therefore not subject to U.S. federal tax liability. As long as a non-U.S. person can make a substantial decision regarding the trust, such as the appointment or removal of trustees or the timing of distributions, the trust will be classified as a foreign person. Failing the control test will prevent U.S. trust status even if the trust meets all of the requirements of the court test. If a trust is foreign, federal tax liability and reporting will only be required to the extent that the trust has U.S. source income, holds U.S.-situs property, or has U.S. beneficiaries (requirements that would have existed even if the trust had not been settled in a U.S. jurisdiction).<sup>31</sup>

Beyond the question of actual tax and other reporting obligations imposed on onshore and offshore trusts, there is the issue of perception, particularly the perception of fiscal authorities in various jurisdictions. Offshore settlors of U.S. trusts may benefit from the U.S.' lack of reputation as a tax haven, although the tax-friendly status and favorable trust laws of states like Delaware have led some nations to consider the U.S. and England as potential tax havens. Many nations now blacklist traditional offshore jurisdictions, imposing new reporting and tax requirements on settlors of trusts located in such jurisdictions.<sup>32</sup> This has yet to occur against an onshore jurisdiction, but re-

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<sup>27</sup> Carlyn S. McCaffrey et al., *U.S. Taxation of Foreign Trusts, Trusts with Non-U.S. Grantors and Their U.S. Beneficiaries*, 26 ACTEC NOTES 159, 159 (2000).

<sup>28</sup> *Id.* (citing I.R.C. § 7701(a)(31) (1994) (amended 1996)) (discussing that the pre-1996 law merely stated the consequences of a foreign trust status, but did not provide a clear definition of a foreign trust).

<sup>29</sup> *Id.* at 160.

<sup>30</sup> See I.R.C. § 7701(a)(30)(E) (2011).

<sup>31</sup> Whitaker, *supra* note 24, at 37.

<sup>32</sup> *Id.* at 38; Frederick J. Tansill, *Asset Protection Planning: Planning Strategies for the Protection of Family Assets from Claims of Creditors and Other Predators*, SR042 A.L.I.-A.B.A. 271, 293 (2010); Holden, *supra* note 24, at 64.

mains possible, if not likely, to occur in the future.<sup>33</sup>

No U.S. trust jurisdiction is, so far, subject to similar blacklist or tax haven treatment, decreasing the possibility that a non-U.S. settlor will face tax inquiries outside the U.S. concerning her trust (which is onshore for U.S. purposes, but offshore from the perspective of her own home jurisdiction). But even if an offshore situs does not trigger blacklist or tax haven treatment, many such jurisdictions have earned reputations (deserved or not) as tax and creditor shelters, creating the possibility of suspicion and hostility from the government of the settlor's nation of domicile.<sup>34</sup>

There are a few possible tax disadvantages to creating U.S. trusts for foreign persons. First, fiscal legislation in a taxing jurisdiction such as the U.S. is arguably at greater risk of change than that of a non-taxing jurisdiction. For example, the Cayman Islands law permits a trustee to obtain a certificate from the Governor-in-Cabinet exempting a trust from any taxation in that jurisdiction (even if there is a change in fiscal law or policy) for fifty years from the date a trust is settled, although settlors of exempted trusts must file an application and register with the Registrar of Trusts.<sup>35</sup> In addition, one must take into account that submission to a particular jurisdiction's laws entails more than just submission to its tax laws.<sup>36</sup> But repatriation

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<sup>33</sup> See Robert Eugene DiPaolo, *Brazil Declares Delaware a Tax Haven. Nevada and Wyoming Might Be Next*, BRAZZIL (Sept. 11, 2008, 5:04 PM), <http://www.brazzil.com/articles/196-september-2008/10111-brazil-declares-delaware-a-tax-haven-nevada-and-wyoming-might-be-next.html>.

<sup>34</sup> Cf. Worldwide Tax Daily, *U.S. Cayman Islands Debate Tax Haven Status Amid Calls for Cooperation*, CAYMAN FINANCE (Sept. 23, 2009, 1:48 PM), <http://www.caymanfinances.com/Industry-News/us-cayman-islands-debate-tax-haven-status-amid-calls-for-cooperation.html>

(Eduardo D'Angelo P. Silva, vice chair of the Cayman Islands Financial Services Association, faulted the United States for allowing some states within its border to accommodate shell corporations without requiring any information about their customers. He said Delaware, Nevada, and Wyoming promote tax evasion and money laundering and qualify the United States as a tax haven.)

<sup>35</sup> The Trusts Law (Supp. 2009) §§ 73-86 (Cayman Is.); Antony G.D. Duckworth & Richard Lyle Finlay, *Cayman Islands*, in 3 ASSET PROTECTION: DOMESTIC & INT'L LAW & TACTICS § 33:38 (Duncan E. Osborne & Elizabeth M. Schurig eds., 2011); ROBERT C. LAWRENCE III, INTERNATIONAL TAX AND ESTATE PLANNING: A PRACTICAL GUIDE FOR MULTINATIONAL INVESTORS § 6:3.4 (13th release 2010).

<sup>36</sup> For example, locating a foreign trust in a U.S. jurisdiction will likely provide local courts in with personal jurisdiction over the trust's fiduciaries regarding trust matters and the trust's beneficiaries to the extent of their interests in the trust. WYO. STAT. ANN. § 4-10-202(a) (2011); accord UNIF. TRUST CODE § 202(a) cmt. (2005) ("[T]he courts of the principal place of administration have jurisdiction to enter orders relating to the trust that will be binding on both the trustees and beneficiaries."). Such persons should evaluate the substantive and procedural laws of a U.S. jurisdiction and determine whether they are willing to be subject to such laws and to be called before the courts of such jurisdiction. If the trust



need not be permanent: a jurisdiction that confers flexible authority to migrate or decant a trust should enable future migration in the event that a domestic jurisdiction fails to maintain its trust-friendly tax or substantive trust laws. For example, Wyoming law permits trustees to adhere to their duty of administering a trust in the place most appropriate to its purposes, administration, and beneficiary interests by transferring a trust's principal place of administration to another U.S. or foreign jurisdiction.<sup>37</sup> Unlike in some jurisdictions, unless there has been a court order to the contrary, Wyoming courts do not retain continuing supervision over Wyoming trusts.<sup>38</sup> Consequently, a foreign trust may temporarily migrate to Wyoming for a period of time and then repatriate to a different jurisdiction if demanded by the needs of the trust administration and the interests of the trust's beneficiaries.

Second, the revised amendments to the Bank Secrecy Act Regulations, which became effective March 28, 2011, reject the federal income tax definition for determining whether a trust is domestic or foreign.<sup>39</sup> They instead adopt the rule that a trust is domestic for purposes of determining whether it has an obligation to file a foreign accounts report on TD F 90-22.1 (Rev. March 2011) if it has been created, organized, or formed under the laws of the U.S. or any state thereof.<sup>40</sup> Imposing Foreign Bank Account Report (FBAR) filing requirements on trusts that are foreign for tax purposes may diminish the attraction of the U.S. as a jurisdiction for the administration of a trust that has no U.S. beneficiaries.<sup>41</sup>

## B. Asset Protection Considerations

Both U.S. and non-U.S. persons sometimes settle offshore trusts to achieve asset protection goals. Settlers have tended to create such trusts in jurisdictions known for their debtor-friendly trust laws, such as the Cook Islands, Jersey, and Bermuda. Asset protection for beneficiaries other than the settlor has routinely and historically been regarded as a legitimate object of trust planning, but asset protection for the trust settlor is highly controversial and many jurisdictions prohibit it.

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ever becomes the subject of litigation, it is possible such litigation will occur in the U.S. jurisdiction and both fiduciaries and beneficiaries should be prepared to contest matters in the jurisdiction in which the trust is administered. UNIF. TRUST CODE § 202 cmt. (2005).

<sup>37</sup> WYO. STAT. ANN. § 4-10-108(b)-(c) (2011).

<sup>38</sup> *Id.* § 4-10-201(b).

<sup>39</sup> Amendment to the Bank Secrecy Act Regulations – Reports of Foreign Financial Accounts, 76 Fed. Reg. 10,234, 10,238 (Feb. 24, 2011) (codified at 31 C.F.R. 1010 (2011)).

<sup>40</sup> 31 C.F.R. § 1010.350(b)(3) (2011).

<sup>41</sup> *See, e.g.*, 31 U.S.C. § 5314(a) (2011); *id.* §§ 5321–5322 (imposing civil and criminal penalties on individuals who fail to report).

Asset protection is achieved by limiting the control that a beneficiary has over the disposition of trust assets. If the beneficiary cannot alienate the right to trust distributions, then creditors are effectively prevented from attaching trust assets (provided that assets were not conveyed to the trust pursuant to a fraudulent transfer).<sup>42</sup> The long-standing common law rule, recognized by all U.S. jurisdictions until recent years, was that a settlor could not create a valid spendthrift trust for his or her own benefit.<sup>43</sup>

The Cook Islands and certain other havens filled the void by offering self-settled spendthrift trusts (also known as Offshore Asset Protection Trusts).<sup>44</sup> In response, many high-net-worth individuals and families (often medical practitioners fearing malpractice liability) created trusts in such jurisdictions.<sup>45</sup> Since the Cook Islands enacted the International Trusts Amendment Act in 1989, at least sixteen offshore jurisdictions have enacted some form of asset protection statute.<sup>46</sup> In addition to the validity of self-settled spendthrift trusts, such jurisdictions typically impose heavier burdens of proof on creditors seeking to prove a fraudulent transfer, shorten the time in which a creditor may bring a fraudulent transfer claim, refuse to grant comity to foreign judgments, require litigation be conducted in the offshore jurisdiction with the use of local professionals (who may not work on a contingent fee basis), and provide more comprehensive spendthrift protection. Some creditors may be reluctant to pursue litigation in a foreign jurisdiction that is perceived as having unfamiliar (and even hostile) laws.<sup>47</sup> Such practical and psychological barriers may chill a creditor's willingness to pursue a litigation strategy and increase the probability that the creditor will offer the defendant a debtor-friendly settlement.<sup>48</sup>

In recent years, some U.S. states, led by Alaska and Delaware, have adopted laws permitting settlors to create self-settled spendthrift trusts.<sup>49</sup> For example, Wyoming authorizes a settlor to transfer

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<sup>42</sup> See GEORGE GLEASON BOGERT, *THE LAW OF TRUSTS AND TRUSTEES* §§ 3-6, 3 n.4 (3d ed. 2007) (discussing the history of the Statute of Uses).

<sup>43</sup> *E.g.*, IIA AUSTIN WAKEMAN SCOTT & WILLIAM FRANKLIN FRATCHER, *THE LAW OF TRUSTS* § 156.2 (4th ed. 1987); GEORGE GLEASON BOGERT, *THE LAW OF TRUSTS AND TRUSTEES*, § 223 (3d ed. 2007); RESTATEMENT (THIRD) OF TRUSTS § 58(2) (2003); UNIF. TRUST CODE § 502 cmt. (2000).

<sup>44</sup> Tansill, *supra* note 32, at 298. See International Trusts Act 1984 § 13C (Cook Is.).

<sup>45</sup> David R. McNair, *Cook Islands Asset Protection Trust Law*, 3 J. BUS. ENTREPRENEURSHIP & THE L. 321, 322 (2010).

<sup>46</sup> *Id.* at 327.

<sup>47</sup> See James J. Flick & Jonathan Gopman, *Offshore Asset Protection Trusts*, in ASSET PROTECTION IN FLORIDA, § 10.2 (2d ed. 2011).

<sup>48</sup> Rothschild, *supra* note 11, at 48.

<sup>49</sup> See ALASKA STAT. § 34.40.110 (2011); DEL. CODE ANN. tit. 12, §§ 3570(11)(a)-(b), 3572 (2011); HAW. REV. STAT. § 554G-5 (2011); MO. REV. STAT. § 456.5-505 (2011); NEV. REV.

property to a Wyoming Qualified Spendthrift Trust (WQST) for his or her own benefit if the trust instrument states that it is a qualified spendthrift trust governed by the laws of Wyoming, the property is held subject to a spendthrift provision, and the trust is irrevocable.<sup>50</sup> Transfers to a WQST must be accompanied by an affidavit negating the possibility of a fraudulent transfer and stating that the settlor has adequate personal liability insurance.<sup>51</sup>

The settlor of a WQST can receive the following without causing the trust to lose its irrevocable status: trust income; GRAT, GRUT, CRUT, and CRAT distributions;<sup>52</sup> annual distributions of up to five percent of the trust's initial value; distributions at the trustee's sole discretion or subject to an ascertainable standard; and the use of real property held in a qualified personal residence trust.<sup>53</sup> A settlor may also retain the following rights without losing irrevocable status: veto distributions; an inter vivos or testamentary, general or limited power of appointment; the power to add, remove, or replace trustees, trust advisors, or trust protectors with someone other than the settlor; and act as an investment advisor.<sup>54</sup>

Like all domestic asset protection trusts, a WQST is not fool-proof. The spendthrift protection provided by a WQST is not effective against child support claims or property held by the WQST that was listed on an application or financial statement to obtain or maintain credit other than for the benefit of the WQST.<sup>55</sup> A settlor of an asset protection trust that purports to put property beyond the reach of his own creditors must also recognize that a transfer may be subject to immediate federal gift treatment.<sup>56</sup>

As in all U.S. jurisdictions, creditors may avoid fraudulent transfers to a WQST.<sup>57</sup> Wyoming imposes the Uniform Fraudulent

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STAT. § 166.040 (2010); N.H. REV. STAT. ANN. § 564-D:2 (2010); OKLA. STAT. tit. 31, §§ 16, 18 (2010); R.I. GEN. LAWS § 18-9.2-2(10) (2011); S.D. CODIFIED LAWS § 55-16-2 (2011); TENN. CODE ANN. §§ 35-16-101 to -112 (2010); UTAH CODE ANN. § 25-6-14(1)(a) (LexisNexis 2011); WYO. STAT. ANN. § 4-10-510 (2011).

<sup>50</sup> WYO. STAT. ANN. § 4-10-510(a).

<sup>51</sup> *Id.* §§ 4-10-512(b), 523.

<sup>52</sup> Grantor retained annuity trusts (GRATs), grantor retained unitrusts (GRUTs), charitable remainder unitrusts (CRUTs), and charitable remainder annuity trusts (CRATs) are popular estate planning devices that permit settlors to transfer assets with little or no gift tax exposure. David A. Herpe & Jeanette Suarez Hunter, *Proposed Regulations Clarify Includability of Grantor Retained Annuity Trust in Grantor's Gross Estate*, 33 ACTEC J. 131, 131 (2007).

<sup>53</sup> WYO. STAT. ANN. § 4-10-510.

<sup>54</sup> *Id.*

<sup>55</sup> *Id.* § 4-10-520(a)(i), (ii).

<sup>56</sup> See *Paolozzi v. Comm'r*, 23 T.C. 182, 187 (1954); Rev. Rul. 76-103, 1976-1 C.B. 293; I.R.S. Priv. Ltr. Rul. 93-32-006 (Aug. 13, 1993).

<sup>57</sup> WYO. STAT. ANN. §§ 4-10-520(a)(iii), 521(a) (2011).

Transfer Act's limitations periods on creditors seeking to avoid a fraudulent transfer, which are longer than what are typically provided by an offshore jurisdiction.<sup>58</sup> Wyoming law also imposes a less stringent burden of proof on such creditors, only requiring them to prove that a transfer was fraudulent by a preponderance of the evidence as to settlors and by clear and convincing evidence as to beneficiaries and trustees.<sup>59</sup> Creditors also face fewer barriers to bringing an action to avoid a transfer in Wyoming.<sup>60</sup> Wyoming courts use a typical common law court system that will be familiar to most creditors. The State of Wyoming also offers a wide range of legal and other professionals for creditors to employ, a task that would be daunting in many offshore jurisdictions.

A WQST's effectiveness may also be limited by constitutional considerations. The largest shortcoming of any domestic asset protection trust is that U.S. courts must give full faith and credit to the final judgments of sister courts in other U.S. states.<sup>61</sup> This has given rise to much scholarly debate as to whether a court in a state like Wyoming must enforce a judgment against a self-settled spendthrift trust obtained in a state that does not recognize such trusts.<sup>62</sup> To date, no court has resolved the question of whether a self-settled spendthrift trust is susceptible to attachment on such grounds, and there is an argument that a Wyoming court should not enforce such judgments because they conflict with the strong public policy of the forum state. Yet the Full Faith and Credit issue poses inherent risk and uncertainty to WQSTs that will persist until courts have had a chance to develop case law on the subject. Such risks do not exist with regard to offshore asset protection trusts,<sup>63</sup> but conflicts of laws issues may apply

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<sup>58</sup> *Id.* §§ 4-10-514, 34-14-210(a).

<sup>59</sup> *Id.* § 4-10-521(b).

<sup>60</sup> Richard C. Ausness, *The Offshore Asset Protection Trust: A Prudent Financial Planning Devise or the Last Refuge of a Scoundrel?*, 45 DUQ. L. REV. 147, 158 (2007) (noting that domestic jurisdictions generally lack the litigation barriers of offshore jurisdictions).

<sup>61</sup> U.S. CONST. art. IV, § 1.

<sup>62</sup> See David A. Lockwood, *U.S. Domestic Trusts as Asset Protection Planning Tools: An Oxymoron*, in ASSET PROTECTION STRATEGIES, *supra* note 11, at 15, 19; Lynn Foster, *Fifty-One Flowers: Post-Perpetuities War Law and Arkansas's Adoption of USRAP*, 29 U. ARK. LITTLE ROCK L. REV. 411, 432-33 (2007); Karen Gebbia-Pinetti, *As Certain as Debt and Taxes: Estate Planning, Asset-Protection Trusts, and Conflicting State Law*, SC60 A.L.I.-A.B.A. 179, 242-43 (1998); John Paul Parks, *Evaluating the Alaska Trust's Ability to Shield Assets from the Claims of Creditors*, 35 ARIZ. ATT'Y 28, 29-30 (1998). *But see* David G. Shaftel & David H. Bundy, *Domestic Asset Protection Trusts 10-11* (2005) (unpublished manuscript) (on file with author), available at [http://shaftellaw.com/docs/article\\_23.pdf](http://shaftellaw.com/docs/article_23.pdf); Richard W. Nenno, *Planning with Domestic Asset-Protection Trusts* 63 (Apr. 29, 2005) (unpublished manuscript), available at [http://apps.americanbar.org/rppt/meetings\\_cle/2005/spring/pt/AssetProtectionPlanning/NE\\_NNO\\_hand.pdf](http://apps.americanbar.org/rppt/meetings_cle/2005/spring/pt/AssetProtectionPlanning/NE_NNO_hand.pdf).

<sup>63</sup> Other constitutional issues include the contracts clause and the supremacy clause. See Leslie C. Giordani & Duncan E. Osborne, *Will the Alaska Trusts Work?*, 3 J. ASSET PRO-

that can affect the practical effectiveness of a spendthrift or protective trust established in offshore jurisdictions.

In addition to Full Faith and Credit, any settlor of a transnational trust must consider the issue of international comity. While the comity doctrine has been characterized in a variety of ways and has evolved over time, it generally stands for the principle that domestic courts should apply foreign law or limit domestic jurisdiction when necessary to respect foreign sovereignty.<sup>64</sup> Full Faith and Credit and comity may pose less of an issue to WQSTs that do not have U.S. settlors or beneficiaries, provided that the trust assets are under the control of a U.S. court. While a U.S. court may grant comity to a foreign judgment, the Constitution does not require it to grant full faith and credit. No uniform foreign comity rule exists among U.S. jurisdictions, although the Supreme Court has stated in the past that comity should be granted if a competent foreign court, with jurisdiction over a matter, renders a final judgment for a sum of money following a fair proceeding that provides an opportunity to defend and creates a formal record.<sup>65</sup> State courts need not apply this test.<sup>66</sup> Nonetheless, U.S. jurisdictions generally grant comity as to the parties and underlying claims of “a valid judgment rendered in a foreign nation after a fair trial in a contested proceeding.”<sup>67</sup>

However, foreign settlors of WQSTs do have a few safeguards against comity. For example, a Wyoming court may hold that enforcement of a judgment against assets held by a WQST offends well-settled policy articulated by the Wyoming legislature. Further, in the absence of a tax treaty, a Wyoming court will likely not grant comity to a foreign court’s “judgments for the collection of taxes, fines, or penalties rendered by the courts of other states.”<sup>68</sup> Finally, there is a

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SECTION 7, 11-13 (1997); Duncan E. Osborne et al., *Asset Protection and Jurisdiction Selection*, 33 HECKERLING INST. ON EST. PLAN. ¶ 1404.5 (1999); Duncan E. Osborne & Mark E. Osborne, *Asset Protection: Trust Planning*, SR034 A.L.I.-A.B.A. 201, 250-55 (2010).

<sup>64</sup> Joel R. Paul, *The Transformation of International Comity*, 71 LAW & CONTEMP. PROBS. 19, 20-21 (2008); Joel R. Paul, *Comity in International Law*, 31 HARV. INT’L L.J. 1, 3 (1991).

<sup>65</sup> *Hilton v. Guyot*, 159 U.S. 113, 205-06 (1895).

<sup>66</sup> See *Tahan v. Hodgson*, 662 F.2d 862, 867-68 (D.C. Cir. 1981) (noting that the *Hilton* test is no longer a federal mandate: “It is unlikely that reciprocity is any longer a federally mandated requirement for enforcement of foreign judgments or that the District of Columbia itself has such a requirement that this court is obliged to follow.”); *McCord v. Jet Spray Int’l Corp.*, 874 F. Supp. 436, 439 (D. Mass. 1994) (applying state reciprocity law, rather than the *Hilton* test).

<sup>67</sup> RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 98 (1988).

<sup>68</sup> RESTATEMENT (THIRD) OF FOREIGN RELATIONS LAW § 483 (1987); *accord* Annotation, *Conclusiveness as to Merits of Judgment of Court of Foreign Country*, 148 A.L.R. 991 (Cum. Supp. 2011) (“Common law revenue rule holds that courts generally will not enforce foreign tax judgments, just as they will not enforce foreign criminal judgments, although they will enforce foreign nontax civil judgments unless due process, jurisdictional, or fundamental public policy considerations interfere . . .”). Some courts have criticized the per se applica-

strong likelihood that the foreign court will lack personal jurisdiction over the trustee of a WQST if the trustee has no legal presence in that jurisdiction, which should bar comity.<sup>69</sup> If the trust assets are not located in the U.S.; however, the relevant recovery proceedings might take place outside of the U.S. and in a jurisdiction that would be prepared to recognize and enforce the foreign judgment. Correct structuring of an arrangement is crucial for effective asset protection structures.

While a domestic asset protection trust with U.S. settlors and beneficiaries may never offer the same degree of substantive asset protection as an offshore trust, for such persons other factors may tip the scales in favor of onshore trusts. First, offshore asset protection trusts have grown less attractive to U.S. persons following the enactment of substantially enhanced tax and reporting requirements in 1996, requirements that have been repeatedly augmented since then, most recently by FATCA and the HIRE Act.<sup>70</sup> Second, penalties for non-compliance with reporting of foreign trusts and foreign accounts have been materially increased to the point of being confiscatory, and criminal prosecutions have become more common for evasion that has utilized unreported foreign trusts, entities, and accounts.

Third, even offshore asset protection is not absolute. Settlers of offshore trusts subject themselves to the risk of being held in contempt by a domestic court for failure to repatriate offshore assets.<sup>71</sup> What a domestic court lacks in jurisdiction over offshore assets, it can make up for by asserting jurisdiction over the settlor of the trust and exercising its inherent authority to fine or imprison the settlor for not complying with a court order. Even if the terms of the trust render it impossible for the settlor to repatriate offshore assets, a judge may

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tion of the common law revenue rule and limited its scope, particularly in situations concerning criminal and civil actions that have the indirect effect of enforcing foreign revenue laws, but are based on U.S. statutes. See *Pasquantino v. United States*, 544 U.S. 349, 362 (2005) (holding the revenue rule did not prohibit a criminal wire fraud prosecution by the U.S. that had the collateral effect of enforcing a foreign revenue law); *European Cmty. v. RJR Nabisco, Inc.*, 150 F. Supp. 2d 456, 481 (E.D.N.Y. 2001) (holding that the revenue rule is discretionary and refusing to apply it a suit arising from the Racketeering and Racketeer Influenced and Corrupt Organizations (RICO) Act). But see *European Cmty. v. RJR Nabisco, Inc.*, 424 F.3d 175, (2d Cir. 2005) (distinguishing *Pasquantino* because it involved an action brought by the U.S. as a sovereign to enforce federal law, rather than a foreign nation appearing as a plaintiff attempting to enforce its revenue laws); *Att'y Gen. of Canada v. R.J. Reynolds Tobacco Holdings, Inc.*, 268 F.3d 103, 126 (2d Cir. 2002) (holding that the RICO Act did not abrogate the common law revenue rule insofar as it applies to a foreign sovereign's attempt to directly or indirectly enforce its substantive revenue laws in U.S. courts).

<sup>69</sup> Bove, *supra* note 24, at 21.

<sup>70</sup> See *supra* text accompanying notes 16-20.

<sup>71</sup> See *FTC v. Affordable Media, LLC*, 179 F.3d 1228, 1238-39 (9th Cir. 1999); *In re Lawrence*, 238 B.R. 498, 500-01 (Bankr. S.D. Fla. 1999).

find that such self-created impossibility does not bar a contempt order.<sup>72</sup> The fact that a settlor established a trust in a traditional asset protection jurisdiction may also increase the perception that the settlor has engaged in fraud, contributing to the overall hostility and skepticism of the court and the possibility that the transfers will be deemed fraudulent.

### C. Structural Considerations

The very features that make an offshore trust a challenge for a creditor seeking to attach assets of a debtor may make a settlor with no particular interest in asset protection wary. Clients may feel uncomfortable with having their trusts managed in a jurisdiction with which they have never had personal contact, that is far away, and has unfamiliar laws.

An onshore jurisdiction such as Delaware, South Dakota, or Wyoming would not cause most U.S. resident settlors the same level of nervousness as a foreign (to them) jurisdiction; the onshore jurisdiction must afford sound, well-developed infrastructure for the management of trusts in order to be competitive with sister state jurisdictions vying for trust business.<sup>73</sup> Such infrastructure should include an efficient court system, a modern trust law, a political atmosphere conducive to the maintenance of user-friendly trust legislation, the presence of skilled trust service providers (which might but need not necessarily include major nationally recognized financial institutions), and local professionals having demonstrated competence to provide counsel on trust and estate planning matters.

Well-developed infrastructure can also be found in several of the well-known offshore jurisdictions. Jurisdictions such as the Cayman Islands, Bermuda, and the British Virgin Islands (among others) inherited their trust laws from England and made numerous highly creative improvements to English trust law during the last thirty years.<sup>74</sup> These improvements were in some cases initially scorned in England but have since been acknowledged both there and in many U.S. states, which have been quick to borrow and adapt for themselves concepts such as the trust protector and the non-charitable purpose trust.<sup>75</sup>

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<sup>72</sup> *Lawrence*, 238 B.R. at 501. See *Affordable Media*, 179 F.3d at 1239, 1240.

<sup>73</sup> See Holden, *supra* note 24, at 64-65.

<sup>74</sup> See Denis Kleinfeld, *Choosing an Offshore Jurisdiction*, in ASSET PROTECTION STRATEGIES, *supra* note 11, at 73, 74-85 (discussing trust law developments in several common law nations that derive their laws from the British legal system).

<sup>75</sup> See Stewart E. Sterk, *Trust Protectors, Agency Costs, and Fiduciary Duty*, 27 CARDOZO L. REV. 2761, 2764 (2006) (discussing the origin of trust protectors in the context of offshore

In addition to developing and enacting innovative statutory improvements, many of the offshore jurisdictions inherited case law precedent dating back almost 1,000 years, carrying great certainty in meaning and effect of trust arrangements and consistency of court decisions.<sup>76</sup> Furthermore, most of those jurisdictions have never deviated from the property law basis of trusts law, thus ensuring consistency across those jurisdictions in the way in which a trust may be structured and operate. Some jurisdictions, including many U.S. states, have deviated from the strict property law approach with the result that jurisprudence in those jurisdictions differs in some cases quite markedly from what might be found in jurisdictions that have adhered more closely to English judicial precedent.<sup>77</sup> Some settlors

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trusts and their use in England and the U.S.) (citing Antony Duckworth, *Protectors—Fish or Fowl?*, 4 J. INT'L TR. & CORP. PLAN. 137, 168 (1995)); Rebecca Probert, *Acts Inter Vivos Related to the Estate*, in 2 INT'L ENCYC. OF LAWS: FAMILY AND SUCCESSION LAW § 3 (2011) (discussing limited circumstances in which the courts of England and Wales will recognize a non-charitable purpose trust); Wendy S. Goffe, *An Introduction to Lesser-Known But Useful Trusts—Part 2*, 37 EST. PLAN. 3, 3-5 (2011) (discussing the development of purpose trusts).

<sup>76</sup> The same may not be the case in offshore jurisdictions that are civil law governed, even if a form of trusts law has been introduced by statute. Fundamental to the enforcement of a trust in common law jurisdictions is the property law concept of divided property rights, so that there is an equitable property interest that can be enforced in equity. Absent that, it is difficult to see how the courts in those jurisdictions can apply what would be recognized in a common law jurisdiction as ordinary equitable remedies. See M. Read Moore, *Tax and Estate Planning Issues for U.S. Clients Who Own Foreign Property*, SS010 A.L.I.-A.B.A 1885, 1892 (2010) (noting civil law nations' lack of bifurcation of legal and equitable interests). The results of litigation in such jurisdictions and the meaning and proper construction of trust documents is far less predictable. Such jurisdictions include Panama, Jersey, and Guernsey. See Keith S. Baker & Edward Devenport, *Jersey*, in ASSET PROTECTION, *supra* note 35, § 39:55 (discussing Jersey's balance of English common law, Norman common law, and the French Civil Code); *id.* § 39:63 (discussing the statutory and common law basis for Jersey trusts); Peter J.G. Atkinson et al., *Guernsey*, in ASSET PROTECTION, *supra* note 35, § 37:63 (discussing the statutory and common law background for Guernsey trusts). There has, however, been trust litigation and statutory refinement in both Jersey and Guernsey that has served to address and resolve many of the questions that originally arose from the grafting of trust law on to the law of a civil jurisdiction (such as the proper disposition of the Norman sham trust doctrine of *donner et retenir ne vaut rien*). See, e.g., *Rahman v. Chase Bank and Trust Co.*, (1991) Jersey L.R. 103, 168-69 (Roy. Ct.) (discussing Jersey's sham trust doctrine). In addition, the trust and estate bars of Jersey and Guernsey are well developed and highly conversant with modern trust doctrine as it has evolved in the offshore jurisdictions including the U.S. Additionally, by not receiving England's common law of trusts, Jersey and Guernsey have not had to repeal the RAP.

<sup>77</sup> Most U.S. states have for well more than a century adhered to the proposition established by *Clafin v. Clafin*, 20 N.E. 454, 456 (Mass. 1889), that the wishes of a settlor should prevail over those of the beneficiaries, contrary to the English property law principles, so that, for example, the principle known as the *Rule in Saunders v. Vautier*, which permits property rights to be alienated, does not apply. Compare *Saunders v. Vautier*, (1841) 49 Eng. Rep. 282 (M.R.)

(When a legacy is directed to accumulate for a certain period, or where the payment is postponed, the legatee, if he has an absolute indefeasible interest [in the legacy], is not bound to wait until the expiration of that period, but may require payment the moment he is competent to give a



may see this as desirable, providing them with greater control over the disposition of their property. Additionally, undesirable results from inflexible irrevocable trusts can be addressed through reformation and modification principles.<sup>78</sup> The more reputable offshore jurisdictions also have the advantage of the presence of quality trustees and advisors of the highest caliber.<sup>79</sup>

An offshore trust structure might require the employment of professionals in a variety of jurisdictions, increasing costs and exposing the settlor to liability in multiple jurisdictions.<sup>80</sup> The same issue could apply in the context of the U.S. federal system, where the fifty states have enacted their own trust laws and established their case law, but such risks are mitigated by the use of uniform statutes, fairly analogous common law, close geographical proximity, and professional entities that routinely operate in the stream of interstate commerce.

If a conflict arises with respect to a trust, there is risk in some of the offshore jurisdictions, particularly those that do not have a long tradition of providing trust services to foreign parties, that there will be inadequately trained personnel to deal with the complexities of a particular problem. There is also the possibility that it will be difficult or impossible for a foreign settlor or beneficiary to retain competent, non-conflicted counsel due to local professionals' expectation and fear of offending local financial institutions in a lightly populated jurisdiction. There are instances in which foreign trust litigation has grown extremely expensive as a result of the need to import overseas attorneys and experts.<sup>81</sup>

Another factor that can affect the choice of location for a trust is that of local political and economic stability. The U.S. has the advantage of long established political stability and, in the case of those states that have an established record of attracting trust business, reasonable financial stability. Offshore trust havens such as the Cayman Islands, a British Overseas Territory, likewise enjoy political stability due to their continuing links with Great Britain and their

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valid discharge.),

with *In re* Will of Hamburger, 201 N.W. 267, 271 (Wis. 1924) (giving effect to the settlor's intent and holding that property must be held in trust for a widow's benefit, regardless of her wishes).

<sup>78</sup> See, e.g., WYO. STAT. ANN. §§ 4-10-411 to 417 (2011).

<sup>79</sup> In the Cayman Islands, for example, available trustees include (to name but a few) affiliate companies of Bank of America (Merrill Lynch), Bank of New York, HSBC, Royal Bank of Canada and Standard Chartered.

<sup>80</sup> Ziegler, *supra* note 24.

<sup>81</sup> See *Court Fiasco*, BERMUDAPOLICE.COM, [http://www.bermuda.org.uk/court\\_fiasco.htm](http://www.bermuda.org.uk/court_fiasco.htm) (last visited Jan. 8, 2012). The infamous Bermuda case of *Baron HH Thyssen-Bornemisza v. G.H. Thyssen-Bornemisza & Ors* provides an example of how expensive and difficult such a dispute can become.

English common law traditions and the absence of any local manifestation of a desire to sever such links.<sup>82</sup>

Cost can also be a relevant factor to a settlor's decision of where to locate a trust. How much the settlor is willing to spend to create and maintain a trust will depend upon the settlor's net worth and objectives in setting up a trust structure. An onshore trust should be less expensive to create and administer if the settlor is a U.S. person, but if the settlor is a foreign person, there is no assurance that the costs of familiarizing with U.S. laws, customs, and habits will be any less than they would be if one of the established offshore havens were selected.

#### D. Substantive Law Considerations

A settlor's selection of trust situs will often be influenced by the flexibility of the substantive law of the situs. Old English common law is, in many cases, not responsive to modern estate planning, tax mitigation, asset protection, and investment management needs. Jurisdictions, both onshore and offshore, have been engaged in a healthy competition for the past thirty years to develop new law that is responsive to clients' needs.

Particularly noteworthy has been the race among jurisdictions to abolish or significantly relax the common law RAP. The purpose of this is to facilitate long term trust planning aimed at mitigating taxes, affording greater asset protection, and precluding arbitrary trust terminations, which may destroy family wealth depending upon circumstances at the moment of termination. Other recent developments, both onshore and offshore, include the following:

- The power to elect the application of the local law of the jurisdiction (rather than what is called the "whole law" for conflicts of law purposes) in order to avoid forced heirship laws that may apply in the settlor's domicile;
- Enhanced privacy protection;
- Directed trusts (otherwise known as reserved power trusts);
- Protectors or protector committees and trust advisors or trust advisor committees (i.e., recognized roles for supernumeraries);
- Special purpose entities;
- Charitable and non-charitable purpose trusts;
- Limited investment standards;
- Non-judicial settlement agreements;

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<sup>82</sup> The Crown (essentially operating through the British Government) is represented in the Cayman Islands by a Governor. The Leader of Government Business of the Cayman Islands is democratically elected and, within the confines of being a British Overseas Territory, the jurisdiction enjoys relative autonomy in government.

- Flexible trust modification, reformation, and migration procedures;
- Decanting;
- Virtual representation;
- Regulated and unregulated private trust companies;
- Protected mandatory and discretionary distribution interests; and
- LLC and Family Limited Partnership (FLP) statutes.<sup>83</sup>

An advantage of a U.S. situs that diverges from traditional English common law principles is the indisposition of American courts to void a trust based upon the claim that it is a “sham in form” due to the reservation by the settlor or substantial powers over the trust. A trust may be disregarded under English common law principles if the settlor retains too much control over the trust.<sup>84</sup> In essence, the doctrine may cause a trust not to be validly established if the settlor fails to set up an arrangement under which equity may intervene sufficiently for him to have parted with dominion over the settled assets. In those circumstances, the trust may be regarded not as an *inter vivos* disposition but a “testamentary” disposition that requires different formalities for its execution that are generally not observed. In one notable case, a Jersey, Channel Islands, court held that a trust settled by a Lebanese settlor to avoid forced heirship in his home nation was a sham for reasons that included the level of control the settlor retained, the failure of the parties to adhere to the terms of the trust instrument, and the settlor’s lack of personal knowledge about how trusts operate.<sup>85</sup>

Perceiving that most modern settlors want to reserve substantial powers over their trusts unless there are compelling tax or asset protection reason for them not to do so, and that they will not cede certain powers during their lifetime either to an unrelated trustee or even to a family committee known as a “protector,” numerous offshore jurisdictions, the Cayman Islands among them, have addressed common law concerns about the effect of excessive reserved settlor powers by legislating the right of a settlor to reserve certain specifically enumerated powers without risk of his trust being held void as an invalid testamentary instrument.<sup>86</sup>

Almost as lively as the argument over reserved powers, which has led some English commentators to brand American style trusts

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<sup>83</sup> See Reimer, *supra* note 4, at 197-98 (explaining that care needs to be taken concerning how such entities might be recognized or treated in other jurisdictions under conflict of laws principles).

<sup>84</sup> See Ziegler, *supra* note 24, at 23.

<sup>85</sup> Rahman v. Chase Bank and Trust Co., (1991) Jersey L.R. 103, 168-69 (Roy. Ct.).

<sup>86</sup> See, e.g., The Trusts Law (Supp. 2009) §§ 13-15 (Cayman Is.).

“shams in form,” has been the debate over the so called “black hole” trusts, a form of totally discretionary English trust from which it is impossible to discern who the beneficiaries are without resorting to a “letter of wishes” containing the real substance of the trust declaration, deed, or agreement.<sup>87</sup> Trusts in which the real essence can be found in the letter of wishes are sometimes called “shams in substance.”

The English disposition to set out the expectations and hopes of a settlor in a letter of wishes which is characterized as legally non-binding but nonetheless legally meaningful is something of a mystery to American practitioners who are often justifiably faulted for giving a trustee virtually no guidance in respect of the exercise of discretions after their lifetime other than the tax driven “health, education, support and maintenance” standard. Although the letter of wishes is not without its own problems (including the often contested issue of access to the letter), at least one modern American commentator has urged American planners to consider its potential benefits.<sup>88</sup>

## II. Different Migration Methods

There exist three principal means to migrate a trust (or its assets) from one jurisdiction to another with the effect that there is a change of governing law:

- (1) Resignation of the original trustee and appointment of a new trustee in the target jurisdiction to administer the trust;
- (2) “Decant” the original trust’s assets by having the trustee appoint or otherwise transfer them to an independently established trust in the target jurisdiction either on its own initiative or pursuant to a direction from a protector or family advisory committee;
- (3) Termination of the trust and creation of a new trust by the beneficiaries.<sup>89</sup>

The ideal means of changing a foreign trust’s situs will depend on the terms of the trust, the situs and nature of the assets of the trust, the goals of the settlors and beneficiaries, and the governing law of the old trust.

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<sup>87</sup> See GRAHAM MOFFAT ET AL., TRUSTS LAW: TEXT AND MATERIALS 232-33 (4th ed. 2005).

<sup>88</sup> See Alexander A. Bove, Jr., *The Letter of Wishes: Can We Influence Discretion in Discretionary Trusts?*, 35 ACTEC J. 38, 39, 44 (2009).

<sup>89</sup> See LAWRENCE, *supra* note 35, § 6:7.1 to .3 (discussing the three basic repatriation methods).

Each method carries inherent features that may be advantageous or disadvantageous to the parties' needs and to the tax consequence of the restructuring. For example, a migration of a foreign trust to the U.S. offers more certainty that the restructuring will not produce an accelerated recognition of U.S. federal income tax on the undistributed net income of the foreign trust than a decanting.<sup>90</sup>

Often, the most effective method may be one explicitly authorized by the terms of the original trust instrument (especially in the case of trust terms conferring a special power of appointment or other distribution upon a trustee to establish new trusts over assets). If the terms of the trust do not provide such authority, a trustee may need to obtain court approval. In many jurisdictions, such approval may depend on the terms of the trust and any extrinsic evidence of the settlor's intent, or evidence as to the benefit to be achieved for the beneficiaries by granting approval.

### III. The Power to Change Governing Law

In the U.S., like in most other jurisdictions, absent a designation in the instrument, questions of a trust's construction and administration are typically governed according to the laws of the jurisdiction in which the trust is primarily administered.<sup>91</sup> Questions of a trust's validity are usually determined by the laws of the jurisdiction designated by the trust instrument so long as that jurisdiction has a substantial relationship with the trust and that jurisdiction's law does not offend the strong public policy of a jurisdiction with a closer relationship to the trust.<sup>92</sup>

Jurisdictions that have ratified and formally adopted the Hague Convention Governing the Law Applicable to Trusts and on their Recognition (the "Hague Convention") arguably confer almost untrammelled ability upon a settlor to freely to choose a governing law for his trust regardless of nexus, but only a few jurisdictions have ratified the 1985 Hague Convention.<sup>93</sup> The American Uniform Trust

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<sup>90</sup> Rev. Rul. 91-6, 1991-1 C.B. 89.

<sup>91</sup> See RESTATEMENT (SECOND) OF CONFLICT OF LAWS §§ 268, 272 (1971).

<sup>92</sup> *Id.* §§ 269, 269 cmt. i, 270 (1971). See also *Wilmington Trust Co. v. Wilmington Trust Co.*, 24 A.2d 309, 313 (Del. 1942) (holding that a court should not disregard a settlor's intent that a trust be administered according to the laws of a jurisdiction with a material connection to the trust).

<sup>93</sup> Antipathy of the U.S. (in particular those states which seek to attract out-of-state trust business, among which New York was the pioneer) and of many of the offshore trust jurisdictions to the Hague Convention Governing the Law Applicable to Trusts and on their Recognition may be attributed to the choice of law provisions which provide *inter alia* that

[t]he Convention does not prevent the application of provisions of the law designated by the conflicts rules of the forum, in so far as those provisions cannot be derogated from by voluntary act, relating in particular

Code (UTC), which has served as a template for the modern trust law of many U.S. states, grants similarly untrammelled authority to a settlor to choose the governing law for his trust.<sup>94</sup>

Any choice of law pursuant to the authority conferred by the Convention or the law of a state following the UTC model that entirely ignores the nexus is at risk of being challenged on the ground that the choice offends the *ordre public* of a jurisdiction having a close connection with the trust—typically the jurisdiction of the settlor’s domicile. If that happens, query whether the forum provided by the place of trust administration will be inclined to apply the chosen law of a foreign jurisdiction that has no meaningful connection with the trust.

The original choice of law and the enforceability of such choice will affect a later endeavor to change the governing law. The Convention provides simply that “[t]he law applicable to the validity of a trust shall determine whether that law or the law governing a severa-

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to the following matters – a) the protection of minors and incapable parties; b) the personal and proprietary effects of marriage; c) succession rights, testate and intestate, especially the indefeasible shares of spouses and relatives; d) the transfer of title to property and security interests in property; e) the protection of creditors in matters of insolvency; f) the protection, in other respects, of third parties acting in good faith.

Hague Convention on the Law Applicable to Trusts and on Their Recognition art. 15, July 1, 1985 [hereinafter Hague Convention]. Historically, Anglo-American law has not imposed forced heirship and, in consequence, trust jurisdictions subject to Anglo-American law have enhanced their attractiveness to civilian settlors (and to overseas U.S. citizens) by providing that the local law shall govern heirship matters to the exclusion of the whole law which might import the law of the settlor’s domicile.

<sup>94</sup> UNIF. TRUST CODE § 107 (2000). Commentary published by the National Conference of Commissioners on Uniform State Laws observes that:

Usually, the law of the trust’s principal place of administration will govern administrative matters and the law of the place having the most significant relationship to the trust’s creation will govern the dispositive provisions.

This section is consistent with and was partially patterned on the Hague Convention on the Law Applicable to Trusts and on their Recognition, signed on July 1, 1985. Like this section, the Hague Convention allows the settlor to designate the governing law. Hague Convention art. 6. Absent a designation, the Convention provides that the trust is to be governed by the law of the place having the closest connection to the trust. Hague Convention art. 7. The Convention also lists particular public policies for which the forum may decide to override the choice of law that would otherwise apply. These policies are protection of minors and incapable parties, personal and proprietary effects of marriage, succession rights, transfer of title and security interests in property, protection of creditors in matters of insolvency, and, more generally, protection of third parties acting in good faith. Hague Convention art. 15.

*Id.* § 107 cmt. (2006).

ble aspect of the trust may be replaced by another law.”<sup>95</sup> The UTC is substantially more expansive. It imposes upon the trustee the “continuing duty to administer the trust [in] a place appropriate to its purposes, its administration and the interests of the beneficiaries” and, subject to the power of a court to override or a qualified beneficiary to object, grants the trustee the power to “transfer the trust’s principal place of administration to another [s]tate” or outside the U.S.<sup>96</sup>

For an existing foreign trust whose law governing validity does not foreclose a change of governing law, Wyoming law enables simplified in-bound trust migration through the appointment of a Wyoming trustee to administer the trust.<sup>97</sup> Once a Wyoming trustee accepts trusteeship of the trust and some administration occurs in the State of Wyoming, state law considers the trust to have transferred situs to Wyoming.<sup>98</sup> Thereafter, Wyoming law should apply to questions of construction and administration if the trust instrument does not designate a governing law.<sup>99</sup> Without such a designation, the administration of a Wyoming trust will be governed by “the law of the jurisdiction having the most significant relationship to the matter at issue.”<sup>100</sup> The statute specifies that a trust’s principal place of administration (Wyoming) will “be the most heavily weighted factor,” followed by the location of trust property, followed by the domicile of beneficiaries and settlors.<sup>101</sup> Thus, if a Wyoming trustee is appointed to administer the trust in Wyoming and trust assets are located in Wyoming, it is almost certain that the situs transfer will be effective and Wyoming law will govern questions of construction and admin-

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<sup>95</sup> Hague Convention *supra* note 93, art. 10. According to the Explanatory Report for the Convention, article 10 was the subject of considerable debate regarding the specific circumstances under which power could be derived to change the law of a trust, it finally being agreed that the question would have to be referred back to the law governing the validity of the trust when created. See ALFRED E. VON OVERBECK, EXPLANATORY REPORT FOR THE HAGUE CONVENTION GOVERNING THE LAW APPLICABLE TO TRUSTS AND ON THEIR RECOGNITION ¶¶101-02 (1985), available at <http://www.hcch.net/upload/expl30.pdf>.

<sup>96</sup> UNIF. TRUST CODE § 108 (2000). Commentary published by the National Conference of Commissioners on Uniform State Laws observes that:

This section prescribes rules relating to a trust’s principal place of administration. Locating a trust’s principal place of administration will ordinarily determine which court has primary if not exclusive jurisdiction over the trust. It may also be important for other matters, such as payment of state income tax or determining the jurisdiction whose laws will govern the trust.

*Id.* § 108 cmt. (2006) (citations omitted).

<sup>97</sup> WYO. STAT. ANN. §§ 4-10-107, 108, 202 (2011).

<sup>98</sup> *Id.* §§ 4-10-108, 202 (2011).

<sup>99</sup> *Id.* § 4-10-107(a).

<sup>100</sup> *Id.* § 4-10-107(a)(ii).

<sup>101</sup> *Id.*

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Some trust instruments may designate which jurisdiction's law should govern the administration of a trust without providing circumstances under which the law governing trust administration may or should change. An unequivocal proviso that a trust's administration should forever be governed by the law of a particular jurisdiction can become problematic on account of both the possibility that one of the reasons for the change of governing law might have been to escape some aspect of the original administrative law and the practical reality that it is difficult and expensive for the court of one jurisdiction to apply the administrative laws of another jurisdiction. The problem is exacerbated once such a trust becomes irrevocable.

Wyoming law permits a court to modify a restrictive provision regarding the law that governs trust administration. Wyoming's version of the UTC permits a court to "modify the administrative terms of a trust if continuation of the trust on its existing terms would be impracticable or wasteful or impair the trust's administration."<sup>102</sup> This section implements the general principle that a trust should be administered for the benefit of its beneficiaries. It cannot be directly traced to the common law, although some U.S. states provide similar means of modification by statute.<sup>103</sup>

Wyoming law further provides that "[t]he law of the jurisdiction designated in the terms of the trust may be changed to the principal place of administration by a court with subject matter jurisdiction."<sup>104</sup> This provision is unique to Wyoming and is unavailable in most of the other twenty-two jurisdictions that, as of early 2012, have adopted some version of the UTC.<sup>105</sup> Utah and Ohio also deviate somewhat from the UTC by allowing trusts to be administered according to the local law of administration.<sup>106</sup>

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<sup>102</sup> UNIF. TRUST CODE § 412(b) (2000); WYO. STAT. ANN. § 4-10-413 (2011).

<sup>103</sup> UNIF. TRUST CODE § 412(b) cmt. (2006) (citing MO. REV. STAT. § 456.590.1 (2006)).

<sup>104</sup> WYO. STAT. ANN. § 4-10-107(b) (2011).

<sup>105</sup> See ALA. CODE § 19-3B-107 (2011); ARIZ. REV. STAT. ANN. § 14-10107 (2011); ARK. CODE ANN. § 28-73-107 (2011); D.C. CODE § 19-1301.07 (2011); FLA. STAT. § 736.0107 (2011); KAN. STAT. ANN. § 58a-107 (2010); ME. REV. STAT. tit. 18-B, § 107 (2011); MICH. COMP. LAWS ANN. § 700.7107 (West 2011); MO. REV. STAT. § 456.1-107 (2011); NEB. REV. STAT. § 30-3807 (2011) (except terms pertaining to Nebraska real estate title); N.H. REV. STAT. ANN. § 564-B:1-107 (2011); N.M. STAT. ANN. § 46A-1-107 (West 2011); N.C. GEN. STAT. § 36C-1-107 (2010) (except the rights of non-trustees and non-beneficiaries); N.D. CENT. CODE § 59-09-07 (2011); OR. REV. STAT. § 130.030 (2011); 20 PA. CONS. STAT. § 7707 (2011); S.C. CODE ANN. § 62-7-107 (2010); TENN. CODE ANN. § 35-15-107 (2011); VA. CODE ANN. § 55-541.07 (2010).

<sup>106</sup> See UTAH CODE ANN. § 75-7-107(3)-(4) (LexisNexis 2011) (providing that a trust created on or after December 31, 2003, will be governed by Utah law if it is administered in the State of Utah); OHIO REV. CODE ANN. § 5801.06(B) (LexisNexis 2011) (permitting a trust to be governed by the law of its principal place of administration).



Wyoming also provides an express provision for the importation of a preexisting self-settled spendthrift trust. If a trustee transfers assets from a valid non-Wyoming self-settled spendthrift trust to the trustee of a WQST, the transfer will relate back to the date of the original transfer to the foreign trust.<sup>107</sup> For example, if the trustee of an international trust established in the Cook Islands transfers the trust's assets to a WQST, the periods within which creditors may bring fraudulent transfer claims are determined by the date of transfer to the Cook Islands trust, not the date of repatriation.

Wyoming law substantially eases the future migration of a Wyoming trust to another jurisdiction regardless of the methodology chosen to effect the departure. First, a trustee of a WQST may resign in the event that a court declines to apply Wyoming's spendthrift law to the trust, permitting migration by transferring the trust's assets to an out-of-state trustee.<sup>108</sup> A trust instrument may also include a provision authorizing such a procedure, although that may present other problems, which are discussed in section IV(E). Second, Wyoming law provides that "[w]ithout precluding the right of the court to order, approve or disapprove a transfer, the trustee . . . may transfer the trust's principal place of administration to another state or to a jurisdiction outside of the United States."<sup>109</sup> A Wyoming trustee even has a duty to administer a trust in the place that is most appropriate to the trust's purposes, unless the trust instrument provides otherwise.<sup>110</sup> Wyoming law provides some limits on such a power, requiring that all qualified beneficiaries must be notified in writing of the transfer at least sixty days before its initiation, unless the beneficiaries waive notice by written consent.<sup>111</sup> Qualified beneficiaries also have at least sixty days to object to a proposed transfer.<sup>112</sup>

#### IV. Challenges to a Change of Governing Law

##### A. The Rule Against Perpetuities

Determining which law will govern the terms of a trust or the disposition of assets into it will be crucial, especially if part of the motivation for international migration is to take advantage of a perpetual or near-perpetual perpetuities period. According to the common

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<sup>107</sup> WYO. STAT. ANN. § 4-10-515(b) (2011).

<sup>108</sup> *Id.* § 4-10-522.

<sup>109</sup> *Id.* § 4-10-108(c).

<sup>110</sup> *Id.* § 4-10-108(b).

<sup>111</sup> *Id.* § 4-10-108(d) (stating that the notice must include the name of the new jurisdiction, the address and telephone number of the new trustee, an explanation of the transfer's rationale, the date of the proposed transfer, and the date within which a beneficiary must notify the trustee of an objection (no fewer than sixty days after notice is given)).

<sup>112</sup> WYO. STAT. ANN. § 4-10-108(e).

law RAP, if the RAP applies to trust property, all interests in that property must vest no later than twenty-one years after the death of some life in being when the interest was created.<sup>113</sup> While the RAP's relevance might have declined—largely due to the widespread ownership of property by corporations and other business entities and the common exemption of commercial transactions from the rule—it remains a serious concern for those seeking to preserve dynastic family wealth through trusts.<sup>114</sup>

Many jurisdictions have exempted certain trust interests from the RAP, often in an effort to attract trust and estate planning business.<sup>115</sup> Wyoming illustrates an alternative solution of implementing a term-of-years approach, whereby a trust interest in non-real property must vest within 1,000 years of its creation<sup>116</sup> if the trust opts out of the RAP.<sup>117</sup> In durational terms, this approach has practically the same effect as a full repeal, since few individuals can make realistic estate planning decisions that extend beyond that timeframe.<sup>118</sup> Other jurisdictions have simply introduced a fixed perpetuity period of more modest duration.<sup>119</sup>

A trust that is subject to the RAP may be held void or voidable if it fails to comply with the limits imposed by the applicable RAP.<sup>120</sup> As a matter of American law, avoidance of the RAP through purposeful choice of other law does not offend the strong public policy of the home state.<sup>121</sup> Thus, for example, a non-Wyoming settlor can create a 1,000-year Wyoming trust. However, if the assets disposed of into the trust are not Wyoming assets, conflict of laws issues might need to be considered, especially if the assets are not U.S. assets at all. For ex-

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<sup>113</sup> JOHN CHIPMAN GRAY, *THE RULE AGAINST PERPETUITIES* 191 (Roland Gray ed., 4th ed. 1942); W. Barton Leach, *Perpetuities in a Nutshell*, 51 HARV. L. REV. 638, 639 (1938).

<sup>114</sup> Note, *Dynasty Trusts and the Rule Against Perpetuities*, 116 HARV. L. REV. 2588, 2588-89 (2003) (citing UNIF. STATUTORY RULE AGAINST PERPETUITIES §§ 4(1), 4 cmt. A (2001) (exempting commercial transaction from the RAP)).

<sup>115</sup> Lynn Foster, *Fifty-One Flowers: Current Perpetuities Law in the States*, PROB. & PROP., July/Aug. 2008, at 30, 31 (discussing the RAP in the U.S.); Robert H. Sitkoff & Max M. Schanzenbach, *Jurisdictional Competition for Trust Funds: An Empirical Analysis of Perpetuities and Taxes*, 115 YALE L.J. 356, 420 (2005).

<sup>116</sup> The British Virgin Islands adopted a similar legislative approach. A 100-year period may be selected when there as an alternative to the common law life in being approach. Trustee Ordinance, 1961 § 68 (1993) (Br. Virg. Is.).

<sup>117</sup> WYO. STAT. ANN. § 34-1-139 (2011).

<sup>118</sup> William J. Turnier & Jeffrey L. Harrison, *A Malthusian Analysis of the So-Called Dynasty Trust*, 28 VA. TAX REV. 779, 789-97 (2009) (discussing how truly perpetual dynasty trusts may be of limited utility because of inflation, growing tax burdens, and the potentially geometric growth of beneficiaries over time).

<sup>119</sup> See The Perpetuities Law § 5(1) (1999 rev.) (Cayman Is.) (stating that the Cayman Islands have a 150-year period and also use a wait and see approach.).

<sup>120</sup> RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 269 cmt. d (1971).

<sup>121</sup> *Id.* §§ 269 cmt. i, 270 cmt. d.

ample, as a general rule, real property may only be subject to the perpetuity limitations of the jurisdiction in which it is sited, irrespective of the governing law of a trust. However, there are ways to overcome these issues including ownership of assets through the medium of a corporation incorporated in the jurisdiction of the governing law of the trust.

Moving a preexisting trust to a new jurisdiction to eliminate application of the RAP is unlikely to be achievable because the RAP is construed by practically all jurisdictions as an issue of validity rather than administration.<sup>122</sup> But decanting may make it possible to apply a new perpetuities rule to a preexisting trust. For example, under the law of Delaware, as presently interpreted, the limitations imposed upon the duration of a trust by the jurisdiction subject to whose laws it has been settled may be avoided by use of a limited power of appointment to appoint (decant) assets first into a new Delaware trust and thereafter into a second trust located in Delaware that is not subject to the RAP.<sup>123</sup>

Delaware takes the position that the law of the jurisdiction of the situs of the trust governs the exercise of a power of appointment established under such trust.<sup>124</sup> It is the prerogative of Delaware to allow power to be exercised over assets that have flowed into a Delaware trust from a foreign trust and are subject to the jurisdiction of Delaware to create a new trust of potentially perpetual duration, notwithstanding such exercise could not have been effected under the law that governed the trust from which the assets had first been decanted.<sup>125</sup> Other U.S. states, even those that have themselves repealed the RAP, have thus far been reluctant to sanction the avoidance by process of decanting of a RAP that applies to a trust under the law of the jurisdiction from which its assets have derived.<sup>126</sup>

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<sup>122</sup> See Martin M. Shenkman, *Trust Situs: Planning, Drafting and Tax Considerations*, in 41ST ANN'L EST. PLAN. INST., at 425, 436 (Tax L. & Est. Plan. Series, Course Handbook Ser. No. D-356, 2010). See also DEL. CODE ANN. tit. 12, § 3332(a) (2011) ("The duration of a trust and time of vesting of interests in the trust property shall not change merely because the place of administration of the trust is changed from some other jurisdiction to this State.").

<sup>123</sup> Richard W. Nenko, *Delaware Trusts*, in 2 ASSET PROTECTION, *supra* note 35, § 14A:77 (citing *Wilmington Trust Co. v. Wilmington Trust Co.*, 24 A.2d 309, 313 (Del. Ch. 1942); *Wilmington Trust Co. v. Sloane*, 54 A.2d 544, 550-51 (Del. Ch. 1947)). See William R. Culp, Jr. & Briani Bennett Mellen, *Trust Decanting: an Overview and Introduction to Creative Planning Opportunities*, 45 REAL PROP. TR. & EST. L.J. 1, 46 (2010); Richard W. Nenko, *The Trust from Hell: Can it be Moved to a Celestial Jurisdiction?*, PROB. & PROP., May/June 2008, at 60, 63.

<sup>124</sup> Nenko, *supra* note 123, § 14A:77.

<sup>125</sup> *Id.*

<sup>126</sup> See, e.g., Act to Revise Various Trust Provisions, 2011 S.D. Sess. Laws 212 § 9 (codified as amended at S.D. CODIFIED LAWS § 55-2-20) (providing that the power conferred by South Dakota law to decant "may not be exercised to suspend the power to alienate trust property

It is unlikely settlors could achieve a similar result in non-U.S. jurisdictions that remain closely aligned with English common law principles. Such jurisdictions would likely regard the RAP as attaching to a disposition into trust, rather than to a trust itself, such that changing the governing law of a trust or decanting a trust's assets would not change the RAP that would have attached to the asset at the time of disposition. A special or limited power of appointment (arising under an irrevocable trust) could not be used to achieve a change to the perpetuity restriction; however, a general power of appointment (within the traditional English common law meaning) could be used to do this because it would effect a fresh disposition for perpetuity purposes.<sup>127</sup>

However, when the trust in question remains revocable (without restriction or limitation) then any form of decanting might impose a new perpetuity period (or an infinite period, if permissible) on the basis that RAP does not apply to a disposition into trust until the trust becomes irrevocable.<sup>128</sup>

### B. Decanting Statutes: Are They Necessary to Change Governing Law?

Not all jurisdictions have a decanting statute, but decanting statutes arguably codify a trustee's common law ability to appoint assets in further trust.<sup>129</sup> A trustee's discretion to distribute trust income and principal may be regarded, in U.S. jurisdictions, as a power

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or extend the first trust beyond the permissible period of any [RAP] applicable to the first trust").

<sup>127</sup> A different result may apply under the law of Jersey, Channel Islands, which permits the appointment of assets out of one Jersey trust limited as to duration into another potentially perpetual Jersey trust provided such action does not offend an express provision of the original trust instrument. Trusts (Jersey) Law 1984 art. 39 (amended 2007) (permitting trust terms to allow the trustee to appoint trust property for the benefit of any person). The Jersey difference may be ascribed to Jersey's civil law heritage and to the fact that its trust law, which has been created exclusively by statute, does not recognize the English common law rule in respect of remoteness of vesting. See Baker & Devenport, *supra* note 76, § 39:67 (noting that Jersey does not recognize the common law RAP).

<sup>128</sup> This appears to be the principle applied through the U.S. and, although there is no English authority in support, there would seem no reason why it should not equally apply to English common law based jurisdictions. See generally J.H.C. MORRIS & W. BARTON LEACH, *THE RULE AGAINST PERPETUITIES* 232-37, 321-27 (2d ed. 1962).

<sup>129</sup> Rashad Wareh, *Trust Remodeling*, TR. & EST., Aug. 2007, at 18, 20 (citing Phipps v. Palm Beach Trust Co., 196 So. 299, 301 (Fla. 1940)). See Bartlett v. Sears, 70 A. 33, 39 (Conn. 1908) (holding a beneficiary's exercise of a power of appointment to distribute property in further trust was legitimate); *In re Estate of Spencer*, 232 N.W.2d 491, 496 (Iowa 1975); RESTATEMENT (SECOND) OF PROP.: DONATIVE TRANSFERS §§ 11.1, 11.1 cmt. d, 12.2, 19.3, 19.3 cmt. a (1986); Joel E. Smith, Annotation, *Power to Appoint Realty in Fee or Personality Absolutely as Including Power to Appoint Lesser Estate or Interest*, 94 A.L.R.3d 895 § 3[a] (1994); 1 THE LAW OF TRUSTS, *supra* note 43, § 17.2.

of appointment<sup>130</sup> and therefore “authority, other than as an incident of the beneficial ownership of property, to designate recipients of beneficial interests in property.”<sup>131</sup> Absent contrary intent on the part of the settlor, the possessor of such a power of appointment may exercise that power to create an estate that is less than that specified in the trust instrument.<sup>132</sup> Although a trustee who possesses a power of appointment has broad authority to decide how to exercise that power, the trustee may only use its power to benefit “permissible appointees” (e.g., a trust’s beneficiaries)<sup>133</sup> and not in a manner that conflicts with the settlor’s intent as expressed in the trust instrument.<sup>134</sup> Thus, in U.S. jurisdictions the common law may permit a trustee to distribute assets in further trusts if doing so does not conflict with the terms of the trust instrument or the trustee’s fiduciary duties and doing so benefits the beneficiaries of the original trust.<sup>135</sup>

Some differences exist between a power of appointment and a trustee’s discretionary power to distribute trust assets, which leads some U.S. commentators to question whether decanting will work in the absence of statutory or court authority.<sup>136</sup> It may be possible to obtain approval from a court in the jurisdiction where the original trust is located before attempting to decant to a U.S. trust. However, this may be more difficult in a nation or state that does not recognize decanting or may require a showing of necessity before allowing a trustee to effectively change a trust’s governing law.

Such ambiguity does not exist in jurisdictions more closely aligned with English common law principles such as the Cayman Islands and Bermuda. In jurisdictions that apply English case law and

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<sup>130</sup> RESTATEMENT (SECOND) OF PROP.: DONATIVE TRANSFERS § 11.1 cmt. d (1986). *See also* I.R.C. § 2514(c) (2011) (“[G]eneral power of appointment’ means a power which is exercisable in favor of the individual possessing the power, . . . his estate, his creditors, or the creditors of his estate . . . .”); *id.* § 2041(b)(1).

<sup>131</sup> RESTATEMENT (SECOND) OF PROP.: DONATIVE TRANSFERS § 11.1.

<sup>132</sup> *See id.* § 19.3 (“Unless the donor has manifested a contrary intent, a donee of a non-general power is permitted to make any appointment that benefits only objects of the power that the donee could make of owned property in favor of those objects.”); *In re Will of Hart*, 28 N.Y.S.2d 781, 785 (N.Y. App. Div. 1941) (holding that, in the absence of words to the contrary, a party with the power to appoint a fee may appoint a lesser estate).

<sup>133</sup> RESTATEMENT (SECOND) OF PROP.: DONATIVE TRANSFERS § 19.3 cmt. a, illus. 1.

<sup>134</sup> *Id.* § 12.2; RESTATEMENT (THIRD) OF PROP.: WILLS & DONATIVE TRANSFERS § 19.14 (Tentative Draft No. 5, 2006); Diana S.C. Zeydel & Jonathan G. Blattmachr, *Tax Effects of Decanting – Obtaining and Preserving the Benefits*, 111 J. TAX’N. 288, 289 (2009).

<sup>135</sup> *See* RESTATEMENT (SECOND) OF PROP.: DONATIVE TRANSFERS § 19.3; Richard B. Covey & Dan T. Hastings, *Recent Developments in Transfer and Income Taxation of Trusts and Estates and State Trust and Estate Law*, 43 HECKERLING INST. ON EST. PLAN. ¶ 101.3[B] (2009) (“[T]he power to appoint outright to permissible appointees includes the power to appoint in further trust for them.”); 1 AUSTIN WAKEMAN SCOTT ET AL., SCOTT AND ASCHER ON TRUSTS § 3.1.2 (5th ed. 2006).

<sup>136</sup> Covey & Hastings, *supra* note 135.

the English interpretation of powers to apply funds for the “benefit” of beneficiaries,<sup>137</sup> it is clear that new trusts are capable of being established by the exercise of trustee powers. However, the application of a RAP cannot be changed in exercise of such powers, at least not if the trust is irrevocable at the time of exercise.

### C. The Implications of the Delaware Tax Trap for a Decanting

The trustee or protector who uses or directs decanting to extend the term during which assets are held subject to trust within the limits of governing trust law must carefully consider the possible application of an arcane tax impediment known as the “Delaware tax trap.” The Delaware tax trap imposes transfer tax if a person exercises a power of appointment to create a new power of appointment that can be used to postpone the vesting of an interest in property or suspend ownership or alienation of property for a period that is not measured from the date of creation of the first power.<sup>138</sup>

In order to avoid the trap, a limited power of appointment should provide that exercise is to be treated as having occurred at the time of the creation of first trust.<sup>139</sup> Delaware law includes a statutory saving provision to prevent inadvertent triggering of the trap by an unwary drafter when a trust has a generation skipping transfer tax inclusion rate of zero or is not subject to generation skipping transfer tax.<sup>140</sup>

Some commentators have questioned how a trustee can ever exercise a limited power of appointment to decant from a potentially perpetual trust without springing the Delaware tax trap.<sup>141</sup> Their

<sup>137</sup> See *Pilkington v. Inland Revenue Comm’rs* [1962] H.L. 612 at 615 (Eng.).

<sup>138</sup> I.R.C. § 2041(a)(3)(B) (2011)

(The value of the gross estate shall include the value of all property . . . [t]o the extent of any property with respect to which the decedent . . . exercises a power of appointment created after October 21, 1942, by creating another power of appointment which under the applicable local law can be validly exercised so as to postpone the vesting of any estate or interest in such property, or suspend the absolute ownership or power of alienation of such property, for a period ascertainable without regard to the date of the creation of the first power.);

*id.* § 2514(d) (deeming the exercise of such powers to be a transfer of property by the individual holding the power).

<sup>139</sup> Covey & Hastings, *supra* note 135, at ¶ 101.8[C]; accord William R. Culp, Jr. & Briani L. Bennett, *Use of Trust Decanting to Extend the Term of Irrevocable Trusts*, 37 EST. PLAN. 3, 11 (2010).

<sup>140</sup> DEL. CODE ANN. tit. 25, § 504 (2011).

<sup>141</sup> Foster, *supra* note 62, at 431-32 (citing widespread scholarly disagreement as to which states avoid the Delaware tax trap); Richard W. Nenko, *Choosing and Rechoosing the Ju-*

concern is based upon the controversial contention that a power of appointment may not be used to create a new trust for a period which is open ended because, if there is no termination point, the issue of whether the period should be measured from the creation date or the exercise date is as a matter of logic rendered moot. The rebuttal to such concern is that the Delaware tax trap rule does not mandate a closed period, merely that measuring of the period must begin as from the creation of the power by the original trust, not from the date of its exercise. A leading treatise contends that the trap rule has no relevance in a jurisdiction that has abolished the RAP.<sup>142</sup>

Richard Nenno, speaking in favor of Delaware, which rejects the notion that a finite trust period is a prerequisite to avoidance of the tax trap rule, has asserted that if a finite period were in fact required, a very long period (e.g., the 1,000 years provided by Alaska law) which he characterizes as a “phony period” would not withstand IRS challenge. An IRS representative reportedly advised Nenno that the Service would disregard “phony” term-of-years periods that extend beyond the common law period of lives in being plus twenty-one years and the USRAP period of ninety years if it should be determined that an ending period is essential to the avoidance of the Delaware tax trap.<sup>143</sup>

Wyoming, following Alaska and Florida, rather than South Dakota and Delaware, has opted to place a 1,000-year time limit upon the duration of a trust created by exercise of a limited power of appointment. Decanting to a Wyoming trust avoids the trap if the trustee with limited power of appointment exercises the power to create a new power that is tested with reference to the first powers’ date of creation or if the instrument exercising the power includes appropriate limiting language. Wyoming’s term-of-years approach complies with the safe harbors to the Delaware tax trap if “(1) there is a real possibility of a vesting or alienation of the trust interests, and (2) that method of vesting is described in the statute.”<sup>144</sup>

Powers of appointment created by a Wyoming 1,000 year trust will not avoid the Delaware tax trap in every instance because there could be a period during which the power may be validly exercised

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*risdiction for a Trust*, 40 HECKERLING INST. ON EST. PLAN. ¶ 404.4[D][6] (2006) (citing Stephen E. Greer, *The Alaska Dynasty Trust*, 18 ALASKA L. REV. 253, 276 (2001); Stephen E. Greer, *The Delaware Tax Trap and the Abolition of the Rule Against Perpetuities*, 28 EST. PLAN. 68, 68 (2001)).

<sup>142</sup> DALE S. ADAMS & ROBERT B. SMITH, FEDERAL ESTATE AND GIFT TAXATION ¶ 4.13[8][b] n.121 (2011).

<sup>143</sup> Nenno, *supra* note 141.

<sup>144</sup> Daniel G. Worthington & Mark Merric, *Which Situs is Best?*, TR. & EST., Jan. 2010, at 54, 63 n.7.

that is not tested with regard to the date of the first power's creation. Wyoming law states that the RAP does not apply to non-real property interests held by post-2003 trusts if, among other requirements, "[t]he instrument creating the trust states that the trust shall terminate no later than one thousand . . . years after the trust's creation."<sup>145</sup> Wyoming's statute does not provide a period within which a special power of appointment conferred by a trust must vest or terminate.

In the 2011 General Session, the Wyoming Legislature sought to amend its statute to repeal the requirement that trusts opt out of the RAP and to provide that non-real property may be held in trust for up to 1,000 years if "[t]he trust terms require that any power of appointment over the trust property terminate and all interests in the trust property vest or terminate no later than one thousand . . . years after the trust's creation, or such earlier date as set forth in the trust instrument."<sup>146</sup> This may have ensured that trusts could decant to near perpetual Wyoming trusts without falling afoul of the Delaware tax trap because it would require that subsequent powers of appointment be tested with respect to the date on which the initial power was created and vest within 1,000 years of that date. It would also describe the method for vesting, requiring termination or vesting of all trust interests within a time defined by the power's creation. Unfavorable amendments to the bill resulted in its rejection by the Wyoming Senate,<sup>147</sup> but a similar statutory fix will likely be introduced in the next legislative session.

When a state has repealed the rule against remoteness of vesting but appears to lack the companion doctrine of the rule prohibiting restraints on alienation, some commentators have argued that limited powers exercised under the laws of such states cannot avoid the Delaware tax trap because one or the other test must be satisfied to avoid a gift or estate tax being imposed upon the power exercise. This argument, which has been aimed primarily at Delaware by proponents of state regimes that have taken the term of years approach, is derived from *Estate of Murphy v. Commissioner*,<sup>148</sup> a decision rendered by the U.S. Tax Court, which evaluated the application of the Delaware tax trap to a Wisconsin trust.

In *Murphy*, the IRS argued that the value of a trust's corpus was includible in a decedent's gross estate because the decedent's will used a special power of appointment to appoint trust assets to a new trust and gave her husband a special testamentary power of appoint-

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<sup>145</sup> WYO. STAT. ANN. § 34-1-139 (2011).

<sup>146</sup> H.B. 158, 60th Leg., Gen. Sess. (Wyo. 2011).

<sup>147</sup> *Id.*

<sup>148</sup> 71 T.C. 671 (1979).



ment over that new trust.<sup>149</sup> The Tax Court disagreed and stated that, while a literal reading of the statute supported the IRS's view, the legislative history, regulations, and policy of § 2041(a)(3) did not.<sup>150</sup> According to the court,

each condition of title is simply shorthand terminology for the local rule against perpetuities . . . . [I]f the local rule against perpetuities is expressed in terms of remoteness of vesting, under section 2041(a)(3) we must determine if vesting of appointed property may be postponed for a period ascertainable without regard to the date of the creation of the first power.<sup>151</sup>

If the local perpetuities law measured the perpetuities period from the time the special power was exercised, the use of such a power to create another power would trigger the Delaware tax trap; but if it was measured from the time of the power's creation, it would not.<sup>152</sup> Wisconsin had abolished the RAP, but it replaced it with a rule against suspension of the power of alienation and concluded that there was no impermissible suspension because the trustee at all times held the power of sale, which was functionally a power to alienate.<sup>153</sup> Thus, the Delaware tax trap did not apply.<sup>154</sup>

#### D. Migrating the Non-Charitable Purpose Trust

Purpose trusts have served a valuable role in offshore estate planning and have received statutory recognition from popular overseas trust jurisdictions, such as the Cook Islands and the Cayman Islands.<sup>155</sup> In a typical offshore asset protection trust structure, a settlor will create a Private Trust Company (PTC) to act as trustee for his or her offshore trusts and transfer shares of the PTC to a purpose trust that has the purpose of holding and voting the PTC's stock. Purpose trusts can also serve other goals, such as managing a family business or a family's real estate holdings.

The Cayman Islands recognized non-charitable purpose trusts in the form of Special Trust (Alternative Regime) (STAR) trusts with the enactment of The Special Trust (Alternative Regime) Law, 1997

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<sup>149</sup> *Id.* at 673-74.

<sup>150</sup> *Id.* at 678.

<sup>151</sup> *Id.* at 680.

<sup>152</sup> *Id.*

<sup>153</sup> *Murphy*, 71 T.C. at 681.

<sup>154</sup> *Id.*

<sup>155</sup> *See* International Trusts Act 1984 § 12 (Cook Is.); Special Trusts (Alternative Regime) Law, 1997 § 6 (Cayman Is.).

(now part of the Cayman Trusts Law (2009 rev.)).<sup>156</sup> Only the person appointed as a STAR trust's enforcer has standing to enforce the terms of such a trust.<sup>157</sup> Many questioned whether a Cayman STAR trust could even be recognized as a trust. This in turn raised the question whether such a trust could be decanted into a second trust in another jurisdiction. Non-charitable purpose trusts were not, however, without proponents, both offshore and onshore.<sup>158</sup>

The U.S. common law of trusts has long provided a strong impediment to purpose trusts because it did not recognize the validity of non-charitable trusts that lack ascertainable beneficiaries.<sup>159</sup> The problem was compounded by the durational limitations imposed by the RAP and the fact that no one would have standing to enforce such a trust.<sup>160</sup> The UTC took a step forward in recognizing non-charitable trusts and making them enforceable, despite the lack of ascertainable beneficiaries or a charitable purpose, but provided that such trusts become unenforceable after twenty-one years.<sup>161</sup> Now, however, several domestic jurisdictions recognize long-term purpose trusts.<sup>162</sup> Wyoming adopted a form of the UTC, but removed the limitation on how long purpose trusts may last and provided that they may be enforced by a trust advisor, trust protector, or some other appointee.<sup>163</sup> Other states have not adopted any form of the UTC, but authorize purpose trusts with independent statutes.<sup>164</sup> In addition, many jurisdictions recognize trusts for the care of pets<sup>165</sup> and the maintenance of cemetery plots.<sup>166</sup> A similar pattern evolved in the offshore jurisdictions, many of which had initially dismissed the STAR trust as a dubious legislative experiment having relevance only in the Cayman Islands.<sup>167</sup>

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<sup>156</sup> See generally Special Trusts (Alternative Regime) Law, 1997 (Cayman Is.).

<sup>157</sup> See David Hayton, *English Fiduciary Standards and Trust Law*, 32 VAND. J. TRANSNAT'L L. 555, 596 (1999) (discussing who may enforce the terms of a Cayman STAR trust).

<sup>158</sup> See Alexander A. Bove, Jr., *Rise of the Purpose Trust*, TR. & EST., Aug. 2005, at 18, 20, 25-26.

<sup>159</sup> See RESTATEMENT (SECOND) OF TRUSTS § 2 cmt. j (1959); 2 SCOTT AND ASCHER ON TRUSTS, *supra* note 135, § 12.1.1 to .3.

<sup>160</sup> Alexander A. Bove, Jr., *The Purpose of Purpose Trusts*, PROB. & PROP., May/June 2004, at 34, 34.

<sup>161</sup> UNIF. TRUST CODE § 409(1) (2000).

<sup>162</sup> See, e.g., DEL. CODE ANN. tit. 12, § 3556 (2011); WYO. STAT. ANN. § 4-10-410(a)(i)-(ii) (2011); *In re Estate of Renner*, 57 A.2d 836, 837-38 (Pa. 1948).

<sup>163</sup> WYO. STAT. ANN. § 4-10-410(a)(i)-(ii).

<sup>164</sup> See, e.g., DEL. CODE ANN. tit. 12, § 3556.

<sup>165</sup> See, e.g., NEV. REV. STAT. § 163.0075 (2009); UNIF. TRUST CODE § 408 (2000).

<sup>166</sup> See, e.g., N.H. REV. STAT. ANN. §§ 31:19, 31:20 (2011).

<sup>167</sup> See Bove, *supra* note 160, at 35 (noting the development of flexible purpose trust statutes in major offshore jurisdictions).

The manner in which some domestic jurisdictions authorize non-charitable purpose trusts may pose problems to individuals seeking to migrate such trusts to U.S. jurisdictions. Typically, domestic jurisdictions enact a statute authorizing purpose trusts and then depend on a separate repeal or modification of the common law RAP or USRAP to allow purpose trusts to exist for perpetual or near perpetual duration. For example, when the Wyoming legislature adopted its modified version of the UTC, it amended section 410 to authorize the creation of enforceable non-charitable purpose trusts without ascertainable beneficiaries.<sup>168</sup> That bill also amended the Model Rule Against Perpetuities Act to permit exempt non-real property interests from the RAP if they are held in trusts that must terminate within 1,000 years of their creation.<sup>169</sup> Professor Adam Hirsch argues that such domestic strategies fail to authorize perpetual purpose trusts.<sup>170</sup> Unlike their offshore counterparts who may have been trained in the norms of English common law, legislators in domestic jurisdictions may have been unfamiliar with the existence of an arguably separate common law rule that requires that non-charitable purpose trusts terminate (rather than merely vest) within the RAP period. The American Restatements of the Law of Trusts may imply this view when it states that the duration of such trusts is limited by the RAP's "period," rather than the RAP itself.<sup>171</sup> According to this argument, Wyoming's statute that simply states that the RAP does not apply to Wyoming trusts that opt out of the RAP and must terminate within 1,000 years does not repeal the common law rule against perpetual non-charitable purpose trusts. This may bring the validity of domestic non-charitable purpose trusts (and the ability to migrate offshore purpose trusts into the U.S. into question.<sup>172</sup>

It is not certain that this separate rule limits the duration of Wyoming purpose trusts. In Wyoming, the enactment of the statute allowing purpose trusts and the modification of the RAP occurred in a single legislative act.<sup>173</sup> The legislature's likely intent was to abrogate the common law rule against non-charitable trusts without ascertain-

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<sup>168</sup> See Act relating to the Uniform Trust Code, 2003 Wyo. Sess. Laws 124 (to be codified at WYO. STAT. ANN. § 4-10-410 (2011)).

<sup>169</sup> See *id.* ((to be codified at WYO. STAT. ANN. § 34-1-139 (2011)).

<sup>170</sup> See Adam J. Hirsch, *Delaware Unifies the Law of Charitable and Noncharitable Purpose Trusts*, 36 EST. PLAN. 13, 22 (2009). See also 3 JOHN A. BORRON, JR., SIMES AND SMITH ON THE LAW OF FUTURE INTERESTS § 1394 (3d ed. 2011) (arguing that honorary trusts are a unique species of trust with their own perpetuities rules).

<sup>171</sup> Adam J. Hirsch, *Trusts for Purposes: Policy, Ambiguity, and Anomaly in the Uniform Laws*, 26 FLA. ST. U. L. REV. 913, 932 n.94 and accompanying text (1999) (citing RESTATEMENT OF TRUSTS §§ 124 cmt. f, 418(b) (1935)); RESTATEMENT (SECOND) OF TRUSTS §§ 124, 124 cmt. b, 124 cmt. f, 418(b), 418 cmt. b (1959); RESTATEMENT OF PROP. § 379 (1944).

<sup>172</sup> Hirsch, *supra* note 170, at 18 n.55 and accompanying text.

<sup>173</sup> See 2003 Wyo. Sess. Laws 124.

able beneficiaries, as a whole, and provide that no perpetuities period of any kind applies to any non-real property interest held in a trust that must terminate within 1,000 years. Prior to the enactment of the UTC, Wyoming adhered to the common law rule that no non-charitable trust without ascertainable beneficiaries was valid, regardless of when it must terminate.<sup>174</sup> It makes little sense that the state would have had a separate rule limiting the duration of trusts that would have been void entirely because they lacked beneficiaries. Professor Hirsch acknowledges that this was the position taken by John Chipman Gray in his oft-cited treatise on the subject.<sup>175</sup>

Case law is by no means unanimous that honorary trusts were governed by a perpetuities rule separate from the RAP. It is true that many scholars have argued that non-charitable purpose trusts presented special perpetuities problems, justifying an arcane, separate rule.<sup>176</sup> But as Professor Hirsch acknowledges, courts typically fail to expressly acknowledge the distinction.<sup>177</sup> In the past, some courts have invalidated such trusts because they directly violated the RAP.<sup>178</sup>

Scholars deduce the parallel rule from the fact that the common law required that non-charitable trusts without beneficiaries terminate, rather than vest, within the perpetuities period.<sup>179</sup> Wyoming's opt out statute replaces the RAP not with a rule requiring vesting, but with a rule requiring that the trust *terminate* within 1,000 years.<sup>180</sup> This suggests that, to the extent that a common law rule requires non-charitable honorary trusts to terminate within a timeframe, that rule has been abrogated and superseded by the alter-

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<sup>174</sup> *E.g.*, *In re Estate of Lohrie*, 950 P.2d 1030, 1032 (Wyo. 1997) (holding that an express trust requires ascertainable beneficiaries) (citing *Hilbert v. Benson*, 917 P.2d 1152, 1157 (Wyo. 1996)); *In re Haworth*, 253 B.R. 478, 481 (Bankr. D. Wyo. 2000). *See also* GEORGE GLEASON BOGERT, *THE LAW OF TRUSTS AND TRUSTEES* § 162 n.43 (Supp. 2010) (noting that the UTC provides an exception to the common law requirement that settlors of express trusts identify beneficiaries); GEORGE GLEASON BOGERT, *THE LAW OF TRUSTS AND TRUSTEES* § 166 n.40 and accompanying text (Rev. 2d ed. 1979) (noting that very little U.S. case law supports non-charitable trusts without beneficiaries).

<sup>175</sup> Hirsch, *supra* note 171, at 932 n.93 (citing GRAY, *supra* note 113, § 909). *See also* J.B. Ames, *The Failure of the "Tilden Trust."*, 5 HARV. L. REV. 389, 390 (1892) (noting that trusts must have beneficiaries and comply with the RAP).

<sup>176</sup> Hirsch, *supra* note 171, at 931 n.89 (citing MORRIS & LEACH, *supra* note 128, at 325-26; J.H.C. Morris & H.W.R. Wade, *Perpetuities Reform at Last*, 80 LAW Q. REV. 486, 531 (1964)).

<sup>177</sup> Hirsch, *supra* note 171, at 933.

<sup>178</sup> *See Note, Private Trusts for Indefinite Beneficiaries*, 45 YALE L.J. 1515, 1517 (1936) (citing *In re Matter of Howells*, 260 N.Y.S. 598, 609 (N.Y. Sur. Ct. 1932); *Shippee v. Indus. Trust Co.*, 110 A. 410, 411 (R.I. 1920)).

<sup>179</sup> Hirsch, *supra* note 171, at 933 n.95 (citing *Foshee v. Republic Nat'l Bank*, 617 S.W.2d 675, 677 (Tex. 1981)); 3 LEWIS M. SIMES & ALLAN F. SMITH, *THE LAW OF FUTURE INTERESTS* § 1394 text accompanying n.24 (2d ed. 1956 & Supp. 2003).

<sup>180</sup> WYO. STAT. ANN. § 34-1-139 (2011).

native 1,000-year rule. The commentary to the uniform version of the UTC states that the section was intended to make non-charitable purpose trusts enforceable for up to twenty-one years: “The trust may not be enforced for more than [21] years.”<sup>181</sup> The UTC drafters put “21” in brackets and explained that states had the option of adjusting the maximum time limit.<sup>182</sup> The fact that the drafters of Wyoming’s version of the UTC omitted the limiting sentence entirely strongly suggests intent to remove any separate restriction on the duration of non-charitable purpose trusts.

It is also unlikely that Wyoming courts would recognize a parallel common law rule against perpetual purpose trusts in the absence of the RAP. No Wyoming court has acknowledged such a rule. If the rule does exist at common law, it is not a matter of positive law that Wyoming courts must accept.<sup>183</sup> Acknowledgments of a parallel rule from courts in other states, commentators, and in the Restatements are, at best, persuasive. Wyoming has adopted the common law of England as of 1607 as modified by statutes and court decisions.<sup>184</sup> Professor Hirsch acknowledges that the issue of the validity of non-charitable purpose trusts did not arise under English common law until the nineteenth century, well after the date as of which Wyoming adopted the common law.<sup>185</sup> More importantly, given (i) the legislature’s clear intent to enable purpose trusts and 1,000 year trusts of any kind other than real property and (ii) the fact that no Wyoming court has ever acknowledged the parallel rule, there is little reason to believe that a Wyoming court would adhere to such an arcane rule, other than to embrace formalism for formalism’s sake.<sup>186</sup> The UTC makes Wyoming purpose trusts enforceable by a trust advisor, trust protector, person appointed by the trust instrument, or person appointed by a court.<sup>187</sup> Further, the problems of excessive dead hand control and runaway purpose trusts are addressed by Wyoming’s flex-

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<sup>181</sup> UNIF. TRUST CODE § 409 (2006).

<sup>182</sup> *Id.* § 409 cmt.

<sup>183</sup> See *Choman v. Epperley*, 592 P.2d 714, 716 and n.4 (Wyo. 1979) (“The adoption of the common law by Wyoming was not an adoption of a set code of law. By nature, common law is not a set code of law. Nor was the adoption one of static and nonchanging law.”).

<sup>184</sup> WYO. STAT. ANN. § 8-1-101 (2011).

<sup>185</sup> See Adam J. Hirsch, *Bequests for Purposes: A Unified Theory*, 56 WASH. & LEE L. REV. 33, 38 (1999) (noting an early suggestion of the beneficiary principal in *Morice v. Bishop of Durham*, (1804) 32 Eng. Rep. 656 (M.R.) *aff’d* 32 Eng. Rep. 947 (Ch. 1805)).

<sup>186</sup> American jurisprudence has come a long way from the Langdellian model in which the practice of law is a science in which jurists discover the preexisting fundamental principles of the common law. See generally Joseph William Singer, *Legal Realism Now*, 76 CAL. L. REV. 465 (1988); cf. O.W. Holmes, *The Path of the Law*, 10 HARV. L. REV. 457, 469 (1897) (“It is revolting to have no better reason for a rule of law than that so it was laid down in the time of Henry IV. It is still more revolting if the grounds upon which it was laid down have vanished long since, and the rule simply persists from blind imitation of the past.”).

<sup>187</sup> WYO. STAT. ANN. § 4-10-410(a) (2011).

ible modification and termination provisions,<sup>188</sup> some of which may be utilized by settlors, trust protectors, and trustees. Purpose trust property that is not necessary for the trust's intended use may be distributed to the settlor or his or her successors.<sup>189</sup> As such, there appears to be little doctrinal or public policy reason for maintaining an antiquated parallel rule.

Even if a parallel rule exists whereby honorary trusts are limited to the "period" of the RAP, rather than by the RAP itself, the Restatements provide a definition of the relevant "period." "The period of the rule against perpetuities is, in the absence of a statute otherwise providing, a period of the lives of designated persons in being at the time of the transfer and twenty-one years."<sup>190</sup> Wyoming's statute arguably provides otherwise, suspending the relevant period for non-real property interests if a trust must terminate within 1,000 years.<sup>191</sup>

Even so, U.S. states have begun to address the problem. Delaware was the first U.S. state to recognize and to address the problem identified by Professor Hirsch.<sup>192</sup> South Dakota has since acted<sup>193</sup> and Wyoming is expected to follow suit in its next legislative session.

### E. Automatic Migration Clauses

Automatic migration clauses (also known as "flee," "Cuba," and "force majeure" provisions) have long been a feature of offshore trusts. They provide a means of immediately transferring trust assets to another jurisdiction in the event that the trust becomes subject to creditor attack or state expropriation, and may purport similarly to change governing law and forum.<sup>194</sup> They were once viewed as necessary features of foreign trusts because they seemingly protected trust assets from political, economic, and military instability. However, the assassination of the Governor of Bermuda in March of 1973, triggering many such clauses, discredited their use.<sup>195</sup> In addition, the political and financial stability of most offshore jurisdictions has demonstrated the lack of genuine need for such a provision.

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<sup>188</sup> See *id.* § 4-10-412 to 415.

<sup>189</sup> *Id.* § 4-10-410(a)(iii).

<sup>190</sup> RESTATEMENT (SECOND) OF TRUSTS § 124 cmt. f (1959); RESTATEMENT OF TRUSTS § 124 cmt. f (1935).

<sup>191</sup> See WYO. STAT. ANN. § 34-1-139(b)(ii) (2011).

<sup>192</sup> DEL. CODE ANN. tit. 25, §503(a) (2011).

<sup>193</sup> Act to Revise Various Trust Provisions, 2011 S.D. Sess. Laws 212 § 40 (codified as amended at S.D. CODIFIED LAWS § 55-2-20).

<sup>194</sup> PETER SPERO, ASSET PROTECTION: LEGAL PLANNING, STRATEGIES AND FORMS ¶ 7.05[2] (2011).

<sup>195</sup> See ROBERT A. HENDRICKSON & NEAL R. SILVERMAN, CHANGING THE SITUS OF A TRUST § 12.02 (15th release 2003) (1982) (discussing the inadvertent triggering of flee clauses by the assassination of Bermuda's governor).

Wyoming has adopted a statute derived from Delaware law that permits automatic migration by allowing the trustee of a WQST to resign if “a court takes any action whereby the court declines to apply [Wyoming law] in determining the validity, construction or administration of the trust, or the effect of a spendthrift provision thereof.”<sup>196</sup> At that point, the trustee will have no authority over the trust’s assets, except to convey them to a successor trustee.<sup>197</sup> If the successor trustee is located in an offshore jurisdiction, the trust will effectively migrate, preventing a Wyoming court from enforcing a judgment against the trust’s assets (such as in the situation where a Wyoming court must give full faith and credit to a judgment obtained in a state that does not recognize self-settled spendthrift trusts). This may eliminate the need for a flee clause if the clause’s only purpose is to ensure enforcement of a WQST’s spendthrift provision.

Automatic migration may present practical difficulties of interpretation. Except for very carefully targeted situations that do not entail subjective judgment, it can be difficult to predict when migration will become necessary.<sup>198</sup> State expropriation of trust assets may not always involve a single, obvious event. For example, a potentially confiscatory tax bill could be adopted and implemented in several steps. In such event, it is impossible for the drafter to determine the point at which migration should occur in consequence of which the decision must be left to a trustee who is in the unenviable position of having to offend the sovereign to whose jurisdiction it is subject, or to a protector who may freeze out of fear of acting too precipitously. Nation states may also engage in “creeping confiscation” through currency depreciation, taxation, and changes in substantive trust law.<sup>199</sup> The drafter is often required to walk a careful line to avoid either triggering an accidental migration or not permitting migration until it is too late to protect the assets, but that is something easier said than done.<sup>200</sup>

An automatic migration provision may create unintended tax consequences and interesting tax planning opportunities. Treasury Regulations provide a court test’s safe harbor for trusts that meets three conditions: “(i) The trust instrument does not direct that the trust be administered outside of the United States; (ii) The trust in fact is administered exclusively in the United States; and (iii) The

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<sup>196</sup> WYO. STAT. ANN. § 4-10-522 (2011).

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

<sup>198</sup> 1 JEFFREY A. SCHOENBLUM, MULTISTATE AND MULTINATIONAL ESTATE PLANNING § 18.20[K] (2010 ed. 2009).

<sup>199</sup> SPERO, *supra* note 194.

<sup>200</sup> See SCHOENBLUM, *supra* note 198.

trust is not subject to an automatic migration provision.”<sup>201</sup> A trust is assured of complying with the court test if it meets all three conditions.

A trust will not fall into the safe harbor if a term of the trust “provides that a United States court’s attempt to assert jurisdiction or otherwise supervise the administration of the trust directly or indirectly would cause the trust to migrate from the United States.”<sup>202</sup> A flee clause will not be considered an impermissible “automatic migration clause” under the Regulations if it limits migration to cases of “foreign invasion of the United States or widespread confiscation or nationalization of property in the United States.”<sup>203</sup>

Settlors who are concerned about complying with the court test’s safe harbor to retain U.S. trust status should be careful about any trust term permitting overseas migration other than in the case of property nationalization or invasion. Settlers who see an advantage in having a trust be classified as foreign for U.S. federal income tax purposes are afforded an easy means by the purposeful inclusion of an automatic migration clause for accomplishing such goal without necessity of conferring any meaningful authority upon a foreign person to make a substantial trust decision.

### Conclusion

There are many options available to settlors seeking to establish new, or migrate already established trusts, from an offshore jurisdiction to the U.S. Recent changes in U.S. law create more pressure on offshore trusts created for U.S. persons to migrate to U.S. jurisdictions. Statutory provisions adopted in several U.S. states designed to facilitate migration of trusts have created opportunities unheard of in the past. Relatively new tools and methods, including modification of irrevocable trusts, decanting, and non-charitable purpose trusts, open the door to tremendous flexibility to structures that may better serve clients upon a change of situs.

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<sup>201</sup> Treas. Reg. § 301.7701-7(c)(1) (2011).

<sup>202</sup> *Id.* § 301.7701-7(c)(4)(ii).

<sup>203</sup> *Id.*