



An Overview of *Battley v. Mortensen*: The End of Domestic Asset Protection Trusts?

By: Jennifer L. Moccia, J.D., LL.M.



In early 2011, a landmark federal bankruptcy case shed doubt on the asset protection powers of the previously lauded domestic asset protection trust (DAPT), alarming many attorneys and distressing certain of those trust-wielding clients. In a decision filed by the United States Bankruptcy Court for the District of Alaska on May 26, 2011, Judge MacDonald set aside Thomas Mortensen's transfer of real property to an Alaska asset protection trust as a fraudulent conveyance. *Battley v. Mortensen*, Adv. D.Alaska, No. A09-90036-DMD (2011). This case deviated from previous DAPT holdings because, not only was Mortensen deemed solvent at the time of the transfer, but Alaska's four-year statute of limitations for reaching the assets transferred to the DAPT had already run. This controversial ruling has sparked heated debates among estate planners on whether its outcome could invalidate thousands of trusts formerly thought to provide exceedingly reliable asset protection.

Following his costly divorce in 1998, Thomas Mortensen personally drafted the "Mortensen Seldovia Trust (An Alaska Asset Preservation Trust)" in February of 2005. Mortensen had admittedly "not recovered from the financial carnage" of his divorce, and created the trust to hold and protect his recreational real property located in Seldovia, Alaska, worth approximately \$60,000 at the time of the transfer. His mother also gave him \$100,000 "to transfer the property to trust because she wanted to preserve it for her grandchildren." In April of 2009, Mortensen became ill, accrued massive credit card debt and filed for Chapter 7 bankruptcy in August of the same year. He disclosed \$26,421 in assets on the itemized personal property list provided to the Court, but did not include his interest in the DAPT (although he revealed the existence of the trust).

Despite Alaska's four-year statute of limitations for reaching assets transferred to a DAPT, the Court applied federal law, which includes a ten-year statute of limitations from the date a bankruptcy petition is filed for setting aside a

fraudulent transfer if the transfer was made with "actual intent to hinder, delay, or defraud" a creditor. *See* Bankruptcy Code Section 548(e). Therefore, the remaining issue to be decided was whether Mortensen made the transfer to his trust with the actual intent required to set aside the transfer.

Since, by the terms of the DAPT, the purpose of its establishment was "to maximize the protection of the trust estate or estates from creditors' claims," the Court held that the transfer was made by Mortensen with the clear intent to hinder, delay or defraud his creditors. Although Alaska law also states that "a settlor's express intention to protect trust assets from a beneficiary's potential future creditors is not evidence of an intent to defraud," the ten-year statute of limitations under federal law was enacted in order to close this self-settled trust loophole, and the Court followed this legislative intent. In determining Mortensen's actual intent, the Court not only looked to the purpose provision within the trust, but also considered his continual steady decrease in income, mounting credit card debt, statements of financial strife after his divorce and his lost stock market investment of the \$100,000 from his mother (rather than using the funds to pay off his substantial credit card debt). Thus, the transfer to the DAPT was set aside and the recreational property was sold to satisfy his creditors.

Is this ruling the beginning of the end of DAPT planning, or was this merely an advisory, fact-specific ruling that provides additional clarity to the current DAPT rules? Lawyers are split as they speculate whether this outcome was a fluke or the new reality. Although the Court did not uphold Alaska's four-year statute of limitations to prevent Mortensen's transfer from being set aside, the four-year rule is still effective and powerful against claims for assets held by a DAPT. However, when Mortensen erred by filing for bankruptcy without consulting an attorney, he unknowingly exposed himself to the Bankruptcy Code and

An Overview of *Battley v. Mortensen*: The End of Domestic Asset Protection Trusts?

By: Jennifer L. Moccia, J.D., LL.M.

its ten-year “clawback” rule. Had he not filed, Mortensen would have remained protected by Alaska’s four-year rule. Despite the concern that this case signals the end of the utility of all DAPTs, many argue that Mortensen was simply a case of bad facts with an unsurprising result, given that the debtor elected to file for bankruptcy prior to the expiration of the ten-year statute of limitations, and openly admitted that the trust was created to protect his assets from creditors – the very intent that is required by federal law to set aside the transfer!

Ultimately, Mortensen was not a proper candidate for a DAPT since he had waning anticipated income, almost no net worth beyond the Alaska recreational property and escalating debt. While some contend that the sky is falling and landmines are erupting in the realm of DAPTs, this case provides clarity and guidelines for properly establishing an asset protection trust. Rather than contributing to uncertainty, the Court ultimately validated those DAPTs that were not established to defraud creditors, as well as those trusts established more than ten years prior to filing for bankruptcy, regardless of their purpose. In light of this holding, DAPTs remain an effective asset protection strategy when properly marketed, drafted and implemented.

About the Author:

Jennifer L. Moccia, an associate at Rack & Olansen, P.C., received her B.A. in Psychology and Business Management from the College of William and Mary, her J.D. from Regent University School of Law, and her LL.M. in Estate Planning from the University of Miami School of Law. She is a member of the Virginia State Bar, and was elected to the Board of Governors for the VSB-YLC. Jennifer is also a member of the HREPC, the American Bar Association Real Property, Trust and Estate Law Section and is an Accredited Veterans Affairs attorney.