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Insights

Indiana's New Legacy Trust: An Asset Protection Strategy for Hoosiers

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Indiana embarks on a bold, new planning strategy on July 1, 2019. As of that date, individuals will be able to avail themselves of "Legacy Trusts" as an additional method by which they can lawfully protect assets against creditors. Indiana residents have long been able to make gifts during life or at death to or for the benefit of *other* individuals (spouses, children, grandchildren, etc.) and have those assets protected from creditors. Currently, Indiana residents avail themselves of such protection by structuring the gift or bequest so that he property passes to an entirely discretionary spendthrift trust for the benefit of the individual. Under current law, however, an individual cannot create and fund a trust with himself or herself as a beneficiary, include spendthrift protections in the trust document, and protect the trust assets from the individual's own creditors. This changes with the new "Legacy Trust" law bringing this ability to individuals wanting to protect assets for themselves.

Indiana's Trust Code will now permit "Indiana Legacy Trusts" under a new chapter in the Trust Code, Ind. Code § 30-4-8 (effective as of July 1, 2019). This new chapter of Indiana law will allow an individual (as settlor of a newly-created, irrevocable trust, or the holder of a general power of appointment) to transfer assets to a "qualified trustee" in the form of a "qualified disposition" and have those assets available for the benefit of that settlor yet still protected from creditors of that settlor. If structured correctly, the Legacy Trust will allow the settlor, as a beneficiary, to enjoy non-mandatory right to receive income or principal distributions from the Legacy Trust under the discretion of an independent trustee, who is given the discretion to make distributions to or for the benefit of the settlor as the beneficiary.

It is important to remember Indiana's Uniform Fraudulent Transfer Act (the "UFTA," Ind. Code § 32-18-2) in structuring a Legacy Trust. Any "qualified disposition" to a Legacy Trust could be subjected to attack by any creditor of that settlor/beneficiary (and now referred to as a "debtor" as well), in an action brought to void the transfer and reach the transferred assets under the UFTA. The UFTA is directly impacted by the Legacy Trust law, however, resulting in changes to the level of proof required by creditors and the time limitations for such actions, both of which, arguably, favor the settlor/beneficiary/debtor. The important language of when the UFTA applies to a Legacy Trust can be re-stated and summarized as a transfer made by a settlor/beneficiary/debtor with actual intent to hinder, delay, or defraud a creditor, or the transfer by gift at a time when the settlor/beneficiary/debtor was engaged or was about to engage in a transaction for which the remaining assets were unreasonably small in relation to the transaction or at a time when there was intent or reasonable belief of intent to incur debts beyond the ability to pay. (*See*, Ind. Code § 32-18-2-14). Other than transactions subject to the UFTA, however, the only other debts or obligations that could be enforced against a Legacy Trust would be child support obligations or obligations incurred in divorce (if the asset transfer occurs after marriage or within 30 days of marriage).

The formalities of the Legacy Trust head off most of the arguments a creditor may have under the UFTA. Before making a "qualified disposition," the settlor/beneficiary/debtor will have to execute a "qualified affidavit." This affidavit is sworn under penalties of perjury that the settlor/beneficiary/debtor (now a "transferor") has full right, title, and authority to transfer the property to the trust, that the transfer will not render the transferor insolvent, that the transferor does not intend to defraud a creditor, that there are no pending or threatened court or administrative actions against the transferor (except as disclosed in the affidavit), that the transferor does not contemplate filing bankruptcy, and that the property transferred is not derived from unlawful activities. In essence, if the transferor is not willing or able to sign such an affidavit then the use of the Legacy Trust is a "non-starter." On the other hand, the ability to do so should give adequate assurance that the trust will work to protect assets.

The formalities of the Legacy Trust also carry one, additional requirement that will give some individuals pause. The Legacy Trust must have at least one "qualified trustee." That trustee cannot be the settlor/beneficiary/debtor/transferor and must be an individual who is a resident of Indiana or an institution authorized by Indiana law to act as a trustee. Further, the qualified trustee must maintain or arrange for providing custody of the trust property in Indiana, maintain complete and accurate records for the trust, prepare or arrange for the preparation of all required tax returns for the trust, and materially participate in the administration of the trust. Again, that required involvement of a third party may not sit well. This is mitigated by the law allowing the settlor/beneficiary/debtor/transferor to stay involved as an investment adviser, maintaining veto power over distributions, allowing for limited powers of appointment to maintain some control to alter the final disposition of the trust assets, and the ability to appoint trust directors who can remove and appoint qualified trustees or other trust directors or direct, consent to, or disapprove distributions from the trust.

With the Legacy Trust statute, Indiana joins approximately seventeen other states that have similar laws pertaining to "domestic asset protection trusts" of some form or another. Other jurisdictions still carry some advantages over Indiana (such as a lack of state-level income tax and the ability for such trusts to continue in perpetuity). Regardless, Indiana's new law of Legacy Trusts allows Hoosiers, and others, to bring their assets "back home again" to Indiana and have those assets protected against future or unknown creditors.