



South Dakota's Situs Advantages Over New Hampshire

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Both South Dakota and New Hampshire have strong trust laws and tax benefits that favor the HNW client. A comprehensive comparison of the states' trust laws reveal many similarities which tend to demonstrate New Hampshire's determination to be a top tier trust jurisdiction. The subtle points of contrast worth noting are found in New Hampshire's fiduciary services industry narrative and it's historical evolution. It is imperative that wealth planning professionals and advisors not only understand the different trust laws and how they affect their clients and beneficiaries, but also the larger landscape of political and economic factors that may directly or indirectly affect their clients in each respective jurisdiction. Trusts established in favorable jurisdictions provide the most effective means of wealth transfer for generations, but without long term stability even the most favorable of laws today may be altogether immaterial tomorrow.

South Dakota has historically instituted the most progressive trust laws in the country. Each term the governor assigns a new trust task force whose sole purpose is to work with state legislators to proactively monitor industry trends and adjust state laws accordingly. This collaboration is exclusive to South Dakota and gives trust industry leaders the unique ability to be directly involved with the development of trust laws.

This commitment and support from the highest levels of state government continually strengthen South Dakota's position as the top destination for trust situs. Grantors, beneficiaries, and their trusted advisors are well served establishing trust structures in South Dakota.

TRUST FRIENDLY STATES

In 1983 South Dakota was the first state to recognize the advantages of dynasty trusts by allowing trusts to last perpetually for all assets. As an estate planning tool, the ability for a trust to exist across multiple generations without terminating allows those trust assets to grow without the taxation that comes with termination and distribution of the trust.

In contrast, New Hampshire did not effectively end its rule against perpetuities until 2004.

The difference in years may be significant, and not just because the 21 year difference shows forethought or because it demonstrates South Dakota's commitment to being a leader in the trust industry, its significance may lie in another reason entirely. South Dakota abolished the RAP in 1983, a decade that also had lawmakers getting creative to plug perceived loopholes in the US tax code. Among those tax minimizing mechanisms to come under scrutiny was the use of trusts as a means to concentrate, preserve, and perpetuate wealth across multiple generations. The loophole closing result was the Generation Skipping Transfer Tax or GSTT. The GSTT is an additional tax on a transfer of property that skips a generation or when there is a transfer of property by gift or inheritance to a beneficiary (other than a spouse) who is at least 37½ years younger than the donor. The GSTT effectively closed the loophole that allowed wealthy individuals to legally gift money and bequeath property to subsequent generations without paying federal estate taxes. The GSTT tax rate is a flat 40%.

The effective date of the current GSTT tax is October 23, 1986. Wisconsin and South Dakota are the only states in the nation that effectively abolished the RAP prior to the implementation of the GSTT tax. The timing may turn out to be significant in the event of a challenge by lawmakers or the Internal Revenue Service claiming that dynasty trusts are a circumvention of federal taxes.

Today, many states permit dynastic trust structures, but not without objection. The volume of opposition to dynasty trusts is ever increasing as lawmakers look to increase taxation on the wealthiest Americans both at the state and federal level. Opponents claim that the super-wealthy are avoiding or reducing their taxes by using dynasty trusts, effectively shifting the obligation to pay for society's investments onto lower- and middle-class households.

In addition to the need to create new tax revenue, there has been an increased level of scrutiny on the finances of the world's highest net worth individuals and families. Controversy surrounding trusts have many calling for transparency in the name of wealth equality and social justice. There are open questions related to the equity and fairness of tax structures, who should pay, who shouldn't and who should pay more.

How do these factors affect the safety and long-term security of dynasty trust structures in South Dakota and New Hampshire? As calls to pass a federal RAP or invalidate states perpetual trust laws intensify, the rationale relies on states permitting or promoting tax avoidance. Tax avoidance is the legal practice of taking advantage of tax provisions that reduce income taxes and thereby avoid paying taxes that are not absolutely necessary or required. Repealing the RAP in many states may very well be interpreted as an example of tax avoidance legislation but that rationale fails in South Dakota's case because the state's RAP was repealed prior to enactment of the GSTT tax. It cannot be argued therefore, that South Dakota repealed the RAP as a purposeful response to the implementation of a multi-billion-dollar tax on trust assets, the same cannot be said of New Hampshire's 2004 repeal of the RAP. The fact is that dynastic trust structures are safer from challenge in the state of South Dakota.

The timing may or may not become a material cog in the proverbial wheel of anti-affluent legal challenges, nonetheless, South Dakota and New Hampshire's repeal of the RAP is just one of the subtle contrasts that make up the larger trust services landscape. South Dakota has the advantage in terms of dynasty trusts and state history lends itself to the commitment, stability, and reliability of South Dakota trusts.

RACE TO THE BANK

South Dakota began to position itself as a pre-eminent trust jurisdiction in the late 1990's when then governor Bill Janklow issued a series of executive orders that created a state trust task force. The task force was made up of trust and

estate attorneys and trust industry executives. South Dakota already had all the makings of an attractive trust jurisdiction with the ability to create a dynasty trust with no state income tax burden, both representing significant advantages over most states at the time. Once South Dakota started to be intentional about attracting trust business, the industry thrived. In 1996 there were just three trust companies in the state of SD, today there are more than 100 with combined assets totaling over \$600 billion, or about 100 times the amount of SD's state budget for 2023. It is estimated that more than 500 South Dakotans are employed directly by state chartered trust companies in addition to the peripheral jobs of accountants, attorneys, and financial advisors.

New Hampshire's trust industry has evolved in a much different way. Trust reforms began in 2003 and took a giant leap forward with the implementation of the Trust Modernization and Competitiveness Act in 2006. Proponents cited job creation and increased state tax revenue as rationale for swift and substantive changes to New Hampshire trust law, the result is a thriving half-trillion dollar fiduciary services industry in the Granite state. 2019 is where the NH trust story takes a twist.

When Senate Bill 98 was introduced in 2019, it's route to passage turned out to be a bumpy one and by the time lawmakers completed the drafting, the once bipartisan support for transforming the state into a trust haven had faltered. Instead of an easy pass, the bill called for the creation of an official study group to determine whether trust legislation is having the desired effect across the state and to ascertain what, if any, unintended consequences trust legislation may have created. The bill, and the posturing surrounding it, indicate that NH lawmakers are pulling back from the states position and purpose to create a top tier trust jurisdiction.

One of the few differences between NH and SD trust law is that South Dakota requires state chartered trust companies have a physical presence in the state, while NH trust companies may be located anywhere. In fact, the largest NH trust companies are actually located in Massachusetts, not NH. Others are

based in places like New York, Washington D.C., Kansas, and even the U.K. Some industry analysts estimate that as many as three-quarters of NH trust companies are actually based out of state. The result has created competing priorities. There is a strong desire to maintain the high volume of NH fiduciary services, but the desired increase to state revenue and job creation has been minimal.

While the fickleness of lawmaker support in NH may be justified, it is a stark contrast to the support that the trust industry enjoys in SD. The natural evolution of the favorable trust landscape in South Dakota is a significant factor in its success. A slow and steady pace of well-considered, well written, and well vetted trust laws that make it a natural choice for high net worth and ultra high net worth individuals and families from around the world. NH has likewise demonstrated a willingness to adjust and respond to industry trends, but will nonetheless have to ride out some growing pains that have come along with it.

GETTING YOUR DAY IN COURT

New Hampshire has a dedicated trust court that oversees complex trust litigation or reformation cases. Since it was created in 2014, the New Hampshire trust court has handled a number of complex cases for individuals and families who needed judicial intervention in their trust matters. Other states (such as Massachusetts) are attempting to follow New Hampshire's lead, but New Hampshire still stands out as having a trust court dedicated to handling complex trust issues.

South Dakota does not have a court created specifically to handle trust litigation, but South Dakota is nonetheless known for expeditious and well respected opinions. Most recently, the South Dakota Supreme Court's ruling in *re Cleopatra Cameron Gift Trust* dtd May 26, 1998, 931 N.W.2d 244 (S.D. 2019) which is widely viewed as a persuasive source when considering a states right to enforce judgements in a sister state.

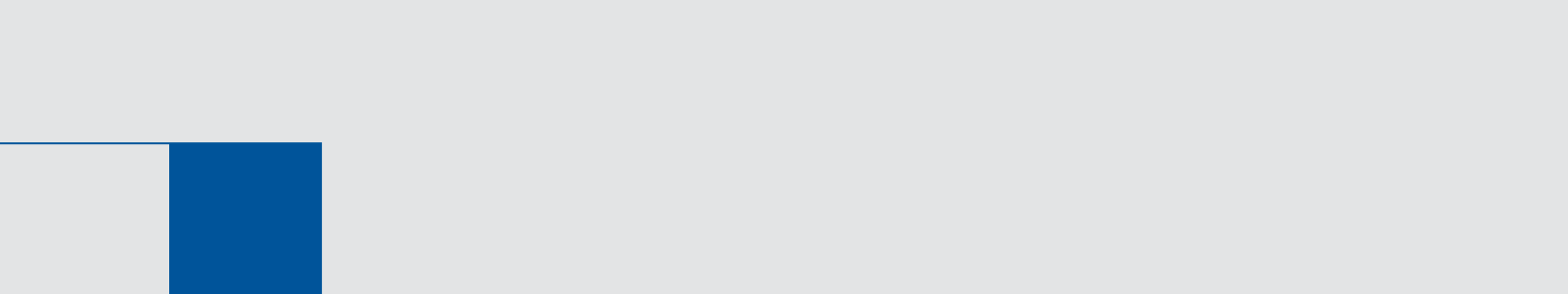
In the Cleopatra case, there was a valid California order to pay child and spousal support, but the enforcement of the order against trusts administered in South Dakota was to be determined by South Dakota law. The California Order was based on an enforcement provision related to a beneficiary's creditor, and South Dakota law does not allow judgments against beneficiaries to be enforced directly against a trust's assets. This case was a major decision in the realm of asset protection trust law and makes clear that creditors asserting claims against trusts administered in South Dakota are subject to the creditor protection and enforcement laws of South Dakota.

STRENGTH OF STATE

Similarities abound between trust law in SD and NH, from modern decanting and modification statutes to quiet trusts, to no state income tax and dynasty trusts, they are both great destinations for HNW and UHNW clients. And while the differences are harder to find than in most state comparisons, they diverge noticeably in terms of the fiscal health and economic strength of state.

On the basis of its solvency in five separate categories, South Dakota ranks 2nd among the US 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 US 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.

On the basis of its solvency in the same five categories, New Hampshire ranks 12th among the US states for fiscal health. New Hampshire has between 0.75 and 2.82 times the cash needed to cover short-term



obligations. Revenues exceed expenses by 4 percent, with an improving net position of \$413 per capita. In the long run, a net asset ratio of -0.02 indicates that New Hampshire does not have any assets remaining after debts have been paid. Long-term liabilities are lower than the national average, at 50 percent of total assets, or \$2,555 per capita. Total unfunded pension liabilities are \$20.85 billion, or 27 percent of state personal income. OPEB are \$2.14 billion, or 3 percent of state personal income.

New Hampshire and South Dakota both represent favorable jurisdictions for establishing and administering trusts to successfully preserve and protect wealth across generations. When a side-by-side comparison of the trust laws reveals so few differences, it is worth investigating further to vet the history of trusts in each respective jurisdiction whilst considering the current political and economic landscape. In terms of stability and predictability, South Dakota maintains a slight edge over its Granite state competitor.

About the authors



Antony Joffe is President of Sterling Trustees, a South Dakota chartered trust company with over \$5 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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