

**UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF ALASKA**

In re: Case No. A95-00200-DMD	)	
	)	Chapter 11
SANFORD WAYNE BROWN and	)	
CARROL A. BROWN,	)	
	)	
Debtors.	)	
_____	)	
	)	Bancap No. 95-3072
VICKEY HIGASHI,	)	Adversary No. A95-00200-002-DMD
	)	
Plaintiff,	)	
	)	
v.	)	
	)	
SANFORD WAYNE BROWN and	)	
CARROL A. BROWN,	)	
	)	
Defendants.	)	
_____	)	

MEMORANDUM DECISION

This is an action by a judgment creditor to determine the validity of certain trusts in which the debtors have an interest. This is a core proceeding in accordance with 28 U.S.C. § 157(b)(2)(B), (E) and (O). I find for the plaintiff.

Background

The defendant, S. Wayne Brown, is a certified public accountant and successful businessman. In late 1989 and 1990, he and his wife Carrol created a series of self-settled trusts. One of these trusts was called the "CAW Family Trust." This trust was formed in the United States and governed by American law. The defendants have acted as trustees of this trust and admit that its trust assets are property of their bankruptcy estate. Two other trusts were formed during this same time period. These trusts were named the "Leones Company" and "American International Retail." Each of these trusts expressly declares that it was executed in the country of Belize and is to be interpreted and construed under the laws of Belize, formerly known as British Honduras. They are common law  4 ABR 280 business trusts, also known as Massachusetts trusts. Both incorporate features found in corporations and trusts. Each trust document provided for the establishment of an irrevocable trust controlled by a trustee who could make discretionary distributions of trust property. The defendant S. Wayne Brown signed the trust documents through an attorney-in-fact in Belize. One Gregory McDonald was the "creator" of the trust. A trust certificate for 100 trust units was executed in favor of Mr. Brown for each trust. Trust certificates are similar to shares of stock. Mr. Brown, through his attorney-in-fact, immediately amended the trust certificates such that 50 were issued in his favor and 50 in favor of his wife in each trust. Immediately upon formation of the Leones Company, the defendants S. Wayne and Carrol A. Brown became the president and secretary, respectively, of FRCVCT of the trust.

The assets of the American International Retail trust are insignificant. That trust has an undocumented loan of about \$11,000 payable from a Washington manufacturing firm. The trust currently has about \$8,100 in cash and no other business assets. Mr. Brown initially placed \$25,000 in the trust.

The Leones Company trust has substantial assets. It owns a Merrill Lynch whole life insurance policy on defendant S. Wayne Brown with a net cash value as of July 31, 1995, of \$202,897.91. The policy was purchased for \$200,000 in October of 1990. The trust also owns a Merrill Lynch annuity with a cash value as of July 31, 1995, of \$148,831. The annuity was purchased for \$100,000 in October of 1990.

There has been no business activity in Belize by either American International Retail or the Leones Company. All communication between the Leones Company and Merrill Lynch has been done by Mr. Brown. The funds utilized to purchase the annuity and the life insurance policy came from Mr. Brown. None of the funds were ever placed in the hands of the trustee, George A. Griffith, nor have any of the trust assets ever been controlled by Mr. Griffith.

The defendants filed for chapter 11 relief on March 31, 1995, after the plaintiff had obtained a judgment against them and their business corporation, Nome Commercial Company, for approximately \$1.4 million. The judgment is on appeal to the Alaska Supreme Court. The defendants have submitted a joint chapter 11 plan for themselves and Nome Commercial

● **4 ABR 281** Company. The plan initially went to hearing on confirmation on January 23, 1996. The confirmation hearing has been continued pending resolution of this proceeding.

Analysis

11 U.S.C. § 541(c)(2) excludes transfers of the debtors' beneficial interest in a trust from the bankruptcy estate when a transfer restriction is enforceable under "applicable non-bankruptcy law." For example, the debtors' interest in a pension trust arising under the Employment Retirement Income Security Act of 1974 (ERISA), is exempt from the estate under applicable non-bankruptcy law. Patterson v. Shumate, 504 U.S. 753 (1992); In re Conner, 73 F.3d 258 (9th Cir. 1996).

The trusts at issue here are not governed by ERISA or any other federal law. Ordinarily, this court would turn to Alaska law to determine whether or not trust assets are included in the bankruptcy estate. In re Anderson, 2 A.B.R. 82 (Bankr. D. Alaska 1991); In re Daniel, 771 F.2d 1352, 1360 (9th Cir. 1985), cert. denied, 475 U.S. 1016 (1986); In re Kincaid, 917 F.2d 1162, 1166 (9th Cir. 1990). Although both the American International Retail and the Leones Company trust documents specifically provide that the instruments are governed by the laws of Belize, under Alaska conflict of law principles, it is inappropriate to apply the law of Belize to this controversy. The driving force behind this bankruptcy and the cause of the debtors' current financial problems is Vickey Higashi's tort judgment for \$1.4 million. Because this case is an outgrowth of that controversy, it should be governed by tort conflicts of law principles. In determining whether or not the trust assets are property of the estate, this court faces the same issues that would confront a state court in post-judgment execution proceedings concerning the trusts. As such, the application of tort conflict of law principles is clearly warranted.

Two tests have evolved over time to determine the proper choice of law in tort cases. The first is the "lex loci delicti" rule. Under this older rule, the law of the place of the wrong was uniformly applied to all tort cases. In later cases, however, the place of injury alone was not the controlling factor. Armstrong v. Armstrong, 441 P.2d 699, 701 (Alaska 1968). Alaska has now adopted a FRCVCT †second test, "the most significant relationship" test, for conflicts of law questions. It requires the court to consider:

- (a) the place where the injury occurred,
- (b) the place where the conduct causing the injury occurred,
- (c) the domicil[e], residence, nationality, place of incorporation and place of business of the parties, and
- (d) the place where the relationship, if any, between the parties is centered.

These contacts are to be evaluated according to their relative importance with respect to the particular issue.

Restatement (Second) of Conflict of Laws, § 145, as quoted in Ehredt v. DeHavilland Aircraft Co. of Canada, 705 P.2d 446, 453 (Alaska 1985)(footnotes omitted).

Applying this test to the current conflict, I conclude as follows: (1) the injury occurred in Nome, Alaska, entirely within the state; (2) the place where the conduct causing the injury occurred was in Nome, Alaska; (3) Vickey Higashi was a citizen of the state of Alaska at the time of the injury, and the Browns had an ownership interest in Nome Commercial Company, although they were residents of the state of Washington just prior to the tortious conduct; (4) the place where the relationship between the parties was centered was Alaska. Since the parties' most significant relationship is with Alaska, Alaska law should determine the outcome of this controversy.

There are other reasons for applying Alaska law in this case. The relevant policies of the forum state and the non-forum state are relevant factors in choosing the applicable rule of law. Restatement (Second) of Conflicts of Laws, § 6 (1971). The relevant policies of the state of Alaska will not be served by applying the laws of Belize. Alaska statutes specifically provide for the invalidation of fraudulent transfers, including transfers to trusts. A.S. 34.40.010 - 34.40.130. Belize, on the other hand, appears to actively encourage such transactions. It does not even have a fraudulent conveyance law. Rather, trusts in Belize are immune from attack from creditors even when created by fraudulent transfers. Moreover, the trusts can be self-settled. As noted by one author:

● **4 ABR 283** C. But Belize is Best.

The Cook Islands adopted at least some version of fraudulent conveyance law; Belize (the former British Honduras) did not even try.

In 1992, Belize adopted a new Trusts Act, a copy of which is appended to this paper. Section 7(6) is quite clear:

(6) Where a trust is created under the law of Belize, the court shall not vary it or set it aside or recognize the validity of any claim against the trust property pursuant to the law of another jurisdiction or the order of a court of another jurisdiction in respect of --

(a) the personal and proprietary consequences of marriage or the termination of marriage;

(b) succession rights (whether testate or intestate) including the fixed shares of spouses or relatives; or

(c) the claims of creditors in an insolvency.

(Emphasis added.)

Section 7(7) provides that the preceding Section 7(6) "shall have effect notwithstanding the provisions of section 149 of the Law of Property Act, section 42 of the Bankruptcy Act and the provisions of the Reciprocal Enforcement of Judgments Act."

Section 12 provides for the establishment of spendthrift trusts, and Section 12(4) specifically allows the settlor to establish a spendthrift trust with herself as beneficiary.

Thomas M. Mayer, Sheltering Assets in 1994: Real Estate Workouts and Bankruptcies 1994, Prac. L. Inst. 383, 446 (1994).

The policies underlying FRCVCT +ing the current law of Belize are diametrically opposed to the fundamentals of Alaskan and American fraudulent transfer law. Belize is a popular trust jurisdiction precisely because it allows the types of fraudulent transfers that are unenforceable in America.

Under these circumstances, application of the law of Belize to the case at bar would be inappropriate. Alaska is the state with the most significant relationship to the controversy. Fundamental policies of ● **4 ABR 284** Alaskan and American law will not be served by applying the laws of Belize. This case will be decided based on Alaskan and American law, not on the law of a foreign jurisdiction which actively solicits U.S. funds to insulate Americans from their creditors.

Alaska law prohibits fraudulent transfers. A.S. 34.40.010 provides that transfers made with the intent to hinder, delay or defraud creditors are void. A.S. 34.40.110 provides that transfers made in trust for the benefit of the person making the transfer are void against existing and subsequent creditors. I find the initial transfer to the Leones Company business trust to be fraudulent and void for several reasons.

The transfer of funds that created the Leones Company was made to hinder, delay or defraud future creditors. The fact that the trusts were established in Belize, a country notorious for its anti-creditor policies⁽¹⁾, rather than Alaska or Washington, indicates an intent to hinder, delay or defraud on the part of the defendants. Further, one of the express purposes for creation of the trust listed by the trustee was the protection of "assets from liability." However, the defendants' retention of control over the Merrill Lynch policies is the primary reason I find their transfers to the Leones Company trust fraudulent. Since the inception of the policies in 1990, Mr. Brown has retained complete control over trust assets. Neither Gregory McDonald, the "creator" of the trust or George Griffith, the trustee, has ever exercised any control over trust assets. They haven't even signed a trust document since the inception of the trust in 1989. The checks sent to Merrill Lynch originated with Mr. Brown and never passed through the hands of the supposed trustee. The Browns retain the ability, as trust officers, to instantly obtain all cash from the Merrill Lynch policies without interference from the trustee. I conclude that the Leones Company trust is simply a sham. The true substance and business of this trust is to avoid creditors and nothing more.

The Browns contend that establishment of the Leones Company trust was simply an estate planning device. If estate planning was the only ● **4 ABR 285** consideration, however, their needs could easily have been addressed through American wills or trusts. Mr. Brown is a shrewd businessman. As such he sought to shield his assets from exposure to creditors through use of friendly foreign jurisdiction. Dramshop liability, for instance, is a problem for Alaskan liquor store and bar owners. A.S. 04.21.020 allows only limited immunity to such owners. When minors are allowed to purchase liquor or when a "drunken" person is served, owners may be liable for the damages that result, which can be catastrophic. The Browns' principal business, Nome Commercial Company, is engaged in the sale of liquor. Although it had liability insurance in 1989, damages from a personal injury claim could exceed policy limits. I find that avoidance of such liability claims to future creditors was a major consideration in the establishment of the trust.

The transfer creating the Leones Company trust is also invalid because it violates the provisions of A.S. 34.40.110, which provides:

A deed of gift, a conveyance, or a transfer or assignment, oral or written, of goods and chattels or things in action made in trust for the person making the deed, conveyance, transfer, or assignment is void as against the creditors, existing or subsequent, of the person.

The Browns' October 1990 transfer of funds to Merrill Lynch Pierce Fenner & Smith to create an annuity and life insurance policy for the Leones Company is void against Vickey Higashi, a subsequent creditor.

Statute of Limitations and Other Defenses

The Leones Trust was created in January of 1989. Transfers for the benefit of the Leones trust were made to Merrill Lynch Life Insurance Company on October 5, 1990. The Browns have failed to produce copies of checks

that would detail the precise dates and amounts of payments. Alaska does not have a specific statute of limitations for fraudulent transfers. This court adopts the holding of Judge Ross in In re Ferrara (Barstow v. Ferrara, et. al.), 3 ABR 472, 491 (Bankr. D. Alaska 1994), which followed the March 12, 1992, ruling of District Judge Singleton in Battley v. Stanton, Case No. A91-0161-Civil. The six-year period contained in AS 09.10.050 is the applicable limitation period for a fraudulent transfer action. In this instance, the limitation period for ● **4 ABR 286** setting aside the fraudulent transfers commenced upon rendition of the state court judgment on February 10, 1995. Austin v. Fulton Insurance Company, 444 P.2d 536, 539 (Alaska 1968); 37 Am Jur 2d Fraudulent Conveyance § 196 (1968). This action was filed July 19, 1995, well within the limitation period. The statute of limitations provides no defense to the Browns.

The Browns allege that Vicky Higashi has no standing to file a complaint regarding the trusts because she will be paid in full under the plan and the trusts are an "abstract issue." I disagree. The Browns seek to cramdown a \$1.4 million tort claim. The plan must be proposed in good faith and be fair and equitable with respect to Vicky Higashi's claim. 11 U.S.C. § 1129(a)(3) and § 1129(b)(1). Determination of the validity of the trusts is a key issue in deciding whether the case meets the confirmation requirements of the Code. It would be very unfair and inequitable, for example, for the Browns to retain all liquid assets while forcing Ms. Higashi to accept non-liquid assets in satisfaction of her claim. If the liquid assets were held in a valid trust, their differentiation in treatment could be warranted. Determination of the validity of the trusts is a significant factor for evaluating the confirmability of the plan.

The Browns claim that Higashi's failure to join George A. Griffith, the supposed trustee of the Leones Company and the American International Retail trusts, warrants dismissal for failure to join an indispensable party. Again, I disagree. When the Browns have in fact dominated and controlled the trusts from their inception, Griffith is merely a figurehead. Higashi's failure to name him as a party is meaningless when he had no control over the trust assets at any time. The Browns are the real parties in interest and have been given proper notice of these proceedings.

American International Retail and CAW Family Trust

I find that the American International Retail trust was created by the Browns for the same reasons as the Leones Company. Its assets are property of the bankruptcy estate.

The CAW Family trust is not really at issue in these proceedings. The Browns concede that the assets of the trust are property of the ● **4 ABR 287** estate. The Browns' California rental home is also property of the estate, as it was never transferred to any trust.

Conclusion

The Belizean trusts established FRCVCTw^l and controlled by the Browns were created by fraudulent transfers. As such, the assets of these trusts are property of the bankruptcy estate. The assets of the CAW Family trust are also property of the estate, along with the Browns' California rental home. An order and judgment consistent with this decision will be entered.

DATED: March 11, 1996.

BY THE COURT
DONALD MacDonald IV
United States Bankruptcy Judge

1.  **4 ABR 284** The policies of Belize and other offshore jurisdictions are discussed at length by Elena Marty-Nelson, in Offshore Asset Protection Trusts: Having Your Cake and Eating It Too, 47 Rutgers L. Rev. 11 (1994).