South Dakota's Situs Advantages Over Illinois

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INTRODUCTION

South Dakota has emerged as the leading jurisdiction for modern trust planning in the United States, setting the gold standard in legal innovation, asset protection, and fiscal stability. This white paper explores the unique advantages of South Dakota's trust laws—most notably, its early abolition of the Rule Against Perpetuities (RAP), comprehensive privacy protections, and cutting-edge statutory mechanisms such as directed trusts, trust protectors, and decanting. These legislative advancements have established South Dakota as the premier location for perpetual and multigenerational trusts.

In contrast, Illinois remains mired in outdated statutes and slow legislative reform. Its delayed response in abolishing the RAP, limited creditor protection, lack of support for directed and quiet trusts, and overall fiscal instability render it a significantly less attractive jurisdiction for individuals and families seeking efficient and flexible trust planning. This paper provides a detailed comparative analysis, highlighting the statutory, financial, and administrative advantages that position South Dakota far ahead of Illinois in trust law and practice.

PERPETUAL TRUSTS

South Dakota stands at the forefront of trust situs jurisdictions, setting the benchmark for trust law reform in the United States. In 1983, South Dakota became the pioneering state to abolish the Rule Against Perpetuities (RAP), a bold move that opened the door for the creation of dynasty trusts capable of lasting in perpetuity. By eliminating the time limits imposed by the RAP, South Dakota offers unparalleled estate planning opportunities, allowing families to preserve and transfer wealth across generations, free from the traditional restrictions that exist in other states. The statutory provision enabling this, SDCL § 43-5-8, has empowered South Dakota as a premier destination for perpetual trusts, securing its dominance in the field.

Illinois has been slower to modernize its trust laws, particularly regarding the Rule Against Perpetuities (RAP). Illinois did not abolish the RAP until much later than other

states, limiting the ability to establish dynasty trusts that can last indefinitely. The delay in recognizing the benefits of perpetual trusts has placed Illinois at a significant disadvantage. The state's hesitation to abolish the RAP earlier means it missed the opportunity to attract long-term, multi-generational trusts that could have provided significant economic benefits. [765 ILCS 305/4]

Not only did South Dakota lead in abolishing the RAP, but it also spearheaded further innovation with the adoption of the Trust Protector statute in 1997. This statute, codified in SDCL § 55-1B-6, revolutionized trust management by introducing a mechanism to ensure flexibility for future generations. A Trust Protector can be vested with broad powers, including the ability to amend trust terms, remove and replace trustees, and resolve disputes, all while preserving the original intent of the grantor. This foresight allows trusts to remain adaptable in the face of changing circumstances, ensuring their resilience over time.

Illinois was also late to adopt a Trust Protector statute, which allows for greater flexibility and oversight of trust management. While some states implemented this statute as early as the 1990s, Illinois did not enact comprehensive Trust Protector provisions until much later. This lack of early adoption has hindered the ability of trustees and beneficiaries to adapt trusts to changing circumstances over generations. The absence of a timely Trust Protector statute highlights Illinois' reluctance to embrace modern trust innovations, limiting the state's appeal for sophisticated estate planning. [760 ILCS 5/16.3]

STRENGTH OF STATE

On the basis of its solvency in five separate categories, South Dakota ranks second among U.S. states for fiscal health. South Dakota has between 4.76 and 6.78 times the cash needed to cover short-term obligations, well above the U.S. average. Revenues exceed expenses by 2 percent, with an improving net position of $106 per capita. In the long run, South Dakota has a net asset ratio of 0.34. Long-term liabilities are lower than the national average, at 8 percent of total assets, or $650 per capita. Total unfunded pension liabilities that are guaranteed to be paid are $13.32 billion, or 32 percent of state personal income. [Mercatus Research, Mercatus Center at George Mason University, Arlington, VA]

Illinois has an alarmingly low cash ratio, with only 0.67 times the cash with a budget deficit around 7% annually. This chronic budget imbalance has resulted in a worsening net position of –$4,098 per capita, indicating that the state spends far more than it earns. The persistent budget deficits and increasing debt levels underscore Illinois' inability to manage financial resources effectively, further eroding confidence in Illinois as a stable financial environment for trusts. [Mercatus Research, Mercatus Center at George Mason University, Arlington, VA] Illinois faces staggering long-term liabilities, significantly higher than the national average. Long-term liabilities account for 53% of total assets, equating to $10,700 per capita. This high debt burden reflects a severe structural imbalance in the state's finances, the result of decades of financial mismanagement and unsustainable fiscal policies. The state's unfunded pension liabilities are among the highest in the nation, totaling $137 billion, or 29% of state personal income.

Illinois consistently ranks poorly among U.S. states for fiscal health, reflecting deep-rooted financial instability and mismanagement. These financial weaknesses significantly undermine Illinois' attractiveness as a jurisdiction for establishing trusts. In the long run, Illinois has a troubling net asset ratio of –0.43, indicating that liabilities far exceed assets. This negative ratio is a clear indicator of the state's financial distress and poor fiscal health, making it a less desirable jurisdiction for trusts and financial planning. A negative net asset ratio reflects the state's inability to cover its liabilities with its assets, pointing to severe financial instability.

STATE INCOME AND CAPITAL GAINS RATES

Since 1942, South Dakota has not imposed a state income tax, whether on individuals or corporations. This policy, integral to the state's financial framework, is embedded in a constitutional prohibition on the imposition of new taxes or the increase of existing taxes without specific voter or legislative authorization.

Article XI, Section 14 of the South Dakota Constitution expressly bars the creation or expansion of taxes unless there is a voter-approved initiative or the proposed measure secures a two-thirds supermajority vote in both the House and Senate of the South Dakota Legislature. This constitutional safeguard against tax increases reflects a long-standing commitment to maintaining a favorable tax environment, aimed at promoting economic growth, attracting businesses, and preserving individual wealth within the state. As a result, South Dakota has become a jurisdiction of choice for businesses and high-net-worth individuals seeking a tax-efficient domicile.

In contrast, Illinois presents a challenging environment for individuals and businesses due to its high state income and capital gains taxes. The state imposes a flat income tax rate of 4.95% on both individuals and corporations, significantly burdening residents and enterprises alike. This high tax rate can deter investment and economic growth, making Illinois a less attractive location for financial activities. [35 ILCS 5/201]

In addition to high taxes, Illinois faces severe fiscal challenges, often resorting to increasing tax rates to cover budget deficits. This trend creates an unpredictable financial environment, further discouraging long-term financial planning and investment. The state's heavy reliance on income and capital gains taxes, coupled with its fiscal instability, makes Illinois a less favorable jurisdiction for those seeking to optimize their financial strategies and maintain higher net returns.

The Illinois Constitution does not provide robust safeguards against new taxes or tax increases, allowing the state legislature significant leeway to impose additional financial burdens on residents and businesses. This lack of constitutional protection contributes to the state's reputation for high and potentially rising taxes, creating an environment of financial uncertainty.

Overall, Illinois' high state income and capital gains tax rates, combined with its fiscal instability and lack of constitutional protections against tax increases, make it a less attractive jurisdiction for trusts and investment compared to states with more favorable tax environments.

PRIVACY

Under South Dakota law, trust documents that would otherwise become part of the public record in judicial proceedings are subject to a permanent seal of privacy. Pursuant to South Dakota Codified Laws (SDCL) § 21-22-28, this privacy protection is automatically applied, ensuring that trust-related documents remain confidential indefinitely. Once the seal is in place, it persists in perpetuity, offering a unique and robust layer of privacy for settlors, beneficiaries, and trustees involved in trust matters.

This statutory framework serves as a significant advantage for individuals and families seeking to safeguard sensitive financial and personal information from public disclosure. Unlike other jurisdictions where court records related to trust proceedings may be accessible to the public, South Dakota's automatic and perpetual seal of privacy provides a high degree of protection. This feature has made South Dakota a preferred jurisdiction for the establishment and administration of trusts, particularly for those who prioritize confidentiality.

In Illinois, trust documents that become part of any judicial proceeding are not automatically sealed and can be accessed by the public. To achieve any level of privacy, parties involved must petition the court to seal the records, which is not guaranteed and must demonstrate good cause. This absence of automatic privacy places a considerable burden on trustees and beneficiaries who wish to keep their financial matters confidential. [760 ILCS 3/813]

The lack of automatic and perpetual privacy protections for trust documents in Illinois makes it a less attractive jurisdiction for establishing trusts. The state's approach requires proactive and often complex legal actions to maintain the confidentiality of trust-related information, thereby exposing sensitive data to potential public scrutiny unless specific court orders are obtained. This significant gap in privacy measures contrasts sharply with jurisdictions that offer more secure and automatic privacy guarantees, highlighting Illinois' inadequacy in this regard.

CREDITORS CLAIMS

If the settlor is foreseeably solvent, South Dakota trusts are shielded from new claims of creditors of the settlor after two years of a transfer to the trust. A window of six months from discovery of the transfer is provided for existing claims, if longer. For self-settled trusts (for the benefit of the settlor) that are "qualified dispositions," there are exceptions for debts of spousal/child support and the division of marital property existing before the transfer. For third-party trusts (not self-settled), there are no such exceptions. [SDCL § 55-1-44] [SDCL § 55-16-10; 16]

Illinois' statutes do not offer the concise and favorable lookback periods that are available in South Dakota. The lookback period in Illinois is four years, creating an extended window during which creditors can challenge transfers to trusts. This prolonged exposure increases the risk for individuals seeking to protect their assets from future creditors. Illinois law provides that creditors can reach trust assets if the transfer to the trust was made with the intent to defraud creditors. The burden of proving the intent can be a significant hurdle, making asset protection less reliable. [740 ILCS 160/5]

Illinois law is particularly unfavorable when it comes to self-settled trusts. In Illinois, assets transferred to a self-settled trust remain accessible to creditors of the settlor. This means that any trust established for the benefit of the settlor offers no protection from the settlor's creditors, negating the benefits of such trusts for asset protection. [735 ILCS 5/2-1402]

Illinois provides exceptions similar to South Dakota for debts related to spousal and child support, but the state's broader creditor-friendly stance makes it more difficult to shield assets effectively. This lack of comprehensive protection can be especially problematic for individuals with complex financial situations or significant personal liabilities.

ASSET PROTECTION

Illinois lacks the comprehensive statutory protections that South Dakota offers. In South Dakota, the law thoroughly addresses numerous arguments made in court cases and disputes, weaknesses caused by the Restatement of Trusts, inadvertent or ill-advised actions by trust settlors and beneficiaries, withholding mandatory distributions to beneficiaries, and vulnerable provisions and drafting errors in trust documents. This comprehensive approach significantly enhances asset protection in South Dakota. [SDCL § 55-1-25, 32, 33, 38, 39]

Illinois does not rank favorably in asset protection compared to South Dakota, which consistently scores high in national rankings for asset protection. South Dakota's top-tier status is supported by its detailed and robust statutory framework designed to protect trust assets comprehensively. In contrast, Illinois' asset protection capabilities are significantly weaker, reflecting its less comprehensive legal framework for trust asset protection.

QUIET TRUSTS

There are detailed provisions in the South Dakota statute for the trust settlor, trust instrument and trust advisors (i.e., trust protector) to restrict or eliminate information to trust beneficiaries and to keep the trust instrument and trust actions quiet. The South Dakota statute directly addresses the ability to restrict the right of a beneficiary to receive a copy of the trust instrument and the right of the settlor, trust protector or trust advisor to retain the power to change the beneficiaries' rights to trust information. [SDCL § 55-2-13]

In contrast, Illinois does not have comparable statutory provisions. Illinois law generally requires that beneficiaries be kept informed about the trust and their rights under it. This lack of flexibility in withholding information can undermine the privacy and confidentiality that some settlors desire. The inability to create truly quiet trusts in Illinois means that beneficiaries must be informed about the trust's existence and their entitlements, which can lead to potential conflicts and a lack of discretion.

Illinois' failure to provide statutory provisions for quiet trusts similar to those in South Dakota represents a considerable disadvantage for individuals seeking confidentiality in their trust arrangements. The state's legal framework mandates beneficiary transparency, limiting the ability to restrict information and maintain discretion. For those prioritizing privacy and control over trust information, Illinois' trust laws fall short, making it a less attractive jurisdiction compared to South Dakota's robust and flexible approach to quiet trusts.

SPECIAL PURPOSE ENTITIES

South Dakota is the only state providing express legislative support for Special Purpose Entities. The 2011 law specifically permits individuals to serve in trust roles (i.e., investment advisor, distribution advisor, trust protector) for a particular family through an entity (i.e., a limited liability company) for their liability protection without meeting formal Department of Banking regulations and requirements. This feature gives individuals more comfort in serving and taking on these trust advisor roles.

Illinois does not provide similar statutory support for SPEs in trust roles. The absence of explicit legislative recognition and protection for SPEs means that individuals serving as trust advisors in Illinois do not enjoy the same level of liability protection. This lack of statutory backing can expose advisors to greater legal and financial risks, making it less appealing for individuals to serve in these capacities within Illinois trusts.

Illinois' lack of express legislative support for Special Purpose Entities in trust roles significantly undermines its competitiveness as a jurisdiction for sophisticated estate planning. The state's failure to offer statutory liability protection and regulatory flexibility for SPEs places it at a clear disadvantage compared to South Dakota. For individuals and families seeking to establish trusts with innovative structures and enhanced advisor protection, Illinois' legal framework falls short, making it a less favorable option for trust administration and asset protection.

DIRECTED TRUSTS

In South Dakota, the directed trustee model is a predominant trust company structure, which significantly limits trustee fees while allowing trusted family advisors to control the distributions and investment decisions of trust assets. This model is highly efficient and cost-effective, providing clear advantages for trust administration. According to the South Dakota Department of Banking, approximately 68% of South Dakota trust business is conducted through a directed trustee out of a total of 1.7 million trust accounts.

In stark contrast, Illinois does not offer a similarly efficient directed trustee model. Illinois law is more restrictive and less accommodating to the directed trustee structure, resulting in higher costs and less flexibility in trust management. This lack of a comprehensive directed trustee framework in Illinois places a greater burden on trustees and can result in higher fees and less efficient trust administration.

Illinois' failure to adopt a robust directed trustee model, similar to that of South Dakota, significantly undermines its attractiveness as a jurisdiction for trust administration. The lack of statutory clarity, increased liability risks, and higher costs associated with trust management in Illinois make it a less favorable option for individuals seeking efficient and effective trust solutions. South Dakota's comprehensive and supportive legal framework for directed trustees highlights the deficiencies in Illinois' approach, underscoring the need for significant reforms to improve its competitiveness in the trust industry.

RELIABILITY

In re Cleopatra Cameron Gift Trust, 931 N.W.2d 244 (S.D. 2019), the South Dakota Supreme Court affirmed a circuit court's decision concluding that the validity of a trust's spendthrift provision prohibiting direct payments of a trust beneficiary's child support obligation to her ex-husband was indeed recognized by South Dakota law. The court effectively sided with the trustees who had stopped paying support claims to the ex-husband because those payments

had been mandated when the trust was previously sitused in Illinois. This case is widely accepted as one of the most favorable creditor protection cases in recent history.

South Dakota's legal framework strongly supports the enforceability of spendthrift provisions in trusts, providing trustees and beneficiaries with a high level of protection against creditor claims. This is critical for individuals seeking to protect their assets and ensure that trust distributions are managed according to their wishes, without interference from external claims.

Illinois, on the other hand, has a less favorable stance towards spendthrift trusts. The protections offered under Illinois law are not as comprehensive, leaving trust assets more vulnerable to creditor claims. This lack of robust protection can be particularly problematic for beneficiaries who need assurance that their trust assets will be safeguarded against external claims.

Illinois' failure to provide robust creditor protection and enforceable spendthrift provisions makes it a far less attractive jurisdiction for trust administration compared to South Dakota. The South Dakota Supreme Court's decision in In re Cleopatra Cameron Gift Trust highlights the significant advantages of South Dakota's legal framework in protecting trust assets from creditor claims. For individuals seeking to establish trusts with strong asset protection, South Dakota offers a clear legal advantage over Illinois. The deficiencies in Illinois' trust laws and judicial support underscore the need for substantial reforms to improve its competitiveness as a trust jurisdiction.

FORETHOUGHT

South Dakota updates its trust law statutes annually through its highly effective Governor's Task Force on Trust Administration Review and Reform, which is very responsive to the legal and advisor community. Examples of new trust laws in recent years in South Dakota include Community Property Trusts in 2016 (allowing nonresidents to get a full step-up in income tax basis of assets upon the death of one spouse), the 2016 Family Advisor (allowing for trusted family advisors to participate on the trust advisor team without taking

on the fiduciary responsibility) and 2006/2008 Purpose Trusts of unlimited duration (trusts for pets, vacation homes or any non-charitable purpose without a beneficiary). [SDCL § 55-17-5]

In stark contrast, Illinois does not have a comparable mechanism for regularly updating its trust laws. The absence of a dedicated task force means that Illinois' trust statutes are not reviewed or revised with the same frequency or foresight as those in South Dakota. This lack of proactive updates can result in outdated laws that do not meet the current needs of trustees, beneficiaries, or advisors.

Illinois' lack of proactive updates to its trust laws, the absence of Community Property Trusts, Family Advisor provisions, and Purpose Trusts of unlimited duration make it a far less competitive jurisdiction compared to South Dakota. South Dakota's innovative and regularly updated trust statutes provide significant advantages in terms of tax planning, flexibility, and modern trust management. For individuals seeking the most advantageous and forward-thinking trust environment, Illinois falls short, highlighting the need for substantial legal reforms to match the progressive approach seen in South Dakota.

DECANTING

South Dakota boasts the most flexible and highly ranked trust decanting statute in the nation. This statute allows for the expansion of an existing trust to a fully discretionary trust, providing the ability to distribute assets for any reason or purpose. Additionally, it permits the inclusion or exclusion of any beneficiaries, allowing both current and future beneficiaries to be changed. This flexibility offers significant opportunities for future planning concerning estate, gift, and income tax purposes for a family. [SDCL § 55-2-15]

Illinois lacks the flexibility offered by South Dakota's decanting statutes. Illinois' legal framework for trust decanting is much more restrictive, limiting the ability of trustees to modify trust terms to adapt to changing circumstances or to better serve the interests of the beneficiaries.

South Dakota's decanting statute allows for a broad range of modifications, enabling trustees to respond dynamically to the evolving needs of beneficiaries and changing financial circumstances. This includes the ability to convert a trust into a fully discretionary trust, which can be crucial for effective estate planning and asset management.

Illinois, however, imposes significant limitations on the decanting process. Trustees in Illinois have far less leeway to adjust the terms of a trust, which can hinder the trust's ability to meet the current and future needs of beneficiaries. This inflexibility can result in missed opportunities for tax planning and may prevent the trust from adapting to unforeseen changes in beneficiaries' circumstances.

One of the standout features of South Dakota's decanting statute is the ability to include or exclude beneficiaries, both current and future. This provides trustees with the crucial ability to respond to changes within the family structure or financial needs, ensuring that the trust remains relevant and effective over time.

Illinois' restrictive and outdated trust decanting statutes make it a far less attractive jurisdiction for modern trust management compared to South Dakota. The lack of flexibility in modifying trust terms, including the limited ability to adjust beneficiary designations and adapt to changing circumstances, significantly undermines the effectiveness of Illinois trusts. South Dakota's robust and flexible decanting statutes provide a clear legal advantage, ensuring that trusts can evolve to meet the needs of beneficiaries and optimize for tax planning. For those seeking the most adaptable and beneficial trust environment, Illinois falls short, highlighting the need for significant reforms to improve its competitiveness in trust administration.

PREMIUM TAX ON PRIVATE PLACEMENT LIFE INSURANCE

For trusts that purchase private placement life insurance, South Dakota has the lowest insurance premium tax at 8 bps (.008%) on premiums in excess of $100,000 for both policies held by the trust or in a limited liability company (LLC) owned by the trust. [SDCL § 10-44-2]

Illinois imposes much higher insurance premium taxes, making it a less favorable jurisdiction for trusts involving PPLI. The insurance premium tax rate in Illinois is significantly higher, which increases the overall cost of maintaining life insurance policies within trusts. This higher tax burden can erode the financial benefits of using life insurance in estate planning and wealth management strategies.

The low insurance premium tax in South Dakota provides substantial savings and makes it easier to structure trusts and LLCs efficiently. This financial advantage allows trustees and beneficiaries to allocate more resources towards the growth and protection of trust assets rather than towards taxes. Additionally, it enhances the attractiveness of South Dakota as a jurisdiction for private placement life insurance programs, which are often used by high-net-worth individuals for sophisticated estate planning.

Illinois, with its higher insurance premium taxes, imposes greater financial constraints on trusts and LLCs. This increased tax liability can discourage the use of Illinois as a situs for trusts, particularly for those involving significant life insurance components. The higher costs associated with Illinois trusts make them less competitive and less appealing for wealth management and estate planning.

CONCLUSION

South Dakota's forward-thinking approach to trust legislation, coupled with its strong fiscal foundation and commitment to privacy, provides unparalleled advantages for successful trust planning. The state's legal infrastructure supports innovation, flexibility, and long-term wealth preservation in ways that few—if any—other jurisdictions can match. By contrast, Illinois' outdated statutes, fiscal vulnerabilities, and lack of robust trust planning tools hinder its competitiveness in attracting sophisticated estate planning structures.

For families, trustees, and advisors seeking the optimal environment for establishing and administering long-term trusts, South Dakota offers a clear and compelling choice. The combination of statutory strength, favorable tax

treatment, and administrative efficiency makes it the jurisdiction of choice for modern trust architecture. Illinois, unless it embraces substantial reforms, will remain at a distinct disadvantage in the evolving landscape of trust law.

Overall, Illinois' slow legislative response and outdated trust laws have made it less competitive compared to states with more progressive trust statutes. The delay in abolishing the RAP and the late adoption of the Trust Protector statute are just two examples of how Illinois has failed to position itself as a leading jurisdiction for trusts. This reluctance to modernize its legal framework has resulted in missed opportunities to attract high-net-worth individuals and families seeking flexible and perpetual trust solutions.

By not prioritizing legislative advancements in trust law, Illinois continues to lag behind more proactive states. The state's inability to offer perpetual trusts and delayed flexibility measures through Trust Protector statutes underscores its lack of commitment to becoming a top-tier trust jurisdiction. Consequently, Illinois remains a less attractive option for those seeking the benefits of modern, long-lasting, and adaptable trust arrangements.

LEARN MORE

Sterling Trustees has been administering trusts of all types for over 18 years. Because the firm is not compensated by commissions or finder's fees, they are completely objective and equipped to do what's in the best interest of all beneficiaries. Sterling is a South Dakota-chartered trust company, helping you leverage the most progressive trust laws in the U.S. To ensure the financial security of your family's trust, contact us today and learn how an independent trust company like Sterling Trustees can safeguard your assets for generations.

About the authors

Antony Joffe is Chairman of Sterling Trustees, a South Dakota chartered trust company with over $9 billion of assets under administration. Sterling acts solely as an independent trustee and does not manage any investment assets. The company has a particular focus on working with wealthy families that wish to domesticate offshore trusts to the US. Sterling Trustees is a member of STEP.

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As an attorney, Nicole Byrum brings a unique perspective to her position as Chief Fiduciary Officer – partnering with her clients and their advisors to craft strategic trust vehicles which provide asset protection, governance and long-term wealth transfer. After a brief stint practicing law, she transitioned into global trust services before joining the Sterling team at our Sioux Falls, SD, headquarters. Nicole earned a JD from the University of South Dakota School of Law and a BA from the University of Washington. She also earned the Certified Trust and Financial Advisor (CTFA) designation from the ABA.

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