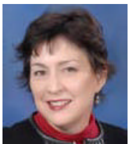
AICPA

Newsletter of the AICPA
Personal Financial Planning Division

planner

January/February 2012, Volume 28, Number 1

Collaborative Divorce: Helping Your Clients Avoid Financial Disaster



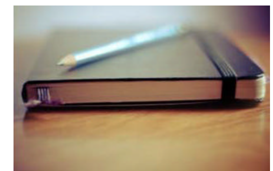
By Tracy B. Stewart and Kevin Fuller

Americans want stability, security, and predictability, three features especially desirable in the current economic environment. Although your clients are loyal to you because you help them achieve and preserve these qualities in their lives, all three are even more difficult to keep or attain when you toss in divorce.

If you have clients who are facing a divorce, you can help them by making certain they know their options in divorce procedures, including a reengineered divorce process known as collaborative law. This is a divorce process with unparalleled efficiency, flexibility, and privacy for your clients. However, it is not for everyone.

Focusing on the Settlement

Some divorces are best resolved at the courthouse and not the negotiating table. Factors that drive negotiating versus litigating decisions include the stubbornness of one or both parties and their lawyers; the existence



WHAT'S INSIDE

5 The Future of the Domestic "Asset Protection" Trust After *Mortensen*

7 CPA/PFS Profile: James A. Shambo, CPA/PFS

10 *Planner* Article Library – 2011

11 PFP News

12 PFP Calendar of Events

Chairman's Corner

In response to member needs and requests, the Personal Financial Planning Executive Committee's (PFP EC) Pathway Task Force has spent the last few years creating materials to assist PFP practitioners in effectively implementing PFP services. These materials include the Practice Center; a course attached to the AICPA Advanced PFP Conference, *Implementing PFP Services: Step-by-Step Plans for Success*; and various web seminars, practice guides, and conference sessions.

We have heard from many practitioners that they need further guidance and resources to effectively serve their clients, while also increasing their own bottom line. In response, we are happy to announce the launch of a new venture with Fox Financial Planning Network (FFPN). The goal of FFPN is to provide CPAs in all business models and firm sizes with the step-by-step processes they need to effectively develop their PFP businesses via a holistic approach. FFPN has created customized training for the CPA practitioner, including a documented workflow system for providing comprehensive financial planning services and a process for delivering financial planning in bite-size pieces. FFPN provides a fast track path to set up the system at deeply discounted rates for AICPA PFP Section members. To learn more, visit www.aicpa.org/PFP/FFPN.

Clark Blackman II, CPA/PFS
Chairman, PFP Executive Committee

Contact Us

We welcome your comments, questions, or article ideas. Please send them to financialplanning@aicpa.org. Visit our PFP homepage: aicpa.org/PFP. Join us on LinkedIn!

The Future of the Domestic "Asset Protection" Trust After *Mortensen*

By Daniel S. Rubin

Although each of the 50 states has long recognized the validity of spendthrift trusts to protect a third-party beneficiary's interest from almost all creditor claims, spendthrift clauses have historically been unenforceable with respect to self-settled trusts, that is, a trust in which the settlor is also a beneficiary.

However, since 1997, 11 states have enacted legislation extending spendthrift protections to the settlor-beneficiary of a discretionary trust, provided, of course, that the funding of the trust was not done in defraud of existing creditors. Those states are Alaska, Delaware, Hawaii, Missouri, Nevada, New Hampshire, Rhode Island, South Dakota, Tennessee, Utah, and Wyoming. Their self-settled spendthrift trusts are sometimes referred to as asset protection trusts or domestic asset protection trusts in order to distinguish them from self-settled spendthrift trusts established under the law of a foreign jurisdiction, such as the Cook Islands.

To some extent, in response to concerns about the proliferation of domestic asset protection trust legislation, Section 548(e)(1) of the Bankruptcy Code was enacted as part of the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005. That section provides for a special 10-year statute of limitations in a bankruptcy proceeding for the avoidance of a transfer of an interest of the debtor in property where such transfer was made to a " … self-settled trust or similar device … with actual intent to hinder, delay, or defraud any entity to which the debtor was or became, on or after the date that such transfer was made, indebted."

Interestingly, until this year, there have been absolutely no reported decisions in any of the 11 domestic asset protection trust states involving a domestic asset protection trust. However, with the decision in *Battley v. Mortensen, et al.* (*Mortensen*), Case No. A09-00565-DMD (May 26, 2011), that is no longer the case.

Facts of the Mortensen Case

Thomas Mortensen, a resident of Alaska, and his then spouse (now his former spouse), acquired real property near Seldovia, Alaska (the "Seldovia Property") in 1994. When Mortensen and his spouse later divorced, Mortensen received his spouse's interest in the Seldovia Property.

Following his divorce, Mortensen became aware of Alaska's asset protection trust laws. He investigated the subject, and using a form he uncovered in his research, drafted a trust document he called the "Mortensen Seldovia Trust (An Alaska Asset Preservation Trust)" (the "Trust"), intending for the Trust to qualify as an asset protection trust under Alaska law. Mortensen deeded his interest in the Seldovia Property to the Trust.

Allegedly, Mortensen's transfer of his interest in the Seldovia Property to the Trust was pursuant to an oral agreement between Mortensen and his mother, whereby he would transfer the Seldovia Property to the Trust to preserve it for his children. Mortensen's mother would pay him $100,000 in consideration for the transfer because the Trust ultimately benefitted her grandchildren. Mortensen claimed that he used some of the funds his mother paid him to pay existing debts, and that he transferred approximately $80,000 to a brokerage account in the name of the Trust as seed money for operating expenses related to the Seldovia Property.

Mortensen's divorce was, however, apparently a bitterly contested matter that, together with a generally poor economy, adversely affected his financial situation. Following the creation and funding of the Trust, Mortensen's financial condition deteriorated and his income became sporadic. Finally, in April 2009, he became sick, required surgery, and a two-week hospitalization. This was followed by a prolonged period of convalescence, after which he was unable to return

to work. Ultimately, Mortensen filed for bankruptcy on August 18, 2009, approximately four and a half years after creating and funding the Trust.

Unfortunately, Mortensen did not find bankruptcy to be the panacea he might have envisioned. The bankruptcy trustee argued, and the bankruptcy court ultimately agreed, that Mortensen's transfer of the Seldovia Property to the Trust should be avoided under Section 548(e) of the Bankruptcy Code because he had the actual intent to hinder, delay, or defraud his creditors, and the transfer fell within the 10-year statute of limitations of that section.

Commentary

Although a cursory consideration of the *Mortensen* decision might lead some to conclude that the case reduces the effectiveness of domestic asset protection trusts, at least for the first 10 years of their existence, a debtor's "… actual intent to hinder, delay, or defraud …" remains a question of fact unique to *every* case. Although certain portions of the *Mortensen* decision effect a broad reach regarding what might constitute evidence of fraudulent intent, the decision does not change the fact that a finding of a debtor's "actual intent to hinder, delay, or defraud" his creditors is required under Section 548(e). In fact, the *Mortensen* court stated that "[t]he determinative issue … is whether Mortensen transferred the Seldovia property to the trust 'with actual intent to hinder, delay, or defraud' his creditors."

In *Mortensen*, the bankruptcy court agreed with the bankruptcy trustee's argument that bad intent could, at least, be inferred from the trust language itself because the trust agreement set forth its stated purpose as being, in part, "… to maximize the protection of the trust estate or estates from creditors' claims of the Grantor …" Conversely, Alaska Statutes Section 34.40.110(b)(1) provides that "… a settlor's expressed intention to protect trust assets from a beneficiary's potential future creditors is not evidence of an intent to defraud." However, the bankruptcy court held that such a provision was not determinative when applying Section 548(e)(1)(D) of the Bankruptcy Code because "[it] would be a very odd result for a court interpreting a federal statute aimed at closing a loophole to apply the state law that permits it."

Seemingly, however, the question of whether the creation of a self-settled trust should be treated as a so-called "badge of fraud" under applicable law, evidencing a debtor's intent to hinder, delay, or defraud creditors, is hardly a loophole. A loophole would seem to be a state statute permitting a bankrupt individual to create a self-settled trust with an actual intent to hinder, delay, or defraud his or her creditors, which, of course, is not permissible in any of the 11 domestic asset protection trust jurisdictions.

In addition, the *Mortensen* court cited other badges of fraud, which it said, in and of themselves, evidenced Mortensen's intent to hinder, delay, and defraud present and future creditors. Specifically, the *Mortensen* court cited the fact that "Mortensen was coming off some very lean years at the time he created the trust …" and that "Mortensen was well 'under water' when he sought to put the Seldovia property out of reach of his creditors by placing it in the trust." In addition, the *Mortensen* court noted that "… when Mortensen received the $100,000 from his mother, he didn't pay off his credit cards. Rather, he transferred $80,000 into the trust after paying a few bills and began speculating in the stock market ... ," concluding "… that Mortensen's transfer of the Seldovia property and the placement of $80,000 into the trust constitutes persuasive evidence of an intent to hinder, delay, or defraud present and future creditors."

Conclusion

If there is any lasting significance to the *Mortensen* decision, it will almost certainly be that the continuing uncertain application of Section 548(e) of the Bankruptcy Code requires individuals who wish to establish the most protective asset protection trust possible to continue to go offshore—where the Bankruptcy Code, of course, does not apply—at least for the first 10 years of the trust's existence.

About the Author
Daniel S. Rubin, JD, LLM (Taxation), is a partner in the Trusts and Estates and Asset Protection practices of Moses & Singer LLP. In January, he presented a session on asset protection at AICPA's Advanced Personal Financial Planning (PFP) Conference in Las Vegas, and, along with several other experts, participated in the "Best Planning Ideas Panel." Look for a summary of the best ideas panel discussion in the 2012 March/April *Planner*. Contact him at drubin@mosessinger.com.

After 10 years have elapsed without a creditor issue having developed, such trusts can safely migrate onshore because the silver lining in connection with the enactment of Section 548(e) is that it actually validates self-settled trusts, even those that may have been established with an actual intent to hinder, delay, or defraud creditors, provided only that more than 10 years have elapsed since the trust was established.

Therefore, CPA financial planners must account for the extended statute of limitations period under Section 548(e) of the Bankruptcy Code when counseling clients in connection with their asset protection planning. In any case when there is even a possibility of existing creditor claims, the right advice will almost always be to forego the use of a domestic asset protection trust in favor of an offshore trust, at least for the first 10 years of the trust's existence. However, when a domestic asset protection trust is already in existence, the right advice will probably be for the settlor to avoid bankruptcy, if at all possible, if the nonbankruptcy, fraudulent transfer statute of limitations period has elapsed, but less than 10 years have passed, since the trust was created and funded.

Reprinted with permission from the AICPA Personal Financial Planning Division.

MOSES & SINGER LLP

Disclaimer

Viewing this or contacting Moses & Singer LLP does not create an attorney-client relationship.

This is intended as a general comment on certain developments in the law. It does not contain a complete legal analysis or constitute an opinion of Moses & Singer LLP or any member of the firm on the legal issues herein described. This contains information that may be modified or rendered incorrect by future legislative or judicial developments. It is recommended that readers not rely on this general guide in structuring or analyzing individual transactions or matters but that professional advice be sought in connection with any such transaction or matter.

Attorney Advertising

It is possible that under the laws, rules or regulations of certain jurisdictions, this may be construed as an advertisement or solicitation.

Copyright © 2012 Moses & Singer LLP
All Rights Reserved