NEVADA ASSET PROTECTION FOR CALIFORNIA RESIDENTS

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Introduction

More and more clients are seeking asset protection as jury awards and the number of frivolous lawsuits continue to increase, in order to preserve their hard-earned assets to pass on to future generations. Such asset protection is available in various forms, including limited liability companies, corporations, homesteads, qualified retirement plans, offshore trusts and domestic asset protection trusts. As of the date of this article, 18 states have adopted some form of Domestic Asset Protection Trust ("DAPT") statute[1]. Such statutes are not solely for the benefit of the residents of those 18 DAPT states. California has not yet passed a DAPT statute, however, many residents of California can still enjoy many of the protections DAPT states afford as long as certain conditions are met. This article discusses and explores the requirements of implementing a successful asset protection plan in such a situation, in which a California resident (a non-DAPT jurisdiction) sets up a Nevada DAPT. This article will show that a Nevada DAPT, structured as outlined below for a California resident, should provide a real benefit to the settlor by either (1) being upheld in its entirety if challenged, or (2), if a dispute arises, lead to an attractive settlement.[2]

First, the California resident must be a good candidate for a Nevada DAPT. To be a 'good candidate' the California resident should not have any impending litigation or creditor issues, and have other reasons for setting up the trust, which may include tax reasons – using up a lifetime exemption, taking advantage of Nevada's income tax laws, gifting assets to reduce an estate for estate tax purposes; or other reasons such as pre-marital planning, protecting beneficiaries (other than him or herself) against potential ex-spouses, their creditors, etc. It is important for the drafting attorney to perform due diligence on the client to ensure that they are a qualified applicant and are not engaging in this type of planning to hinder, delay, or defraud known creditors.

In our example, we will assume that the California resident's DAPT is in compliance with the Nevada DAPT statute and possesses the circumstantial factors described below.

Compliance with Applicable Nevada Statutes:

Nevada Revised Statute ("NRS") Chapter 166, also known as the Spendthrift Trust Act of Nevada, requires that in order to be a valid spendthrift trust, the trust must be (1) in writing, (2) the settlor must manifest an intent to create such a trust, (3) irrevocable, and (4) at least one trustee must be a Nevada resident, (5) not require that any part of the trust's income or principal be distributed to the settlor, and (6) not be intended to hinder, delay or defraud known creditors. *See generally* NRS §166.

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[1] *See* Steven J. Oshins, "8th Annual Domestic Asset Protection Trust State Rankings Chart" (April 2017) (States with some form of DAPT Statute: Alaska, Colorado, Delaware, Hawaii, Michigan, Mississippi, Missouri, Nevada, New Hampshire, Ohio, Oklahoma, Rhode Island, South Dakota, Tennessee, Utah, Virginia, West Virginia and Wyoming).

[2] Thomas E. Greene III, "Structuring Self-Settled Trusts for Non-Resident Settlors," Trusts & Estates, 29-35 (November 2016).

Circumstantial Factors

In addition to complying with the Spendthrift Trust Act of Nevada, the model Nevada DAPT in our example will also be surrounded by the following circumstances:

1. Settlor transfers only a portion of his or her wealth into the DAPT;
2. Settlor has no outstanding claims, lawsuits, or judgments when transfers are made to the DAPT;
3. All of the property owned by the DAPT can be physically located in Nevada and consists primarily of 'moveable' assets, such as marketable securities, bonds, and cash equivalents;
4. A trustee who resides in Nevada (who has minimal contact with California) approves all distributions to the settlor, and preferably actually manages and preserves the assets, limiting the control of the settlor over the DAPT;
5. The DAPT is drafted by competent Nevada counsel and is executed in the state of Nevada.

The trust should meet the above requirements and also contain a "spendthrift clause" which generally prohibits the assignment, alienation, acceleration and anticipation of any interest of the beneficiary under the trust by the voluntary or involuntary act of the beneficiary, or by operation of law or any process at all.[3]

Under Nevada law, when a trust is structured according to the above, "a person may not bring an action with respect to a transfer of property to a DAPT (1) if the person is a creditor when the transfer is made, unless the action is commenced within 2 years after the transfer is made or 6 months after the person discovers or reasonably should have discovered the transfer, whichever is later; [or] (2) if the person becomes a creditor after the transfer is made, unless the action is commenced within 2 years after the transfer is made." NRS §166.170.

While engaging in such planning does not prevent an attack from creditors, in such a situation where the DAPT complies with NRS §166 and the above facts surround the creation and administration of the DAPT, the DAPT should either be upheld in its entirety, or should at least put the settlor in a better settlement position in relation to those creditors.

Attacks from California Creditors

A California creditor may attempt to attack the DAPT in our example through the relatively new Uniform Voidable Transactions Act (the "UVTA").

[3] The following is an example of a spendthrift clause: "The beneficiary shall have no power or capacity to make any disposition whatever of any of the income by his or her order, voluntary or involuntary, and whether made upon the order or direction of any court or courts, whether of bankruptcy or otherwise; nor shall the interest of the beneficiary be subject to any process of attachment issued against the beneficiary, or to be taken in execution under any form of legal process directed against the beneficiary or against the trustee, or the trust estate…The trustee of a spendthrift trust is required to disregard and defeat every assignment or other act, voluntary or involuntary, that is attempted contrary to the provisions of this chapter." *See* NRS §166.120.

The California Uniform Voidable Transactions Act

The UVTA was adopted in California on July 2, 2015 and made effective as California Civil Code Section 3439, *et. seq.*, on January 1, 2016. The UVTA revised and replaced the Uniform Fraudulent Transfers Act, and while discussing all the changes and potential implications of the UVTA is beyond the scope of this article, one of the relevant changes affecting our topic is the Choice of Law provision, which provides that a claim under the UVTA is governed by the local law of the jurisdiction in which the debtor is located when the transfer is made or the obligation is incurred. If the debtor is an individual, they are considered to be located at the individual's principal residence. Cal. Civ. Code §3439.10. This section was meant to clarify the historical ambiguity of which state's law was to apply in a conflict of laws situation. As California's law expressly states that if the UVTA applies, California self-settled spendthrift trusts, as to the settlor, are invalid and assets in such a trust are accessible to those creditors.[4] Of course a creditor would want California law to apply, not Nevada law.

In light of the passage of the UVTA and its choice of law provision, some practitioners have taken the position that asset protection planning for residents of a non-DAPT state is now futile.[5] For California residents, it has been suggested that any asset protection planning engaged in would be per se void, as California by statute does not recognize self-settled spendthrift trusts.[6] That is exactly why many California residents seek to avail themselves of Nevada's DAPT laws. However, in order for the UVTA's choice of law provision to be controlling and dictate a court's choice of law, BOTH the domicile state and the DAPT state must have adopted the UVTA. The UVTA was introduced as Assembly Bill 420 in the 78th Session of the Nevada Legislature in March of 2015 but the bill was dead on arrival. No vote was ever taken, and because no vote was taken within the time period allotted, pursuant to Joint Standing Rule 14.3.2, no further action was allowed to be taken on the bill and it is unlikely that it will ever be passed by the Nevada legislature. Thus, as the UVTA was not adopted by the Nevada legislature, a Nevada court would still have to engage in its own conflict of laws analysis in determining whether to apply California's law if an action is brought in Nevada under the UVTA.[7]

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[4] *See generally* California Civil Code §3439; *see also* Cal. Prob. Code §15304.

[5] *See* Al W. King III, "Tips From the Pros: Be Aware of the Uniform Voidable Transactions Act," wealthmanagement.com (Sep. 21, 2016); *see also* George D. Karibjanian, "The Uniform Voidable Transactions Act Will Affect Your Practice," Trusts & Estates, 17 - 21 (May 2016).

[6] Cal. Prob. Code §15304.

[7] In the Official Comments to the UVTA's choice of law provision, the commentators specifically address the scenario of a non-DAPT settlor establishing a trust in a DAPT state. Official Comment 8 provides:

> "Because the laws of different jurisdictions differ in their tolerance of particular creditor-thwarting devices, choice of law considerations may be important in interpreting [the UVTA] as in force in a given jurisdiction. For example, the language of the [UVTA] historically has been interpreted to render voidable a transfer to a self-settled spendthrift trust. Suppose that jurisdiction X, in which this Act is in force, also has in force a statute permitting an individual to establish a self-settled spendthrift trust and transfer assets thereto, subject to stated conditions. If an individual Debtor whose principal residence in X establishes such a trust and transfers assets thereto, then under Section 10 of this Act the voidable transfer law of X applies to that transfer. That transfer cannot be considered voidable in itself under the [UVTA] as in force in X, for the legislature of X, having authorized the establishment of such trusts, must have expected them to be used. Other facts might still render the transfer voidable under X's enactment of [the UVTA]). By contrast, if Debtor's principal residence is in jurisdiction Y, which also has enacted this Act but has not legislation validating such trusts, and if the Debtor establishes such a trust under the law of X and transfers assets to it, then the result would be different. Under Section 10 of this Act, the voidable transfer law of y

If a creditor brought an action against a settlor in California under the UVTA in order to reach assets held in a Nevada DAPT, the creditor would have to overcome several hurdles. In our scenario, the DAPT trustee and assets are all in Nevada and the settlor had no intent to hinder, delay or defraud this creditor bringing the action. The creditor would likely attempt to name the Trustee of the DAPT as a party to the action, however, the first major hurdle would be to get the California court to assert jurisdiction over the Nevada DAPT. If the California court did not assert jurisdiction over the Nevada DAPT, typically the creditor would have to get a judgment against the settlor, individually, and then seek to enforce that judgment against the trust in Nevada.

It is important to note here that if the UVTA applies, real property located in California, even if transferred to a DAPT, would most likely be susceptible to a creditor judgment in California as California courts have "in rem jurisdiction" over such property. In that situation a California court might argue that by virtue of some property of the DAPT being located in California, the court has jurisdiction over the entire DAPT. Ideally, the California real property would be transferred into an LLC, which would be owned by a separate DAPT other than the DAPT that holds all the 'moveable' assets. Thus, to reach any 'moveable' assets in the second DAPT that owns all the moveables, a creditor would have to first obtain jurisdiction over the Nevada trustee. If the creditor is successful in a California court, then the creditor would either (1) register its money judgment in against the DAPT in Nevada, or (2) seek enforcement of the judgment rendering a transfer to the DAPT void in Nevada.

Ideally, the DAPT created in the above scenario would fall outside the UVTA. A DAPT should fall outside the scope of the UVTA if the UVTA statute of limitations has expired, the transfer of assets was not made to hinder, delay or defraud known creditors, and the transfer did not render the settlor insolvent.[8]

Jurisdiction of a California Court over a Nevada DAPT

Generally, a California court may exercise jurisdiction over a trust on any basis permitted by Section 410.10 of the California Code of Civil Procedure, which states that "a court of this state may exercise jurisdiction on any basis not inconsistent with the Constitution of this state or of the United States." The purpose of §410.010 is to provide plenary power over property located within the state and limited power over property and trusts located outside of California.

Exercising jurisdiction over out-of-state property (and trusts) is limited to instances where a foreign defendant "has certain minimum contacts [with the state] such that the maintenance of the suit does not offend traditional notions of fair play or substantial justice."[9] Such contact may include an analysis of factors including: (1) presence, (2) domicile, (3) residence, (4) nationality or citizenship, (5) consent, (6) appearance in an action, (7) doing business in the state, (8) an act done in the state, (9) causing an effect in the state by an act done elsewhere, (10) ownership, use or possession of a thing in the state, (11) other relationships to the state which make the exercise

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would apply to the transfer. If Y follows the historical interpretation of the above section [which renders voidable a transfer to a self-settled spendthrift trust], the transfer would be voidable under [the UVTA] as in force in Y."

[8] See Cal. Civ. Code §3439.09, *et seq*.

[9] *Int'l Shoe Co. v. State of Wash., Office of Unemployment Comp. & Placement*, 326 U.S. 310, 316 (1945).

of juridical jurisdiction reasonable.[10] Under the model DAPT outlined above, when the trustee is in Nevada, all the property is located in Nevada, and the Nevada DAPT does not own California real property, there would likely be insufficient contact with California to justify a court exercising jurisdiction over the DAPT. Consequently, California courts would be unable to claim jurisdiction over a DAPT.

If the creditor names the Trustee in the original action, the Trustee can appear specially to assert lack of jurisdiction of the California Court to challenge the court's jurisdiction by a motion to quash service of summons within the designated time period.[11] A special appearance to challenge jurisdiction does not constitute a 'general appearance' that would typically allow a court to assume jurisdiction over a party.

Assuming, arguendo, that the Trustee was unsuccessful in challenging jurisdiction and a California court awarded the creditor a judgment against the settlor and the DAPT, the creditor would still have to go to Nevada to enforce the judgment (as all the assets in the DAPT in our scenario are physically located in Nevada).

If the California court did not assume jurisdiction over the DAPT, the creditor would have to bring a completely new action in Nevada to get to the property in the DAPT.

Bringing a California Judgment to Nevada

In order to have a valid foreign judgment in Nevada, the out of state judgment creditor must follow the statutory procedure for registering a foreign judgment in Nevada. In order to bring a judgment obtained in a foreign jurisdiction to bear in a different jurisdiction, a multi-step procedure involving both federal and state law must be followed. First, the clerk of the original court must execute a "Certification of Judgment for Registration in Another District" pursuant to 28 U.S.C. §1963, which states:

> "A judgment in an action for the recovery of money or property entered in any court of appeals, district court, bankruptcy court, or in the Court of International Trade may be registered by filing a certified copy of the judgment in any other district…when the judgment has become final by appeal or expiration of the time for appeal or when ordered by the court that entered the judgment for good cause shown… A judgment so registered shall have the same effect as a judgment of the district court of the district where registered and may be enforced in like manner."

When a judgment is registered in the foreign state pursuant to 28 U.S.C. § 1963, the judgment is controlled by Rule 69 of the Federal Rules of Civil Procedure, which provides: "The procedure on execution, and proceedings supplementary to and in aid of the judgment and in proceedings on and in aid of execution shall be in accordance with the practice and procedure of the state in which the district court is held." Once a judgment is registered in Nevada (from any other jurisdiction) pursuant to 28 U.S.C. § 1963, and according to Federal Rule of Civil Procedure 69, that judgment would be governed and interpreted under Nevada law.

Under Nevada law, the judgment creditor, upon registering the foreign judgment, must: file an affidavit, promptly give notice to the judgment debtor, and verify to the court that the notice was

[10] *Id.*; See also Conflict of Laws Restatement (Second) Section 27.
[11] Cal. Rule Civ. Proc. §418.10.

given. NRS § 17.360. It is important to note here, that unless the Nevada Trustee is named in the original action in the foreign jurisdiction, a judgment against the settlor individually will not be enforceable against the Trustee. In this case, a separate action must be brought to enforce the judgment against the Trustee.

The affidavit must set forth the name and last known post office address of the judgment debtor and the judgment creditor and also must include a statement that the foreign judgment is valid and enforceable, and the extent to which it has been satisfied.[12]

Upon registration of a foreign judgment, a judgment creditor is able to pursue their judgment on the debtor in Nevada. Again, if the DAPT is not named as a party in the original action, this judgment is NOT ENFORCEABLE as against the DAPT. In this instance the attorney for the DAPT would bring a motion to quash the judgment for lack of jurisdiction, and a Nevada court would likely dismiss the creditor's claim against the DAPT. As to the settlor, a district court "may order any property of the judgment debtor not exempt from execution…to be applied toward the satisfaction of the judgment." NRS §21.320. The exemptions from execution are those exemptions that the Nevada legislature has deemed exempt, NOT the exemptions that are allowed under the foreign jurisdiction's laws. Under Nevada law, pursuant to NRS §21.090, interests in self settled spendthrift trusts are exempt from attachment.

Additionally, the Nevada Spendthrift Trusts Act provides strong protections against creditor's claims. A DAPT prohibits the assignment, alienation, acceleration and anticipation of any interest of a beneficiary under the trust by the voluntary or involuntary act of the beneficiary, or by operation of law or any process. NRS §166.120. Payments and distributions by the Nevada trustee are made only to the beneficiary, who specifically can be the settlor. NRS §166.110. The Trustee of a DAPT is required to disregard and defeat every assignment or other act, voluntary or involuntary, that is attempted contrary to the provisions of the Nevada Spendthrift Trust Act. If the DAPT meets all the requirements of the statute and is modeled after the DAPT provisions outlined earlier in this article, under Nevada law a judgment creditor may not execute a judgment against any property in a DAPT.

Judgment Against the DAPT Trustee

Full Faith and Credit.

Article IV of the United States Constitution states that "full faith and credit shall be given in each State to the Public Acts, Records, and Judicial Proceedings of every other State."[13]

However, if a California court erroneously asserted jurisdiction over the DAPT, a Nevada court does not have to enforce such a judgment under the Full Faith and Credit clause of the Constitution, as it is invalid on its face. The United States Supreme Court has held that states have no obligation to give full faith and credit to an invalid judgment offensive to the Due Process Clause of the 14th Amendment. *Hanson v. Denckla*, 357 U.S. 235 (1958).

In *Hanson*, a Florida court assumed jurisdiction over a Delaware Trustee of several Delaware trusts established by a Pennsylvania settlor by virtue of the settlor being domiciled in Florida at the date of her death. The Supreme Court held that the Florida court erred in holding that it had

[12] *See Kabana, Inc. v. Best Opal, Inc*., 2007 WL 556958 (D. Nev. Feb. 15, 2007).
[13] U.S. Const. Art. IV, §1.

jurisdiction over the non-resident corporate trustee defendant, as no trust property was located in Florida and the Trustee did not have enough contacts with Florida to meet the minimal contacts requirement as set forth in *International Shoe* because the trust company had no office in Florida, the Trust company transacted no business in Florida, none of the trust assets had ever been held or administered in Florida, and there was no evidence that the trust company solicited business in Florida.[14]

If a creditor who has been successful in California subsequently brings an action or seeks to enforce the California judgment in Nevada under the UVTA, a Nevada court would engage in a choice of laws analysis. The creditor would push for the court to apply California law, and likely cite *In re Huber* as persuasive authority despite it being a Bankruptcy Court case. *In re Huber* is often used by critics of DAPTS for non-DAPT jurisdiction residents. However, critics that cite *Huber* as a case-in-point that DAPTS do not work for non-DAPT residents fail to mention the 'bad' facts:

- The debtor was aware of the 'gathering storm clouds' of creditor trouble – he had actually already been sued by multiple creditors and had outstanding judgments against him.
- His principal goal, as stated in an email to his estate planning attorney was to "protect…[his] assets from [his] creditors."
- The transfers into the trust were fraudulent – at the time assets were transferred into the trust there were existing judgments and threatened litigation.
- The debtor transferred substantially all of his property (about 70%) into the Trust, essentially rendering him insolvent.
- Actual intent to hinder, delay, and defraud known creditors was found due to the timing of the trust's creation, the facts surrounding its creation, the timing of asset transfers support a finding of motive other than estate planning: that of asset protection at the expense of his creditors.
- There were no substantial ties to the DAPT state (Alaska) – the only asset transferred to Alaska was a $10,000 cd which was a nominal amount compared to the total amount of assets transferred into the trust.
- The estate planning attorney who drafted the trust worked out of Washington, the signing of the Trust took place in Washington.

The court, in its analysis, dove into the facts surrounding the creation of the Trust and ultimately concluded that the transfers to the asset protection trust were fraudulent, and thus void. Understanding *Huber* leads us to conclude that had the facts been different (a proper DAPT with no fraudulent intent by the settlor and sufficient contacts with the DAPT state) a court would uphold such a DAPT for a non-resident. The court looks at specific facts to determine which state law applies. It has also been argued that the court in *Huber* used the wrong Conflict of Laws Restatement section to come to its conclusion.[15]

Thomas E. Greene quoted Barry S. Engel in his commentary that:

[14] *Hanson v. Denckla*, 357 U.S. 235 (1958) quoting *Int'l Shoe Co. v. State of Wash., Office of Unemployment Comp. & Placement*, 326 U.S. 310, 316 (1945).
[15] Thomas E. Greene III, LISI Asset Protection Planning Newsletter #328 (August 17, 2016) at http://www.leimbergservices.com.

> "[T]he Court misapplied [Conflict of Laws] Restatement §270 and instead, should have relied on Restatement §273…the Court resolved the wrong question. Restatement §270 speaks to the 'validity' of the trust, but validity is not the issue, as trusts are inherently valid contracts…rather, the relevant question is 'whether the [valid] trust will be enforceable as against the creditors of that person." [16]

Further, Greene cited Nenno & Sullivan to elaborate on distinguishing the two sections. They argue that, since trusts are inherently valid, the purpose of § 270 in determining the validity of trust matters are confined to issues such as violating the rule against perpetuities or the rule against accumulations. They state that in contrast § 273 deals specifically in determining a creditor's ability to reach trust assets. This interpretation makes perfect sense and sufficiently clarifies the confusion between the two sections. As further illustrated by Greene, it makes a big difference which section is applied because the provisions in § 273 allow greater deference to be given to the choice of law provision in the trust:

> "The title of [Conflict of Laws] Restatement (Second) §273 'Restraints on Alienation of Beneficiaries' Interests,' is prima facie evidence of the [above argument]. Paraphrased, §273 states that whether a creditor may be assigned a beneficiaries' interest is determined by the governing law designated in the trust, 'and otherwise,' by the law of the state to which the administration of the trust is most substantially related. The words 'and otherwise' are crucial, because, in this context, they can only be interpreted to mean the state law designated to govern the trust will prevail in enforcement cases and, only if there is no designation, will substantial relationship factors even come into play….[Thus] the terms of a trust instrument designating the trust state's law to govern, when combined with the trust state's law enforcing the trust's provisions against creditors, present a difficult to refute argument demanding that the state court enforce the trust's terms."[17]

Here, in our scenario, the DAPT would name Nevada as the governing jurisdiction and the Nevada Court would apply its own laws regarding claims against the settlor. In our example, the chances of the creditor succeeding are very slim, as the Nevada Supreme Court recently upheld the validity of properly constructed DAPTs and the protections against creditors they provide.[18]

In *Nelson v. Klabacka*, the Nevada Supreme Court issued a ruling upholding the protections afforded by a DAPT. In this case a husband and wife had executed a transmutation of property (separate property agreement) and then placed their individual property in separate DAPTs, with the intent to occasionally "level off the trusts" to equalize their value. Upon divorce, the wife added the husband's DAPT as a necessary party and sought to collect from it alimony, child support, attorney fees, expert fees, and additional assets to equalize her trust's value. Because there was ample evidence that the parties intended to continue to use the property of both trusts as community property the District Court found that the wife had a continued interest in the assets and could thus reach them. However, because the separate property agreement was clear and unambiguous on its face, the Supreme Court properly denied the consideration of extrinsic

[16] *Id.*
[17] *Id.*
[18] *Klabacka v. Nelson*, 133 Nev., Advance Opinion 24 (May 25, 2017).

evidence and held the separate property agreements and DAPTS to be valid, thus eliminating any rights the wife would have held in the husband's DAPT.

As the requirements for a valid DAPT under NRS §166 were satisfied and the trust was not created to defraud a *known* creditor at the time assets were transferred into the trust, the Supreme Court held the trust to be valid. The Supreme Court held that, pursuant to Nevada Law and the specific bar under NRS §166.120(2), it could not order the Trustee to make a distribution to a discretionary beneficiary (the husband) to satisfy his personal obligations.

Finally, although DAPT laws in South Dakota, Wyoming, Florida, and others specifically allow assets to be reached to satisfy child and spousal support, Nevada statutes explicitly protect beneficiaries from these personal obligations. The Court even analyzed its legislative history to further support this conclusion, and quoted Michael Sjuggerd in *Defeating the Self-Settled Spendthrift Trust in Bankruptcy* that the key difference between Nevada DAPTs is that Nevada "abandoned the interests of child-and spousal-support creditors, as well as involuntary tort creditors." Because the husband's child-and spousal-support obligations were not known at the time the trust was created and the obligations were personal, the Court held that the DAPT could not be made to pay such obligations as a valid spendthrift trust.

Another case that critics of DAPTs for non-DAPT jurisdiction residents cite is *Dahl v. Dahl*.[19] In this case, a Nevada DAPT was at issue during divorce proceedings in Utah. The choice of law provision in the trust mandated that it should be governed according to Nevada law, to which the Utah Supreme Court said they would ordinarily adhere to. However, the Utah Court reasoned that in this instance, due to Utah's strong public policy regarding equitable distribution of marital assets, the Court would use its own laws to interpret the trust. The Court held that, under Utah law, the trust was revocable, and that the wife as a settlor of the trust had a right to revoke the portion of the trust that was funded with her property.

It should be emphasized that the only assets the "creditor" was able to reach were the assets that she had placed into the trust herself and had property rights to. Further, she was only entitled to her equitable share of those assets, not their entire value. Therefore, unless a creditor placed its own assets in a debtor's trust this case gives them no argument that it could lay claim to any property held in a Nevada DAPT. Further, this policy exception is extremely narrow, and only applies if the creditor is a divorcing spouse in Utah. Because this holding only allowed a return of a wife's property rights under an extremely narrow exception it is clear that the majority of DAPTs would be unaffected by this holding and that DAPTs are still alive and well.

Enforcement of Judgment Rendering Transaction Voidable

There are two scenarios in which a creditor can attempt to reach a debtor/settlor's assets: either the creditor obtains a money judgment against the settlor, or the creditor obtains a judgment which states the settlor's transfer of assets into a DAPT was void. Under both scenarios, despite having obtained a judgment against the settlor, the creditor must now seek to enforce it against the DAPT in Nevada, as it is the Trustee who holds the assets which are physically located in Nevada.

As discussed previously, the United States Supreme Court has stated that the full faith and credit clause does not compel "a state to substitute the statutes of other states for its own statutes

[19] *Dahl v. Dahl*, 2015 UT 79 (2015).

dealing with a subject matter concerning which it is competent to legislate."[20] A state such as California would use the UVTA choice of law provisions to determine which laws apply, while Nevada, who has not enacted the UVTA, would use the Restatement 2d Conflict of Laws analysis. If California had determined under their UVTA choice of law provision that their local laws shall apply to invalidate a trust, and that judgment is brought to Nevada, who has specifically rejected the UVTA, then Nevada will be even less likely to give credit to that judgment. This is because Nevada is not required to substitute its Conflict of Laws analysis for that of another state who adopted the UVTA. Further, because Nevada has specifically rejected the UVTA when it was presented to the legislature it is clear they will not be eager to give effect to its provisions. Had a California judgment still used the Conflict of Laws analysis under the Restatement 2d, as they would have done prior to the UVTA, Nevada may have been forced to give full effect to the analysis since the Nevada Court would have undergone the same analysis. By enacting a different choice of laws provision under the UVTA, California has effectively distanced itself from the Conflict of Laws rules of Nevada, which supports the position that Nevada need not give full faith and credit to a judgment of a California court under certain circumstances.

As mentioned previously, an exception to the Full Faith and Credit Clause exists if enforcing another state's judgment would violate the policy of that state.[21]

Much has been debated about this policy argument, but the real question is how a Nevada court would react to it. In 2011 the Supreme Court of Nevada was presented with this argument to enforce a California judgment in *Donlan v. State*.[22] Here, a California judgment terminated its requirement for a defendant to register in another state as a sex offender, and the defendant subsequently filed with Nevada to conform to the amended judgment under the Full Faith and Credit clause. Nevada refused to honor the judgment, stating that California "lacks power to dictate the means by which [Nevada] can protect its public."[23] The Nevada Court refused to substitute its laws for conflicting California laws dealing with the same issue which violated Nevada policy in which Nevada was competent to legislate.[24] Specifically, the Nevada Court quoted the United States Supreme Court: "the full faith and credit clause does not require one state to substitute for its own statute, applicable to persons and events within it, the conflicting statute of another state, even though the statute is of controlling force in the courts of the state of its enactment."[25]

Using the same line of reasoning as *Donlan*, because Nevada statutes protect property within Nevada which is controlled by a Nevada Trustee held within a Nevada Trust, the Nevada courts would be under no obligation to allow laws of another state (California) to mandate how disputes regarding such property should be resolved.

Thus, it is clear that the Nevada Supreme Court recognizes this policy argument against the Full Faith and Credit Clause and is not afraid to use it to support its policies and legislation. Further,

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[20] *Pacific Ins. Co. v. Industrial Accident Comm'n.*, 306 U.S. 493(1939).
[21] *Id.;* see also *Baker v. General Motors Corp.*, 522 U.S. 222 (1998).
[22] *Donlan v. State*, 127 Nev. 143 (2011).
[23] *Rosin v. Monkin* 599 F .3d 574, 577 (7th Cir. 2010)
[24] *Nevada v. Hall*, 440 U.S. at 421-22, 99 (1979); *Pacific Ins. Co. v. Industrial Accident Comm'n* 306 U.S. 493, 502 (1939); see also *Baker v. General Motors Corp.*, 522 U.S. 222 (1998).
[25] *Pacific Ins. Co. v. Industrial Accident Comm'n* 306 U.S. 493, 502 (1939).

it is clear in the recent *Nelson* case, discussed herein, that Nevada has a strong public policy of supporting properly formed DAPTS and will protect the assets in such trusts from attachment by creditors.

Conclusion

Based on the above analysis, Nevada asset protection planning is still a viable option for eligible California residents, as engaging in such planning (following the model trust provisions and under the right circumstances) would benefit a settlor in the event of a creditor attack as the DAPT would either be upheld in its entirety or at least put the settlor in a better settlement position in relation to that creditor.

For clients who want even more protection and peace of mind that their legacies will be preserved to pass on to future generations, we recommend the Passport Trust™.

The Ultimate Asset Protection Vehicle – the Passport Trust™

Clients that come into our office looking for asset protection in the form of a domestic asset protection trust ("DAPT") often ask us what additional protections an offshore trust could offer them. Some of those additional protections include a shorter statute of limitations for creditors to attack assets after the assets have been transferred in to the trust, a higher standard of proof that creditors must meet to undo a transfer into an offshore trust, and the fact that the creditor must go to the foreign jurisdiction to pursue their claims and bring an entirely new cause of action. After reviewing these benefits, many clients are anxious to set up an offshore trust, but that excitement wants considerably when we discuss the high set up costs and maintenance fees, the formalities and complexities that must be adhered to in order to enjoy those extra protections, and the need for an offshore trustee.

To obtain the additional protections for our clients, but reduce the upfront costs and eliminate the need for the appointment of an immediate offshore trustee and the more stringent formalities of an offshore trust, JEFFREY BURR, LTD. has created the Passport Trust™. The Passport Trust™ is an asset protection vehicle that combines the flexibility and simplicity of a DAPT with the advantages of an offshore jurisdiction's additional protections against creditors, if the need arises.

A Passport Trust™ includes "passport" provisions in the trust agreement that enable a DAPT to be redomiciled in a foreign non-US jurisdiction such as the Cook Islands if there is ever a distress event. Typically, there will be no new waiting period for creditor claims in the offshore jurisdiction – the original transfer date of assets into the DAPT will also be used as the transfer date for purposes of the Cook Island's rules regarding creditor claims.

Passport Trusts™ lower the entry cost to obtain the additional protections an offshore jurisdiction can provide by allowing clients to begin with a DAPT and 'start the clock' on the state and offshore waiting period for protection from creditor claims and later convert to an offshore trust, if necessary, for the best of both worlds.

The Passport Trust™ begins as a DAPT with all the protections that Nevada's self-settled spendthrift law provides, but includes a special passport provision that enables the Trustee to move the trust's domicile to a foreign jurisdiction. In conjunction with this passport provision, application will be made to a foreign trust company (SouthPAC) upon the creation of the DAPT

to pre-approve the DAPT for redomiciliation. The foreign trust company shares in the due diligence regarding the creation of the trust. As a result of their early involvement, the foreign trust company agrees to serve as a special trustee, dormant and waiting with 'open arms' to receive the trust assets if a distress event occurs. If a distress event does not occur, clients enjoy the flexibility and simplicity of a DAPT with the comfort of knowing that their assets are protected in the event of a lawsuit or other misfortune, and will pass that protection on to their children.

Advantages of Beginning with a DAPT

There are other advantages to starting out with a DAPT in Nevada. They are as follows:

1. Greater Flexibility. The Spendthrift Trust Act of Nevada statute (the "Act") is very flexibly constructed to allow the Settlor the following powers:
    a. The Act allows the Settlor to be an Investment Trustee of the Trust. This is true even if the Settlor is a nonresident of Nevada.
    b. In all cases where the Settlor is also a trustee, the Act requires that another person or entity have discretion over the right to make distributions to or for the benefit of the Settlor. This person or entity is often referred to as a "Distribution Trustee" or "Administrative Trustee." The Settlor has the first right to select who the Distribution Trustee will be. Thereafter, a Trust Advisor can remove and replace the Distribution Trustee. The Settlor, however, can make all decisions regarding the investments of the Trust and can even make distributions to other beneficiaries of the Trust.
    c. If the Settlor chooses to not serve as the investment trustee, the Act gives the Settlor a veto power to veto any proposed distribution by the Trustee of the Trust. So if for jurisdictional reasons or otherwise a Settlor doesn't serve as Trustee, the Settlor still has power over proposed distributions by the Trustee.
    d. An alternative to the Settlor serving as Investment Trustee is to have a Nevada resident or Trust Company serve as Trustee and have the Trust form a Nevada LLC with the Settlor as the Manager of the LLC. This allows the Settlor to manage the assets of the Trust.
    e. The Settlor retains a lifetime and testamentary power of appointment to direct the disposition of Trust property during the Settlor's lifetime or at the Settlor's death. Because the DAPT is irrevocable, it cannot be amended by the Settlor. However, the Settlor can, in effect, amend or change the dispositive provisions of the Trust through the exercise of his or her power of appointment. Of course, the Settlor's power to appoint excludes the power to appoint to the Settlor, the Settlor's creditors, the Settlor's estate and creditors of the estate.
    f. The Trust Advisor will have the power to make administrative changes to the Trust to cause the Trust to be current and relevant in the event of new statutory changes or due to judicial decisions.
    g. The Trust Advisor can also be given the power to add or remove beneficiaries from the Trust.
    h. Most DAPTs are drafted to cause the Trust to be a grantor trust for income tax purposes. This causes all income and deductions to be reported on the Settlor's

income tax return and alleviates the need to file a separate tax return for the DAPT.

i. In effect, except for a need to have a separate Nevada Distribution Trustee, the DAPT is substantially similar to a revocable living trust in terms of flexibility but provides additional protection from creditors that a revocable trust does not provide.

2. Full faith and credit should be given to a DAPT by sister states. Upon occurrence of a distress event, the DAPT Trust Advisor will have the option of defending the DAPT in state court or can move the jurisdiction to the Cook Islands. By having an option, the Trust Advisor can consider all relevant facts and circumstances. If the Trust one is trying to protect is not drafted pursuant to a self-settled spendthrift trust statute, the only option is to seek to move the jurisdiction offshore.

Moving the Trust to an offshore jurisdiction may be an easy decision when the Trust has mainly cash, bonds and marketable securities, but what if the Trust owns real estate? It is commonly agreed that ownership of real estate in an asset protection trust, even if the real estate is in an LLC is problematic. If an action is brought in a non-DAPT state where real estate is located then the court may seek to exercise *in rem* jurisdiction over the real estate. Plus, the Trust owning real estate or business assets in a non-DAPT state may cause the Trust, and all its other assets, to be subjected to the jurisdiction of that state.

The solution is to form two separate Trusts. One Trust will hold moveables such as cash, stocks and marketable securities, and the other Trust will own real estate and vulnerable business assets.

The moveables Trust can be easily redomiciled to the Cook Islands and receive additional protection if necessary.

All is not lost, however, for the real estate/business Trust if the facts are right and relevant formalities are met, there is still a fighting chance that the Trust will be held valid under the Full Faith and Credit Clause. If these assets are held in a non-DAPT Trust then no such argument can be made. Even if the real estate/business DAPT is vulnerable, the creditor still has to jump through a lot of extra hoops to reach the Trust assets. This could result in a favorable settlement with the Trust and/or Settlor.

It may be argued that a settlor is better off with a DAPT than an offshore right away, as settlors could be held in contempt of court for failing to pay a judgment from an offshore trust.[26] It is better to have a DAPT come up in a California court, where courts are bound by the Full Faith & Credit Clause of the United States Constitution to honor Nevada's laws. States have no

[26] *FTC v. Affordable Media, LLC*, 179 F.3d 1228 (9th Cir. 1999) (Debtor jailed for refusing to repatriate assets); *U.S. v Plath*, 2003 WL 23138778 (U.S. Dist. Ct., So. Dist. Fla. 2003) (Debtor held in contempt for refusing to obey court order to disclose details about offshore accounts despite the fact that there was no fraudulent transfer); see also *Eulich v. U.S.*, 2004 WL 1844821 (U.S. Dist. Ct., N.D. Tex. 2004) (Debtor found in contempt, threatened with fines and jail time until assets repatriated); *SEC v. Solow*, 682 F.Supp.2d 1312 (2010) (Debtor jailed for contempt of court for refusing to repatriate assets).

obligation to honor the law of foreign jurisdictions, just as foreign jurisdictions have no obligation to honor judgments from a US court.

3. The Passport Trust™ Offers These Benefits:

> The Passport Trust appears to have a great degree of flexibility and an easy and quick path to redomiciliation to an offshore jurisdiction if necessary. A Passport Trust™ begins as a DAPT and does not require approval as a foreign trust in order to have the special offshore trust to pre-qualify the Trust and allow the holding period of the Trust to also meet the holding period of the offshore jurisdiction.
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> In addition, it is our opinion that because the Passport Trust™ is statutorily authorized as an asset protection vehicle, a court is less likely to find a Settlor of a DAPT in contempt as a result of the removal of the asset to an offshore jurisdiction than it would a settlor of a foreign trust. The Nevada statute, for example, specifically allows for the Trustee of a DAPT to transfer the assets of the DAPT into another irrevocable trust and allows the Transferee Trust to use the holding period of the Transferor Trust for purposes of creditor claims.

The Passport Trust™ is the preeminent asset protection vehicle as it combines the simplicity and flexibility of a DAPT with the ultimate strength and protections afforded by an offshore jurisdiction, providing clients with ease of mind that their assets will be preserved and protected under both domestic and foreign asset protection laws.