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ASSET PROTECTION TRUSTS (APTs): NON-TAX ISSUES

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Exhibits

A	Overview of Selected [Offshore] Jurisdictions By Duncan E. Osborne, Esq. and Mark E. Osborne, Esq., of Austin, Texas reprinted with consent
B	Comparison of Domestic Asset Protection Trust Statutes, updated through June 30, 2012, edited by David G. Shaftel, Esq., of Anchorage, Alaska, with contributions by lawyers in all 15 states, as listed, reprinted with consent
C	Local Counsel and Representative Banks and Trust Companies in Certain Offshore Jurisdictions
1	Affidavit of Solvency (Sample)
2	"What ACTEC Fellows Should Know About Asset Protection, by Duncan E. Osborne and Elizabeth M. Schurig, reprinted from the ACTEC Journal.
3	No U.S. Connections Allowed With an Offshore Trust? Wrong! Use Onshore Contracts "by Frederick J. Tansill," reprinted From the Journal of Asset Protection
4	Letter of Wishes (Sample)
5	"Litigation Boom Spurs Efforts to Shield Assets" by Rachel Emma Silverman, reprinted from the Wall Street Journal
6	"Shelter from the Storm" by Russ Alan Prince and Richard L. Harris, reprinted from Trusts and Estates.

OFFSHORE ASSET PROTECTION TRUSTS: NON-TAX ISSUES

I. BRIEF SUMMARY OF TAX TREATMENT OF A TYPICAL ASSET PROTECTION TRUST[1]

A. Typical Design.

For purposes of this discussion I assume that the typical design of an asset protection trust is an irrevocable discretionary trust established by a U.S. citizen or resident alien settlor in a jurisdiction whose law recognizes "self-settled" spendthrift trusts (i.e., for the benefit, inter alia, of the settlor), under and subject to the laws of that jurisdiction, with an institutional trustee which will have authority to make most substantial decisions. (There is an alternative scenario, not infrequently used, especially by non-resident aliens: the offshore bank serves as settlor and trustee. The name of the real settlor and principal beneficiary may appear nowhere in the body of the trust for extreme confidentiality.) The beneficiaries of the trust will include beneficiaries who are citizens of or resident in the U.S., i.e., members of the settlor's family, including the settlor. (However, in this practice area a U.S. lawyer may be asked by a non-resident alien to establish such a trust, and in this case the trust may be established in a U.S. asset protection jurisdiction or offshore. If such a trust for a non-resident alien is established offshore, there will be no U.S. nexis at all unless trust funds are invested in the U.S. Wealthy foreigners may come to U.S. lawyers simply because the U.S. has a reputation for producing sophisticated, scrupulous trust lawyers. Unless there are U.S. investments such an engagement raises no U.S. tax issues.) The trust will frequently hold its assets in an offshore LLC or corporation owned and controlled by the trust, maybe established in the jurisdiction in which the trust is established. In turn, that LLC or corporation will often create subsidiary LLCs to hold assets in any other jurisdiction in which trust assets are located, e.g., London or Zurich, Singapore or Wilmington.

B. Income Tax Treatment.

If the trust is established offshore ("OAPT" -- offshore asset protection trust), because the trust is designed so that no U.S. court will exercise primary jurisdiction over the administration of the trust, and because U.S. trustees do not have authority to control all substantial decisions of that trust (which are reserved to offshore trustees), the trust will be considered a "foreign" trust for U.S. tax purposes. Internal Revenue Code ("Code") Section 7701(a)(30)(E) and (31)(B).

If the foreign trust will have U.S. beneficiaries, under Code § 679 the trust is treated as a grantor trust for U.S. income tax purposes. All income is taxed to the grantor.

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[1] The tax issues with respect to foreign trusts are covered comprehensively in seminar outlines of Henry Christensen III, Michelle B. Graham, Carolyn S. McCaffrey, Jr. and Ellen K. Harrison. This brief summary is included in the interest of clarity and completeness of this outline.

If the trust is established in the U.S. ("DAPT" -- domestic asset protection trust) in a jurisdiction which recognizes asset protection trusts, such as Delaware or Alaska, it will normally be designed to be "defective" for income tax purposes, i.e., a grantor trust under Code §§ 671-678. Here again all income will be taxed currently to the settlor.

C. Tax Reporting Requirements of an Offshore Trust.

The creation and continued existence of an offshore trust must be reported to the IRS on Form 3520 within 2-1/2 months of the end of the first trust tax year (normally by March 15, as grantor trusts share the calendar year of settlors) following --

- the creation of the trust;
- the funding of the trust during settlor's life or at settlor's death;
- the death of the settlor;
- the immigration to the U.S. of a person who transferred property to a foreign trust within five years of establishing U.S. residency.

The trust must file an annual return/accounting on Form 3520-A within 3-1/2 months of the end of each trust tax year (normally by April 15).
NOTE: the difference between the dates represents a trap for the unwary, who may assume April 15 is the deadline for both filings.

Offshore asset protection trusts created by U.S. taxpayers have to be reported to the IRS on Form TDF 90-22.1 Report of Foreign Bank and Financial Accounts (commonly referred to as the "FBAR form") annually as will be more fully explained in the outlines of John Staples, Scott Michel and John McDougal. In addition, beginning in 2011, grantors of grantor trusts are treated as owning the foreign financial assets of the trust and must file IRS Form 8938, Statement of Specified Foreign Financial Assets, with their annual income tax returns.

The new regime under the Foreign Account Tax Compliance Act (FATCA) is dealt with comprehensively in John Staples' outline.

I really want to emphasize that very substantial penalties are imposed for failure to comply with the tax reporting requirements. NOTE -- this is unusual, even unprecedented in the tax law for large penalties to be imposed without respect to whether tax is due.

D. Estate Tax Treatment.

Because asset protection trusts, domestic and offshore, are typically designed under the estate and gift tax law so that transfers to such trusts will not be completed gifts (the settlor will retain a power, such as the power with the consent of the Protector to

name new beneficiaries or a special testamentary power of appointment), assets held in asset protection trusts are typically included in the taxable gross estate of the U.S. settlor at death, and the assets held in the trust at that time will receive a tax-free step up in basis. Therefore, normal U.S. testamentary estate tax planning will be included in an OAPT and DAPT for a U.S. settlor: (1) bypass trust planning to shelter the applicable credit amount; (2) marital deduction planning; and (3) generation-skipping transfer tax (GST) planning. The dispositive provisions effective at the settlor's death will look like those in a typical revocable trust in the U.S.

E. 2004 Article and 2013 ALI-ABA Program.

The July 2004 issue of Trusts and Estates contains a helpful article by Alexander A. Bove, Jr., "Drafting Offshore Trusts." Also see ALI-ABA's program materials for the Asset Protection Trust Planning outline presented by Duncan Osborne in Scottsdale, Arizona on April 17-19, 2013 at the program Planning Techniques for Large Estates.

SUMMARY

There is no tax "angle" when a U.S. citizen or resident establishes a typical asset protection trust. Its income is included in the Settlor's taxable income; its assets are included in the Settlor's gross taxable estate. Such a transaction is tax neutral. The crackdown by the IRS on tax fraud through undisclosed offshore accounts which began with Present Obama's election, and particularly the attack on UBS leading to a settlement in which the names of more than 4,000 U.S. taxpayers holding non-compliant accounts in Switzerland were disclosed, clearly indicate the increased enforcement of offshore tax fraud that may be anticipated by the Obama administration.

II. SELECTING A SITUS FOR THE FOREIGN ASSET PROTECTION TRUST -- ISSUES OTHER THAN ASSET PROTECTION

A number of factors must be considered in selecting the situs for a foreign trust, which is frankly more of an art than a science.

A. Developed and Favorable Trust Law.

To belabor the obvious, it is impossible to establish a foreign trust in a nation which does not recognize the concept of a trust, which is a creature of British common law. Most civil law countries -- most countries in which English is not the official language -- do not recognize trusts as legal entities. This includes almost all of South and Central America, non-English speaking Europe, most of Asia and Africa. While some civil law countries have adopted the trust concept by statute, e.g., Liechtenstein which has "issues," one should not necessarily equate the mere statutory adoption of the common law concept of a trust with the existence of a mature and

developed law of trusts. Even if a prospective situs nation has a well-developed law of trusts, it is necessary to examine those aspects of its trust law that may be particularly important to the ease of management and the financial success of a trust with U.S. beneficiaries. Asset preservation issues will be discussed below. Even countries with strong common law ties may differ with respect to their perpetuities and accumulation rules, which may determine the trust's ability to establish a desired sequence of interests or to make the accumulations necessary for the financial success of the trust.

Certain civil law countries have ratified the Hague Convention on the Law Applicable to Trusts and on Their Recognition: Italy, Luxembourg, and Switzerland. Residents in such countries should be able to transfer domestic assets to trusts. Switzerland hosts more than 6,000 private trust companies, and under provisions of the Hague Convention, as adopted in Switzerland, trust settlors may invoke the law of another country, such as an asset protection jurisdiction, while utilizing the services of a Swiss trustee. (See "Achieving Asset Protection with the Swiss Hybrid Trust," IFC Review, 2012).

B. Burden of Taxes and Administrative Costs.

It is important to examine the tax burden of the prospective situs jurisdiction of the foreign trust. Of course, no general statement may be made with respect to the taxation of foreign trusts by the many jurisdictions around the world which recognize some version of a trust. For purposes of this section, which emphasizes foreign trusts which are grantor trusts for U.S. income tax purposes and therefore subject to income tax in the U.S., it should be sufficient to observe that the only attractive foreign jurisdictions to U.S. grantors will be the so-called "tax havens" which impose no material taxes on such trusts. In this sense Delaware is a tax haven; it imposes no trust income tax. In examining the local taxes, one should be aware that foreign jurisdiction may impose taxes, such as documentary or stamp taxes, which are unusual from the perspective of the U.S. practitioner. Normally, such taxes will be relatively nominal.

Typically a U.S. grantor will select an institutional foreign trustee, and the prospective institutional trustee's fees for establishing and maintaining the trust should be reviewed. The Trustee may charge a "set-up" fee, pass through legal fees from its outside counsel to review a draft trust and charge the annual trustee's fee in advance. If there is an outside investment manager, that fee will be in addition.

Unless U.S. counsel either has experience with drafting documents in the foreign jurisdiction or is comfortable reviewing, revising and editing sample documents that the foreign fiduciary provides, it may be necessary to incur the costs of engaging local counsel (possibly in addition to paying the bank trustee's counsel) for assistance on behalf of the U.S. grantor and his counsel.

C. Currency and Controls/U.S. Affiliates.

Careful consideration should always be given to the selection of the currency in which the trust will hold its assets and pay its expenses. Currency stability is important. If the trust will have U.S. beneficiaries, consideration must be given to the complicated rules adopted under the Tax Reform Act of 1986 for determining gains and losses on transactions involving foreign currency.

Some countries impose significant restrictions on the investment of U.S. dollars within the country. Other nations may impose restrictions on currency withdrawals, which could limit payments to U.S. beneficiaries or the repatriation of trust assets.

If the trust is established in Europe, e.g. in Gibraltar, the Isle of Man, the Channel Islands of Guernsey or Jersey, or in Liechtenstein, will the investments be denominated in euros rather than in dollars?

Consider also that in 1989, a New York state court froze the account of a European bank at its New York correspondent (Goldman v. Goldman, New York Supreme Court, unreported decision). The foreign bank held an account in the name of a U.S. customer at its foreign headquarters. A third party who had brought a claim against such customer was able to successfully argue that since the customer's account was denominated in U.S. dollars, the depository bank's dollar funds held by its New York correspondent should be frozen until they were turned over to the U.S. state court in which the claim against the bank's customer was pending. Even though the petition for the injunctive order was made on an ex parte basis, and even though the underlying claim had not been reduced to judgment or even tried in court, the New York court granted the request. Because an appeal of the court's order would have taken several months, the plaintiff, whose claim was later determined in the underlying action to be wholly without merit, was able to achieve the upper hand in negotiating a settlement, and this probably wrong court decision ultimately cost the defendant/depositor millions of dollars.

Though most U.S. lawyers who review this case are in general agreement that the New York court's action described above was beyond the scope of applicable law and would have been overturned on appeal, this fact would provide cold comfort to the individual whose assets were improperly frozen. The case is illustrative of the belief of segments of the U.S. judiciary as to the extraterritorial reach of their judicial powers. Thus, the prudent planner would be wise to consider avoiding trustees and depository institutions with U.S. subsidiaries, branches or other affiliates, at least beginning with any point in time that the first hint of "trouble" in the form of a potential claim looms on the horizon. As the case described above demonstrates, it may even be prudent to avoid holding deposits in U.S. dollars.

D. Investment Media.

Related to the question of currency is the question of investment media for the foreign trust. On the one hand, the foreign trustee may maintain a general account with a New York institution through which the assets of numerous foreign trusts which it administers may be invested in publicly-traded American securities. (See the author's article, *No U.S. Connections Allowed with an Offshore Trust? Wrong! Use Onshore Contacts*, Journal of Asset Protection, Vol. 1, No. 5, May/June 1996, Exhibit 3) More typically, the offshore trustee may use an intermediary institution to hold assets on its behalf in the U.S., e.g., an offshore corporation and/or a U.S. LLC, e.g., a Bahamian Trust establishes a Bahamian IBC (International Business Corporation) which establishes a subsidiary U.S. LLC. On the other hand, in view of the global approach more and more Americans are taking to securities investment, it might make sense to take advantage of the foreign trustee's experience in foreign securities markets to invest at least some of the trust's assets offshore. In that case the intermediary entity owned by the trust will establish the investment account in London, Zurich, Honk Kong, or Singapore. Large foreign trust institutions may have more experience in investing in European Community and Pacific Rim securities and exchanges than their American counterparts, and consideration should be given to using that expertise. The grantor may rely on the foreign institutional trustee for investment management, and some such institutions have performance records comparable to the best U.S. trust companies and investment managers. This approach has the additional virtue of providing a non-creditor-avoidance business purpose, which, in turn, will be useful in defeating a fraudulent conveyance claim. Or the grantor may direct or request that the foreign trustee engage the services of a U.S. or offshore investment manager trusted by the grantor for investment choices. The typical offshore institution is very comfortable with either arrangement, and may have a bifurcated fee schedule depending on the scope of investment responsibilities it will be asked to assume. This is a difficult concept to grasp, because the typical U.S. trust company will generally insist on managing the assets. But the growing popularity of "open architecture" in U.S. trust companies is a step in this direction. Where the client has a need to preserve U.S. real estate from prospective future creditors, the foreign trust may hold title to the property, or more likely hold a 99% limited partnership interest in the property, with the grantor holding the 1% general partnership interest and thereby retaining management control. (See discussion at III. B.(3) below.) Or the foreign trust bank may loan the Settlor the equity in the U.S. real estate, taking a deed of trust or mortgage on the U.S. property. The Settlor will then reinvest the equity removed in the OAPT, perhaps putting the cash right back into the bank trustee in the form of a C.D. issued by the trustee bank held by the trust. Large international financial institutions will be much more comfortable holding in trust only liquid investment assets. It may be difficult to persuade such established institutions to hold such exotic assets as limited partnership interests in partnerships holding U.S. real estate, at least unless it is also holding substantial liquid investment assets. Whenever the foreign trustee is asked to hold exotic or illiquid assets, the trustee's fees with respect to such assets must be explicitly addressed in advance. Smaller boutique trust companies may be more likely to be willing to hold illiquid interests such

as partnerships.

E. Stability/Reputation.

In a world of political, economic and social instability, the stability of the situs nation is an important factor. Consider that Lebanon, Cyprus, and Panama were once known as investment havens for their favorable tax and non-tax laws. Today jurisdictions like Bermuda, The Bahamas, the Cayman Islands, Gibraltar, the Isle of Man and Jersey and Guernsey in the Channel Islands exemplify the desired stability. The Cook Islands and Liechtenstein will be seen by some to have a somewhat "shady" reputation.

F. Availability of Competent Trustees.

The financial success of any trust depends in large part upon the competence of the trustee chosen. This may be particularly true in the case of foreign trusts because of the general desire to direct trust investments towards growth at the expense of current income and because of the risk that injudicious actions of a trustee could cause the trust to become a U.S. trust. Obviously consideration should be given to the age and general reputation of the institution in the financial and legal communities, the amount of assets the institution has under management and the institution's historic performance. Coutts & Company, the world's oldest trust company, now owned by the Royal Bank of Scotland, Queen Elizabeth's trust company, was founded in the 1780's. Southpac Trust Company in the Cook Islands has not been around quite that long. Caribbean and other offshore law firms often have their own trust companies and most typically those "captive" trust companies will use outside investment managers. A listing of selected trust companies and trust counsel in seven jurisdictions with asset protection trust statutes is found in Part II of this Outline. Sometimes a large institution, such as Swiss-based UBS, Credit Suisse, and EFG Bank, or France-based SG Hambros, or JP Morgan or HSBC, will have small outposts in jurisdictions known for favorable law regarding asset protection trusts, such as The Cook Islands. The sophistication of the home office may reassure potential customers anxious about the meager local presence.

G. Changing Situs, Governing Law, Institutional Trustee, Force Majeure Clause.

For various reasons, it may become desirable or necessary to change the situs and/or governing law and/or Trustee of a foreign trust -- e.g., to avoid deteriorating political stability or unfavorable legal developments -- by moving it to another country or repatriating it to the U.S. Therefore it is important to avoid being locked into any jurisdiction or governing law (or any trustee for that matter). The possible need for a future change of situs raises a number of tax and non-tax issues that should be considered in drafting the trust instrument and before making any such change. It has been previously noted that civil, economic and political stability should be considered in

selecting the initial situs for a foreign trust. However, there is always the possibility that problems may arise in the future that would make the host country an undesirable situs for the trust. This possibility makes it important that the trust be able to alter its situs when necessary. Absent such a provision, known as a force majeure clause when it applies to dramatic unforeseen events such as political revolution or a devastating hurricane wiping out the banking infrastructure, the beneficiaries and trustee would always face the latent threat of unexpected developments such as an attempt to seize trust investments in the wake of civil disturbances.

Beware of the effect of an automatic flight clause under the U.S. tax rules, especially as they apply to non-grantor offshore trusts. Care should be taken to ensure maximum flexibility in the change of jurisdiction/change of trustee clause because of the potentially adverse income tax consequences in the event of an injudicious change in the situs of a foreign trust. The trust instrument should expressly permit a change to another offshore situs for the trust either by the trustee, with or without requiring the trustee's resignation, or by a "trust protector" named in the instrument. The instrument should also permit the trust's situs to be shifted to the U.S., but only if the trustee finds compelling reasons for such a change. The trust instrument might enumerate the factors that should be considered in determining whether to change the situs of the trust.

A trust's transfer to the U.S. may give rise to significant U.S. income, estate and gift tax consequences. Again this issue particularly applies to non-grantor offshore trusts. Generally the tax consequences of repatriation of a foreign trust depend on the form of domestication and how the I.R.S. or the courts view the transaction.

There are at least four methods for relocating a foreign trust.

(1) The trust can be liquidated, its assets distributed to the beneficiaries, and a new trust established in another jurisdiction.

(2) The trust may establish a subsidiary entity in another jurisdiction and transfer all or some portion of its assets to the subsidiary. This is sometimes accomplished by granting the transferee entity a protective option to acquire the assets of the foreign trust under certain circumstances.

(3) Another trustee may be appointed for the trust in a different country and the administration of the trust shifted to that new country with a wire transfer of title to securities.

(4) Using a "decanting" provision thoughtfully drafted into the original trust, the trustee may resettle some or all of the trust assets into one or more new trusts which may have a different trustee in a different jurisdiction with different governing law.

Normally the Trust Protector in an asset protection trust is given the authority to –

- change trustees
- change jurisdictions
- change governing law.

H. Consider the Impact of OECD, FATF, FSC on Choice of Jurisdiction[2].

Anti-tax haven initiatives emanating from the Organization for Economic Cooperation and Development (OECD) and the Financial Action Task Force (FATF) must bear on a practitioner's advice to his client on choice of jurisdiction within which to establish an asset protection trust. Issues relating to the matters may also bear on the practitioner's evaluation of the motive of his client under the "know-your-client" principles that should guide even careful practitioners in this area.

The OECD has identified particularly "uncooperative tax havens," and cautious practitioners should be particularly careful about encouraging a client to engage in any kind of banking or trust arrangement in these jurisdictions, not the least because these jurisdictions are red flags in a governmental review or reporting of client accounts.

The FATF seeks to inhibit money laundering, and identifies "Non-Cooperative Countries and Territories" ("NCCTs") which refuse to comply with its recommended standards. Since its first listing of such countries in 2000 and 2001, when 23 NCCTs were listed, all have through improved practices found themselves removed from the list. Lately the NCCT evaluation process has been dormant, but it could restart.

For some time the FATF has been working on draft "Guidance for Designated Legal Professionals on Implementing a Risk-Based Approach" to anti-money laundering. The merits review by a practitioner consider about the motivations of clients or prospective clients. Lawyers and accountants and others are characterized in these guidelines as "Gatekeepers." The FATF in 2006 released a report on the "Misuse of Corporate Vehicles, Including Trust and Company Service Providers" which is worth reviewing by the scrupulous practitioner.

While Senator in 2007, Barack Obama introduced the Stop Tax-Haven Abuse Act, and his Treasury Department has clearly followed up on the initiative with its pursuit of disclosure from and recent settlement with UBS regarding offshore accounts of U.S. taxpayers. It is clear that one way this administration plans to close the huge budget deficit is to crack down on tax avoidance by U.S. taxpayers using offshore trusts, corporations, foundations, etc., and much closer scrutiny of offshore arrangements by American taxpayers may be expected in the future.

The OECD maintains a "grey list" of countries that have committed to meet OECD standards on tax information sharing but have not fully implemented the rules.

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[2] This material is dealt with comprehensively in the outline of Bruce Zagaris, "Ethical Issues in Offshore Planning" presented at this same program. Brief treatment is included here for clarity and completeness of this outline.

III. ADVANTAGES OF FOREIGN ASSET PROTECTION TRUSTS OVER U.S. TRUSTS ESTABLISHED UNDER GENERAL U.S. TRUST LAW

A. Advantages Of Foreign Asset Preservation Trusts

(1) Characteristics of Favorable Asset Preservation Jurisdictions.

A person concerned about potential future claims or creditors may arrange to transfer or establish the situs for some of his or her assets in another country, for instance through an asset preservation trust in that jurisdiction. While the location of the assets and the existence of the trust will be discoverable in a creditor collections proceeding or in bankruptcy (unless the grantor is prepared to perjure or expatriate himself or herself -- and under the 2010 tax law changes expatriation has its own tax consequences), a state court in which a judgment is awarded against the grantor has no jurisdiction to enforce the judgment against assets in another jurisdiction. And while a federal bankruptcy court has national jurisdiction, it cannot enforce its judgments in an overseas jurisdiction. The judgments of U.S. courts will have to be perfected and enforced, if that is possible, in the foreign jurisdiction where the assets are located, which will involve time delay, trouble and expense in the form of local counsel fees, among others. Although a U.S. court may exercise jurisdiction over a U.S. grantor, the grantor, having established an irrevocable discretionary trust with an independent institutional trustee offshore, will be powerless to regain control of the assets which he or she has placed in trust. But see the Anderson and Lawrence cases discussed below.

A favorable foreign asset preservation jurisdiction will have three particular characteristics: (1) it will not recognize or enforce U.S. judgments, or it will be reluctant to; (2) it will countenance spendthrift trusts for the benefit of a grantor; and (3) it will have less stringent fraudulent conveyance laws than the U.S. Elaborate summaries of the laws of ten offshore asset protection jurisdictions -- Bahamas, Bermuda, Cayman Islands, Cook Islands, Guernsey, Gibraltar, Jersey, the Isle of Man, Liechtenstein, and Nevis -- and comparisons of their virtues are found in Exhibit A of this Outline (courtesy of Duncan and Mark Osborne). It is virtually impossible to stay current on the laws of multiple offshore jurisdictions, or even one, because these laws are constantly evolving and changing to seek competitive advantage over rival jurisdictions. So you really need to rely on local counsel for the current state of the law.

To further assist you in Exhibit C is a listing of what I understand to be competent and honest and sophisticated lawyers and trust companies in certain offshore jurisdictions.

(a) An Asset Preservation Jurisdiction Does Not Recognize or Enforce U.S. Judgments, or Is Reluctant To.

The courts of many foreign jurisdictions recognize U.S. judgments obtained by U.S. creditors against U.S. debtors and, as a matter of comity, will permit such judgments to be filed, recorded and enforced against assets of the U.S. debtor located in the foreign jurisdiction. In such a jurisdiction the U.S. creditor will not have to prove his case again in the foreign jurisdiction. The only action necessary in such a foreign court is, in effect, a collection action on debt which is deemed by the foreign court to have been finally established. Assets held by a U.S. debtor in his own name in such a foreign jurisdiction may be seized by the U.S. creditor if it succeeds in the prosecution of the collection action, which should not be difficult. Normally the creditor's biggest problem will be locating the foreign assets, not obtaining the foreign court order to seize them.

Examples of such a jurisdiction are Bermuda, The Bahamas, the Cayman Islands, which recognize U.S. judgments but requires a local action to enforce them. The creditor will, however, have to raise any claim to the assets in a trust sitused in such jurisdiction in the courts of such jurisdiction. For instance, if the creditor wants the trustee to disburse assets to the creditor, and the trustee refuses -- e.g., because the trust is an irrevocable discretionary spendthrift trust -- or if the creditor argues that assets in the trust were transferred to the trustee in fraud of such creditor's rights, the creditor will have to file suit against the trust or trustee in the court of the host jurisdiction. The host jurisdiction will apply its own trust law -- e.g., regarding the effectiveness of a spendthrift trust held for the benefit of the grantor and the use of a trust protector to delete the grantor from the class of permissible beneficiaries of the trust -- and its own law of fraudulent conveyance and its own burden of proof.

It should also be recognized that jurisdictions that theoretically will enforce foreign judgments may in practice be reluctant or slow to do so and reluctant to let foreign creditors successfully attack trusts in their jurisdictions. And even these jurisdictions usually have "firewall" provisions that limit the

enforcement of foreign judgments in relation to trusts governed by local law. For example, in Cayman Islands and many other jurisdictions, such as the Bahamas, Bermuda, Isle of Man, and the Channel Islands, foreign court orders concerning rights arising out of a "personal relationship" to the settlor, e.g. marriage or forced heirship, will not be enforced. See "Defending Offshore Trusts from Foreign Attack," by Rachael Reynolds, Trusts & Estates, November 2011.

In certain other jurisdictions, like Cook Islands, Nevis and Colorado, the local courts by law will not recognize foreign judgments in general, so that a judgment obtained in a U.S. court against a U.S. debtor has no legal consequence in such jurisdictions. In such jurisdictions there would have to be two legal proceedings, one to prove the Settlor of the trust had a liability to the creditor, and a second to prove that the transfer to the trust was a fraud on the creditor under local law, so that the creditor should have access to trust assets to satisfy the liability. If the U.S. debtor (or a trust established by the debtor) has assets in the foreign jurisdiction which the U.S. creditor wants to attach, the creditor must bring the entire principal case de novo in the courts of the foreign jurisdiction. In other words, the creditor must engage local counsel, file suit on the merits, bring evidence and witnesses to the foreign jurisdiction, and deal with the procedural rules and substantive laws of the foreign jurisdiction, for instance as to causes of action and burden of proof, possibly deal with a foreign language and unfamiliar legal system, which may make it much more difficult to obtain the desired judgment against the debtor than it was or would have been in the U.S. This burden is in addition to whatever further problems the creditor will have in collecting on the judgment against assets in the foreign jurisdiction in the event he is able to obtain a favorable judgment from the foreign court on his underlying theory of claim.

Bringing the cause of action in a foreign jurisdiction obviously presents a daunting financial burden. In addition to other difficulties, there may be language barriers, concern over hostile judicial attitudes to foreign plaintiffs, and an exotic -- i.e., non common law -- legal system. For example, the Channel Islands, Jersey and Guernsey, to some extent recognize "Norman" law, which is observed nowhere else in the world. Liechtenstein is a civil law jurisdiction with statutory trust law written in a foreign language. In the Caribbean, a judge may be inclined to discourage

foreign litigants by his desire that his descendants may have the opportunity to be international bankers rather than cabana boys, waiters, black jack dealers or lifeguards.

Needless to say, the intimidating burden of having to bring a cause of action de novo in a foreign jurisdiction may give the debtor much greater leverage in dealing with the creditor to avoid the claim altogether or compromise the claim favorably.

Examples:

Bermuda, The Bahamas, Cayman Islands. While Bermuda, The Bahamas and Cayman Islands are hospitable to asset preservation trusts in that they recognize spendthrift trusts for the benefit of the grantor and have Asset Preservation Trust ("APT") laws which impose less strict fraudulent conveyance standards than the U.S., these jurisdictions do recognize and will enforce most types of U.S. judgments (not family law judgments).

Cook Islands, Nevis, Barbados, Belize, Liechtenstein and Colorado. These jurisdictions do not recognize or enforce foreign judgments at all. The Isle of Man will not recognize or enforce U.S. judgments, but it will enforce judgments obtained in certain other countries.

(b) An Asset Preservation Jurisdiction Countenances Spendthrift Trusts for the Benefit of the Grantor.

Some foreign jurisdictions, including virtually all English common law jurisdictions other than the U.S., permit a grantor to establish a spendthrift trust for a class of beneficiaries including the grantor which is immune from claims of the grantor's future creditors. The formerly universal public policy of the United States -- Alaska, Delaware, Rhode Island, Utah, Oklahoma, Missouri, Nevada, South Dakota, Tennessee, Wyoming, New Hampshire, Hawaii, Virginia, and Ohio, are now exceptions -- supported by statutory and case law, is that a grantor may not establish a revocable or irrevocable trust of which he is a permissible beneficiary which is effective to insulate the trust assets from the grantor/beneficiary's creditors. In Virginia, for example, with respect to whose law I will allude because it is typical of most U.S. jurisdictions, unless the asset protection trust

meets the strict tests of the new statute, a transfer by a grantor of non-qualified assets to a non-qualified "spendthrift" trust of which he is a possible beneficiary is void vis-a-vis his existing creditors. Code of Va. § 64.2-747.

(i) General U.S. Law/Virginia Law

Putting aside for the moment the states which have adopted asset protection statutes in the last few years, including Delaware, Virginia, and Alaska, whose laws are discussed below, the general rule in the U.S. (and we will examine Virginia's general law for non-qualified assets in non-qualified trusts in some detail as an example of typical state law) if a grantor is a permissible beneficiary of a trust he created, is that his creditors may reach the maximum amount the trust could pay to him or apply for his benefit. Restatement (Second) of Trusts, § 156(2). This is true even though the trustee in the exercise of his discretion wishes to pay nothing to the grantor or his creditors and even though the grantor could not compel the trustee to pay him anything. Vanderbilt Credit Corp. v. Chase Manhattan Bank, 100 A.2d 544 (1984). The same rule should apply if the grantor procured the creation of a trust for himself, e.g., by creating reciprocal trusts with a family member. Bogert, The Law of Trusts and Trustees, § 223 (1979). Similarly, creditors may reach trust assets which are subject to a general power of appointment created by the donor in favor of himself. Restatement (Second) of Property, Donative Transfers, § 13.3. (1984). Because it is against public policy to allow a grantor to create an interest for his own benefit in his own property that cannot be reached by his own creditors, it is immaterial whether there is intent to defraud creditors or not. Petty v. Moores Brook Sanitarium, 10 Va. 815, 67 S.E. 355 (1910); In re O'Brien, 50 Bankr. 67 (Bankr. E.D. Va. 1985). See generally Scott and Fratcher, The Law of Trusts, § 156 (4th ed. 1987).

Under earlier case law courts generally would not automatically require a grantor of a revocable trust for the benefit of persons other than the grantor to revoke it for the benefit of his creditors or treat the grantor as the owner of such a revocable trust so his creditors could reach it. Scott, The Law of Trusts, § 330.12 (3rd ed. 1967). But some

recent cases have recognized the rights of the grantor's creditors to reach trust assets following the grantor's death where the grantor held a right of revocation at death. See State Street Bank & Trust Co. v. Reiser, 389 N.E. 2d 768 (Mass. App. Ct. 1979). And the trend in the law may be to permit the grantor's creditors to assert rights against revocable trusts during the grantor's life on the theory that a power of revocation is a form of general power of appointment. Restatement (Second) of Property, Donative Transfers, § 11.1 comment C. (1984).

For the same public policy reasons, if the grantor of an irrevocable spendthrift trust is also a beneficiary of that trust, it is ineffective to insulate the trust assets from the grantor/beneficiary's creditors. Where a grantor having current creditors makes a transfer to a spendthrift trust of which he is either sole beneficiary or one of several beneficiaries, the transfer is void.

If the grantor of an irrevocable trust is a beneficiary of the trust, his creditors may reach any amount required to be paid to or for the benefit of the grantor as well as the maximum amount the trustee, in the exercise of discretion, could pay to or for the benefit of the grantor. On the other hand, if the grantor's rights as beneficiary are clearly secondary and inferior to those of other beneficiaries, and the trustee has no current discretionary authority to distribute to or for the grantor's benefit, it is possible that courts will not permit post-transfer creditors of the grantor to assail the trust. Of course, such a creditor could obtain any trust assets actually distributed to the grantor.

(ii) Foreign Law

In contrast to the general rule in the United States, some foreign jurisdictions permit a grantor to establish a spendthrift trust for his own benefit which is immune from claims of his creditors. Properly drawn, such a foreign trust may qualify as a U.S. trust for U.S. tax purposes, as a grantor trust, but as a foreign trust for other legal purposes.

Foreign Jurisdictions With Favorable Asset Protection

Trust Legislation: Anguilla, Antigua, Bahamas, Barbados, Belize, Bermuda, Cayman Islands, Cook Islands, Cyprus, Gibraltar, Labuan, Marshall Islands, Mauritius, Nevis, Niue, St. Vincent, St. Lucia, Seychelles, Turks and Caicos Islands. These jurisdictions recognize the validity of irrevocable spendthrift trusts of which the grantor is a beneficiary as a shield from creditors of the grantor who did not exist and were not contemplated when the trust was established. The Channel Islands (Jersey & Guernsey) and the Isle of Man have statutes that permit self-settled spendthrift trusts, and are sometimes used, but they do not have elaborate asset protection trust statutes.

(c) An Asset Preservation Jurisdiction Has Less Stringent Fraudulent Conveyance Law

(i) U.S. Law/General Virginia Law of Fraudulent Conveyance

1. Overview.

Except for the new narrowly-defined Qualified Self-Settled Spendthrift Trusts, permitted after July 1, 2012, Virginia is a common law state, and at common law a debtor has the absolute right to pay one creditor in preference to another and can, without the imputation of fraud, secure one creditor to prevent another from getting an advantage. Williams, et al. v. Lord & Robinson, et al., 75 Va. 390 (1881). Therefore, the debtor has the right to prefer one creditor to another in the absence of any state or federal statute prohibiting such a preference. Giving such a preference to a bona fide creditor is not fraudulent, even though the debtor is insolvent and the creditor is aware at the time of the transfer that it will have the effect of defeating the collection of other debts. Such a transfer does not deprive other creditors of any legal right, for they have no right to a priority.

Other sorts of transfers by debtors, including gifts and sales on favorable terms, may trigger objections from creditors. Creditors may take the view that transfers by debtors disadvantageous to such creditors worked a fraud upon them. However, it is a fundamental principle of law that fraud must be alleged and proven, and every presumption of law is in favor of innocence and not guilt.

These principles have long been recognized in Virginia law, see generally Johnson v. Lucas, 103 Va. 36, 48 S.E. 497 (1904), Hutcheson v. Savings Bank, 129 Va. 281, 105 S.E. 677 (1921), and have recently been reaffirmed. Mills v. Miller Harness Company, 229 Va. 155, 326 S.E.2d 665 (1985). In the case of preferring one creditor over another, the key in preserving the transaction is that the creditors preferred be bona fide creditors. Simply because a transaction is completed which is disadvantageous to creditors will not in and of itself cause it to be set aside as long as it was made in good faith, and unsecured creditors, in the absence of fraud, cannot question the contracts of their debtors and undo all that is not beneficial to them. Catron v. Bostic, 123 Va. 355, 96 S.E. 845 (1918).

2. Virginia's Fraudulent Conveyance Statutes.

Virginia has enacted two fraudulent conveyance statutes which are typical of those in many states:

Intentional Fraud.
Every gift, conveyance, assignment or transfer of property, real or personal, made with the intent to delay, hinder or defraud current or anticipated future creditors of the transferor is voidable. Virginia Code § 55-80.

(a) Regardless of the transferor's intent, a bona fide purchaser for value takes good title, assuming the transferee had no notice of the fraudulent intent. On the other hand, if the transferee had notice of the fraudulent intent, the transferor's creditors may attach the property transferred. The transferee will be deemed aware of the fraudulent intent if he or she has knowledge of such facts and circumstances as would have excited the suspicions of a person of ordinary care and prudence.

(b) "Hinder", "delay" and "defraud" are not synonymous. A transfer may be made with intent to hinder or with intent to delay, without any intent absolutely to defraud. Any of the three intents is sufficient.

(c) There may be a fraudulent transfer even if fair consideration is paid.

Donative Transfer by Insolvent Transferor.
As to existing creditors, gift transfers are voidable without any finding of intent to delay, hinder or defraud, but the attacking creditor must prove that the transferor was insolvent or was rendered insolvent by the transfer. Virginia Code § 55-81.

(a) Creditors of the transferor may have no claim under this section --

- if they were not creditors at the time of the transfer.
- if fair consideration was paid.
- if the transferor was solvent after the transfer.

(b) NOTE: This section did not have an insolvency test until a relatively recent amendment.

3. Voiding the Transfer.
A creditor's suit is necessary to void the conveyance (Virginia Code § 55-82), the burden of proof is upon the one attacking the conveyance and the fraud must be proved by evidence that is clear, cogent and convincing, McClintock v. Royall, 173 Va. 408, 4 S.E.2d 369 (1939). Although the fraud must be proven and is never to be presumed, Land v. Jeffries, 26 Va. (5 Rand) 599 (1827), the evidence necessary to satisfy the court may be and generally is circumstantial, Witz, Biedler & Co. v. Osburn, 83 Va. 227, 2 S.E. 33 (1887), and courts have frequently held that there are certain indicia or "badges of fraud" from which fraudulent intent may be inferred, prima facie.

4. Badges of Fraud. These include:
   (a) retention of an interest in the transferred property by the transferor;
   (b) transfer between family members for allegedly antecedent debt;
   (c) pursuit of the transferor or threat of litigation by his creditors at the time of the transfer;
   (d) lack of or gross inadequacy of consideration for the conveyance;
   (e) retention of possession of the property by

the transferor;

(f) fraudulent incurrence of indebtedness after the conveyance.

(g) secrecy about the transfer;

(h) deviation from normal activities;

(i) transfer of all (or substantially all) of debtor's property; and

(j) transfer to family members (but cases of family transfers are surprisingly unpredictable, depending on the "flavor" of the facts).

Badges of fraud will inevitably be present in asset protection situations.

Hyman v. Porter, 37 Bankr. 56 (Bankr. E.D. Va. 1984), Hutcheson v. Savings Bank, 129 Va. 281, 105 S.E. 677 (1921). When the proof shows a prima facie case of fraud, i.e., where there are sufficient badges of fraud, the burden of proof shifts to the upholder of the transaction to establish that he or she intended to accomplish bona fide goals as a result of the transfer. If a conveyance is set aside under Section 55-82, the court will attempt to put the parties to the conveyance in the same position as if the conveyance had never taken place. Judgment creditors may interrogate the debtor under oath about all matters involving assets. Virginia Code § 8.01-506, et seq.

5. Definition of Insolvency.

Virginia Code § 55-81, supra, uses the word insolvent, but does not define it. The Uniform Fraudulent Conveyance Act (which Virginia has not adopted) provides that a person is deemed insolvent if, at the time of a transfer, the present fair salable value of the transferor's non-exempt assets is less than the amount required to pay his liabilities on existing debts. The Bankruptcy Code defines insolvency of an individual as the financial condition in which the sum of the person's debts is greater than all of the person's property, at fair valuation, exclusive of property transferred, concealed or removed with intent to hinder, delay or defraud creditors, and property that may be exempted from property of the estate under the Bankruptcy Code. 11 U.S.C. § 101(31). This is generally known as the "balance sheet test." Insolvency is generally presumed if the debtor

is not paying debts as they come due.

6. Limitations of Action/Statutes of Limitation.
In Virginia a creditor may generally bring an action for damages from fraud under Virginia Code § 55-80 (for transfers with the intent to hinder, delay or defraud) for two (2) years from the date the cause of action accrues under Virginia Code § 8.01-243(a). In the case of a donative transfer by an insolvent donor as described in Virginia Code § 55-81, a creditor may bring an action for damages from fraud for five (5) years from the date of the gift's recordation; or, if not recorded, within five (5) years from the time the transfer was or should have been discovered under Virginia Code § 8.01-253.

7. Federal Law.
The scope of this article does not permit any sort of detailed discussion of Federal bankruptcy law or Federal banking law, both of which have provisions forbidding fraudulent conveyance to defeat creditors' claims.

Suffice it to say that if fraudulent conveyance is proven, the bankruptcy discharge will be disallowed and the creditor will be free to pursue his lawsuit. In a recent case in Virginia, the court invoked the crime/fraud exception to the attorney-client privilege in a case where it found a prominent estate planning partner in a very reputable firm – a former chairman of the ABA Taxation section -- to have assisted in a fraudulent conveyance, disallowed the discharge in bankruptcy and caused the attorney to turn over his entire estate planning file, including his hand-written notes, to the creditor's attorney. It is not surprising that this led to a post-bankruptcy settlement between creditor and debtor. In re John Andrews, Memorandum Opinion, U.S. Bankr. E.D.VA., Adv. Pro. No. 93-1012, 7/8/96, and associated cases.

(ii) Foreign Law of Fraudulent Conveyance.
Modern fraudulent conveyance laws in English common jurisdictions, including Virginia, have their origin in 16th Century England, in the Statute of 13 Elizabeth (13 Elizabeth. Ch. 5 (1571)). Most common law jurisdictions have adopted either the Statute of Elizabeth or the concepts

embodied therein. However, while virtually all foreign jurisdictions (even non-common law) recognize the concept of fraudulent conveyances as against public policy and to some extent susceptible to nullification, the general British common law view of fraudulent conveyance is broader than the U.S. view, is that a conveyance may be set aside even if it defrauds only potential future creditors. (This serves as a counterpoint to permitting spendthrift trusts for the grantor.) See Re Butterworth (1882) 19 Ch.D. and Cadogan v. Cadogan (1977) All E.R. 200. However, a number of small island jurisdictions take a more narrow view of what is a fraudulent conveyance than do U.S. jurisdictions and use certain objective tests to cut off rights of certain parties alleging fraudulent conveyance. These jurisdictions have adopted since 1989 asset protection trust statutes.

For example, the law of the Bahamas permits allegedly defrauded creditors to assail a trust for only two years after the trust's creation. U.S. statutes of limitation are generally longer than those in offshore asset protection trust jurisdictions. It will normally take a creditor more than two years to find out the debtor has put any money in a Bahamian trust. The laws of the Cook Islands in the South Pacific (near New Zealand) and Nevis in the Caribbean permit creditors to allege fraudulent conveyance, but impose a criminal burden of proof -- beyond a reasonable doubt (prosecutors of O.J. Simpson for Nicole Simpson's murder and of George Zimmerman for Trayvon Martin's murder could not meet this burden) on the creditors to show that the trust was funded or established with principal intent to defraud that creditor and that the establishment of or disposition to the trust made the settlor insolvent or without property by which that creditor's claim (if successful) could have been satisfied. Nevis also requires every creditor initiating proceedings against a trust to deposit a $25,000 bond with the Ministry of Finance. Nevis law prohibits contingency fees and requires all legal proceedings to be undertaken by counsel licensed in Nevis. Nevis law is virtually identical to Cook Islands law. Interestingly SouthPac, one of the best known Cook Islands Trust Companies, also has a Nevis trust license and will serve as trustee of a Nevis trust, and the fees are cheaper than for a Cook Islands trust. And Nevis is not on any "watch" lists. Gibraltar has adopted legislation encouraging asset

preservation trusts of which the grantor may be a beneficiary, and permits no challenge after recordation of the fact of the trust by creditors alleged to have been defrauded so long as the grantor who established the trust was not insolvent immediately after the transfer to the trust. (However, to date only 27 APTs have been "registered" in Gibraltar, although many more have been created).

Asset preservation trusts, whereby the grantor irrevocably transfers assets to an independent fiduciary under the laws of the foreign jurisdiction, may be particularly immune from creditor claims of fraudulent conveyance. Foreign jurisdictions seek to establish a hospitable environment for asset protection trusts with U.S. and other foreign-domiciled grantors by enacting specific Asset Preservation Trust ("APT") legislation, the principal precepts of which may include:

1. allowance of recovery by a creditor only if the creditor's obligation existed at or before the time of the grantor's absolute disposition in trust;

2. creation of a malicious intent (to defeat creditors) test with respect to the debtor grantor;

3. elimination of the void ab initio concept with respect to the insolvent grantor's trust in favor of a voidable concept;

4. preservation of the rights of trustees and non-collusive beneficiaries to costs and benefits enjoyed in advance of a set-aside; provided, in the case of the trustee, that it acted prudently in establishing the solvency of the grantor; and

5. limitation of any set-aside to the amount of the debtor's disposition necessary to satisfy the obligation of the petitioning creditor.

In 1989 the Cook Islands adopted the world's first APT Statute. While it was apparently drafted by John McFadzien, then of SouthPac Trust (now practicing law on his own in the Cook Islands), many people believe (although Mr. McFadzien firmly denies it) with the assistance of or encouragement by Barry Engel, a prominent attorney of Colorado, specializing in offshore asset protection planning whom many credit with "inventing" this practice in the U.S. (Incidentally, at one time a substantial portion of

Barry Engel's firm's practice evolved into helping creditors attack offshore arrangements and eventually Ron Rudman left his firm, presumably recognizing the impossible conflict, to establish his own law firm specializing in representing creditors attacking offshore trust arrangements.) Since the Cook Islands first exploited the growing market for asset preservation spurred by the impact of U.S. recession and the U. S. tort award explosion, a number of foreign jurisdictions have adopted statutory schemes particularly tailored for asset preservation. Some are rather broad, others rather narrow. There are now more than 60 offshore jurisdictions which have adopted some sort of asset protection trust statute.

Examples: Cayman Islands, Bahamas, Bermuda, Gibraltar, Turks and Caicos Islands, Belize, Cyprus, Labuan, Nevis and Mauritius.

Numerous other jurisdictions are considering such legislation.

SUMMARY: The evaluation of the attractiveness of a situs as an asset preservation jurisdiction must take into account not only the existence of the three factors discussed above and whether, and to what extent, the jurisdiction has asset preservation trust legislation. One must also consider the general factors which make an offshore jurisdiction an attractive trust situs discussed in Section II. above. For instance, the Channel Islands, Jersey and Guernsey, and the Isle of Man have many general virtues as situses for asset protection trusts, but none of them has an asset protection trust statute. Perhaps perversely, some practitioners like to establish asset protection trusts in the Channel Islands or the Isle of Man for just that reason. If challenged, they are in a position to argue that they had no intent to defraud creditors, and as proof of their clean heart note that they could have established the trust in a jurisdiction with an asset protection trust statute, but chose not to. And specific consideration must be given to the type of liability sought to be avoided and the contemplated means of avoidance.

A February 6, 2006 article in the Wall Street Journal highlighted Singapore's almost overnight move into the stratosphere of offshore tax and trust havens, now being Credit Suisse's largest private banking center after Switzerland. Singapore serves as a tax haven for both Europeans fleeing the stricter tax regimes imposed by the EU and Asia's booming economy and demand for private banking services. In December 2004 Singapore adopted new trust laws permitting the avoidance of forced heirship regimes in other countries, such as EU jurisdictions. By 2004 over $50 billion was held in Singapore Trusts. See "Swiss Fight Against Tax Cheats Aids Singapore's Banking Quest," WSJ February 6, 2006.

Choose the jurisdiction considering the type of creditor sought to be avoided. For example, if avoidance of a forced heirship statute in the domiciliary jurisdiction is the motive, and assets are to be moved offshore for sophisticated management, Barbados, Bermuda or Jersey may be suitable. If the creditor to be avoided is a malpractice plaintiff and the asset to be preserved is a U.S. office building, the best strategy may be to put the office building into a U.S. family limited partnership with the grantor/debtor being a one

percent (1%) general partner with management authority and a Cook Islands or Nevis Trust having the ninety-nine percent (99%) limited partnership interest. Or pledge the U.S. real estate as collateral for a loan from the offshore bank trustee, and invest the borrowed capital in the offshore trust. An entrepreneur who has sold a business and has no current liabilities but wishes to protect himself from a "buyer's regret" lawsuit may want to put the proceeds of sale into a Bahamian or Gibraltar Trust.

Characteristics of the asset protection trust statutes of 10 offshore jurisdictions - Bahamas, Bermuda, Cayman Islands, Cook Islands, Gibraltar, Guernsey, Isle of Man, Jersey, Liechtenstein and Nevis - are summarized in detail in Exhibit A to this outline, which was prepared by Duncan E. Osborne (President of the American College of Trust and Estate Counsel – ACTEC) and Mark E. Osborne and published as part of their handout for the Asset Protection Trust Planning program for ALI-ABA of April 17, 2013 in Scottsdale, Arizona's Seminar "Planning Techniques for Larger Estates" and is published with their consent. The full outline is available from ALI-ABA. The author of this outline gratefully expresses his appreciation to them for permitting him to use these materials. (deosborne@ohkdlaw.com, meosborne@ohkdlaw.com).

Please see also "Asset Protection and Jurisdiction Selection." by Duncan E. Osborne, 33rd Heckerline Institute on Estate Planning.

To reiterate, the selection of the "right" offshore jurisdiction in which to establish an asset protection trust in a given set of circumstances is an art, not a science. In practice, US professionals typically get comfortable with two or three jurisdictions, perhaps with different virtues, with their laws, their lawyers, their banks and trust companies, and use and re-use those jurisdictions, lawyers and banks, over and over. This pattern of usage is subject, however, to the point made above: the need to vary the jurisdiction based on the type of creditor being avoided.

NOTE: An Isle of Man lawyer predicted at a June 2009 conference that no more that twelve (12) offshore international financial centers will survive the current crackdown by the OECD and European and American governments. He predicted many weaker offshore jurisdictions may not survive as viable financial centers. So pick a jurisdiction you believe is strong enough to survive. The current economic crisis has empowered wealthy nations to accuse tax haven jurisdictions of undermining global financial transparency and stability (notwithstanding any evidence of a causal connection).

B. <u>How a Settlor Retains Elements of Control Over a Foreign Asset Protection Trust</u>.

Common sense tells us that no settlor of an offshore trust is going to completely give up control of that trust and the property in it. There are two principal mechanisms whereby the settlor maintains "control" over assets in an offshore asset protection trust.

(1) Letter of Wishes.

The Settlor or the Settlor's attorney will typically give the trustee of the Foreign asset protection trust a non-binding precatory letter of wishes which might crudely be paraphrased as follows:

"Dear Trustee:

While of course the trust which I have established is irrevocable and may not be amended or revoked by me, and recognizing, of course, that you have complete unfettered discretion to accumulate or distribute income or principal from time to time, and if you distribute it, you may or may not distribute any to me, nevertheless I thought you might find it helpful if I expressed to you in writing some thoughts I had on how you might administer the trust. Of course, my suggestions are precatory only, as you may do as you wish.

a. Under no circumstances should you give a dollar to any alleged creditor of mine;
b. If I do not have creditor problems, please give me whatever I want when I ask;
c. If I have creditor problems, give me nothing, but provide for me and my family and pay our expenses.
d. I may send you a new letter of wishes from time to time."

An example of an actual Letter of Wishes is attached as Exhibit 4. Alexander A. Bove, Jr. recently authored a useful article, "The Letter of Wishes: Can We Influence Discretion in Discretionary Trusts?" published in the ACTEC Journal Volume 35, No. 1, Summer 2009. See article in STEP Journal September 2009 by Morven McMillan "Friend or Foe," considering the pros and cons of letters of wishes.

To Americans and American lawyers obsessed with enforceable contract rights, reliance on a precatory letter of wishes seems "loosey-goosey," but offshore bankers have a strong tradition of scrupulously honoring letters of wishes and their business is built on trust that they will do so.

(2) Trust Protector.

The Settlor will typically appoint in the document a trust protector with absolute authority to change trustees, change jurisdictions, and change governing trust law. Bluntly, if the trustee does not do what the Settlor wants, e.g., if the trustee fails to follow the letter of wishes, the Settlor will whisper in the protector's ear, and, lo and behold, a new trustee will be appointed. If a creditor claim arises in the U.S., it is probably best if the Protector is not in the U.S. so the trust should contain a mechanism to replace the U.S. Protector and appoint one

offshore in the event a U.S. claim looms on the horizon. Alexander Bove recently debunked "The Case Against the Trust Protector" in ACTEC Journal Vol. 37, Number 1, summer 2011. Also, "Solving the Mystery of the Trust Protector" by the same author in the September 2009 STEP Journal.

(3) Family Limited Partnership ("FLP") of Which Settlor is Managing Partner.

The Settlor may establish a FLP (or FLLP) to hold assets, retaining the 1% managing general partner's interest and all authority over the partnership and conveying to the foreign asset protection trust the 99% limited partnership interest. The Settlor then may convey to the FLP real estate, tangibles, cash, securities, etc.

If creditor problems loom on the horizon, the Settlor may first of all have normal creditor protection benefits of a partnership under U.S. law, i.e., a creditor's only remedy is a charging order, creditor gets partnership K-1 for partnership income interests with respect to which he has a charging order. As a second alternative, the Settlor as general partner will have authority to liquidate the FLP, leaving himself with a 1% interest in partnership assets as tenant in common with the foreign asset protection trust, which holds the other 99% interest in what had formerly been partnership assets as tenant in common. The portable assets representing 99% of what were formerly partnership assets may then be moved offshore into the direct control of the foreign Trustee. The Settlor may also resign in favor of a third party as managing general partner.

(4) Retained Powers Authorized by Statute.

As noted below in IV, Delaware and Alaska law expressly authorize certain powers to be retained by the Settlor without risk of forfeiting the asset protection features of the trust. Similarly, certain foreign jurisdictions expressly sanctioning foreign asset protection trusts authorize the Settlor to retain certain powers. For instance, Cook Islands law provides that a Settlor of an asset protection trust may retain (a) power to revoke, (b) power to appoint, (c) power to amend, (d) power to retain a beneficial interest, (e) power to remove or appoint trustees and trust protectors, (f) power to direct a trustee or protector on any matter.

(5) Domestic Trustee and Foreign Trustee.

One model has a U.S. Trustee, typically a non-beneficiary individual, family member, friend or attorney, as Co-Trustee with a Foreign Trustee, typically an institution, presumably on the assumption that the U.S. Settlor would appoint someone as U.S. Trustee over whom he felt he or she had more influence. However, the tax issues raised by having a U.S. Co-Trustee and the authority of

the U.S. Co-Trustee must be carefully considered.

(6) (a) Selection of Cooperative Trustee/Trust Protector.

Typically in an OAPT the U.S. Settlor appoints a party he completely trusts, not infrequently his attorney, as Trust Protector with power to discharge a trustee, move the trust to another jurisdiction, and hire a new trustee and adjust the law of the new jurisdiction as the governing law of the trust. If trouble looms in the horizon for the Settlor in the U.S., the Trust Protector should be outside of the U.S.

See Exhibit 3, *No U.S. Connections Allowed With An Offshore Trust? Wrong! Use Onshore Contacts*, by Frederick J. Tansill.

(b) For further control, the settlor may require the trustee to use an investment manager/asset custodial known to and trusted by the settlor.

(7) Tension Between Protection and Control.

It is worth recalling the truism of asset protection planning: the more control a Settlor retains, the more vulnerable is the trust to the Settlor's creditors. This principle resonates through all of the "bad" cases cited below.

C. Multiple Structures.

To further discourage potential future creditors, multiple foreign asset protection trusts may be established with different, more and less safe structures, in different jurisdictions with different laws, with different trustees. "Hot" liability attracting assets -- Lear Jets, office buildings -- may be segregated from each other and from liquid investment assets. Trusts may hold as "subsidiaries" corporations, LLCs and partnerships established under the same or different laws than the trust holding various assets and types of assets in different jurisdictions.

IV. COMPARISON OF FOREIGN ASSET PROTECTION TRUST TO TRUSTS ESTABLISHED UNDER DELAWARE OR ALASKA OR SIMILAR U.S. ASSET PROTECTION STATUTE

Recent legislation in Alaska and Delaware (1997) and, more recently, in Rhode Island and Nevada (1999), Utah and Oklahoma (effective 2004), Missouri and South Dakota (effective 2005), Wyoming (effective July 1, 2007) and Tennessee (effective July 1, 2007), New Hampshire (effective 2009), Hawaii (effective July 2011), Virginia (July 1, 2012) and Ohio (March 27, 2013) has modified two common law rules, the Statute of Elizabeth (regarding fraudulent conveyance) and the Rule Against Perpetuities. Undoubtedly more states are coming.

In the January 2012 issue of Trusts & Estates, David G. Worthington and Mark Merric evaluated 28 domestic jurisdictions for general appeal as potential situses for trusts, considering asset protection planning and many other characteristics, with a very helpful chart, "Which Situs is Best in 2012?"

NOTE: With fifteen of the fifty states (Shaftel counts one state – Colorado – which some other commentators do not) having passed trust statutes encouraging the protection of assets from prospective future creditors, it would seem to this author that public policy in the U.S. has shifted, at least slightly, in favor of debtor defendants, who might expect a more sympathetic hearing from judges than before this trend started in 1997. The trend will likely continue.

This trend should also cause lawyers who at one time believed that asset protection planning was "shady" to ask themselves this question: If 15 state legislatures and governors representing all areas of the country have effectively encouraged asset protection planning, how shady can it be? More than 30% of the states have officially sanctioned asset protection planning as appropriate public policy.

As previously noted, the Statute of Elizabeth (regarding fraudulent conveyance) is the source of modern fraudulent conveyance rules, and under the rule a creditor of a settlor of a trust may reach the trust property to the maximum extent that the trustee may distribute such property to the settlor. Most states limit the term of a trust so that it cannot continue to exist beyond 21 years after the death of the last individual in a designated class living at the inception of the trust.

The Alaska Law, effective April 2, 1997, is found in Alaska Statutes §§13.12.205(2)(A); 13.36.035(a)(c); 13.36.045(a)(2); 13.36.310; 13.36.390; 34.27.050(a)(3); 34.40.010.

The Delaware law, effective July 1, 1997, is found in Del. Code, Title 12, §§3570-3576, amended to repeal §3573(b) retroactively, and Title 25, §503(a). The current State of Delaware's asset protection trust statute is summarized and analyzed in detail in Part II hereof. Delaware's legislative history states that the aim of the statute is to "maintain Delaware's role as the most favored jurisdiction for the establishment of trusts." Delaware's law has been amended (and improved) almost annually to address areas of concern which have arisen based on experience with the statute.

One purpose of these 15 relatively new domestic statutes is to provide creditor protection for certain self-settled spendthrift trusts that permit purely discretionary income and principal distributions to the settlor.

Characteristics of the laws of all 15 U.S. jurisdictions are summarized in detail in Exhibit B to this outline, which was edited by David G. Shaftel of Anchorage, Alaska with contributions by lawyers in all 15 states, and is published with David's consent. (dshaftel@shaftellaw.com). The author of this outline gratefully expresses his

appreciation to David G. Shaftel and his contributors (who are listed) for permitting him to use these materials.

Wilmington Trust publishes an annually updated book, the latest Delaware Trust 2012 by Richard Nenno which is subtitled "Asset Protection: Domestic and International Law and Tactics," which also appears as a chapter in Duncan Osborne's and Elizabeth Schurig's treatise Asset Protection: Domestic and International Law and Tactics published by West, probably the best treatise in the asset protection area. (Mr. Nenno is taking a hiatus and is not publishing a 2013 edition.)

A. Irrevocable Trusts.

Both Delaware and Alaska asset protection trust statutes apply only to irrevocable trusts.

B. Retained Powers.

Both statutes provide that certain powers retained by the settlor will not cause the trust to be deemed revocable, including:

(1) a settlor's power to veto a distribution from the trust

(2) a testamentary special power of appointment or similar power

(3) a settlor's potential or actual receipt of a distribution of income, principal or both in the sole discretion of a trustee who is neither the settlor nor a related or subordinate party within the meaning of I.R.C. §672(a) (in the case of the Delaware statute) or in the discretion of a trustee who is someone other than the settlor (in the case of the Alaska statute).

(4) Alaska permits the Settlor to retain the rights (a) to income distributions of charitable remainder trusts in the DAPT, (b) to receive distributions from a GRAT or GRUT in the DAPT, (c) the right to use real estate held in a QPRT, (d) an interest in an IRA.

C. Specific Incorporation of State Law.

Both statutes require a trust instrument to expressly incorporate the relevant state law to govern the trust's validity, construction and administration.

D. Spendthrift/Anti-Alienation Provision.

Both statutes require a trust instrument to contain a spendthrift or anti-alienation provision.

E. Resident Trustee.

Both statutes require a resident trustee, either a natural person resident in the state or a bank or trust company authorized to act as a trustee in the state.

F. Administrative Activities in State.

Both statutes require that certain administrative activities be performed in the relevant state including:

(1) custody of some or all trust assets

(2) maintenance of trust records on an exclusive basis

(3) preparation or arrangement for preparation of fiduciary income tax returns; and

(4) other material participation in the administration of the trust.

G. Exceptions to Creditor Protection.

Both statutes generally prohibit legal actions against trust property that is subject to the statutes, with several exceptions.

(1) Fraudulent Conveyances. The asset protection trust statutes do not override the state's fraudulent conveyance statutes. Alaska's law has recently been amended to provide that a transfer may be set aside if the transfer has been proven to have been motivated by the intent to defraud a current or contemplated creditor, but it will NOT be sufficient to prove intent to hinder or delay, which are considered equivalent in general fraudulent conveyance statutes. Delaware law provides that the burden of proving fraudulent conveyance in connection with a Delaware asset protection trust is clear and convincing evidence.

As to pre-transfer creditors, actions must be brought within the later of (a) 4 years after the transfer was made, or (b) one year after the transfer is or reasonably could have been discovered by the creditor.

As to post-transfer creditors, actions must be brought within 4 years after the transfer in trust is made.

(Nevada has the shortest statute of limitations -- two years after the

transfer or, if later, 6 months after transfer reasonably should have been discovered. If the claim arose after the transfer, the two-year limit is absolute. As in Delaware, in Wyoming the creditor must prove fraud by clear and convincing evidence.)

(2) Child Support Claims. The Alaska (and Utah) statute provides that trust assets will not be protected from child support claims if, at the time of the transfer, the settlor was in default by 30 days or more in making child support payments, but otherwise such a trust can avoid child support claims that arise in the future, a surprising public policy for a "family values" state such as Utah?

The Delaware (and Rhode Island) statute also provides that trust assets will not be protected against child support claims, with no express requirement comparable to the Alaska/Utah requirement that the transferor be delinquent in payments at the time of the transfer. (Nevada has no spendthrift trust exception for child support.)

(3) Spousal Claims. The Delaware (and Rhode Island and Utah) statute excepts marital property divisions or distributions from protection, again with no express limitation to outstanding divisions or distributions at the time of the transfer to the trust.

Alaska (and Nevada) has no exception for spousal claims, but the surviving spouse's statutory right to elect against Settlor's Will might apply in Alaska to DAPT assets.

(4) Tort claims from Injuries Occurring On or Before the Date of Transfer to the Trust.

The Delaware statute does not insulate trust property from a person who suffers tort injuries (death, personal injury, or property damage) on or before the date of the transfer to the trust, in cases where the injury or damage is caused in whole or in part by an act or omission of the transferor or by someone for whom transferor is or was vicariously liable.

The Alaska statute does not have a comparable provision.

(5) Claims Arising from Reliance Upon the Settlor's Written Representation that Trust Assets Were Available to Satisfy Claims.

In original form, the Delaware statute provided that its creditor protection should not apply to any creditor who became a creditor of the settlor in reliance upon an express written statement that the trust property remained the settlor's property following the transfer and was available to satisfy any debt of the settlor to the creditor. As discussed below, this provision raised potential transfer tax problems. It has been repealed in a bill signed by Delaware Governor Carper on March 30, 1998.

The Alaska statute does not have a comparable provision.

NOTE: As with an offshore asset protection trust, pick your state in which to establish a DAPT based on the type of creditor and claim you are worried about.

H. Jurisdictional Issues.

The Alaska statute provides that for trusts qualifying for the statute's protections, Alaska courts will have exclusive jurisdiction over and will apply Alaska law in proceedings regarding the internal affairs of trusts.

The Delaware statute provides that for trusts qualifying for the statute's protections, no action can be brought to attach or otherwise reach trust property, and that Delaware will not enforce other state's judgments on such actions.

I. Transfer Tax Issues.

(1) Completed Gift: Whether a settlor makes a completed gift in funding a trust of which the settlor is a beneficiary depends upon: (i) the extent of the settlor's retained interest in the trust; and (ii) the extent to which the settlor's creditors can reach the trust property.

Purely discretionary interest in trust. If the settlor's only interest or power under a trust is to receive purely discretionary distributions of income or principal from a third party trustee, then the settlor's gift to the trust will be complete. Treas. Reg. §25.2511-2(b).

Creditor access to trust. To the extent the settlor's creditors can reach the trust assets because of the settlor's retained interest, then the gift will be incomplete.

Where "...the [settlor] cannot require that the trust's assets be distributed to the [settlor] nor can the creditors of the [settlor] reach any of the trust's assets..." the settlor has parted with

dominion and control sufficient to have made a completed gift of the assets transferred to the trust." Rev. Rul. 77-378, 1977-2 C.B.347.

"If and when the [settlor's] dominion and control of the trust assets ceases, such as by the trustee's decision to move the situs of the trust to a state where the [settlor's] creditors cannot reach the trust's assets, then the gift is complete for federal gift tax purposes under the rules set forth in §25.2511-2 of the Regulations." Rev. Rul. 76-103, 1976-1 C.B.293.

Because under the common law rule of many states, as restated in the Restatement (Second) of Trusts §156(2), a settlor's creditors can reach trust property to the maximum extent that the trustees may distribute the property to the settlor, a settlor in those states will be deemed to have rights to the property within the meaning of I.R.C. §2511. See Outwin v. Commissioner, 76 T.C. 153(1981) and Paolozzi v. Commissioner, 23 T.C. 182(1954). This would be the result in Virginia by virtue of the law cited above.

(2) Removal of Assets from Estate.

(a) Avenues for Estate Inclusion.

1. I.R.C. §2036. I.R.C. §2036(a)(1) provides that a transferor's gross estate includes the value of any transferred property over which the transferor retained the right to possession, enjoyment or income for life or for a period not ascertainable without reference to the transferor's death. Does the discretionary power of a trustee to distribute income to the grantor create a potential rationale for the IRS to argue for including the assets of a Delaware or Alaska Trust in the grantor's taxable estate? Professor Jeffrey Pennell argues maybe yes. (Pennell, 2 Estate Planning, §§7.3.4.2 and 7.345 (Aspen 2003)) Mal Moore, on the other hand, argues that "the proponents of non-inclusion have the better part of the argument." ("Comments on Alaska/Delaware Trusts," Malcolm A. Moore, ALI-ABA Video Law Program, May 20, 1998.) Dick Covey is reported to agree with Mal Moore's position.

2. I.R.C.§2038. I.R.C. §2038(a)(1) provides that a transferor's gross estate includes the value of any transferred property over which the transferor, at the time of his death, had a power (in any capacity) to change the enjoyment, through a power to alter, amend, revoke or terminate.

(b) Cases and Rulings. A number of cases and rulings have been cited for the proposition that the transferred assets may be removed from the estate for estate tax purposes. See, e.g., Estate of German v. United States, 85-1 U.S.T.C. (CCH) ¶13,610 (Ct.Cl. 1985); Estate of Paxton v. Commissioner, 86 T.C. 785 (1986); Estate of Wells v. Commissioner, 42 T.C.M. (CCH) 1305 (1981); Estate of Skinner v. United States, 316 F.2d 517 (3d Cir. 1963); Estate of Uhl v. Commissioner, 241 F.2d 867 (7th Cir. 1957); Private Letter Ruling 9332006; Private Letter Ruling 8829030; Technical Advice Memorandum 8213004; Private Letter Ruling 8037116; Private Letter Ruling 7833062.

(c) Facts and Circumstances. Many of the above cited cases are clear in outcome if not always in reasoning. The courts looked at all facts and circumstances surrounding the creation and administration of the trusts. Facts and circumstances helpful to the desired estate tax result (exclusion of the trust assets from the estate) include: the absence of any pre-arrangement that all trust income be paid to the settlor; the absence in fact of payment of all trust income to settlor; the failure of the settlor to place all of his or her assets in the trust; and the reporting of the creation of the trust as a gift for gift tax purposes.

(d) Delaware Statute. The Delaware statute in its original form had a fatal transfer tax defect. Because Section 3572(b) originally allowed the transferor to make the transferred property subject to the claims of the transferor's creditors by means of an express written statement to that effect, this would appear to have prevented a completed gift and triggered includability under I.R.C. §2038(a)(1), as it would amount to a retained right to indirectly terminate the trust by giving creditors recourse to it for payment of claims. This problematic section has been repealed retroactive to the effective date of the Act.

David Shaftel in the article cited in the ACTEC Journal has a helpful analysis of the transfer tax issues.

(e) Recent Tax Developments in DAPT - - Estate Inclusions? The American Taxpayer Relief Act of 2012 (ATRA), setting the transfer tax exemption at $5,120,000 indexed for inflation ($5,250,000 in 2013), has focused renewed attention on whether it is possible to create a "Completed Gift Asset Protection Trust" in a domestic (DAPT) or offshore (OAPT) jurisdiction to accept a $5.25 million (or lesser) gift. The benefits, if they may be achieved, would be to permit a donor to put up to $5 million into an irrevocable self-settled spendthrift/asset protection trust which includes the settlor among the class of potential beneficiaries. The settlor donor would allocate gift tax exemption and, especially if establishing a perpetual trust, e.g., under Delaware Law, allocate GST exception, to the trust.

Under Revenue Ruling 77-378 it is possible to make a gift to such a trust which is a completed gift for federal gift tax purposes. See also PLR 9837007 relating to gifts to an Alaska Trust. This PLR found the transfer to such a DAPT with the settlor among the class of discretionary beneficiaries to be a completed gift for federal gift tax purposes, but expressly did not rule on whether the assets would be included in the settlor's estate for federal estate tax purposes.

Revenue Ruling 2004-64 indicated that applicable local law subjecting the trust assets to the claims of settlor's creditors may cause the inclusion of trust assets in the settlor's gross estate for federal estate trust purposes.

In a very interesting PLR 200944002 the settlor created an Alaska APT for a class of beneficiaries including himself. The PLR concurred with the above authorities that the gift was a completed gift, but also concluded that the trustee's discretionary authority to distribute income or principal to the settlor did not, by itself, cause the trust to be included in the settlor's estate under code section 2036 (a) (1). However, neither this PLR nor Revenue Ruling 2004-64 addressed whether Code Sections 2036 (a) (2) or 2038 will cause the inclusion of assets held in a self-settled DAPT in the settlor's estate for federal estate tax purposes.

All states that have DAPT statues other than Alaska and Nevada allow certain creditors to access the trust. Is this access fatal to the issue of estate inclusion, or do transfers to Alaska and Nevada DAPTs enjoy uniquely favorable tax treatment. Michael M. Gordon of Gordan, Fournaris & Mammarella, P.A. in Wilmington, Delaware argued in a paper presented to STEP (Society of Trust and Estate Practitioners) on June 1, 2011 that because of the doctrine of "acts of independent significance," Delaware (and other DAPT jurisdictions) should have as good an argument as Alaska and Nevada to estate exclusion.

Jonathan G. Blattmachr also argues (e.g. in a presentation made to Wells Fargo contacts attending a Washington DC forum in June 2011) that estate exclusion is possible for settlors of self-settled DAPTs with some creative drafting tips to help secure the goal.

Of course these analyses are motivated by the temptation/risk of giving away $5.25 million in 2013 but retaining potential access to it ... a Holy Grail if it may be achieved.

The tax problem with this objective is that there is no statuary authority, no case law, only a half-way helpful Revenue Ruling and some half-way helpful PLRs, all of which expressly refuse to hold that transfers to DAPTS of which the settlor is in the class of beneficiaries will not be included in the settlor's gross estate for the estate tax purposes.

(f) Recent Tax Developments in DAPTs -- Incomplete Gift to Non- Grantor Trust? Michael Gordon in the same STEP outline discussed above indicates possible means for a settlor to establish a DAPT which will be treated as a non-grantor trust for income tax purposes and as an incomplete gift for transfer tax purposes (DING Trust - - Delaware Incomplete Gift Non-Grantor Trust). The perceived opportunity is for domiciliaries of high income tax states, such as New York, New Jersey, Massachusetts and California, to minimize or avoid state income tax on assets held in Delaware APTs. The federal tax authorities are inconsistent and confusing, and one can only imagine the vigor with which tax-starved states with huge budget deficits would fight this attempt to avoid state income tax.

J. The Enforceability of Foreign Judgments.

(1) Jurisdiction of Out-of-State Courts.

(a) The Issue. Despite Alaska's statutory announcement of exclusive jurisdiction over self-settled spendthrift trusts created under its statute, and despite Delaware's statutory prohibition against actions attaching assets in self-settled spendthrift trusts created under its statute, can a non-Alaska or non-Delaware court obtain jurisdiction over the trust and decide the validity of the spendthrift provisions? For a thorough analysis of this and related jurisdictional issues, see Cannon, *The New Self-Settled Trust Statutes*, California Trusts and Estates Quarterly, Vol. 3, Number 4 (Winter 1997) and Giordani and Osborne, *Will the Alaska Trusts Work?* Journal of Asset Protection (September/October 1997).

(b) The Authorities.

1. Statutory extra-territorial impact. A state statute that purports to have extra-territorial impact outside of that state may not be effective to prevent another state from deciding a matter in which that state has an interest. See generally Thomas v. Washington Gas Light Co., 448 U.S. 261 (1980); Alaska Packers Association v. Industrial Accident Commissioner of California, 294 U.S. 532 (1935); Tennessee Coal, Iron & Railroad Co. v. George, 233 U.S. 354 (1914). Hence, it is unclear that either the Alaska statute, which purports to give Alaska exclusive jurisdiction over trusts created under its statute, or the Delaware statute, which prohibits actions to attach or otherwise reach the property of a trust created under its statute, is effective to prevent another state from ruling on the validity of the trust spendthrift provisions when that other state has an interest in the trust and a basis for jurisdiction

over the trust.

2. Jurisdictional bases for non-Alaska or non-Delaware forum courts over Alaska or Delaware trusts.

(i) The due process clause of the 14th Amendment to the U.S. Constitution in general requires a forum court to have either personal jurisdiction over the trustee of the trust or in rem jurisdiction over the trust assets. See Hanson v. Denkla, 357 U.S. 235 (1958).

(ii) Presumably, so long as a trust has exclusively Alaska or Delaware trustees, those trustees have no contacts in the forum state, and all of the trust assets are held in Alaska or Delaware, a non-Alaska or non-Delaware forum state would fail to have jurisdiction over the trust. A national corporate trustee with offices in many states may effectively be subject to the jurisdiction of the courts of each of those states.

(iii) Note that a forum court that could legitimately exercise jurisdiction may decline to do so, either because the forum is not convenient or because the court does not want to interfere with the courts of another state.

(2) Conflicts of Laws.

(a) The issue: can a non-Alaska or non-Delaware forum court which has jurisdiction over the settlor of an Alaska or Delaware self-settled spendthrift trust created under one of these statutes, apply the law of the forum state rather than that of Delaware or Alaska? Consider In re Brooks, 1998 Bkrptcy, LEXIS 60, 1998 WL 30018 (B. Conn. 1998) discussed infra at VI under Conflict of Laws Issues. See the 2013 Washington State Bankruptcy court decision In Re Huber, discussed below.

(b) The Authorities.

1. As a general rule, a settlor of an inter vivos trust may create a spendthrift trust in another state and take advantage of that state's spendthrift trust laws. See Fratcher, Scott on Trusts §626 (1989) and Restatement (Second) of Conflict of Laws §273(b) (1971).

2. Note that the common law underlying the Scott and Restatement authority likely dealt with non-self-settled spendthrift trusts, as most states traditionally did not permit self-settled spendthrift trusts.

3. In at least one case, In re Portnoy, 201 B.R. 685 (S.D.N.Y. 1996), a U.S. court has ignored the foreign law (Jersey) incorporated into an offshore self-settled asset protection trust and instead applied New York law.

NOTE: There are dark clouds over DAPTS – There is no case law on critical Constitutional issues. However, with 11 states having such statutes and more on the way, full faith and credit and conflict of laws challenges are less likely in the future.

(3) Full Faith and Credit.

(a) The issue: if a non-Alaska or non-Delaware forum court which has jurisdiction over an Alaska or Delaware trust created under one of the statutes applies the forum state's own law and finds the spendthrift provisions invalid, must Alaska or Delaware recognize that judgment?

(b) The Authority.

1. The full faith and credit clause of Article IV of the U.S. Constitution requires that each state give full faith and credit to the judicial proceedings of every other state.

2. However, whether assets are exempt from the claims of creditors is determined by the law of the state where the assets are located. See Restatement (Second) of conflict of Laws §132 (1971). Therefore, when a creditor asks an Alaska or Delaware court to enforce a sister state judgment against the trust assets, the Alaska or Delaware court would use Alaska's or Delaware's exemption laws.

3. Note that in theory an Alaska or Delaware court could, under general conflicts of laws principles, decide that a sister state has a greater interest in the trust and apply that state's law, but query how likely this is given the clear legislative purposes of these statutes.

(4) "Supremacy Clause" Concerns.

Under the U.S. Constitution's Supremacy Clause, in Article VI, Section 2, federal courts are not bound by state laws. Accordingly there is a risk that if a judgment creditor is able to obtain jurisdiction over a judgment debtor or the debtor's assets in a DAPT by virtue of federal question jurisdiction or diversity jurisdiction, the creditor will have the opportunity to avoid the debtor-friendly provisions of the DAPT laws. The harsh provisions of the new federal bankruptcy laws discussed in K.(1)(a)(2) below are a particular threat to DAPTs.

(5) "Contract Clause" Concerns.

The Constitution prohibits states from enacting any law that impairs the obligation of contracts (in Article I, Section 10), and this clause was particularly intended to prevent states from enacting extensive debtor relief laws.

(6) Sham or Alter Ego.

A court outside the DAPT venue could invalidate the DAPT on the grounds that it is a "sham" or the "alter ego" of the Settlor, under legal precedents for such attacks.

K. Advantages and Disadvantages of Offshore Trusts Versus Alaska or Delaware Trusts.

(1) Advantages of Offshore Trusts.

(a) Legal.

1. Absence of full faith and credit. Some foreign jurisdictions will not honor judgments of United States courts, thereby forcing a creditor to relitigate its claims in the offshore jurisdiction. In contrast, Alaska and Delaware are required by the full faith and credit clause of Article IV of the U.S. Constitution to honor valid judgments of other states.

2. Shorter statutes of limitations for fraudulent conveyances. Some foreign jurisdictions have statutes of limitations for fraudulent conveyances of two years or less. In contrast, the Alaska and Delaware (and Utah and Rhode Island) statutes do not disturb the four year statutes of limitations for fraudulent conveyances generally applicable

in those states. The Nevada statute of limitations is two years. And generally these states have a "discovery exception" which allows a creditor to assert a fraudulent transfer attack after the expiration of the general statute of limitations for attacks "within one year (six months in Nevada) after the transfer was or could reasonably have been discovered by the claimant." But Alaska in 2003 adopted a statute that should curtail this exception and more certainly cut off claims four years after the transfer.

3. Offshore trusts are beyond the jurisdiction of U.S. bankruptcy courts and bankruptcy law. NOTE: The Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (P.L. 109-8) ("BAPCPA") substantially amended the Bankruptcy Code. Relevant to state asset protection trust statutes, the new Bankruptcy Act gives the bankruptcy trustees a 10 year look-back period in connection with alleged fraudulent transfers to self-settled trusts and "other similar devices," presumably including GRITS, GRATS, GRUTS, QPRTS, CRTS, and CLTS. Accordingly, whatever statute of limitation period Delaware, Alaska and other U.S. asset protection trusts jurisdictions adopt to limit challenges to the trust, the federal government has preempted state law with a federal 10-year statute of limitations. This development certainly damages U.S. APTs in a comparative analysis vis a vis offshore APTs, because U.S. courts would have to enforce the federal limit, while offshore courts might not.

Battley v. Mortensen, Adv. D. Alaska, No. A09-90036_DMD (2011). In this case in the U.S. Bankruptcy Court for Alaska, the judge set aside a transfer of real property to an Alaska asset protection trust as a fraudulent conveyance, even though the transferor Mortensen was solvent at the time of the transfer and even though Alaska's 4-year statute of limitations for reaching assets transferred to an Alaska asset protection trust had run. Needless to say the case has received a great deal of attention because of the cloud it casts over the effectiveness of DAPTs generally.

The Court applied the 10-year look-back rule and found intent to hinder, delay or defraud creditors.

A consolation and lesson taken from the case is that had Mortensen not voluntarily filed in bankruptcy, he would not have exposed himself to the federal 10-year look-back. So clients and planners should be cautioned over improvidently filing bankruptcy petitions when assets are protected by a DAPT.

In re Huber, 201 B.R. 685 (Bankr. W.D. Wash., May 17, 2013) is a very recent U.S. Bankruptcy Court decision which held that an Alaska self-settled trust essentially was invalid with respect to claims of the settlor's creditors in bankruptcy. See "Avoiding the Adverse Effects of Huber," by Jonathan D., Jonathan G., and Matthew D. Blattmachr, July 2013 Trusts & Estates.

The Court refused to apply Alaska law but instead applied the law of Washington, where the settlor lived, finding the contacts with Alaska so minimal and the contacts with Washington so substantial that Washington law applied. In Washington the Court found a strong public policy against self-settled spendthrift trusts.

The Court also permitted the bankruptcy trustee to invoke the 10-year look-back provision of Section 548(e)(1) of the Bankruptcy Code in light of the "badges of fraud." The Court also found under the authority of Bankruptcy Code Section 544 that transfers to the trust were invalid fraudulent conveyances under the state law of Washington.

Messrs. Blattmachr have elaborate suggestions for drafting and administering Alaska self-settled spendthrift trusts to avoid the result in Huber.

BAPCPA also limits generous "homestead" exemptions in Florida and Texas law to $125,000 if the debt in question arises from –

- violation of federal securities laws
- RICO civil penalties
- criminal acts
- intentional, willful or reckless torts
- misconduct causing serious bodily injury or death

But consider that many debtors do not file for bankruptcy, and do not need to, so the 10 year look-back rule in bankruptcy does not apply.

It is worth noting that Senator Schumer proposed an amendment to this Bankruptcy Act which would have imposed a limit of $125,000 on transfers to offshore or domestic asset protection trusts, but Senator Hatch of Utah, whose state has a new asset protection statute, opposed the amendment and it was defeated. This was a positive development for APTs, but especially for OAPTs.

4. Child support claims may not be avoided under certain circumstances in Delaware or Alaska, and spousal claims and certain tort claims may not be avoided in Delaware.

(b) Practical. A creditor's practical difficulties in both discovering the existence of a trust and its underlying assets and instituting legal proceedings against it are far greater with offshore trusts than with Alaska or Delaware trusts.

(2) Disadvantages of Offshore Trusts

(a) Concerns about economic stability of the selected jurisdiction.

(b) Concerns about political security of the selected jurisdiction.

(c) Substantial IRS-mandated reporting requirements for foreign trusts with U.S. beneficiaries.

(d) Cost vs. Benefit – It is probably not worth establishing an OAPT to hold less than $1-$2 million. The set-up and maintenance fees will be too expensive.

(e) With the IRS crackdown on tax fraud through OAPTs and the consequent elaborate reporting requirements by both settlors and trustees (FATCA), many offshore trust companies are wary of establishing trusts for US taxpayers, or refuse to, or if they will, must pass through in increased fees the cost of compliance with US

government reporting.

L. Potential Uses for Alaska or Delaware Self-Settled Spendthrift Trusts.

(1) Encourage Lifetime Gifting Programs. Although the transfer tax benefits of lifetime gifting programs are well documented, even very wealthy individuals may be reluctant to part with assets in the face of uncertain future needs. If it is possible for a donor to create an irrevocable trust, make a completed gift to the trust for gift and estate tax purposes, and nevertheless retain the possibility of receiving distributions from an independent trustee at the trustee's discretion in the event of financial need -- and this tax issue is not free from doubt -- this may help motivate the donor to make additional gifts in a more traditional fashion. If the donor becomes comfortable with the idea that this trust could be a safety net in the event of financial need, the donor may be less reluctant to make additional gifts for traditional estate planning purposes. If such a result becomes confirmed in tax law, Delaware and Alaska would have a very powerful attraction in offering the possibility of (a) transferring property out of the grantor's taxable estate, (b) while retaining the grantor as a discretionary beneficiary, (c) while protecting the assets from the grantor's creditors.

(2) Possible Coupling with Traditional Irrevocable Trusts. The statutes may prove useful not only with perpetual dynasty trusts but also with, for example, Crummey trusts, grantor retained annuity trusts after the annuity interest expires or charitable lead trusts after the charitable interest ends.

(3) Possible Legitimate Protection from Certain Future Creditors. Because the statutes permit a trust to be irrevocable but not necessarily a completed gift for gift tax purposes (when, for example, the settlor retains a limited testamentary power of appointment), these trusts could be used as asset protection vehicles apart from estate planning vehicles, subject to the general U.S. asset protection limitations discussed above. An individual seeking professional investment management may see a benefit to hiring a Delaware or Alaska corporate fiduciary to manage assets as trustee of an irrevocable trust, and obtaining possible protection from future creditors that would be unavailable were the individual's account managed outside of those states which have adopted DAPT statutes.

(4) Perpetual Duration. The fact that trusts may be established in Delaware and Alaska for perpetual duration offers an opportunity that even most offshore jurisdictions do not afford.

(5) For Foreigners. See page 70 below and the article by Mark Holden cited there.

(6) If a debtor in trouble has used a U.S. asset protection trust, he might consider moving to the state of trust situs in hopes of receiving a more sympathetic hearing from local judges.

M. Continuing Evolution of U.S. Asset Protection Statutes. It must be said that with the continuing evolution of DAPTs, each year new states adopting DAPT statutes more aggressively pro-debtor than those which have gone before and with older statutes constantly evolving to be more pro-debtor, more serious consideration should be given to DAPTs, particularly where offshore trusts are for whatever reason not to be considered. But the almost total lack of case law on the efficacy of DAPTs continues to discourage reliance on them where OAPTs may be used.

V. IS IT WISE FOR THE FOREIGN ASSET PROTECTION TRUST TO HAVE U.S. CONTACTS?

See Exhibit 3 attached, the author's article from the Journal of Asset Protection, May/June 1996, "No U.S. Connections Allowed With an Offshore Trust? Wrong! Use Onshore Contacts."

VI. HOW CREDITORS ATTACK FOREIGN ASSET PROTECTION TRUSTS AND THOSE WHO ESTABLISH THEM: HOW TO PROTECT AGAINST SUCH ATTACKS

As a preliminary matter keep in mind Gideon Rothschild's reassuring words in the June 16, 2005 ALI-ABA Program: "There never has been a successful seizure of assets held in an offshore asset protection trust." So far as the author is aware, that statement continues to be accurate.

U.S. creditors and U.S. courts are not without recourse when it comes to attacking offshore trusts and those who create, or seek to create, them. Interestingly, Ron Rudman, who with his partner in the law firm of Engel and Rudman invented the U.S. law practice of offshore asset protection trusts when they were involved with the drafting of the first such statute for the Cook Islands in 1989, later separated his practice from Engel and concentrated his practice on the representation of creditors seeking to recover assets offshore. He admitted that his livelihood depends on clients and lawyers who try to do effective offshore asset protection trust planning but either do not know how to or fail to attend to all details.

The following are some instructive case citations with brief comments. Notice that almost every celebrated case in this area reflects a combination of bad facts and terrible lawyering.

U.S. v. Matthewson, 93-1 U.S.T.C., CCH ¶ 50, 152, wherein the court injunctively

restrained the defendant from leaving the U.S., in effect holding him under "house arrest" in the U.S. to keep him from moving himself and his assets to the Caymans. He owed $5 million in back taxes to the I.R.S. The Court upheld a writ of Ne Exeat Republica, which Latin scholars will recognize as a writ to detain a resident from leaving the U.S. to enable the Government to have discovery, both on issues of liability and with respect to the location, value and legal status of taxpayer property.

Securities and Exchange Commission v. Giuseppe B. Tone, et al. and Certain Purchasers of the Common Stock of St. Joe Minerals, 638 F. Supp. 596 (S.D.N.Y. 1986), aff'd 638 F. Supp. 629 (2d Cir. 1987), and S.E.C. v. Certain Unknown Purchasers of Common Stock of Santa Fe Resources, Fed. Sec. L. Rep. (CCH) p. 99, 424 (1983), and S.E.C. v. French, et al., 817 F.2d 1018 (2d Cir. 1987). These are related cases wherein a federal judge ordered that all accounts held by a Swiss bank in the U.S. be frozen pending disclosure of information from the Swiss bank. The judge also ordered substantial daily fines pending disclosure of the information.

S.E.C. v. Levine, 1986 U.S. Dist. LEXIS 24576; Hercules Incorporated v. Leu Trust and Banking Limited, a Bahamian Corporation, and Bank Leu, a Swiss Corporation, 611 A.2d 476 (Del. 1992); and Litton Industries, Inc. V. Dennis Levine, et al., 767 F. Supp. 1220 (S.D.N.Y. 1991). American authorities were able to persuade the American branch of a Swiss bank parent corporation to provide information on Mr. Levine's large bank account with a Bahamian subsidiary of the Swiss bank, notwithstanding Bahamian bank secrecy law.

U.S. v. Bank of Nova Scotia, 740 F.2d 817 (11th Cir. 1984). The Miami branch of the Bank of Nova Scotia suffered daily fines of $25,000 pending receipt of information from the Bahamian branch of the same bank. The Miami branch cooperated.

Orange Grove, in the High Court of the Cook Islands. In this case in which Barry Engel characterized the decision as an example of "bad facts make bad law," creditors obtained a California judgment against a debtor and made an application in the Cook Islands for a Mareva Injunction (which is like a Temporary Restraining Order in the U.S.) to restrain parties from removing the administration of the trust and any property from the jurisdiction of the Cook Islands. The Court granted a temporary Mareva Injunction. The initial Mareva Injunction was set aside as not having been brought timely. On appeal the Mareva Injunction was reinstated and the creditors were permitted to proceed against the international trust. The Court made a controversial ruling on when the creditors' cause of action accrued for purposes of determining the statute of limitation, after which, a Cook Islands trust cannot be assailed.

The creditors were still left with the burden of proving beyond a reasonable doubt that the trust was created with intent to defraud them.

The funding of the trust left the settlors insolvent.

Barry Engel pledged to amend Cook Islands law to clarify the issue which he believed the Court misconstrued, but I am not sure whether that has ever happened.

Brown v. Higashi, U.S. Bankr. Court for the District of Alaska, No. 95-3072 (1996). The bankrupt had set up an offshore trust in Belize. The case considered whether the assets in the offshore trust were included in the debtor's bankruptcy estate. The Court concluded that the trust was a sham, and the assets of the trust were found to be part of the bankrupt's estate. This was another case with very bad facts for the bankrupt.

In re Portnoy, 201 Bankr. 685, 1996 Bankr. LEXIS 1392. The debtor Portnoy transferred virtually all of his assets into an irrevocable offshore trust in Jersey at a time when he knew his personal guaranty was about to be called. The party to whom the guaranty was given brought a New York lawsuit against Portnoy. Portnoy was the "principal beneficiary" of the trust. The Court cited numerous occasions on which Portnoy and his wife were not truthful or credible in their dealings with creditors and the Court. These facts were viewed by the Court as being indicia that Portnoy was intentionally attempting to hinder and delay his creditors. The Court denied his discharge in bankruptcy. There is no indication that the creditors ever pursued the assets in Jersey. See also in re Brooks, 217 B.R. 98 (Bankr. D. Conn. 1998).

Grupo Torras, S.A. v. S.F.M. Al-Sabh, Chemical Bank & Trust (Bahamas) and Private Trust Corp., (Sawyer, J.) (Sup. Ct. of the Bahamas, Sept. 1, 1995). Kuwaiti Sheikh Fahad obtained assets through illegal means and then transferred those assets to Bahamian trusts. Creditors sought to set aside the transfers to these trusts. The Court emphasized that the protections to a settlor made available through the use of Bahamian trusts would not apply to assets that the settlor did not legitimately own at the time of the transfer to trust.

In a recent outline on "international asset recovery" Ronald L. Rudman makes the following observation:

"In cases involving claims brought against American settlors or debtors, there may be no necessity to resort to foreign courts in the event the planner and settlor have selected a major international bank as the trustee of the trust or the depository for trust assets. This is due to the increasingly extraterritorial reach of the U.S. courts. A growing body of law in the United States now clearly provides that a foreign parent or affiliate of a bank or other entity operating within the U.S. must disclose any information in its possession outside of the United States, pursuant to a U.S. court proceeding, even if such disclosure would constitute a criminal violation of the confidentiality or other laws of the foreign parent or affiliate's domicile. This is true even though the domestic U.S. entity is not even a party to the subject litigation. This trend creates the potential for extension to

the compulsion of further acts, beyond the mere disclosures of information."

He cites Societe Nationale Industrielle Aerospatiale v. U.S. District Court, 482 U.S. 522, 107 S. Ct. 2542 (1987), United States v. First National City Bank, 379 U.S. 378 (1965), United States v. Vetco, 691 F.[2d] 1281 (9th Cir. 1981), and Richmark v. Timber Falling Consultants, 959 F.[2d] 1476, in addition to United States v. Bank of Nova Scotia, cited above.

Conflict of Laws Issues.

Offshore trusts denominate the law of the trust's domicile as governing the interpretation and administration of the trust. Such a provision may not be given effect by courts of other jurisdictions, or even courts of the trust's domicile, with respect to issues relating to the funding of the trust, particularly where fraudulent conveyance is alleged. The Hague Convention dealing with the recognition of foreign trusts treats the funding of the trust as a preliminary matter outside the scope of the Convention and therefore a matter of local law.

In the U.S., courts hearing a creditor claim will apply public policy tests to apply the law least offensive to U.S. public policy, which will invariably be U.S. law. In Dearing v. McKinnon Dash & Hardware Co., 165 N.Y. 78, 58 N.E. 773 (1900), the New York court stated:

"Judicial comity does not require us to enforce any clause of the [trust] instrument, which even if valid under the lex domicili, conflicts with the policy of our state relating to property within its borders, or impairs the rights or remedies of domestic creditors ..."

In a very recent case, In re Brooks, 1998 Bkrptcy., LEXIS 60, 1998 WL 35018 (C. Conn. 1998), the Connecticut bankruptcy court held that certain assets transferred by the debtor to his wife, which she in turn transferred to offshore trusts, naming the debtor as the beneficiary, were property of the debtor's bankruptcy estate. In 1990, in an alleged estate planning exercise, debtor transferred corporate stock certificates to his wife who, within days, transferred them to offshore trusts in Jersey (Channel Islands) and Bermuda. The trusts designated Jersey and Bermuda law as controlling, contained spendthrift clauses and named the debtor sole beneficiary. In 1991 an involuntary Chapter 7 bankruptcy petition was filed against debtor, which was converted to a Chapter 11.

The court concluded that the trusts were self-settled by the debtor. The court dismissed the ideas that the wife settled the trusts and that they were motivated by estate planning considerations, not asset protection. The wife was viewed as debtor's agent in a scheme to protect the assets from creditors but leave the debtor with the income.

Importantly, the court determined the enforceability of the spendthrift provision

under Connecticut law and found that Connecticut law did not acknowledge the validity of self-settled spendthrift trusts. Should the court have applied Jersey and Bermuda law, which recognize self-settled spendthrift trusts? Would a Connecticut court take a similar view of Delaware or Alaska self-settled spendthrift trusts? Were the facts just too bad?

One may not even assume the law of the situs of real estate will govern where fraudulent conveyance is alleged. In James v. Powell, 19 N.Y. 2d 249, 225 N.E. 2d 741 (1967) a New York court warned that "if, in exploring the law of Puerto Rico [regarding the transfer of land situated in Puerto Rico], it were to be found that it was specifically designed to thwart public policy of other states ... by denying a remedy to all judgment creditors ... in order to attract foreign investment in real estate, the courts of this State would be privileged to apply the law of New York rather than that of Puerto Rico."

As noted above in citing In re Portnoy, the bankruptcy courts will apply a similar standard. In Hong Kong and Shanghai Banking Corp., Ltd. v. HFH USA Corp., 805 F. Supp 133 at 140 (W.D.N.Y. 1992), a Federal District Court applied the law most favorable to the creditor, remarking that a choice of law provision "will not be regarded where it would operate to the detriment of strangers to the agreement, such as creditors or lienholders." See also Broadcasting Rights Int'l Corp. V. Societe du Tour de France, 675 F. Supp. 1439 (S.D.N.Y. 1987), Carlson v. Tandy Computer Leasing, 803 F.[2d] 391 (8th Cir. 1986) and Ferrari v. Barclays Business Credit (In re Morse Tool, Inc.), 108 B.R. 384 (Bankr. D. Mass. 1989).

The Anderson Case and Its Progeny.

Federal Trade Commission v. Affordable Media, LLC, and Denyse and Michael Anderson, 179 Fd 1228 (9th Cir., 1999) (commonly referred to as the "Anderson" case), is a very important case for the lawyer practicing in the area of asset protection planning and the client considering implementing an asset protection strategy.

In 1995 Mr. and Mrs. Anderson established an irrevocable Cook Islands trust, with Asiaciti Trust Limited as the foreign situs trustee. The original beneficiaries of the trust were their children, but some six months after establishing the trust the Andersons were added as beneficiaries. This was their first major mistake. The Andersons initially served as co-trustee and as trust protector. This was their second major mistake. The trust contained "event of duress provisions." According to the General Manager of Asiaciti Trust, it conducted "its usual due diligence procedures to ensure that the property being settled on the trust was neither the result of a fraudulent conveyance nor derived from any illegal activity." (See Anderson Case - The Offshore Trustee's Perspective, by Adrian L. Taylor, Esq., in the May/June 2000 issue of the Journal of Asset Protection, hereinafter cited as "Mr. Taylor's article."

The property settled in the trust included a nominal amount of cash and a 98%

interest in a U.S. corporation, The Anderson Family LLC (Anderson LLC). Anderson LLC carried on business in the U.S. as a telemarketer. From 1995 through May 1997 Anderson LLC made regular distributions to the trust in accordance with the operating agreement.

Sometime after April 1997, two years after the Cook Islands trust was created, Mr. and Mrs. Anderson became involved in a telemarketing venture that offered investors the "opportunity" to invest in $5,000 "media units," each of which consisted of 201 commercials to be aired on late night television. Investors were to receive a share of each product sold as a consequence of the commercials composing their media units, and extraordinary returns were described. In fact, the investments were simply a Ponzi scheme. According to the FTC, in its enforcement action brought in April of 1998, investors lost some $13 million and the Andersons pocketed $6.3 million in commissions. Further distributions to the Cook Islands Trust were made by Anderson LLC from June 1997 to February 1998 and it is these later distributions that the FCC challenged, for in April 1998 the FTC obtained an ex parte temporary restraining order (TRO) against the Andersons. The TRO had the effect of freezing all assets owned by the Andersons and required the Andersons to repatriate to the U.S. all assets held by them outside of the U.S. A federal district court incorporated the terms of the TRO into a preliminary injunction in May 1998, prior to any judgment in regard to the alleged wrongdoing against the Andersons, and through the end of 1999, according to Mr. Taylor's article, no judgment had been entered against the Andersons.

The Andersons faxed the TRO/Preliminary Injunction to Asiaciti Trust demanding repatriation as required. In May 1998 Asiaciti Trust, on advice of counsel, refused because --

- the TRO constituted "duress" under the terms of the trust;

- under the trust duress automatically triggered removal of the Andersons as trustees, leaving Asiaciti Trust the sole trust;

- because the Andersons' children were also beneficiaries, Asiaciti refused to disburse, viewing its responsibilities as running impartially to all beneficiaries. The District Court ordered the incarceration of the Andersons for civil contempt in June, 1998, rejecting their defense of impossibility of performance. The Andersons appealed, and their appeal from the finding of civil contempt was the issue before the 9th Circuit. The Court of Appeals affirmed the District Court.

The Court of Appeals described three issues for its review of the contempt finding: 1) it reviewed the civil contempt order for abuse of discretion; 2) it reviewed the trial court's findings of fact for clear error; and 3) it reviewed the trial court's rejection of an impossibility defense proffered by the Andersons for clear error. The third issue was

pivotal and the Court of Appeals held that the defendants had not satisfied their burden of proving the affirmative defense.

The court cited precedent that stated that the party claiming impossibility as a defense to civil contempt must show "categorically and in detail" the nature of the alleged impossibility. The appellate court cited the fact that the Andersons were protectors of their own trust, standing alone, as an appropriate basis for a finding that they had not satisfied their burden of proof, and the West Publishing key number system cites the case under "Trusts key number 153" for the proposition that "A protector of an offshore trust can be compelled to exercise control over the trust to repatriate assets if the protector's powers are not drafted solely as the negative powers to veto trustee decisions or if the protector's powers are not subject to the anti-duress provisions of the trust." But the court's holding extends beyond that relatively narrow issue of drafting.

The court held that in the asset protection context, the burden of proof for the party asserting the impossibility defense is "particularly high," at least in part because of what the court characterized as a "likelihood" that any attempted compliance with court orders will be a mere charade. Together, the requirement that impossibility be proved "categorically and in detail" and the "particularly high" burden of proof give a trial court considerable latitude in which to reject the impossibility defense. Because of the limited ability of parties to appeal a trial court's finding of fact, assuming the trial court applied the correct standard, beneficiaries of offshore protection trusts may have considerable difficulty in avoiding contempt, at least in the 9th Circuit, even if the trust avoids the particular drafting pitfalls present in the Anderson case.

Although arguably *dicta*, the Court of Appeals expressed "skepticism" that a rational person would send millions of dollars overseas and retain absolutely no control over the assets, and it cited the fact that the Andersons were able to obtain approximately $1 million to pay taxes as evidence that they retained some measure of control.

In *dicta*, the court went considerably further and speculated that a "self-induced" impossibility might not be a defense at all. Although it left that "more difficult question" for another day, because it was able to dispose of the appeal on the grounds that the defendants had not met their burden of proof, the court suggested that it would not regard such self-induced impossibility to be a defense. Obviously, such a finding would vitiate one of the key defense strategies touted for offshore asset protection planning.

Three points should be noted. First, the fact that the Andersons established their offshore asset protection trust approximately two years before the conduct that gave rise to the claim against them and the fact that the court does not mention any evidence suggesting that the creation of the trust otherwise made them insolvent indicates that conventional fraudulent conveyance theory played no part, explicit or implicit, in the outcome. Second, building on the court's analysis regarding payment by the trust of the

Andersons' tax liability, so long as the judgment creditor could show evidence of payments for the benefit of the judgment debtor after the event of duress, it would seem that a trial court could always find evidence tending to refute the affirmative defense of impossibility that would justify a finding that the proponent of the defense failed to meet his burden of proof. Thirdly, it was a mistake for the Andersons (or anyone under their control) to serve as Trustee or Protector, and it gave a bad flavor to the facts that the Andersons themselves were added as beneficiaries after the trust was executed.

Subsequently the Andersons were released from jail on the condition that they would appoint a new trustee and new protector of the Cook Islands trust. They attempted to do so. However, the Cook Islands High Court refused to recognize the Anderson's appointed -- and FTC-controlled -- trustee and protector. (See Butterworths International Trust and Estate Law Reports at 2 ITELR 482.) The Court's rejection of the new trustee was mandatory under the terms of the trust documents. The High Court determined that the FTC was an "excluded person" and therefore its nominee was also. Undoubtedly at least in part because of the High Court decision in the Cook Islands, and upon motion of the FTC, the preliminary injunction was amended to keep funds under the control of the foreign court except for the payment of legal fees and administrative costs. Additionally, the registrar of the High Court of the Cook Islands was made a signatory on the trust account.

The FTC also initiated proceedings in the Cook Islands, but ruling that the statute of limitations under Cook Islands law had expired, the FTC was denied recourse and assessed costs. The FTC appealed again, and High Court in the Cook Islands in December of 2001, following English common law, refused to enforce what it considered a "penal" law of the U.S., which was the basis of a monetary judgment against Settlors for false representations and deceptive practices under the FTC Act. Interestingly, the Court cited two U.S. cases in support. It is understood that a settlement has recently been reached in the Anderson case for $4 million.

Summary

Although the procedural posture of the Anderson case somewhat limits the actual holding, both the District Court and the Court of Appeals demonstrated considerable antipathy to offshore asset protection planning. In its holding, the court stated that the burden of proof to assert impossibility as a defense to civil contempt is "particularly high" in asset protection cases and found that the defendants failed to meet it. In dicta, the court challenges the fundamental premises of asset protection planning by suggesting that an impossibility defense to a charge of civil contempt (for failure to repatriate assets held overseas) may be unavailable when the alleged impossibility is "self-induced," and the court's opinion expresses skepticism generally about allegations of impossibility.

Cases Subsequent to Anderson.

Two cases in 2000 purportedly follow Anderson--one in the 8th Circuit and one in the 11th. Chicago Truck Drivers Union Pension Fund v. Brotherhood Labor Leasing, 207 F.3d 500 (8th Cir. 2000) cites Anderson for the proposition that a party asserting an inability to comply with a court order as a defense to civil contempt must show (1) "categorically and in detail" the nature of the inability and (2) the inability must not be self-induced. The court cited a line of cases from 1991 and earlier for the second proposition, e.g., In Re Power Recovery Systems, Inc., 950 F.2d 768 (1st Cir. 1991), at 803. Chicago Truck Drivers Union is not an asset protection planning case; rather the judgment debtor was basically arguing that he could not pay because he spent all the money.

The second case in 2000 citing Anderson is an asset protection planning case. In In Re Lawrence, 238 B.R. 498 (U.S. Bankruptcy Ct., S.D. Florida 1999) the debtor failed to comply with a "Turnover Order" entered by the court and the Trustee sought civil contempt. Much like the Anderson case, the trust -- in this case a Mauritian Trust -- appears to have been inartfully drafted, and the debtor was apparently as bad a witness as it is possible to imagine, so the case is not one that the asset protection planning bar would choose to showcase. The court characterized Mr. Lawrence's sworn testimony as "shockingly less than candid." That said, the court found that the debtor failed to carry his burden of proof regarding impossibility and it expressly based its finding on the entire record, including the court's refusal to believe that the debtor would give up control over 90% of his liquid assets to a stranger on the far side of the earth. The court cites Anderson for the "particularly high" burden of proof in such cases and Pesaplastic, C.A. v. Cincinnati Milacron Co., 799 F.2d 1510 (11th Cir. 1986) for the proposition that impossibility is not recognized when the impossibility is self created. *The court appears to hold as a matter of law that impossibility is unavailable because the trust was the debtor's own, voluntary creation. Lawrence, at 501.* In this case the court hammered the debtor--$10,000/day fine (beginning immediately) and incarceration in approximately two weeks if he did not turn the money over. Unlike Anderson, the bankruptcy context does not appear to leave any question as to the substantive merits of the underlying "turnover order." Mr. Lawrence's most obvious problem with the Court was that the Court concluded that he systematically and shamelessly lied throughout the proceedings. So far as the author has been able to determine, there has been no recovery of assets by creditors from Mr. Lawrence's Trust in Mauritius. However, Mr. Lawrence apparently spent at least 27 months in jail for contempt, and may still be there. See Lawrence v. Goldberg, 279 F.3rd 1294 (11th Cir. 2002).

The July 2004 issue of Trusts & Estates contained a very interesting article by Wendy Davis on "Asset Protection's Bad Boy," who is this Stephen Jay Lawrence. He has been in jail for contempt of court in a bankruptcy case because of planning he did involving a Mauritius asset protection trust he created and funded with $7 million in 1991, Bear Sterns obtaining a $20 million judgment against him in 1991. Lawrence

battled against the judgment until 1997 when he filed for bankruptcy. In 1993 he had amended the trust to add a "duress" clause, directing the Trustee to ignore all instruction from him made under coercion, including "from a process of law for the benefit of his creditors." In 2002 the Eleventh Circuit Court of Appeal ruled Lawrence's "impossibility of performance" defense to contempt of court findings for not repatriating the trust was invalid, because he created the impossibility when he amended the trust. All courts involved in his case also expressed the belief that he could repatriate the funds if he wished to.

He apparently is relying on the Elizabeth Morgan precedent that he will eventually be released. Elizabeth Morgan went to jail for years for hiding her daughter (in New Zealand it turned out) in a child custody dispute case.

The article's author quotes a critic of offshore trusts, Jay Adkisson, as reporting that about six contempt cases in OAPTs have gotten to court in the U.S. and "no court has ever denied to hold a debtor in contempt for [ignoring] a repatriation order. Creditors are batting 1,000." Contrast this with Gideon Rothschild's quote on page 44. This is a classic example of the adage that the glass is either half full or half empty depending on your perspective. This is frankly an anomaly: there are many harsh US judicial decisions attacking offshore asset protection trusts, but in no case has there been a recovery from the offshore trust by the US creditor except by voluntary settlement with the debtor. Consequently it may be said that even fraudulent transfers to offshore asset protection trusts "work."

MOST RECENT CASES

The Brennan Case

Robert Brennan, who frequently appeared in TV ads for his brokerage firm, First Jersey Securities, in the 1980's, has had ongoing legal battles with the SEC and other federal and state regulators for more than a decade. The SEC has charged him with fraud civilly and criminally and has attempted to have him held in contempt. The U.S. Government has admitted to spending over $1 million in costs in its effort to trace any attempt to recover $45 million Brennan allegedly transferred to offshore trusts and "various tax havens."

The first SEC action for fraud was filed in 1985, and after trial in 1994 it obtained a judgment against Brennan in the amount of $75 million. In 1993-1995 Brennan established three offshore trusts in Gibraltar with a total value of some $25 million. Brennan's sons and his charitable foundation were beneficiaries of the trusts. Brennan himself has a reversion after 10 years, or later if the Trustee determines. Under the flight clause the trust was subsequently moved first to Mauritius, then to Nevis.

Brennan's bankruptcy trustee has filed suit in Nevis, so far without success.

In 2000 state and federal prosecutors brought criminal fraud charges against Brennan, for which he went to trial in 2001. The charges were bankruptcy fraud and theft, money laundering and obstruction of justice. He was convicted and was given a five-year sentence without parole and the obligation to make $4.6 million in restitution payments.

Brennan's lawyers have denied fraud in the establishment of the trusts, defending them as legitimate estate planning devices in light of Brennan's family circumstances.

An interesting feature of the Brennan case was the cooperation received by the U.S. attorney prosecuting the case from Isle of Man authorities, who were described by the prosecutor as "quite helpful." A Manx court ordered Peter Bond, who managed Brennan's offshore companies through Valmet in the Isle of Man, to give evidence. His testimony in a New Jersey courtroom helped convict Brennan. The Bank of Scotland, which claimed it was an "unwilling conduit" for the sale of $4 million in hidden bearer bonds by Brennan, also cooperated with prosecutors.

On the other hand, in 2000 a U.S. federal appeals court held that one of Brennan's overseas asset protection trusts could not be invaded by creditors, and a jury failed to convict him on another count of bankruptcy fraud relating to his failure to disclose over $500,000 of Mirage casino chips. Brennan has apparently agreed to repatriate another $20 million in a Gibraltar asset protection trust, but that agreement may or may not be approved by a Gibraltar court. The author understands that this case has recently settled under confidential terms and that most of Brennan's secreted assets remain protected offshore.

At least three important points should be gleaned from Brennan and Anderson: (1) all bets are off if the creditor sought to be avoided is the U.S. government, and most bets are off if the creditor is a powerful and motivated corporate entity, like a U.S. bank, as in the Weese case cited below. These have resources, tenacity and influence other creditors do not; and (2) even in those cases, the government's vast efforts apparently did not yield complete recovery, so the Trusts "worked," at least to some extent, as the debtors hoped; and (3) bad facts made "bad law" in all of these cases.

Other Cases

In Re Coker, 251 B.R. 902 (Bankr. M.D. Fla. 2000). Prior to filing bankruptcy Cokers established an OAPT. The Court ruled that OAPT funds should be turned over to trustee. Cokers cite impossibility. Citing Lawrence and Affordable Media (Anderson) the court held the Cokers could not use the defense of impossibility when the impossibility was self-created. Debtors held in contempt. (The creation of the OAPT was done at the "11th Hour.")

SEC v. Bilzerian, 112 F. Supp. 2d.12 (DC 2000). Mr. Bilzerian was convicted of

securities fraud and conspiracy to defraud the U.S. SEC filed civil suit, obtained judgment and an order in 1993 forcing Bilzerian to disgorge $33 million. Two years after disgorgement order he established a Cook Islands Trust and transferred $15 million to it. He was a beneficiary but removed as beneficiary by trust protector in 1998. He argued "financial inability" to meet the disgorgement order. The court held Mr. Bilzerian to an "especially high" standard in his impossibility defense. When he failed to provide the court with a copy of the trust, the court questioned whether he held an indirect beneficial interest. The District Court found him in contempt and incarcerated him. The trust was not repatriated.

Eulich v. U.S. (N.D. Tax Case No. 99-CV-01843, August 18, 2004) In the early 1990s Mr. Eulich established an OAPT in The Bahamas with $100 million (possibly to avoid U.S. taxes). IRS asked for information, he said he could not obtain information. Court refused to accept impossibility as a defense because it was self created and required the Settlor to sue for the information in Bahamian Courts. Eventually fine of $10,000/day imposed for failure to produce documents.

Federal Trade Commission v. Ameridebt, 373 F. Supp. 2d 558 (D. Md. 2005) There was an FTC investigation of Ameridebt and Mr. Pukke, its controlling shareholder, for allegedly defrauding consumers. After learning of the FTC investigation in 2002, Pukke made transfers to friends and relatives and established trusts in Delaware, Nevis and Cook Islands. Court required defendants to turn over assets to a receiver during pendency of investigation to avoid prejudicing FTC's ability to recover. A federal district court stated that plaintiff FTC could move for contempt if the defendant failed to comply with a repatriation order, allowing that the defendant would be free to argue an impossibility defense.

U.S. v. Grant, 2013 WL 1729380 (S.D. Fla. April 22, 2013). In this case, an 84-year-old widow was held in contempt for receiving money indirectly from her offshore trusts in Bermuda and Jersey while she was subject to a US tax deficiency. Each trust provided for the annual payment of trust income to her. Before he died, she and her husband had incurred a $36 million tax liability to the IRS. The IRS doggedly pursued her and her trusts without success until it discovered that trust funds were flowing through US bank accounts of her children to fund her living expenses. The court found her in contempt and ordered her to request and turn over income distributions from the trusts, forbidding anyone in her family from communicating to the trustee that her requests for distributions were made under duress.

This case reaffirms two realities: (1) even the IRS cannot get at offshore trust assets directly; and (2) that the US federal government is a "super creditor" with powers to compel payments that no other creditors have.

Morris v. Wroble, Case No. CIV-06-80479 (S.D. Fla.) aff'd. Appeal No. 06-80452-CV-

DTKH (11th Cir. Nov. 16, 2006) Mrs. Morris executed a post-nuptial agreement with her husband which provided for a $1.5 million payment and contained an non-contestability clause providing that she would forfeit the payment if she ever contested the agreement. In 2001 they divorced, and she received a $1.5 million payment. In 2003 she brought an action which she claimed was not a contest, but the court determined it was a contest and ordered her to repay $1.5 million plus costs and attorneys' fees. While appealing she transferred most of her assets to a Cook Islands Trust. Court found the transfer fraudulent and ordered her to repatriate. When she refused to appear and fled the jurisdiction, she was found in criminal contempt and her appeal was dismissed.

The Weese/Bibelot vs. Allfirst Bank and Bank of America Case in Baltimore

In the spring of 2001 Allfirst Bank and Bank of America, claiming they were owed millions of dollars by the owners of the bankrupt Bibelot Bookstores in Baltimore, the Weeses (heirs to the Rite-Aid fortune), filed suit to recover the debts and an injunction seeking to force the Weeses to give creditors access to an estimated $25 million in assets in offshore trusts. The claim by the banks was that the Weeses, in transferring assets to a Cook Islands asset protection trust, had committed a fraudulent conveyance with intent to hinder, delay or defraud their creditors. The banks' claim was that the Weeses had assets to pay their debts when they fell due.

In 2000 a $17 million promissory note by Bibelot personally guaranteed by the Weeses fell due. Subsequently a judgment was entered against the Weeses for repayment of the loan. Months later Bibelot filed for bankruptcy. After the Bank of America note was due the Weeses borrowed another $1.6 million from Allfirst. Within a month thereafter, in July of 2000, Bank of America initiated arbitration proceedings. On the day they entered into arbitration proceedings with the Bank the Weeses created a Cook Islands trust with Cook Islands Trust Ltd. and Mrs. Weese's father as Co-Trustees and transferred $25 million of assets to it. Among the assets transferred to the trust were a Baltimore house appraised at $3 million, which was transferred in consideration of a $10 payment. At the time the house was security for a $1.7 million loan from Wachovia. The Weeses subsequently consented to the entry of an arbitration award for $17.6 million.

The Weeses were apparently represented in the creation of the trust by Allan Gibber, a well-known, respected practitioner and author of the definitive treatise on Maryland probate law. Mr. Gibber, in turn, apparently engaged the services of Barry Engel as special counsel to assist in the creation and funding of the Cook Islands trust.

The bank creditors pursued litigation in both Maryland and overseas. In fact, trial was scheduled in New Zealand for February 2003 in the Cook Islands case. The debtors defended the establishment and funding of the Cook Islands trust by general and vague allusions to "estate planning" and "providing for the children." The trusts are grantor trusts includible in the Grantor's estate. Settlor Elizabeth Weese's father was initial Co-Trustee with Cook Islands Trust Company, and as between the two, his authority was

governing. Elizabeth Weese was initial protector with authority to veto any decision of the Trustee.

In the past year there were two important decisions in the Weese case, both going against the Settlors. First, the High Court in the Cook Islands rejected the Trustees' and Settlors' claim that the privacy provisions of the International Trust Act prevented a plaintiff from obtaining discovery of documents. Second the Court of Appeals upheld the High Court's denial of a claim of attorney-client privilege attaching to certain specified documents because it ruled a prima facie case of fraud had been established. Apparently a Mareva injunction was obtained freezing the trust assets.

A settlement was ultimately reached in this case in which substantial funds were paid to the creditor bank by Settlor's father, who apparently purchased his daughter's note at a discount. Again, at least to some extent, the trust "worked."

Interestingly, the Settlor of the Weese Trust is the daughter of former Rite-Aid CEO Martin Grass, who recently plead guilty to what the Wall Street Journal characterized a "massive accounting fraud." Reportedly Martin Grass bought the bank note due from his daughter for a very substantial payment to settle this matter.

Also very interesting is the fact that the Plaintiff U.S. bank creditors who brought suit in the Cook Islands applied for discovery of certain documents in the drafting attorney's file which the defendant and counsel tried to protect as privileged. The Court refused to uphold the attorney-client privilege of the documents because it found that the client's interest in seeking legal advice was to further a crime or fraud. The Court found that it was not relevant to its ruling on the privilege issue whether or not the attorney was cognizant of the client's nefarious purposes. In effect, the Court invoked the crime/fraud exception to the attorney-client privilege, taking in fact an expansive view that there is no privilege not only where there is fraud, but even "where there are commercial practices or business dealings that would readily be described as dishonest to the point of fraud by a reasonable businessman." The Court did require a "strong prima facie case of fraud or dishonest purpose or a strong probability there was fraud" and found that test met in this case. The Court found that the asset protection trust statute did not modify this privilege rule and quoted with approval another Cook Island case: "It should not be lightly assumed that Parliament intended to defeat the claims of creditors by allowing international trusts to be used to perpetuate a fraud against a creditor."

Weitz v. Weitz, 2012 NY Slip Op. 30767 (U), N.Y. Sup. Ct No. 016811-08 (March 22, 2012). In a divorce proceeding that involved fraudulent transfer allegations, a New York court held that it had jurisdiction over the offshore trustee of a Cook Islands asset protection trust because it had participated in a fraudulent conveyance to avoid the satisfaction of a judgment in New York. The trustee, Southpac Trust, had no other contact with New York. The case seems likely to be appealed, but the case certainly had bad facts: apparently a transfer by

husband of $7 million of assets to a Cook Islands trust for his fiancé in the midst of divorce proceedings.

Sec. & Exch. Commis v. Solow, 2010 WL 303959 (S.D. Fla. Jan. 15, 2010) The defendant was jailed for civil contempt for failing to satisfy the government's judgment from assets held in an OAPT, the court rejecting his impossibility defense on the ground that it was self-created.

Actions in Foreign Courts.

The general rule of international law is that countries will grant comity to the courts of other countries such that one country will enforce the judgments and find orders of the courts of other countries provided that certain minimal "due process" standards are met, e.g., notice, jurisdiction, fundamental fairness, etc. Therefore, it may be a mistake to assume that a foreign trust will not be bound by a domestic judgment in favor of creditors.

Certain jurisdictions have by statute provided that foreign judgments against trusts domiciled in such jurisdiction will not be recognized or enforced, but these jurisdictions are relatively few and obscure: Belize, the Cook Islands, Labuan, Nevis, Niue and St. Vincent and the Grenades. Other jurisdictions may have court decisions in which comity was refused, as the Isle of Man is reported to have, but it may be perilous to rely on local common law in the absence of an express statute.

In the courts of English common law jurisdictions a U.S. or other foreign judgment for a liquidated claim may be recognized pursuant to summary proceedings provided that certain standards are met:

- foreign court must have been a court of competent jurisdiction
- foreign judgment must be final and conclusive
- the judgment must be for a fixed and definite sum of money
- judgment must not have been obtained by fraud
- judgment must not be contrary to public policy of the host court

In order to keep the assets from disappearing once proceedings are commenced in an English common law jurisdiction, a remedy similar to a temporary restraining order may be obtained. Following the name of a 1975 English case, Mareva Compania Naviera S.A. v. International Bulkcarriers S.A., 2 Lloyd's Rep. 509, this remedy is commonly referred to as a Mareva injunction. Such an injunction allows the freezing of assets on an

ex parte basis pending the outcome of other ancillary proceedings either in the courts of the jurisdiction in which relief is sought or in another jurisdiction. The injunction may be sought and granted either before or after a judgment on the merits has been obtained.

See "Mareva Mechanics" by Andrew Rogerson in the June 2013 STEP Journal.

Bankruptcy Law Considerations.

Where a debtor is foolish enough to settle an offshore asset protection trust and then file for bankruptcy or immediately before being involuntarily forced into bankruptcy, a bankruptcy trustee steps into the debtor's shoes and may exercise all of his rights, including any over the administration of the offshore trust. In some jurisdictions however, such as the Cook Islands, there is no recognition of bankruptcy decrees of foreign courts.

Contempt of Court.

While impossibility of performance is a defense to a contempt of court citation, where an obviously fraudulent conveyance has very recently been made the defense will not serve. A typical offshore trust will instruct a trustee to ignore instructions given under the compulsion of court order. But where the settlor's defense of impossibility of performance was caused by the settlor/debtor's actions shortly before the court order, impossibility of performance is no defense.

Flight Clause Issues.

A typical offshore asset protection trust contains a provision granting the trustee or others the power to take action to defeat the impact of adverse court orders in the trust's domicile by various evasive maneuvers such as changing the trust's domicile or governing law or the appointment of new trustees in a new jurisdiction.

A Mareva order, as noted above, may render such a flight clause nugatory. Upon a prima facie showing of a fraudulent conveyance or similar claim against a trustee, the judgment creditor or claimant may be able to obtain a court order barring the trustees from moving assets any further anywhere in the world, resigning or appointing new trustees, surrendering or distributing trust assets, or changing the governing law of the trust.

No case comes to mind with sympathetic facts for the debtor which received harsh judicial treatment in the U.S. Like family LLP/LLC tax cases, bad facts for the debtor (taxpayer) lead to adverse decisions against the debtor (taxpayer). By and large offshore asset protection trusts cases, like FLP/FLLC cases, have been handled by US courts as they should have been handled.

Conclusion.

Not surprisingly, careful lawyers and well-advised clients will be rewarded, careless lawyers and foolish and unscrupulous clients will be punished. A properly chosen strategy carefully and thoughtfully implemented will effectively shield assets from claims of future creditors. The wrong choice of trust domicile, bad timing in making transfers to the trust, the wrong choice of a third country in which to hold trust assets, the wrong choice of trustees, trust protectors, investments or depositary institutions can leave offshore trust assets vulnerable to attack by creditors of beneficiaries.

As general guidelines, move only liquid assets to an OAPT and less than 50% of net worth, use independent trustees and protectors, make adequate provision from U.S. assets or from OAPT assets to pay successful claims by the U.S. government, maybe by large corporate creditors.

VII. HOW TO USE AN OFFSHORE ASSET PROTECTION TRUST TO HOLD U.S. REAL ESTATE OR OTHER U.S. ASSETS WHICH ARE NOT LIQUID[3]

A U.S. citizen concerned about potential future creditors and wishing to protect a valuable real estate holding or other U.S. assets faces an obvious dilemma if he wants to maintain some kind of control over the property. If he retains an interest in or control over the property, any domestic conveyance is unlikely to be effective. On the other hand, he obviously cannot physically transfer real estate overseas and outside of the jurisdiction of the local courts, and he may simply be unwilling to transfer more liquid assets out of his control.

One approach is for the U.S. domiciliary to establish a U.S. family limited partnership to hold such U.S. assets, real or personal, retaining one percent (1%) general partnership interest which has all management rights, and conveying the ninety-nine percent (99%) limited partnership interest to a foreign asset protection trust. The trust may create a "subsidiary" controlled foreign corporation of which the grantor and those beholding to him are directors.

In the event of a suit against the grantor, he will disclose on his balance sheet the existence of the trust and his one percent (1%) interest. He will explain to his creditor that the other ninety-nine percent (99%) interest is owned by the offshore Asset Protection Trust, under which the trustees have complete discretion to distribute income or principal or neither to him or his spouse or his descendants. He will explain the trust is irrevocable so he cannot dissolve it or get at the assets; that the jurisdiction does not

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[3]See *Asset Protection Aspects of Art*, Peter Spero, Journal of Asset Protection, January/February 1998, Vol. 3, No. 3.

recognize foreign judgments, that the creditors must prove fraudulent conveyance beyond a reasonable doubt and that the suit must be brought within two years of the creation of the trust; that the jurisdiction is 9,000 miles away; and that the partnership has been liquidated and the limited partner's interest as 99% tenant in common has been distributed to the foreign corporation.

The local court will have no jurisdiction over the foreign trustee who owns ninety-nine percent (99%) of the real estate. For this purpose one only uses foreign trustees with no U.S. nexus which might support jurisdiction in the U.S. of a law suit. That portion of the real estate or other assets owned overseas should therefore remain immune to creditor claims.

VIII. WHAT YOU SHOULD HOPE TO ACCOMPLISH USING A FOREIGN ASSET PROTECTION TRUST

A. Scope and Focus of Asset Preservation.

The foreign situs trust is best seen as facilitating accomplishment of the following goals vis-a-vis creditors:

- Deter Litigation.
- Provide Incentive for Early and Inexpensive Settlement.
- Level the Litigation Playing Field.
- Enhance Bargaining Position.
- Provide Options if the Claim/Litigation is Pursued.
- To Completely (if possible) or Partly (at least) Defeat the Claim.

The grantor of such an APT and his attorney will frankly disclose the existence and character of the foreign trust to any creditors who materialize, to discourage the creditors from bringing or pursuing a claim or to foster settlement.

Barry Engel claims to have settled claims against his clients with offshore APT arrangements at an average of fifteen percent (15%) of the initial claim. This figure highlights the important point that offshore APTs are best viewed as a way to minimize, rather than to eliminate, exposure to claims.

Consider why a lawyer advises corporations operating exclusively in Kansas to incorporate in Delaware:

- The law of Delaware is more protective of management, and management is the lawyer's client.
- Delaware law is clear and established with respect to the rights and duties of corporations, their officers, directors and shareholders.
- Delaware Chancery Courts hear exclusively corporate law cases, and the judges of that court understand the law they are interpreting.

The same approach would guide an estate planning attorney to suggest the appropriate foreign jurisdiction as a situs for a trust intended to shelter assets from possible future creditors.

If an appropriate trust is established in an appropriate jurisdiction in a timely fashion and especially if multiple tiers of complex foreign entities are used, trusts and corporations in different jurisdictions, as a practical matter attachment may be impossible. See Suyfy v. U.S., 818 F.2d 1457 (9th Cir. 1987) for an example of intriguing planning ideas. To the extent that the creditor or his attorney lacks cleverness, money, staying power or tenaciousness, foreign situs asset preservation planning may prove effective.

IX. APPROPRIATE CANDIDATES FOR FOREIGN ASSET PROTECTION TRUSTS/INAPPROPRIATE CANDIDATES

One of the fascinating aspects of asset protection practice that one comes to notice is that every new economic crisis, every new economic cycle in the US, creates new classes of potential asset protection clients. New classes of prospective clients were created by the Great Recession, the economic crisis which began with the collapse of Lehman Brothers in September 2008, including anyone in residential or commercial real estate, banking, or fiduciaries whose investment strategies blew up, etc.

Those debtors who have thoughtfully and aggressively pursued asset protection strategies, even late-in-the-day "uglification" strategies, were rewarded and retained more assets and repaid less of their debts.

Reciprocally, those debtors who were not proactive in protecting themselves retained less of their assets and income and repaid a greater percentage of their debts.

A. Examples of Appropriate Candidates:

Highlighted By Recent Events

(1) Those adversely affected by the currently slow economic environment, including
   (a) partners in large law firms facing layoffs
   (b) physicians facing shrinking revenues resulting from Obamacare

(c) hedge fund and private equity professionals being laid off as funds under perform

(d) owners and senior executives of government contracting in the defense industry whose businesses are suffering from the sequester

(e) founders/key executives/directors of companies which may go public or involved with a public company with a speculative run-up, who may be concerned about shareholder derivative suits and SEC suits if the stock price collapses.

NOTE: Be on the lookout – who will be tomorrow's debtors? Clearly investigation and pursuit of high-net worth individuals committing tax fraud with elaborate over-the-line tax shelters and particularly offshore trusts and corporate and foundation accounts is going to be targeted and aggressively pursued by the IRS under President Obama's IRS. Under Bush's IRS, offshore tax fraud was not aggressively pursued. But query, how much can we do for someone with this sort of tax problem?

Generally

(2) (a) A physician concerned that he or she cannot have enough malpractice liability insurance to protect himself or herself from potential future claims, or who is considering going partially or totally "naked" (without liability insurance coverage) because of the prohibitively high cost of the premiums.

(b) Another professional, such as an accountant, lawyer, architect or engineer, who has similar concerns.

(c) A present or former outside member of a corporate board of directors who is concerned about potential directors' liability for which he or she may not be adequately insured or indemnified.

(d) An individual with substantial net worth or notoriety who is concerned that his or her wealth or notoriety may make him or her a target for vexatious claims in our litigious environment.

(e) A person engaged in a business from which personal liability could arise, or in a business representing the greater part of his or her net worth, where the inherent nature of the business is such that the potential for serious future claims is sufficient.

(f) Someone seeking to avoid forced heirship provisions of state law, e.g., to limit the rights of a surviving spouse to inherit.

(g) A married person concerned he or she may someday be facing divorce or alienation from his or her current spouse, seeking to posture his or her assets to limit his or her exposure to an expensive divorce property settlement in the event he or she may someday divorce.

(h) An entrepreneur who has recently sold or expects to sell a closely-held business who is concerned to preserve the proceeds of sale from potential claims for indemnification by the buyer, who may be disappointed with the performance of the business.

(i) Someone who presently owns or previously owned real estate with potential environmental liability associated, who is concerned that some day there could be a gigantic environmental liability imposed upon him or her.

(j) Wealthy East Asians, e.g., Chinese and Indians, who will seek the benefits of these arrangements. To Wit: At the November 2009 STEP Conference on international trusts scheduled for Singapore, a Hong Kong trust banker from JP Morgan is scheduled to speak on asset protection trusts. What does JP Morgan's interest in touting this in the East Asian market say?

B. Inappropriate Candidates for Use of Foreign Asset Preservation Trusts: There are many of these after the Great Recession.

(1) Individuals for whom the financial picture is bleak: where there are substantial loan defaults, contract defaults with severe potential penalties, apparent business tort liabilities.

(2) Individuals who are, for all practical purposes, insolvent.

(3) A lawsuit has been threatened or filed against the individual or his or her business, or an adverse judgment against the individual or his or her business is threatened.

(4) Bankruptcy of the individual or his or her business appears imminent.

(5) The individual's net worth is negative.

(6) A substantial judgment has been entered against the individual or his or her business.

(7) The individual or his or her business is bankrupt.

Even the offshore centers which have recent statutes tailored to attract APT

business want "clean business," and subject potential grantors of such trusts to substantial due diligence screening to determine their current solvency and the status of any current creditor problems. For example, despite numerous petitions, as of a year ago Gibraltar had cleared and approved fewer than twenty (20) APTs.

X. PROPERLY USED, FOREIGN ASSET PROTECTION TRUSTS ARE AN INTEGRAL AND INTEGRATED PART OF THE OVERALL ESTATE AND FINANCIAL PLAN

Asset Preservation Planning with foreign APTs should be integrated into the overall financial and estate planning for the client, and should complement it. Structuring such planning in this manner is not only sensible, it provides the best argument possible to rebut the suggestion that the planning was motivated by intent to defraud, hinder or delay creditors. Be prepared to offer some justification for establishing the foreign APTs in the nature of a business purpose OTHER THAN asset protection. Its purpose should be to plan against a possible future event that would result in economic and financial devastation to the grantor's estate.

The law recognizes the right of individuals to arrange their affairs to limit their liability to potential future creditors. In re Heller, 613 N.Y.S. 2nd 809 (N.Y. Sur. Ct. 1994) This is analogous to Learned Hand's famous opinion that everyone has a right to organize his affairs to minimize his taxes.

Foreign situs asset preservation planning can and should foster accomplishment of the following general estate planning and financial planning goals, which would constitute other business purposes:

- Probate Avoidance.
- Confidentiality of Value and Nature of Assets.
- Vehicle for Global Investing.
- Ease in Transferring Assets to Family Members.
- Avoidance of Possible Monetary Exchange Controls.
- Will Substitute/Avoid Multiple Wills in Various Jurisdictions Where Assets Are Held.
- Privacy for Estate Plan.
- Facilitate Handling of Affairs in the Event of Disability or Unavailability.

- Flexibility.
- Minimization of Taxes
- Preservation of Assets for Dependent Family Members
- Diversification of Asset Management by Using Offshore Trust Company
- Diversification of Investments into Overseas Securities Markets

To do this sort of asset preservation planning the lawyer must know his clients, screen them with some level of due diligence investigation,[4] and obtain Affidavits of Positive Net Worth/Solvency with satisfactory disclosure of details to ensure that the grantor is not engaged in a fraudulent conveyance.

XI. OAPTs and DAPTs ARE USEFUL OTHER THAN FOR ASSET PROTECTION: FOR CENTRALIZED, CONFIDENTIAL, TAX-HAVEN MANAGEMENT FOR INTERNATIONAL CELEBRITIES, ATHLETES AND OTHER FAMOUS HNWIs

An APT should not simply be considered for use in the narrow circumstances of a U.S. citizen or resident seeking protection from potential future creditors.

An asset protection trust may have the following benefits which should attract the wealthy, including entertainment, sports and other celebrities from around the world.

- Confidentiality. In many OAPT jurisdictions it is a criminal offense for a bank officer or court official to disclose even the existence, let alone the particulars, of a local trust arrangement. For obvious reasons the rich and famous will appreciate the discreetness of such arrangements, particularly from the prying eyes of criminals, business rivals, spouses, ex-spouses, lovers, ex-lovers, children, alleged children, media, those with a grudge or claim. Even, perhaps especially, as to family member beneficiaries, many Settlors would like to keep the existence, text and operation of a trust confidential, and while that is virtually impossible under general common law fiduciary principals, it is permitted in OAPT jurisdictions. For a view that this is bad public policy, see Professor Robert Whitman's article "Full Disclosure is Best" in the July 2004 issue of Trusts & Estates. In support of

[4]See *Steps in Investigating Potential Asset Protection Clients*, James Mintz, Journal of Asset Protection, January/February 1998, Vol. 3, No. 3 and May/June 1998, Vol. 3, No. 5., and *Completing a Due Diligence Investigation on a Potential Client*, John W.M. Chaud, Journal of Asset Protection, September/October 1997, Vol. 3, No.1.

the value of confidentiality, see "Go Offshore to Avoid Transparency" by Ian Marshand, Michael Ben-Jacob in the March 2004 issue of Trusts & Estates.

- Non-Susceptibility to Spouse's or Child's Claim at Divorce or Death/Alternative to Prenuptial Agreement. Many OAPT jurisdictions do not recognize or enforce spousal claims arising out of divorce, "palimony" claims, paternity claims or marital or child's claim for forced heirship. Such claims are chronic concerns of the rich and famous. An OAPT may serve as a substitute for a Pre- or Post-Marital Agreement.

- Tax Haven. The U.S. is said to be the only country on earth which imposes income tax and transfer tax on the worldwide income and assets of its citizens and residents. In contrast, citizens and residents of many countries may legally avoid income or transfer tax by their jurisdiction of domicile by using appropriate structures in tax haven jurisdictions. In other countries tax enforcement is lax or corrupt permitting the shrewd and well-informed to avoid carelessly or randomly enforced tax laws. Many OAPT jurisdictions expressly refused to recognize tax avoidance in another jurisdiction as criminal or penalties or remedies for tax avoidance as enforceable.

- Centralized Financial Coordination/De-Centralized Investment and Management/Global Accessibility. In the global electronic financial network of 2010, communication, investment commitment, management, record keeping and reporting are virtually instantaneous. The local branch of a sophisticated global financial institution in an APT jurisdiction may serve as "host" for the locally situsted OAPT which serves as the quarterback/general partner of the estate plan/financial plan/investment plan/asset protection plan/tax plan of the High Net Worth Individual (HNWI), which through local and multinational subsidiary LLCs, corporations, trusts and foundations manages the wealth using various other institutions for the skill and expertise and various other jurisdictions for the specialized advantages. Each of the various entities may be managed for its idiosyncratic advantage while each serves as a bulkhead which will contain "trouble" in any one venture within that entity, protecting the HNWI and his other investments from ancillary liability of any kind. Consider the opportunities now available to do this in one corporate entity, for example SG Hambros, the trust arm of Societé Generale, HSBC, JPMorgan, Goldman Sachs, UBS, EFG Bank, all with offices on every continent. Through this sort of global conglomerate HNWIs have access to the best investment advice available globally and trust and corporate and foundation entity management around the world.

Moreover, the tiering and layering of various types of entities in various jurisdictions under various sets of laws around the world may serve it the further purposes of advancing the confidentiality which may be so important

in our litigious world, making the structure and the assets virtually impenetrable to outside scrutiny.

- Asset Protection Planning. Add to all of these virtues the asset protection planning inherent in an OAPT, and these structures should have an irresistible appeal to HNWIs around the world. For U.S. HNWIs, the arrangement is tax neutral and no less attractive for its non-tax charms.

- Foreigners Are Using DAPTs in the U.S. Certain foreign countries, including Mexico, Venezuela, Argentina and Brazil, have blacklisted certain traditional tax havens such as Cayman Islands, Channel Island and Cook Islands and forced their citizens to disclose offshore structures in such jurisdictions. This has had the curious result of making U.S. DAPTs in Delaware, Alaska etc. attractive hosts for offshore structures from citizens of such countries. The U.S. is not "blacklisted" by any of these countries. Typically these customers are looking to the estate planning, avoidance of forced heirship and possibly tax shelter advantages. See the article by Mark G. Holden, "Surprise: The U.S. is the New Tax Haven" in the December 2003 issue of Trusts & Estates.

XII. USE OF AFFIDAVIT OF SOLVENCY

Attorneys consulting with and advising clients with regard to asset protection planning in general, and foreign APTs in particular should consider the use of an Affidavit of Solvency. Where the issue of asset protection arises in an engagement, obtain such an Affidavit from the client. In the Affidavit the client should represent, state and affirm that he or she has no pending or threatened claims; that he or she is not presently under any investigation of any nature, and that he or she is not involved in any administrative proceedings; that no situation has occurred which the client has reason to believe will develop into a legal problem in the future; that following any transfers the client intends to remain solvent and able to pay his or her reasonably anticipated debts as they become due; and that none of the assets which the client may transfer were derived from any of the "specified unlawful activities" under the Money Laundering Control Act of 1986. To the extent any legal disputes or other problems exist, they should be disclosed in the Affidavit and the Affidavit should provide that either sufficient assets will be retained with which to satisfy any liability arising from the problem, or the documents should be drafted with provisions requiring that any liability resulting from the disclosed problem(s) be satisfied by the foreign APT if the liability is finally and legally established and not otherwise satisfied.

The internet affords the opportunity for lawyers to do additional due diligence investigation of new asset protection clients, for instance lexis searches for judgments, liens, pending litigation.

The asset protection lawyer should maintain a file containing a memorandum explaining the facts of each case which the lawyer has refused to take. This may prove helpful someday if the integrity of the lawyer and the types of cases accepted are challenged. A sample Affidavit of Solvency is attached as Exhibit 1.

The recent Florida bankruptcy case of Goldberg v. Rosen (in re Akram Nirromand), 493, Fed. Appx. 11 (11th Circ. Fla. 2012) indicated the self-defense effectiveness for a planning attorney of obtaining an Affidavit of Solvency. The Bankruptcy trustee Alan Goldberg sued debtor's lawyer, Howard Rosen, to recover attorney's fees and costs as fraudulent transfers, on the theory that Mr. Niroomand was insolvent when he paid the fee for an offshore asset protection trust drafted by Mr. Rosen. He also sued Rosen for legal malpractice and unjust enrichment. The Bankruptcy Court ruled in favor of Mr. Rosen because the Trustee did not prove insolvency, the only evidence of which was debtor's testimony. Mr. Rosen impeached that testimony with an Affidavit of Solvency sworn to by debtor obtained by Mr. Rosen before he undertook the legal work.

XIII. DISTINGUISH LEGITIMATE ASSET PROTECTION PLANNING FROM ASSET PROTECTION RELYING ON BANK SECRECY OR PERJURY, OR RELATING TO TAX FRAUD OR OTHER CRIMINAL ENTERPRISE

Foreign Asset Preservation Trusts should NOT be seen as a means or excuse to defraud creditors, hide assets or evade U.S. or foreign taxes.

The grantor of an offshore APT will happily acknowledge the existence of the foreign trust and details about it in interrogatories, depositions and in sworn testimony. The grantor will pay U.S. tax on all income of the trust. It will be a grantor trust under Code § 679.

Liechtenstein and UBS have paid the price for helping clients commit tax fraud.

The grantor will be very careful to avoid transfers to foreign trusts which could be seen to be a fraudulent conveyance under state, Federal Bankruptcy, or foreign situs law. Failure to fully disclose and turn over all assets belonging to the grantor is a ground for not obtaining a bankruptcy discharge. 11 U.S.C. § 727.

In any context in which a Federally chartered bank is a potential creditor, the grantor must be mindful of the Comprehensive Thrift and Bank Fraud Prosecution and Taxpayer Recovery Act of 1990, which imposes severe criminal penalties for concealment of assets owed to the Federal Deposit Insurance Corporation or the Resolution Trust Corporation.

Grantors also should be aware of the Money Laundering Control Act of 1986,

which imposes severe criminal penalties where funds involved in a financial transaction -- e.g., offshore deposits -- represent proceeds of certain unlawful activities if the intent is to promote the unlawful activity or evade income tax.

2008-2013 Scandals Highlight Risks of Attempting to Commit Tax Fraud Using Offshore Jurisdictions: UBS, Credit Suisse, Wegelin, Etc.

UBS Problems – UBS (Union Bank of Switzerland), one of the world's largest wealth managers, has a huge problem with the U.S. tax authorities. It recently became public that UBS was actively soliciting U.S. clients touting the virtues of "secret" offshore arrangements. UBS' problems came to light when Bradley Birkenfeld, a former UBS private banker, pleaded guilty on June 20, 2008, acknowledging that he and other UBS colleagues helped wealthy Americans hide money abroad, advising them, among other schemes, to put cash and jewelry in Swiss safe deposit boxes, buy or trade art and jewels using offshore accounts and setting up accounts in the names of others. Mr. Birkenfeld is expected to tell federal prosecutors what he knows in hope of lenient sentencing. Mr. Birkenfeld's boss, Martin Liechti, former head of UBS wealth management business for the Americas, has been detained in connection with the investigation. Another co-conspirator appears to be Mario Staggli, a Liechtenstein financial advisor, who owned New Haven Trust Company in that country.

U.S. prosecutors in late June 2008 asked a federal judge in Miami to let the IRS issue a summons to Zurich-based UBS for client information. Very recently the U.S. government, which had sought to obtain information on 52,000 Americans with UBS Swiss bank accounts, informed the judge it had settled with UBS in exchange for information on some 4,500, probably figuring that was enough to worry all 52,000 and cause many of them to turn in themselves under an amnesty program which expires in September of 2009. Under the amnesty program taxpayers who admit to the IRS information on previously undisclosed offshore accounts can limit their exposure to criminal penalties. If granted, this would be the first ever summons issued by the U.S. against an offshore bank. This case is a very ominous warning for U.S. tax cheats and other violators of federal law who have long attempted to hide assets in secret offshore trust and other accounts.

UBS clients caught in this dragnet may get off by paying back taxes, interest and penalties if they come forward early and voluntarily to the IRS. Those who do not will risk criminal prosecution, and any outside advisors in the U.S. who facilitated the secret, fraudulent offshore arrangements may face consequences from the IRS.

The U.S. is seeking to have UBS produce records identifying U.S. taxpayers with UBS accounts in Switzerland from 2002-2007 not declared to the IRS. Mr. Birkenfeld, cooperating with the U.S. Government as part of his plea arrangement, has told U.S. prosecutors that UBS held $20 billion in assets for U.S. clients in undeclared accounts.

In 2001 UBS entered into an agreement with the IRS to identify U.S. citizens among its account holders and to withhold taxes on their behalf. Subsequently UBS flaunted the agreement and bragged to the U.S. clients that "information relating to your Swiss banking relationship is as safe as ever." Reportedly as many as 20,000 UBS clients may be involved. Sources indicate that UBS frequently worked in tandem with a Liechtenstein bank, LGT Group to hide U.S. funds. Typically these arrangements involved offshore corporations and occasionally trusts.

In August the Wall Street Journal reported the guilty plea of Swiss-American lawyer Edgar Paltzer to helping wealthy Americans hide millions of dollars from the IRS overseas for more than a decade. His cooperation with the IRS is "complete and without limitation." His principal platform was Zurich's Bank Frey.

QUERY: As a result of this new aggressiveness of the U.S. government towards offshore tax cheats and the greatly increased scrutiny by the U.S. government of tax haven accounts, will such offshore centers be more reluctant to establish even legitimate tax-compliant trusts and accounts for U.S. clients, wary of the hassle "factor?" Apparently yes according to anecdotal information I have heard from offshore bankers. Offshore trust companies may well insist on proof from Settlor of U.S. tax compliance and may charge more for the burdens of dealing with U.S. clients.

Swiss/Cayman Banker Hands Over Data to WikiLeaks. A former Swiss Banker who headed Julius Baer's Cayman operation turned over data on hundreds of offshore account holders to WikiLeaks founder Julian Assange in 2011.

After dealing with UBS, the IRS went after at least 11 more Swiss Banks, including Credit Suisse. Wegelin, a 270-year-old Swiss private bank, which brazenly pursued UBS American customers, went out of business under pressure from the US government when it acknowledged its participation in tax fraud. A former Swiss banker was said to be cooperating with the IRS.

BVI, Cook Islands, Singapore Accounts Disclosed. On April 5, 2013 the New York Times reported the intentional leak of 2.5 million files relating to offshore accounts made to the International Consortium of Investigative Journalists, relating to assets estimated at $21 trillion held in offshore havens, particularly BVI, Cook Islands, and Singapore, including accounts beneficially owned by the Budget Minister of France.

European Crackdown. Since President Obama took office more than 39,000 U.S. taxpayers have stepped forward to pay back taxes and stiff penalties on undeclared offshore accounts, the Wall Street Journal reported in May of this year. The taxpayers have paid more than $5.5 billion to resolve their cases, with another estimated $5 billion more to come.

And European countries are following suit. In April of this year, Germany, France, Britain, Italy and Spain agreed to develop an information-sharing system that would make it easier to clamp down on tax evasion by their citizens and residents using tax haven jurisdictions. For example, Luxembourg, sometimes seen as a place to hide money, has agreed to exchange information with the rest of the European Union.

The UK government in particular is aggressively cracking down on offshore tax fraud, and has recently negotiated tax disclosure agreements with Switzerland, Liechtenstein, Jersey, Guernsey, and the Isle of Mann. See "No Safe Havens" by Ronnie Pannu and Iain Sanderson in the July 2013 STEP Journal.

Caribbean Crackdown. The IRS announced in April of this year that it is going after Canadian Imperial Bank of Commerce First Caribbean International Bank with offices in 18 Caribbean nations pursuing tax fraud. An Irish journalist got his hands on a purloined hard drive containing the names of holders of some 130,000 Caribbean accounts.

Asia Crackdown. In March 2013 the Wall Street Journal reported that the IRS was pursuing tax fraud by US taxpayers using banks in India, Israel, Hong Kong, and Singapore.

Rand Paul's View. It is interesting that Senator Rand Paul has assailed the U.S. government's attempts to get access to Swiss banking records of Americans and tried to slow down treaty negotiations, saying "There needs to be some constitutional protections to your banking records."

Liechtenstein Connections.

At least seven other countries investigated their own citizens for allegedly hiding assets in Liechtenstein using the services of the same LTG Bank which worked with UBS as described above. This investigation began when data from LGT Truehand AG, which sets up "foundations" (frequently used like trusts with non-charitable beneficiaries) was stolen, apparently by Heinrich Kieber, a former employee of LGT. Mr. Kieber, now apparently living in Australia, has offered confidential client data to tax authorities on several continents. Reports say that about 100 Swedes, 100 Canadian, 20 Australians, several hundred French and about 1,400 Germans had such accounts reflected in Mr. Kieber's data. Apparently Germany paid Mr. Kieber $6-$7.5 million for the data.

LGT is owned by Liechtenstein's ruling family.

Tax cheats should be aware that a law enacted in 2006 authorizes the IRS to pay sharply higher rewards to informants in large cases, as high as 30% of what the IRS

collects.

XIV. ETHICAL AND MALPRACTICE ISSUES FOR THE ATTORNEY; THE ATTORNEY'S EXPOSURE TO CIVIL LIABILITY AND CRIMINAL PROSECUTION

The general ethical rules governing lawyers practicing in asset protection follow the law of fraudulent conveyance: if a client has no current or "contemplated" creditors (he is not known to intend shortly to enter into a transaction which will create creditors), but is only concerned about potential future creditors, it is clearly perfectly ethical to assist.

Examples: An obstetrician concerned that she will eventually deliver a sick baby and will inevitably be sued.

A board member of a startup company or even a public company concerned that if the stock price collapses (after public offering in the case of a start-up), he will be liable. Consider that all the board members of MCI, including the impecunious Dean of Georgetown Law School, were "fined" by the SEC 10% of their net worths for negligence in overseeing the activities of Bernie Ebbers.

What is an example of a perfectly clean asset protection endeavor? Consider almost any kind of entrepreneur who sold the stock of his small company to a big public company for $50 million right before the collapse of Lehman and the economy and the stock market in the Fall of 2008. He would have been required to provide contractual representations and warranties with a duration of 4 years.

When the economy collapsed, and the value of the acquisition was seen to be much less than what was paid, probably many buyers referred the representations and warranties to their 1,000-lawyer Wall Street law firms with instructions: find a breach and get our money back. In such a situation, it does not matter what the facts or law are, the buyer's larger firm can bully the seller into a large settlement. But if the proceeds were protected before there was any problem, for instance in an offshore APT, the seller would have been safe. There could be no question of challenging the ethics of a lawyer who suggested such a prophylactic strategy.

Evolution of Perception of Legal Ethics in Asset Protection

The legal practice of asset protection arose out of the nationwide collapse of the value of commercial real estate in 1989-1992. When Denver real estate collapsed, a Denver lawyer with clients in trouble, Barry Engel approached the Cook Islands and suggested the adoption of the world's first asset protection trust statute. When it was adopted in the Cook Islands, Mr. Engel set up trusts for many of his clients, and other

offshore jurisdictions soon followed suit and developed similar statutes.

Initially most lawyers were very uncomfortable with the ethics of helping clients "hide" assets from creditors.

Over the years, 40 plus offshore jurisdictions and some 15 US states have adopted such statutes and it seems indisputable that a concept so widely endorsed and enacted into law by so many legislatures is now comfortably within the public policy mainstream and can hardly in that light be seen as unethical.

Moreover, such luminaries as Duncan Osborne, who is the current President of the American College of Trust and Estate Counsel (ACTEC), and Gideon Rothschild, who has chaired the ABA Special Committee on Asset Protection, have authored articles suggesting not only is it not unethical to do asset protection planning, but it may also be civilly negligent --i.e. legal malpractice --NOT to recommend asset protection planning to clients for whom it is obviously appropriate.

So while you may be damned if you do asset protection planning -- it is a grey, subtle area without bright ethical lines -- you may be damned if you do not.

Certain areas of asset protection planning are certainly thorny and require close examination and analysis. If a client asks you to help him avoid a child support claim, are you comfortable assisting, morally or ethically? Some states permit it under certain circumstances. What about helping a client protect assets in the event of future divorce? Consider has the other spouse been a client of yours? Is the property sought to be protected community property? Has a divorce action been filed or is filing contemplated? What if the assets sought to be protected were earnings during the marriage in a non-community property state, where the non-earning spouse's interest is inchoate? These are dangerous, reef-filled waters in which to sail.

BEWARE: In the case of insolvent clients or clients with a clear intent to hinder, delay or defraud existing creditors, it may be unethical for an attorney to counsel or assist a client in a conveyance which perpetrates a fraud on the client's creditors. As an example, See Virginia Code of Professional Responsibility, Canon 1 generally, and Disciplinary Rule 1-102(A)(4) and 7-102(A)(7), Ethical Considerations 1-5, 7-3, 7-4, 7-5, 7-6, and 7-8, Virginia Legal Ethics Opinion 1140 (October 18, 1988).

A. Virginia Ethics Rules as an Example.

According to Disciplinary Rule 7-102(A)(7), a lawyer shall not counsel or assist his client in conduct that the lawyer knows to be illegal or fraudulent. To do so would not only expose the attorney to censure or disbarment, but also to suit for fraud as a co-conspirator or in malpractice.

Canon 4 deals with the obligation of the lawyer to preserve the confidences and secrets of the client. A "confidence" generally refers to information protected by the attorney-client privilege under applicable law, and a "secret" generally refers to other information gained in the professional relationship that the client has requested by held inviolate or the disclosure of which would be embarrassing or detrimental to the client. In actual practice the attorney-client privilege is not as protective as attorneys tend or want to believe. Courts seem increasingly willing to find a means, basis or exception to compel disclosure.

Moreover, according to Disciplinary Rule 4-101(D), a lawyer must reveal the intention of his client, as stated by his client, to commit a crime or information which clearly establishes that his client has perpetrated a fraud related to the subject matter before the tribunal with respect to which the lawyer is representing the client. If the client acknowledges to the attorney that he has committed a fraud, that clearly establishes it. Not to make the required revelation could subject the attorney to censure or disbarment.

Under Disciplinary Rule 4-101(C)(3) a lawyer may reveal information which clearly establishes that his client has, in the course of the representation, perpetrated upon a third party a fraud related to the subject matter of the representation. Recognizing the risk that the lawyer may well be sued as a co-conspirator in the fraud or for malpractice, the lawyer may want to avail himself of this opportunity, in which he is excused from breaching the attorney-client privilege.

If a client has committed a fraud using his attorney's services without the attorney's prior knowledge, the attorney may reveal his client's fraud to a damaged third party without breach of attorney-client privilege to protect himself from implication.

On the other hand, if a client consults with his attorney for advice as to whether an activity he engaged in without the attorney's involvement was illegal or fraudulent, and the attorney advises him that it was, and he thanks the attorney and terminates the professional engagement, the attorney's advice is clearly privileged, and the attorney may not disclose any information obtained in the engagement. The attorney is not thereby implicated in the illegal or fraudulent act.

B. Ethical Rules in Other States.

In South Carolina Bar Ethics Advisory Committee Opinion 84-02 it was held that unless there is an immediate reasonable prospect of a judgment being entered against the client, particularly one that would render him insolvent, the attorney can participate in a transfer of the client's property where the sole purpose of the transfer would be to avoid the possibility that a creditor would recover a deficiency judgment against the property conveyed. On the other hand, In re Pamphilis, 30 N.J. 470 (1959), is an example of a case where an attorney was disciplined for suggesting transfers of property to a relative in

satisfaction of a non-existent debt prior to filing bankruptcy. See also Townsend v. State Bar of California, 197 P.2d 326 (1948). In re Greene, 557 P.2d 644 (Ore. 1976) sets forth the principle that if an attorney assists a client in making a transfer that any reasonably competent attorney should have recognized as fraudulent, or if the attorney should have reasonably discovered facts that would manifest the transfer as fraudulent, the attorney may have violated his or her ethical duty to provide competent representation. Cincinnati Bar v. Wallace, 700 N.E. 2d. 1238 (1998), In re Kenyon and Lusk, 491 S.E. 2d 252 (1997), and In re Hackett, 734 P. 2d 877 (1987, Oregon).

C. Planning Attorney's Liability.

Attorneys engaging in asset protection planning have certain unique liability issues of which they must at all times be mindful.[5] Would it not be wise, as Duncan Osborne has suggested, to require a retainer to cover the time and cost of a due diligence background check to confirm the bona fides of asset protection clients, to back-up the Affidavit of Solvency?

(1) Civil Liability

In a federal case applying New Jersey law, Morganroth & Morganroth v. Norris, McLaughlin & Marcus, P.C., 331 F. 3rd 406 (3rd Circuit 2003) the Court held that persons -- lawyers -- who assist fraudulent transfers may have liability for various common law wrongs, even if they do not receive the property in question, and even if they commit no overt acts in support of the conspiracy. These common law liabilities may include the tort of creditor fraud, aiding and abetting, civil conspiracy to commit creditor fraud.

(a) And consider McElhanon v. Hing, 151 Az. 386, 728 P.2d 256 (Ct. App. 1985), aff'd. in part and vacated in part, 151 Az. 403, 728 P.2d 273 91986), cert. denied 107 S. Ct. 1956 (1987), which involved an attorney who was held liable ($286,120 in damages) for participating in a conspiracy to defraud a client's judgment creditor. The facts of this case are rather egregious and illustrate the point made above that while attorneys have the ethical obligation to zealously represent their clients, they should not be foolish. A disgruntled creditor may very well allege fraud by the planning attorney for a number of reasons, including as a means of obtaining discovery from the attorney. Lawyers in the Weese case were very fortunate not to be sued as co-conspirators in fraud by creditors. The good news for lawyers engaged in asset protection planning today is that creditors have historically been reluctant to sue planning attorneys. Sooner or later that may

[5]See *Minimizing Attorney Liability in Asset Protection Representation*, Parts 1, 2 and 3, William L. Siegel, Journal of Asset Protection, September/October 1997, Vol. 3, No. 1, and January/February 1998, Vol. 3, No. 3, and March/April 1998, Vol. 3, No. 4.

change. But see Bosak v. McDonough, 549 N.E.2d 643 (111.App. 1st Dist. 1989), in which the Court found that absent evidence that the attorney counseled the debtor to defraud the lender or agreed to participate in any fraud, the attorney is not liable for conspiracy. Another "good" case refusing to find a lawyer liable is Nastro v. D'Onofrio, 263 F. Supp 2d 446 (D. Conn. 2003), in which a Court refused to hold a lawyer civilly liable to a creditor of a client for whom the lawyer created an offshore spendthrift trust, citing the strong public policy of Connecticut in not imposing a liability on lawyers to third parties. As to a claim that an estate planning lawyer might have "aided and abetted" a tort, the seminal case is Haberstam v. Welch, 705 F. 2d 472 (D.C. Cir 1983, decided by a 3-judge panel including Judges Scalia and Bork).

(b) The other extreme involves the possibility of an attorney being sued by an estate planning client, or his heirs, successors and beneficiaries, after his death, when the client or his estate subsequently suffers a judgment. The claim might be asserted that the attorney was delinquent in that techniques were in fact available to protect the estate during the client's lifetime, but the attorney negligently failed to raise or otherwise explore them with the client in the estate planning process. See Duncan Osborne's article cited on page 81. You may be damned if you do asset protection planning for your clients, and damned if you refuse to. See also Gideon Rothschild's article in the September 2003 issue of Trusts & Estates, "Asset Protection Planning Ethical? Legal? Obligatory?"

(c) Consider also F.D.I.C. v. Porco, 552 N.Y.S. 2d 910 (Ct. App. 1990), wherein the New York Court of Appeals held that "under long-standing New York law, a creditor has no cause of action against a party who merely assists a debtor in transferring assets where, as here, there was neither a lien on those assets nor a judgment on the debt."

(d) Goldberg v. Rosen, 2012 WL 4933299 (11th Circ., Unpublished, October 17, 2012). In a bankruptcy case, the trustee in bankruptcy sought to recover as a fraudulent conveyance the legal fees paid to a well-known Florida asset protection attorney Howard Rosen who created an OAPT for the bankrupt. The attorney vigorously defended and produced the Affidavit of Solvency he had obtained from the bankrupt and relied upon. The court held for the attorney, finding no evidence of fraudulent transfer, malpractice, or unjust enrichment.

(e) Do U.S. Attorneys Have An Ethical Duty With Respect to Non-U.S. Law? France in 2011-2012 adopted new rules subjecting to inheritance and gift tax all transfers of French-situated property held in a trust or by a trust of which a French tax resident is a settlor, deemed settlor, or beneficiary. Do non-French attorneys assisting French residents have a duty to (1) know about this law and advise their clients about it; or (2) help the French government enforce it. See "French Traps"

by Sophie Berenstein, STEP Journal December 2012.

(2) Criminal Liability

It goes without saying that an attorney assisting a client in asset preservation planning must scrupulously avoid conduct which could implicate the attorney himself in possibly criminal activity. See, for example, 11 USC Section 152, the Crime Control Act of 1990, Bankruptcy Crimes, and Internal Revenue Code Section 7206, as well as:

- Racketeering Influenced and Corrupt Organization ("RICO") statute, 18 U.S.C. section 1961 et seq.

- Bankruptcy Crimes --

  - 18 U.S.C. Section 152 for anyone "knowingly and fraudulently concealing from a trustee ... any property belonging to the estate of a debtor."

  - 18 U.S.C. Section 157 for anyone "having devised, or intending to devise, a scheme or artifice to defraud and for the purpose of executing or concealing such scheme files a [bankruptcy petition] or makes a fraudulent representation in a [bankruptcy] proceeding."

    This risk suggests that the wise strategy is never to counsel a voluntary bankruptcy filing. Avoiding bankruptcy also avoids the 10-year look-back risk.

- Internal Revenue Code Section 7212(a) for anyone who "corruptly endeavors to ... impede any officer of the United States or obstructs or impedes the administration [of the tax law.]" See United States v. Popkin, 943 F.2d 1535 (11th Cir. 1991) in which Mr. Popkin, an attorney, was convicted for assisting a client in disguising the source of undeclared funds being repatriated from offshore.

- Money Laundering Control Act, 18 U.S.C. sections 1956 and 1957.

- Conspiracy to Defraud the U.S., 18 U.S.C. Section 371.

- Mail and Wire Fraud, 18 U.S.C. Section 1341.

- The Patriot Act signed into law by President Bush on October 25, 2001

designed to thwart the financial underpinning of terrorism. See the June 3, 2002 article in *The Washington Post* Exhibit 5 regarding developing technology for tracing and monitoring illicit funds developed partly as a result of The Patriot Act.

(3) No Available Malpractice Insurance.

Attorneys should be advised that virtually every legal malpractice policy excludes fraud from the scope of its coverage. If a lawyer knowingly gives advice that assists his client in perpetrating a fraud, he is liable to suit for fraud or malpractice without benefit of insurance coverage.

(4) Planner Due Diligence is Required to Avoid Civil, Criminal or Ethical Liability. See Mr. Zagaris' outline.

See "What ACTEC Fellows Should Know About Asset Protection" (An article by Duncan Osborne and Elizabeth M. Schurig, published in 25 ACTEC NOTES at p.367 (2000, published with consent) (Exhibit 2). At least six other articles have suggested that a lawyer engaged in estate planning may have a duty to clients to advise on asset protection planning in addition to more traditional trust and estate and tax planning advice. While there are risks in giving asset protection advice, you may be "damned if you do, damned if you don't." Duncan Osborne framed the matter in this way:

> "The debate between advocates of creditors' rights and advocates of asset protection cannot ... turn on whether asset protection planning is proper. Rather, the only meaningful debate is the determination of the lawful and proper scope of asset protection planning ... Nowhere is it written that an individual must preserve his assets for the satisfaction of unknown future claims and claimants. The focus on causality -- a causal link between an asset transfer and the injury allegedly suffered by a creditor -- provides a means to distinguish between the actions that operate directly to prejudice a particular creditor and those actions that in some remote, not foreseeable way, have after the passage of time or the occurrence of an intervening cause, compromised a creditor's financial interest."

XV. CLIENTS WANT ASSET PROTECTION PLANNING

Two recent surveys, one reported in the Fall of 2003 in The Wall Street Journal, "Litigation Boom Spurs Efforts To Shield Assets," by Rachel Emma Silverman, and

another reported in the September 2003 issue of Trusts & Estates in an article entitled "Shelter From the Storm," by Russ Alan Prince and Richard L. Harris, document the rapidly increasing interest in and demand for asset protection expertise in their professional advisors by HNWI. With the phase-out of the importance of estate tax planning with the dramatic recent and scheduled increases in the estate tax exemption, trust and estate planning lawyers and other financial service providers -- accountants, financial planners, investment advisors, trust bankers -- have a strong motivation to increase their expertise in the asset protection area as the opportunity presents itself to find other profit centers in their practices. According to a survey, 69% of investors holding $5 - $25 million are fearful of being targeted by an unfounded lawsuit. 1.8 million Americans were sued in 2004, the most recent year for which figures are available.

These two articles are attached as Exhibits 5 and 6.

According to the Trusts & Estates article, while less than 28% of lawyers agreed strongly with the assertion that "Asset protection is legal and should be discussed with most wealthy clients," 55% of high net worth clients were reported as "very" or "extremely" interested in asset protection planning. Interesting, more successful lawyers were more in tune with their clients' sensitivity to asset protection. Fewer than 13% of wealthy investors have any type of asset protection planning. Clients need asset protection planning. Clients want asset protection planning. Yet many estate planning lawyers are not providing this service to their clients. With the opportunities for tax-oriented estate planning shrinking, estate planning lawyers have an opportunity to grow their practices into asset protection planning.