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Coordinating an Asset Protection Plan With an Estate Plan – The Often Overlooked Essentials

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Integration of Asset Protection Planning into an Estate Plan

Over the last decades the concept of a "typical" estate plan has expanded and evolved in direct proportion to the increasing size of the average estate. In the not-so-distant past, a typical plan for a married couple consisted only of reciprocal Wills, perhaps with testamentary trusts if there were minor children. More recently, a plan would often include two inter-vivos trusts in addition to the Wills, real estate trusts, Durable Powers of Attorney, and some type of advanced directive and appointment of an agent to make health care decisions.

For wealthy families with an interest in tax planning, the typical arrangement would also include tax savings mechanisms such as Grantor Retained Annuity Trusts, Family Limited Partnerships, and Qualified Personal Residence Trusts.

Although estate planners will continue to add new tax savings devices to their arsenals in response to the ever-changing tax laws, the most likely challenge for planners going forward will be to integrate asset protection planning into the estate plan. This will range from relatively simple changes relating to dispositive and trustee powers provisions in standard documents to full-blown asset protection plans built around offshore trusts.

This is perhaps best illustrated by reviewing a hypothetical case and the direction it might take if asset protection is an objective.

Making Changes to Standard Estate Plan

Our clients Dr. Jay, a successful obstetrician, and his wife, Kay, have two children in their early twenties, a home worth $600,000 and liquid assets worth $3.5 million. Although Dr. Jay

carries $2 million/$5 million in professional liability insurance, he worries about exposure in excess of his policy limits. In addition, as with many clients, although he trusts his children, he and Kay also worry about them making bad marriages or otherwise putting their potential inheritances at risk.

Dr. Jay has never actually been sued for malpractice and is not interested in a full-blown asset protection plan, but would like to take reasonable precautions to protect his accumulated wealth. The only step he has taken so far is to put all of the family assets in his wife's name. After attending a free estate planning seminar at the local J.C.C., he realizes that having all the assets in Kay's name might have adverse estate tax consequences if he should die first, and even worse personal consequences in the event of a divorce. Further, there is also the possibility, however remote, that Kay could be the subject of a lawsuit.

What changes should we consider making to a standard estate plan to enhance Dr. Jay's (and Kay's) protection from future creditors without going "offshore" and without sacrificing available estate tax savings?

Lifetime Qualified Terminable Interest Property

As planners know, for tax planning purposes, it is critical to have at least the applicable exempt amount (for convenience, let's say $1,000,000) in Dr. Jay's taxable estate on his death in order to use up his federal estate tax unified credit (now the applicable exclusion amount).[1] Thus, it is not effective for tax planning purposes to have all the family's assets in Kay's name.

To avoid this negative consequence while maintaining a degree of asset protection, Kay can set up an irrevocable lifetime Qualified Terminable Interest Property (QTIP) trust for Dr. Jay, funding it with at least $1,000,000[2]. The trust would contain typical QTIP provisions, providing that all income be distributed to Dr. Jay with discretionary principal distributions for his health, maintenance, education, and support. Dr. Jay could also have a testamentary general power of appointment (GPOA) over the principal. In the event Dr. Jay fails to exercise this power, the property could pass into a QTIP trust for Kay, again with the typical QTIP provisions.

During Dr. Jay's lifetime, if he is sued and the judgment creditor is attempting to enforce a judgment against him, the creditor will be able to reach the income of the trust, but will not have access to any of the trust principal. This may be the case even if Dr. Jay is the trustee of the trust. On Dr. Jay's death, the trust property will be includable in his estate for federal estate tax purposes because of the testamentary GPOA.3 If the trust principal exceeds the unified credit and Dr. Jay does not exercise his power of appointment, a partial QTIP election for Kay's benefit can be made over the excess amount.4 Because of the inclusion of the QTIP assets in Dr. Jay's estate, this election is effective even though Kay, the beneficiary of the QTIP trust, is also the original Settlor.5

What about building in a degree of asset protection for the children of Dr. Jay and Kay? Of course each child's share of the trust property could be left in a discretionary trust for the child's lifetime with a typical spendthrift provision, and this would generally protect those assets against a child's creditors. But Dr. Jay and Kay may not wish to tie up their children's inheritance indefinitely. If this is the case, a small change to "standard" documents which would provide a degree of protection is to make trust distributions available only by the exercise of a general power of appointment by the child. In other words, grant the child a GPOA over one-half the property at say, age thirty and the balance at age thirty-five. Under current law in most states, the child could not be compelled to exercise the power, and the property would be unavailable to creditors until the power was exercised.6

Family Limited Partnership

Another option for Dr. Jay, which actually is already in the estate planner's arsenal, is the family limited partnership (FLP). In general, a Limited Partnership is an entity made up of one or more general partners and one or more limited partners and is formed to carry out a business purpose. The general partner manages the partnership business and is personally liable for partnership obligations. Limited partners, on the other hand, do not participate in the management of the partnership business and their liability is limited to their capital contributions.

In a typical FLP situation, Dr. Jay and Kay will establish the partnership and contribute property such as investment real estate, securities, or a business interest in exchange for both a 1% general partnership interest and a 99% limited partnership interest. To limit exposure, Kay should

serve as general partner. The limited partnership interest can be split between Dr. Jay and Kay as needed to make maximum use of each spouse's unified credit.

Over time, Jay and Kay can make gifts of limited partnership interests to family members, using the $10,000 per year annual exclusion if available. As limited partners, the family members would have no direct say in the operation of the partnership or other key decisions as the general partner maintains authority to manage all partnership assets. Alternatively, the 99% limited partnership shares could be held in one or more irrevocable trusts for the benefit of the children, or even for the benefit of Dr. Jay and Kay.

Many planners recommend FLP's to their high net worth clients because of the valuation discounts available for transfer tax purposes. Discounts of 25% to 50% are common depending on the nature of the assets owned by the partnership and restrictions in the partnership agreement. These valuation discounts are available because of the lack of control and lack of marketability of the partnership interests.7

FLP's are also attractive from an asset protection point of view because creditors of the individual partners have only limited remedies against the partnership assets.8 For instance, if Dr. Jay is sued for a matter outside the partnership business (which is only to manage the partnership assets), the Plaintiff would not be able to reach or attach the property inside the partnership, even if the Plaintiff were successful in obtaining a judgment against him.

The Uniform Limited Partnership Act provides that a judgment creditor can obtain only a charging order against the partnership interest of Dr. Jay, the debtor/partner, to pay the unsatisfied judgment. A charging order leaves the partnership intact but diverts to the judgment creditor the debtor partner's share of the partnership profits.9 Thus, to the extent so charged, the creditor has only the rights of an assignee of Dr. Jay's interest. The assignee is entitled to receive only the distribution to which Dr. Jay is entitled. Because the general partners make all decisions as to distributions of the partnership assets, the creditor is left basically at the mercy of the general partner. Even worse, the creditor runs the risk of receiving phantom income from the partnership as the Internal Revenue Service has ruled that for tax purposes an assignee of a partner is treated as a substitute limited partner.10

Although the concept that the charging order operates, in effect, as a substitute for execution on a judgment, some domestic courts have been unwilling to treat charging orders as a sole remedy for a judgment creditor. For example, in the Crocker National Bank case11, the court held that the judgment creditor was not limited to obtaining a charging order and permitted the sale of the partnership interest itself because the creditor could demonstrate that monies collected under the charging order were not sufficient to satisfy the judgment. Another factor was that foreclosure of the partnership interest would not unduly interfere with the business of the partnership. Because of this case and others which followed,12 many practitioners believe that use of a FLP alone for asset protection purposes compromises the degree of available protection.

A second drawback to the FLP for asset protection planning is that once a charging order is imposed, not only is the client's access to partnership assets cut off, but the partners' ability to carry out the partnership business can be curtailed as well. For example, in one case, a federal district court sitting in Colorado imposed the following restrictions on a partnership after a charging order was entered even though, in the authors' opinion, such an order is contrary to cases establishing the rights of assignees: (1) the partnership could make no loans to a partner or anyone else; (2) the partnership could not sell or encumber partnership property without court permission; and (3) the partnership had to forward copies of all its financial statements to the creditor as well as past tax returns and financial statements.13

In addition, although many partnership agreements permit the partners to take differing distributions as long as the capital accounts are adjusted accordingly, a creditor would certainly have cause to complain if distributions to the debtor were less than those to the remaining partners. Therefore, the debtor's partners ability to freely access partnership property could also be limited by the charging order.

Offshore Asset Protection Plan

Let's say Dr. Jay is so pleased with his plan that he refers his colleague, Dr. Al, to us. Dr. Al has been previously sued for malpractice and although the case was settled within his policy limits, he is more leery than Dr. Jay, and wants more serious protection. He is interested in a full-blown asset protection plan with, perhaps, an offshore trust as its center-piece. What is the

framework of such a plan, why and how do you choose an offshore jurisdiction, and again, how is the asset protection plan coordinated with the estate plan?

The framework of the typical plan involves the establishment of a family limited partnership with one or more irrevocable offshore trusts holding limited partnership interests.

A common mistake made by planners, however, is to narrow their focus to the asset protection aspects of the planning and ignore the basic estate and tax planning methods that they otherwise utilize on a regular basis. For example, all estate planning professionals know the importance of ensuring that each spouse in a family is able to fully utilize the allowable exclusion amount, and in large estates, to take advantage of the so-called run up the brackets. The most basic form of estate tax planning is to ensure that each spouse has a minimum of the allowable exclusion amount in his or her estate, and possibly that the estates are equalized. When a client presents a problem which calls for the implementation of an asset protection plan, the planner often neglects these considerations and forms one offshore trust to hold the entire limited partnership interest, thereby negating the essential elements of a basic estate tax plan.

A second common mistake is to confuse the gift and estate tax rules with the fraudulent transfer rules. Although, for tax purposes, husbands and wives (who are U.S. citizens) can transfer property between themselves free of transfer tax, this concept does not apply to fraudulent transfers. A transfer to a spouse is held up to the same scrutiny as a transfer to any third party, and the planner must be mindful of this in assisting the client with asset allocation.

In our hypothetical, Dr. Al would establish a family limited partnership and transfer some portion of the family assets to the partnership. His wife, Emma, is a 2% general partner. At the same time, Dr. Al and Emma each establish an offshore irrevocable estate planning/asset protection trust, and a 49% limited partnership interest in the Big Al Family Partnership is transferred to each trust. Note that Dr. Al and his wife must each take care not to render himself or herself insolvent by the transfer to the offshore trust. Following the transfer, the partners own the partnership interests rather than the underlying assets themselves, which are owned by the partnership.

Note that if title to a certain portion of the family's assets were already held by Emma, and if Emma were not in a high risk profession herself, she might be comfortable with a classic inter

vivos revocable trust which could hold title to her limited partnership interest in the family partnership.

Let's say though that we recommend an offshore trust for Al and Emma. Sometime later, Dr. Al realizes that a suit against him may be in the offing. Emma, as general partner, then elects to dissolve the family partnership. Upon dissolution, the partnership assets are liquidated or transferred to the individual partners, namely, the offshore trust(s), in proportion to their respective shares. Since the offshore trusts "own" 98% of the partnership assets, that portion of the proceeds or assets will be transferred to the offshore Trustees who immediately assume control of those assets.

With this type of plan, a significant portion of the wealth will remain on-shore and under the clients' control until the partnership is liquidated. The risk is that the assets might be frozen by a court order before they are moved, but this is seldom the case. A second method is to skip the family partnership step altogether and to transfer the assets directly to the offshore trusts with a foreign Trustee and subject to the laws of the foreign jurisdiction, severing all ties to the United States, from the beginning.

Tax Reporting

When a partnership is formed, the partnership must file a form 1065 (partnership return) each year. States with income taxes require a similar form. Revocable and irrevocable trusts must also file returns (U.S. tax form 1041) and if they are "grantor" trusts (those where all trust income and losses are passed through to the Settlor14) the returns will simply show that the income is being reported by the grantor.15

In cases where an offshore trust is used, however, the question is then whether it is regarded as a "foreign" trust for U.S. tax purposes.16 Briefly, if the trust has only offshore trustees and is not expressly subject to the jurisdiction of a U.S. Court, (which will be the arrangement if the Settlor is sued and the protection plan is implemented), this triggers somewhat extensive reporting requirements for the trust.17 Note however that the reporting requirements are just that - numerous additional annual forms and statements - but not additional income taxes as the typical offshore trust is still treated as a grantor trust.18

Why go offshore?

The answer to the why question relating to offshore trusts has its roots in the common law rule that a person cannot create a spendthrift trust for his own benefit.19 A spendthrift provision in a trust typically provides that neither a beneficiary nor any creditor of a beneficiary can anticipate, reach, or alienate the interests of a beneficiary. Such a provision has generally been respected by the courts on the theory that a Settlor's funds become the property of the trust and not of the beneficiary, and that the Settlor ought to be able, within the bounds of public policy, to dictate the conditions under which these funds may be available to the beneficiary.20

Consequently, as a general rule in the great majority of jurisdictions, a spendthrift provision in a trust established by a party other than the beneficiary will operate to protect the trust assets from the creditors of the beneficiary, with only certain exceptions in the case of necessaries provided to a beneficiary in good faith by a creditor;21 and child support obligations (by Statute in a number of States).22 However, if the beneficiary is also the Settlor of the trust, the Restatement Second Trusts, sec. 156, sets forth the basic and critical guidelines essential to the use of most domestic trusts in asset protection - A creditor can reach whatever the Settlor can reach, as well as whatever benefits the Settlor could enjoy, assuming the trustee exercised its maximum discretion under the terms of the trust.23

A number of offshore jurisdictions have adopted trust legislation specifically providing that the assets of a self-settled discretionary trust will not be reachable by creditors of the Settlor/beneficiary in the absence of a fraudulent conveyance.24 And in the case of a claimed fraudulent conveyance, the burden of proof is on the creditor, who must prove beyond a reasonable doubt that the conveyance was fraudulent.25 Furthermore, the claim, or suit against the trust, must be made in the foreign jurisdiction, as judgments rendered by the United States (or other "foreign" jurisdictions) are not recognized, and typically the action must be commenced within the earlier of two years of the establishment of the trust or one year from accrual of the cause of action.26 Finally, in none of the desirable offshore jurisdictions do attorneys work on a contingent fee basis in such matters, so the creditor must finance the full cost of the litigation in advance.

Drafting the Offshore Trust for Estate Planning

The offshore trust itself, with several significant exceptions, is similar to a typical domestic estate planning trust for a high net worth individual. As there is no reason to duplicate efforts by having a second set of domestic trusts for estate planning purposes, the offshore trusts should, in fact, contain the dispositive provisions of the client's plan. And, as discussed above, offshore trusts are "tax-neutral" in terms of both income and transfer tax, and the same types of tax-planning provisions as those of a domestic trust must be included.27

Although the practitioner can begin with her standard domestic estate planning trust, there are several types of provisions which do not appear in such a trust but which are necessary or desirable in an offshore trust to maximize the protection offered by this type of planning. Of course, as with all other planning, these provisions should be tailored to the client's individual needs, keeping in mind the level of risk, the type of risk, and the client's overall estate planning goals. What follows is a discussion of some of the major differences between a typical domestic trust vs. an offshore estate planning trust, together with some cautionary drafting notes.

Protectors

The Protector is a device common in offshore trusts which is relatively unknown in domestic estate planning. The Protector can be an individual or a corporation, and can be either domestic or foreign, at least until such time as a suit strikes (at that point, a domestic Protector should resign and be replaced by a foreign Protector). The function of the Protector, generally, is to oversee the acts of the Trustee, and/or trust distributions and, normally, the offshore trust document specifies that the Protector acts in a non-fiduciary capacity. Another way to view the role of the Protector is that he exercises powers that are normally retained by the Settlor of a domestic inter-vivos revocable trust, or if not specifically retained, powers that are inherent in the Settlor's power of amendment.

The specific role of the Protector can be refined to suit the individual client's situation. Examples of Protector powers commonly included in offshore trusts are: (1) to remove and appoint Trustees; (2) to veto the Trustee's exercise of discretion in making trust distributions; (3) to consent to the creation or exercise of a special power of appointment; (4) to consent to the exercise of the

flight clause; (5) to add beneficiaries to the Trust and to remove beneficiaries; (6) to consent to the amendment of the administrative and/or dispositive provisions of the Trust; (7) to consent to the delegation of duties by the Trustee; and (8) to consent to the exercise of selected Trustee powers (such as the power to borrow) by the Trustee.

Care must be given in drafting Protector provisions to include a mechanism for the appointment and removal of the Protector; for Protector resignation and for temporary or permanent relinquishment of certain of its powers; for giving the Protector notice of an intended act by the Trustee; for the Protector giving notice to the Trustee of its granting or withholding of consent to an action by the Trustee; for payment of reasonable fee to the Protector for services performed in that role; and how the office of Protector will be carried out if there is more than one person serving in that capacity.

Restrictions on who may serve as Protector are also important. Permitting a beneficiary, a potential beneficiary, or a spouse of either to serve as Protector could not only create a conflict of interest but could also lead to serious income and estate tax implications and a poor estate planning result. This is more fully discussed below in connection with change of beneficiary.

Powers of revocation and amendment

Although it may not necessarily be required by the laws of the foreign jurisdiction, an asset protection trust should be irrevocable as to the Settlor to insulate the Settlor from domestic court orders. As discussed above, however, it is possible for the Settlor to grant to another individual (e.g. the Trustee or the Protector) most if not all of the powers inherent in the power of amendment or even revocation. (The Settlor can also give a disinterested person the power to grant general or non-general powers of appointment).

Even though the Settlor does not retain a power to amend the Trust, it is usually desirable to grant such a power to the Trustee. For many reasons, it is important to build as much flexibility into the trust as possible, and one way of doing this is to give an independent Trustee liberal authority to amend the Trust. In general, the Trustee may be permitted to amend the provisions of the Trust instrument as they may consider necessary to accomplish overall estate planning and income or estate tax savings for the Settlor or any beneficiary; to otherwise benefit a beneficiary; to

satisfy the requirements of a successor Trustee; or to conform the Trust to the laws of another jurisdiction (see below).28

The overall effect is that the trust property can be rearranged to suit the circumstances of the Settlor without transferring the assets out of the Trust.

Assuming that the Trustee holding the power of amendment is a corporate Trustee, a broad exoneration clause should be included exculpating the Trustee from liability to any beneficiary for exercise or failure to exercise the power.

If the Trust is sitused in a jurisdiction which has a rule against perpetuities, the Trustee must be prohibited from exercising the power to amend in a manner which would violate the rule.

The Trustee must also be prohibited from exercising the power of amendment in any way which will cause the trust to fail to qualify for the marital deduction or to cause the imposition of the Generation Skipping Transfer (GST) tax.

There can be numerous and complex tax consequences to the granting of a power to amend the trust. For example, to avoid a taxable gift by the Settlor when creating an irrevocable trust and/or when giving another a general power, the Settlor would normally reserve for himself a special testamentary power of appointment to render the gift incomplete.29 If any power given to another (including a Trustee or Protector) is exercised in a manner that removes the property beyond the Settlor's control, the Settlor will be deemed to have made a completed gift at the time of the exercise by the Powerholder.30

This does not necessarily mean that the Trustee's authority to amend the Trust should be limited, because circumstances may exist which favor the exercise of the power and acceptance of the resulting tax consequences. The planner may, however, want to at least add language reminding the Trustee to take the tax consequences into account in the exercise of its discretion.

Change of Beneficiaries

Unlike domestic trusts, it is common in offshore planning to have expanding and contracting rights to beneficial enjoyment of the trust. For example, Dr. Al's offshore trust might

provide that during a three year term (equivalent to a relevant statute of limitations), Dr. Al has no rights to principal or income distributions, but at the end of such term, he becomes a beneficiary as to both. The trust would also contain a provision that the term could be extended by the Trustee under certain circumstances such as Dr. Al becoming a defendant in a law suit.

Another example is a trust provision which provides that upon the occurrence of a triggering event, a new class of beneficiaries arises which does not include the Settlor. In other words, during Dr. Al's lifetime trust income and principal can be distributed to Dr. Al at the discretion of the Trustee. If Dr. Al is sued, a different class of current beneficiaries is created consisting of the spouse and issue of Dr. Al.

Depending on the wishes of the Settlor, either the Trustee, the Protector, or both, or one acting with the consent of the other, can be given the power to add and exclude beneficiaries, either permanently or for a specified period. In order to avoid treatment of this power as a general power of appointment, if there is an individual Trustee or Protector serving, he should not be permitted to add himself or his creditors, etc. as a beneficiary.

Similarly, as in the case of the power of amendment in granting the power to change beneficiaries, care must be taken to avoid unintended transfer of tax consequences. For example, assuming that the Settlor's Generation Skipping Tax exemption was not allocated to the Trust, you would not want the Protector to remove all beneficiaries other than grandchildren, resulting in the trust being treated as a skip person.31 The authority in the trust should be limited by language which states that the Protector cannot exercise a power in any manner which will cause the trust to be subject to the Generation Skipping Transfer Tax.

Likewise, the planner may want to ensure that the power to add and remove beneficiaries cannot be exercised in a manner which will cause the trust to fail to qualify for the marital deduction, e.g. by adding a discretionary income beneficiary or by granting a special power of appointment in a trust that is designed to qualify for the federal marital deduction. Again, the draftsperson may want to specifically prohibit this in the trust instrument.

Thought should also be given as to whether the Protector and/or Trustee should have the authority to remove the Settlor as a beneficiary. This may be an important power from an asset

protection standpoint if the Settlor is sued. For tax purposes, however, unless the Settlor has retained a special power of appointment, the removal of the Settlor as a beneficiary could result in the transfer to the trust being treated as a completed gift. This would also take the property out of the Settlor's estate for transfer tax purposes and the opportunity for a step-up in basis to the date of death value would be lost.

Excluded Persons

A common drafting technique used in offshore trusts which does not appear in domestic trusts is the addition of a schedule of excluded persons. This is a schedule attached to the trust which lists all of the classes or in some cases, the individual names of persons who may never become beneficiaries, thus serving as a strict limitation on the Trustee's or Protector's authority to add beneficiaries. For asset protection purposes, you would want to list present and future creditors of the Settlor as excluded persons. For tax planning, as noted, you might want to list the Trustee, the Protector, their creditors, estates and their spouses.

Change of Situs

Another inherent difference between offshore planning and domestic planning is that the typical offshore plan contemplates a change of situs, whereas with most domestic trusts, the draftsperson can usually rely on the trust remaining in the same jurisdiction for the whole term. Many offshore trusts provide that upon the occurrence of a lawsuit or an event of duress, the local Trustee is automatically removed and the trust automatically is diverted to another jurisdiction. An event of duress is defined as war, civil disturbances, or political events which may impact on the safety of the trust funds, the enactment of a law which may restrict the Trustee's control over or the disposition of the Trust property, or the entry of any court order which might have that effect.

The possibility of a change in situs can create hidden pitfalls for the draftsperson. For example, Dr. Al's trust may begin its life in Nevis which has no rule against perpetuities and three years later the situs may be changed to the Isle of Man which has a one hundred year rule. Practitioners should be cautious about using a trust provision that simply calls for the longest period allowable under the particular governing law. A recent case in the Cayman Islands held that it was not sufficient to satisfy the rule to provide that the Trust would endure for the longest period

permitted under applicable law, because there was no measuring life to establish the time when the interest will vest.32

This is another other reason to build as much flexibility into the trust as possible, giving the Trustee liberal authority to amend the Trust, inter alia, to comply with local law, or even to change the choice of governing law. To illustrate, Dr. Al's Trust can provide that it is established under the laws of the Cook Islands whose law shall be the "Proper Law" of the trust agreement; provided that the Trustees may by deed declare a change in the forum for administration of the Trust and make such consequential alterations in the trust provisions as the Trustees shall consider necessary or desirable to secure that the trust instrument is as valid under the law of the new jurisdiction as it was under Cook Island law.

Selection Of Trustee

In domestic estate planning, it is common to have the Settlor serve as initial trustee followed by his spouse. It is clearly not desirable from an asset-protection point of view to have the Settlor serve as the original Trustee, although it may be possible to have the spouse serve as co-trustee with a corporate foreign Trustee. If the Settlor is sued, the spouse can resign, removing the trust from the U.S. court's jurisdiction. One of the challenges in setting up an offshore trust is the selection of a foreign Trustee which will also not be subject to the jurisdiction of a U.S. court. Care should be taken in the selection and in the drafting to ensure that the foreign trustee has no U.S. subsidiary, is not a subsidiary of a U.S. Corporation, and has no other presence or nexus to the U.S.

Conclusion

When drafting asset protection plans, practitioners should be careful not to lose focus on the essential estate planning objectives and the related provisions necessary to carry out those objectives. In addition, there are many special provisions that are characteristic to offshore trusts, such as inclusion of powers to amend or the appointment of a Protector. These provisions can give rise to serious tax traps if not properly drafted, but with careful attention and a sound knowledge of U.S. estate tax laws, an asset protection plan can also be a well drafted estate plan.

[1] IRC §2010 Unified Credit Against Estate Tax, IRC §2010(c) Applicable Exclusion Amount.

[2] IRC § 2056(b)(7), To qualify for the marital deduction, an interest passing to a surviving spouse cannot be a terminable interest (e.g. a life estate) unless it qualifies under an exception for "qualified terminable interest" property. To qualify, the spouse must be entitled to all of the income for life, and no one other than the spouse can receive principal. An election for this treatment must be made.

[3] IRC §2041 (a).

[4] Partial QTIPelection can be made over excess amount. IRC § 2056 (b) (7) (iii).

[5] IRC § 2044.

[6] Restatement second property, § 13.2.

[7] IRS Revenue Ruling 93-12, Estate of James Barudin v. Commissioner of Internal Revenue U.S. Tax Court 72 TCM 488 (U.S. Tax Court 1996).

[8] J.Richard Duke & Patrick H. Davenport, *An Update on the Partnership Charging Order and Observations on Partnership Planning*, 1 Asset Protection Journal 9 (Winter 1999)

[9] Rev. Uniform Limited Partnership Act, § 703 (1985).

[10] IRS Revenue Ruling 77-137.

[11]Crocker National Bank vs. Perreton, 208 Cal.App3d 255 (1989)

[12] Madison Hills Limited Partnership II v. Madison Hills, Inc., 35 Conn. App. 811, 6744 A.2d 363 (1994).

[13] Order entered in U.S. District Court, District of Colorado, May 3, 1994 in E.J. and Muriel Rothwell v. Lisa Fertman, civil action # 92 Z1881.

[14] Treasury Regulation § 671-677.

[15] IRC § 674.

[16] IRC § 7701(a)31.

[17] IRC § 6048, IRS Notice 97-34, IRB 1997-25.

[18] IRC § 679.

[19] Restatement of Trusts 2d, § 8, 156 (1959)

[20] Restatement of Trusts 2nd,§ 8, 152-153 (1959)

[21] Bogert, Trusts and Trustees, 1992, § 221 at 405-406

[22] See e.g. ?Alaska, ?Delaware

[23] See also Outwin v. Commissioner, 76 tax Court 153 (1981), for an excellent review of creditors' rights to self-settled domestic trusts.

[24] See e.g., Cook Islands International Trusts Act of 1984, as amended.

[25] Id.

[26] Some jurisdictions, e.g., Gibraltar, offer immediate protection (i.e. a zero open period of limitations) if the transfer to the trust did not render the transferor insolvent. See Gibraltar Bankruptcy Ordinance (1964) sec. 42A.

[27] There remains a question, however, as to whether the application of IRC § 684 will result in a capital gains tax on appreciated property held in the foreign trust on the Settlor's death.

[28] Neill McBryde, *Building Flexibility in Estate Planning Documents*, 30th Heckerling Inst. on Estate Planning (1996).

[29] IRC 25.2511-(2)(b).

[30] Treasury Regulation § 25.2511-(2) (b).

[31] IRC § 2613.

[32] re: Cayman Is.-trust provision for the longest period allowable under the particular governing law.