

TENNESSEE ASSET PROTECTION TRUSTS (“APTs”)

Effective July 1, 2007, Tennessee enacted a law that allows a settlor to transfer assets to an irrevocable trust of which the settlor is a discretionary beneficiary, and have the assets protected from the settlor’s creditors after a four-year waiting period.

The statute sets forth very specific requirements that must be met in order to obtain the benefit of the statute, including:

- (1) the trustee must be a Tennessee resident or authorized by Tennessee law to act as a trustee and subject to supervision by the Tennessee Department of Financial Institutions, the FDIC, the Comptroller of the Currency, or the Office of Thrift Supervision;
- (2) at least some of the assets owned by the APT must be held in Tennessee;
- (3) the Tennessee trustee must materially participate in the administration of the APT; and
- (4) the settlor may not be the trustee.

Upon transferring assets to an APT, the settlor is required to sign an affidavit which states that the transfer to the trust will not render the transferor insolvent, that the transferor does not intend to defraud a creditor by transferring assets to the trust, and that he does not have any pending or threatened court actions against him other than those identified in the affidavit. The affidavit must also state that the settlor does not contemplate filing for bankruptcy.

An APT must be irrevocable. There are certain rights that the transferor is allowed to retain, including: (1) the power to veto a distribution from the trust; (2) a testamentary power to appoint the trust assets; (3) the right to receive income from the trust; (4) the right to receive payments from a charitable remainder trust; (5) the right to receive a fixed percentage of the trust assets each year; (6) the right to receive principal payments at the discretion of the trustee or another advisor; (7) the trustee’s right to remove and replace the trustee or other advisor; and (8) the right to live in real estate owned by a qualified personal residence trust.

If a creditor does not attempt to set aside the transfer to the trust within four years after the transfer to the trust, the creditor will be barred from attaching the property that was transferred to the APT. This four-year statute of limitations is consistent with the four-year statute of limitations currently set forth in the Uniform Fraudulent Transfer Act, TCA § 66-3-301, et. seq. A creditor will still be able to attach any property that is distributed from the APT to the settlor; however, creditors would not be able to attach the assets retained inside the APT.

A creditor is not allowed to sue the trustee of the APT or any advisor involved in the counseling, drafting, preparation, execution or funding of an APT.

The statute contains provisions which allow trusts that were previously established in other states to move to Tennessee and obtain the benefits of the statute as long as the trust complies with the requirements of the statute. This will facilitate the repatriation of numerous trusts established by Tennesseans with trustees located in other states.

Settlors should be aware of the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (“BAPA”) which may extend the 4 year waiting period to 10 years if the Settlor had intent to defraud creditors at the time of the establishment of the APT and then later declares bankruptcy.

It is not expected that APTs will provide income or transfer tax benefits to Tennessee residents. However, they can be utilized by certain nonresidents of Tennessee to reduce state income taxes. See, for example, PLR 200637025.