

ESTATE PLANNING

Update

NEWS FOR THE CLIENTS AND FRIENDS OF BASS, BERRY & SIMS PLC

Tennessee Passes Investment Services Act and Enhances Asset Protection

July 3, 2007

On July 1, 2007, the Tennessee Investment Services of Act of 2007 went into effect, and for the first time Tennessee will allow individuals to create trusts for their own benefit (commonly referred to as self-settled trusts) and have those assets protected from their creditors. Historically, if an individual created a trust for his own benefit, the assets of the trust were subject to the claims of his creditors. Under the new law, if the transferor and the trust meet certain requirements as prescribed by the Act, the assets transferred to a self-settled trust are not subject to the transferor's creditors, even though the trust is for the transferor's benefit. This change in the law provides an asset protection opportunity for individuals who are concerned about losing their assets to unforeseen creditors.

Under the Act, this self-settled, asset protection trust is referred to as an "Investment Services Trust" (IST). An IST must be irrevocable, which means that the trust cannot be amended or revoked by the transferor. In addition, the trustee of the IST must be either an individual residing in Tennessee or a corporate trustee who is authorized to conduct business in Tennessee. Although the transferor cannot serve as trustee himself, the transferor still has very broad discretion in choosing a trustee. For example, the transferor's spouse, child, friend or business partner could serve as trustee.

At least some portion of the assets of the IST must be administered in Tennessee. Also, upon creation of the IST, the transferor is required to provide an affidavit under oath that must provide that the transferor:

- Has full right, title and authority to transfer the assets to the IST;
- Will not be rendered insolvent by the transfer;
- Does not intend to defraud a creditor by transferring the assets to the IST;
- Does not have any pending or threatened court actions against the transferor, except for those identified in an attachment to the qualified affidavit;
- Is not involved in any administrative proceedings, except for those identified in an attachment to the qualified affidavit;
- Does not contemplate the filing for relief under the federal bankruptcy code; and
- Did not obtain the assets being transferred to the IST through unlawful activities.

The IST does not provide asset protection for assets transferred to it until four years after the transfer. At that time, the transferor's creditors are prevented from seizing the assets of the IST to satisfy claims against the transferor. In addition, the IST does not allow an individual to defraud creditors who are already known to him (a so-called fraudulent transfer).

Although the transferor must make an irrevocable transfer of the assets to the IST and although he cannot serve as trustee, he can retain the following powers:

- Direct the investment of the IST assets;
- Receive trust income;
- Request up to 5 percent of trust principal annually;
- Receive additional distributions of principal based upon the discretion of the trustee or another appointed advisor;
- Live in a home owned by the trust;
- Veto distributions to any other permissible beneficiary;
- Direct the distribution of the trust assets upon death to any one or more persons other than the transferor's creditors, estate or creditors of the transferor's estate; and
- Remove the trustee and other trust advisors and appoint their successors, provided they are not related or subordinate to the transferor.

The new legislation also extends the period for which any trust can exist from essentially 90 years to 360 years. This will permit an individual to place property in trust to ensure assets are available to benefit not only his or her children and grandchildren, but also future generations of descendants.

Creating an IST is not a simple or routine process, and it is not suited for everyone. Creating an IST requires adherence to a number of statutory and equitable constraints as well as a thorough understanding of gift, estate and income tax laws and creditor protection laws. An IST allows a transferor to protect assets from creditors while still retaining the ability to manage the assets and economically benefit from them. This is a great new enhancement to Tennessee's law on asset protection.

If you have any questions about the new law, please contact one of our estate planning attorneys, James C. Gooch, Michael D. Sontag and Blaine H. Smith, whose contact information is below:

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