The

Estate Analyst®

May, 2006

Dynastic Trusts Today

An Interview With Steven J. Oshins

By Robert L. Moshman, Esq.

The greatest potential for the accumulation of private wealth involves multi-generational planning in the form of a dynasty trust. When protected by a trust, assets avoid being diminished when they pass from one generation to the next.

Trust assets avoid the liabilities and divorces that affect individual beneficiaries. Trust assets avoid the transfer tax hits that occur at each generation. Trust assets remain intact and focused on long-term objectives instead of being dissipated. But our common law has a historic aversion to tying up assets and imposes the rule against perpetuities.

A modern trend that has abolished or relaxed the rule against perpetuities in many states has opened the door to long-term dynasty trusts. We took this opportunity of revisiting the dynasty trust to call on one of the rising stars in the field of estate planning, attorney Steven J. Oshins.

21st Century Perpetuities

The rule against perpetuities dates from the Duke of Norfolk's case of 1682, but the rule with which every law student is indoctrinated is from Professor John Chipman Gray's classic 1942 synopsis of the common law:

> "No interest is good unless it must vest, if at all, not later than twenty-one years after some life in being at the creation of the interest."

"The Rule has been described as a 'reign of terror,' a 'technicality-ridden legal nightmare' and a 'labyrinth.'"[1] In fact, the California Supreme Court famously excused an attorney who drafted a will that ran afoul of perpetuities; even a lawyer cannot be expected to foresee every potential scenario when applying so complex a rule.

The Rule is intended to protect the free alienability of property by putting a limit on how long it can be tied up in trust. While free alienability of property may still be a worthy social purpose, the onerous application of the Rule led Professor W. Barton Leach to propose reforms in 1953, two of which have caught on.

The "wait-and-see approach" avoids invalidating interests on the basis of events which might have occurred but did not. In other words, a trust won't be invalid based on the remote potential for some unlikely fact pattern when it is possible to just wait and see if the interest vests during the required time or 90 years. This approach was included in the Restatement of the Law of Property (Second) in 1983 and the Uniform Statutory Rule Against Perpetuities of 1986 (USR) which was adopted in 27 jurisdictions.[2]

The "reformation" or "cy pres" doctrine is another reform of the Rule. The court can modify an interest that fails under the Rule so that the essential purpose of the testator or settlor can be fulfilled. Several states have adopted their own statutory wait-and-see laws and/or reformation laws. A few states have court precedents adopting the reformation approach.

Since 1986, a growing number of jurisdictions have expanded the rule to specific long-term durations, such as 360 years in Florida, or 1,000 years in Utah and Wyoming. Six other states have abolished the rule against perpetuities to various extents. *(See chart.)* Only a handful of states still apply the original common law rule against perpetuities.

STATES LIMITING OR ABOLISHING THE RULE AGAINST PERPETUITIES

Alaska	Rule abolished entirely
Arizona	Testator may opt out and create perpetual trust
Colorado	Testator may opt out and create perpetual trust
Delaware	Abolished for personalty; 110 years realty
Dist. Col.	Allows perpetual trusts
Florida	Allows trust to last 360 years
Idaho	Rule abolished for personal property
Illinois	Testator may opt out and create perpetual trust
Maine	Testator may opt out and create perpetual trust
Maryland	Testator may opt out and create perpetual trust
Missouri	Testator may opt out and create perpetual trust
Nebraska	Testator may opt out if trustee can alienate property
Nevada	Allows trusts to last 365 years
New Hampshire	Testator may opt out if trustee can alienate property
New Jersey	Rule abolished entirely
Ohio	Testator may opt out and create perpetual trust
Rhode Island	Rule abolished entirely
South Dakota	Rule abolished entirely
Utah	Allows trust to last 1,000 years
Virginia	Testator may opt out for personalty
Wisconsin	Rule abolished entirely
Washington	Allows trust to last 150 years
Wyoming	Allows trust to last 1,000 years

—***Sources:*** *Schneider, Frederick R., "A Rule against Perpetuities for the Twenty-First Century" (March 2006); Fox, Charles, "Asset Protection and Dynasty Trusts," Real Property, Probate, and Trust Journal, (Summer, 2002).*

Dynastic Trusts

With a growing number of jurisdictions breaking away from the rule against perpetuities, there is the potential to draft dynasty-styled trusts for many clients, i.e., trusts that are designed to last for many generations, anticipate for varied needs, continue accumulating wealth, and provide asset protection long into the future. Note: Long -term plans may also run afoul of a rule against accumulations.[3]

In his home state of Nevada, attorney Steven J. Oshins recently convinced the State Legislature to adopt a law extending the rule against perpetuities to permit a 365-year trust. As a result, Nevada has moved to the forefront of states with favorable tax rules for dynasty trusts.

Having become closely associated with dynasty trusts, and having worked on Nevada's new law, we thought Mr. Oshins could provide some first-hand insights. Fortunately, he was extremely accommodating and accessible, for which we are most grateful.

Interview With Steven J. Oshins

Q: The 365 number for the 365-year dynasty trust reminds one of the number of days in a year. Was there any other significance to that length of time as opposed to, say, 200 years?

A: During the late 1990s I worked on a legislative bill to change the Nevada constitution to allow perpetual trusts. It takes five years to change the constitution because it must go through two legislative sessions and a vote of the people. Unfortunately, although the bill passed through the legislature unanimously two legislative sessions in a row, when it went to a vote of the people in March of 2002, it lost by about a 40% to 60% vote. Rather than again trying to change the Nevada constitution, I wrote a bill in the 2005 legislative session to create a 1000-year term for Nevada trusts.

A few of the legislators opposed the suggested change, and it was passed at only 150 years, which was unacceptable to me since it would not attract out-of-state business. The Senator with whom I was working added the language of our bill to another bill in the same session, and our lobbyist was able to negotiate the term to 365 years. The 365 number was simply a round number just greater than Florida's 360-year statute.

Q: How does the new law in Nevada affect existing dynasty trusts?

A: The new law took effect for any trust under Nevada law that became irrevocable on or after October 1, 2005. Prior trusts cannot take advantage of the new law, and any attempted exercise of a power to extend it would almost certainly violate the Delaware Tax Trap which would trigger a gift or estate tax the moment the attempted extension occurred.

Q: Given the prevalence of divorce, are dynasty trusts safe? Are there any specialized techniques that address divorce in a modern dynasty trust?

A: In order to protect the assets from divorce, the trust should be drafted as a discretionary trust with an independent distribution trustee rather than drafting it as a support trust. Typically, trusts are drafted as support trusts, which are trusts that have some form of support standard for distributions to beneficiaries. The most common example is one with the language, "health, education, maintenance and support."

The problem with using a support standard is that it creates a property right in the hands of the beneficiaries, which can open the trust to a beneficiary's divorcing spouse and other creditors. It is protected from most creditors, however, as long as the trust has a spendthrift provision.

Rather than drafting it as a support trust, the trust should be drafted as a fully discretionary trust with an independent trustee having absolute discretion over distributions. Because the trust is fully discretionary with respect to distributions, no creditor can access it. The primary beneficiary can serve as co-trustee and have all powers to make investments. With divorces being so prevalent in today's world, the fully discretionary trust should be the choice of nearly every client who is given the option.

Q: What level of residency is typically required in the dynasty-friendly states? Must you physically move to these states?

A: You must have at least one trustee in that state who has sufficient powers to give the trust minimum contacts with that state. When I draft a Nevada dynasty trust for my out-of-state clients, I will often add a third trustee to the trust that is generally a Nevada-based bank or trust company. For those clients who wish to give the primary beneficiary control over the trust, this third trustee is given very minimal powers, but enough to obtain Nevada jurisdiction.

Q: A long-term trust may experience dramatic changes. Suppose Nevada has a population boom and, 100 years from now, runs dry of water and money. Instead of being the tax haven it is today, suppose the Nevada of 2106 is toxic with taxes. Can a dynasty trust go mobile?

A: The dynasty trust should be drafted with a provision allowing the trustees to move the trust to another jurisdiction. Since we cannot accurately predict the future, the dynasty trust should be drafted with as much flexibility for change as can be given under the tax laws.

For example, we can give the primary beneficiary the power to amend the trust in nearly any manner upon the beneficiary's death, and we can give a non-beneficiary trustee the power to amend the document during the beneficiary's life.

Q: You have handled estates of $100 million. Tell me everything—what is that like?

A: We have more than a hundred clients with net worths above $100 million, as well as a few billionaires, so I am so used to planning those sized estates. I enjoy planning those sized estates more than more typical estates because there is so much more I can do for them. I can generally save their children tens of millions of dollars, and I enjoy knowing that I have done so much for their families.

Q: How small a dynasty trust truly makes sense? Is there a benefit at the $2-million or $4-million level or do things start to work better at the $10-million or $25-million level?

A: The question really comes down to how much property is worth protecting for the cost of an additional annual income tax return. Even a $1-million estate should be passed in a dynasty trust. From a creditor and divorce protection standpoint, it would be silly to create a trust that requires the million dollars to be distributed. What if a beneficiary gets sued or divorced? In other words, notwithstanding whether there is an estate tax issue, purely for creditor and divorce protection reasons, all gifts and bequests should be made in trust.

As your question would indicate, nearly every law firm that has attorneys who draft dynasty trusts does so only for the very wealthy. The attorneys at my firm draft dynasty trusts as a matter of course, not just for those with very large estates. This philosophy is used because almost every client should have a dynasty trust. We create approximately 20 dynasty trusts per month, which is a lot for a law firm with five attorneys. We will be adding two more attorneys in August and September, respectively, and I anticipate that we will be drafting 25 to 30 dynasty trusts per month within the next year.

Q: You have written some extremely sophisticated estate-planning articles over the past several years. Which one took the most time ..and which one was your favorite?

A: I have two favorites, both of which took quite a lot of time because of the length and amount of detail. In 1998, my father and I co-authored a two-part article in *Trusts & Estates* magazine called "Protecting & Preserving Wealth into the Next Millennium." To this day, that article still serves as the bible on beneficiary-controlled trusts and sophisticated wealth-shifting techniques. The other article that stands out was a three-part article I co-authored with attorney Mark Merric in 2004 in *Estate Planning* magazine called "The Effect of the UTC on the Asset Protection of Spendthrift Trusts." Both of these favorite articles of mine can be read online at *www.oshins.com*.

Editor's Note: The latter article has everything you could ever want to know about drafting trusts for maximum creditor protection. It impacted our industry by raising a number of issues regarding the Uniform Trust Code that resulted in many state legislatures amending their statutes.

Q: Back to those $100-million estates...would any of them consider including this editor as an extra beneficiary? I am available for adoption.

A: Only if there are two available spots since I'm in line ahead of you.

Q: There may come a time when Congress and the Treasury recognize that a fair portion of the nation's assets is locked up in dynasty trusts, and that the tax collection system is no longer competitive. Is there a potential for a new Perpetuity Tax to be imposed to put the Treasury back in the game?

A: It is always possible, but there are really very few attorneys taking advantage of dynasty trusts and the leveraging techniques associated with them.

For every attorney who is using dynasty trusts, there are about a hundred who are not. Those attorneys are using single-generation trusts that cause the assets to be taxed every generation. I will never understand why anyone would ever draft a trust in this manner, but the fact is that this is what is generally being done. So Congress is much better off maintaining a high estate tax rate in order to collect revenue rather than trying to tax dynasty trusts differently than they are today.

Technical References

1. Schneider, Frederick R., *"A Rule Against Perpetuities for the Twenty-First Century"* (March 2006). A 75-page "working draft" of this paper is available online at SSRN: http://ssrn.com/ abstract+8879291.
2. Ibid, at p. 6, footnote 25.
3. Sitkoff, Robert H., *"The Lurking Rule Against Accumulations,"* postulates the impact of a lesser known rule against accumulations on what the author refers to as "the $100-billion perpetual trust industry. This lurking rule may currently apply in states that have already addressed the rule against perpetuities and therefore may require corrective legislation. See footnote 40 for citations to numerous articles on trends re perpetuity laws.