



# Asset Protection Overview

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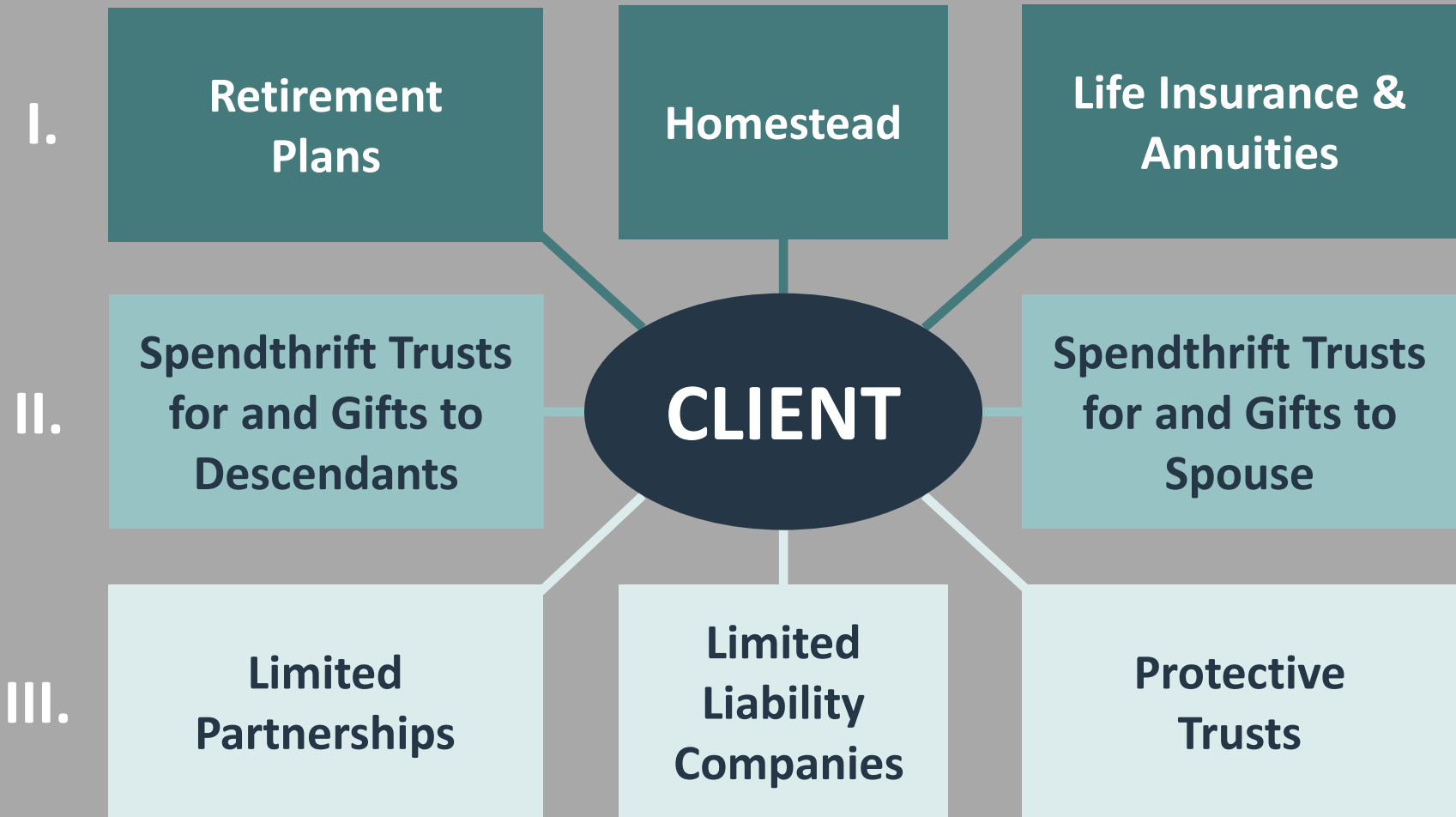
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# Methods to Achieve Asset Protection



# Creditor Protection: *Fraudulent Transfer Law*

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- **General rule**

- A gratuitous transfer of property with the actual or constructive INTENT to avoid creditors is fraudulent and may be set aside by creditors
- Any transfer of assets from nonexempt status to exempt status should be tested to assure that it is not a fraudulent transfer

- **Three classes of creditors**

- Present creditor – solvency analysis
- Potential subsequent creditor – badges of fraud
- Unknown future creditor



# Creditor Protection: *Fraudulent Transfer Law (cont'd)*

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- **Statute of limitations**

- Statute of limitations on fraudulent transfer claims in most states is four years or, if later, within one year of when the transfer could reasonably have been discovered
- A bankruptcy trustee can have a fraudulent transfer set aside if the transfer is made within two years of bankruptcy – certain transfers to a self-settled trust or similar device subject to a ten-year statute of limitations



# Solvency Test

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Total value of assets

**LESS** Liabilities (*including contingent*)

**LESS** Creditor protected assets (*e.g., homestead*)

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**EQUALS** Amount that can be transferred



# What is a Spendthrift Trust?

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- A spendthrift trust is one in which the beneficiary is precluded or restrained from voluntary or involuntary transfers of trust assets
- In some states, this includes a prohibition on the ability to pledge as collateral any interest in a trust
- The consequences of these types of provisions in trust documents is that the beneficiary's creditors are precluded from reaching trust assets
- In most states, settlors cannot utilize a spendthrift trust to protect assets from the settlor's creditors



# What is a Protective Trust?

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- **Definition**

- The Settlor (*the person who transferred assets to the trust*) is a beneficiary of the trust; and
- The assets that the Settlor transferred to the trust are protected from the claims of the Settlor's creditors



# Asset Protection Trusts

## *Two Very Different Options*

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- **Definition**

- The Settlor (*the person who transferred assets to the trust*) is a beneficiary of the trust; and
- The assets that the Settlor transferred to the trust are protected from the claims of the Settlor's creditors

- **Domestic**

- Available in Delaware (1997), Alaska (1998), Nevada (1999), Rhode Island (1999), Utah (2003), South Dakota (2005), Tennessee (2007), Wyoming (2007), and to a lesser extent, Oklahoma (2004) and Missouri (1986)

- **Foreign**

- Available in many foreign countries





# Vulnerabilities of Domestic *Protective Trusts*

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- Access to trust assets through U.S. court system
- U.S. Constitution
- Availability of punitive damages and attorney's fees



# Offshore Asset Protection Trusts

## *Offer Additional Benefits*

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- Creditors cannot reach assets through U.S. court system
- U.S. judgments are not enforceable
- Cost of pursuing assets offshore is high; loser-pay systems



# Offshore Protective Trusts

## *Offer Additional Benefits (continued)*

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- Punitive damages and contingent fee contracts not allowed
- Secrecy and privacy laws prevalent and strictly enforced



# When To Settle a Protective Trust

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- **Before Insolvency**

- Cannot make a fraudulent transfer under state law or bankruptcy law – a 10-year clawback period may apply in bankruptcy
- A gratuitous transfer of property with the actual or constructive INTENT to avoid creditors is fraudulent

- **Before a claim arises**

- Greater distance in time between transfer and claim against assets results in superior protection



# Control and Contacts

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*Less*

Asset Protection

*More*

Asset Protection



Greater Settlor control

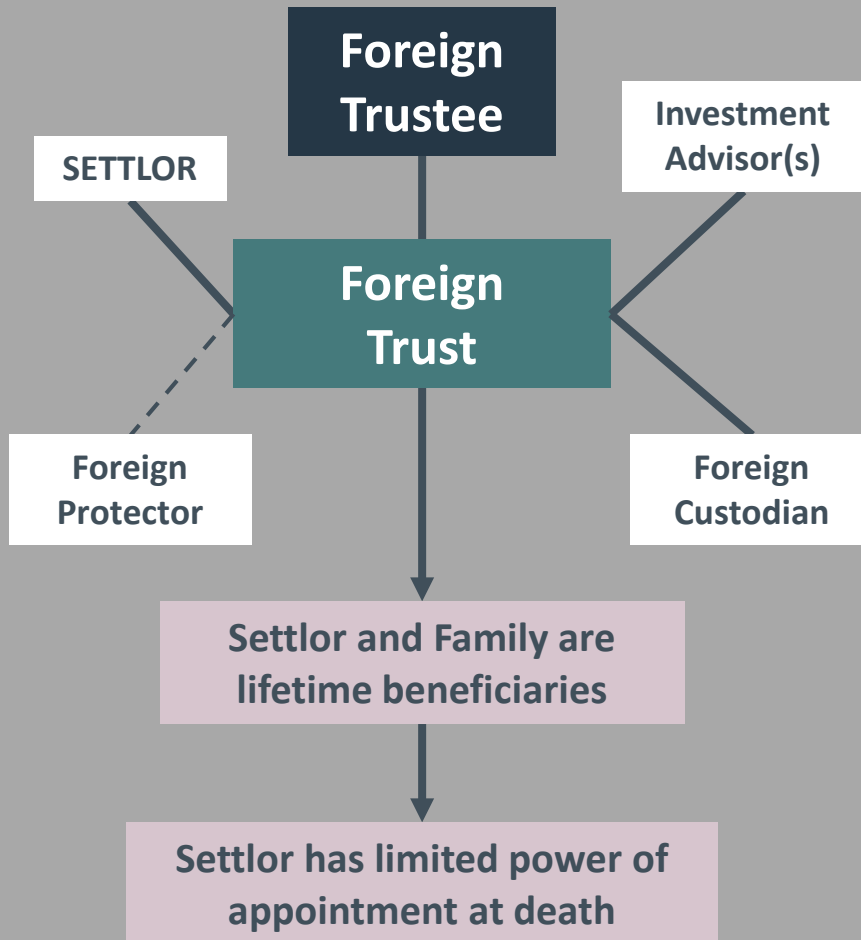
Less Settlor control

More U.S. contacts

Few or no U.S. contacts



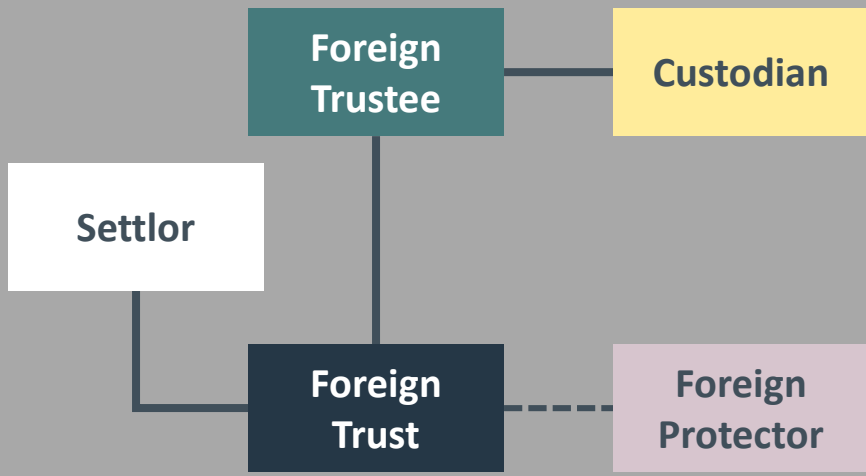
# Typical Asset Protection Trust Structure (*Foreign*)



- Wholly discretionary (rather than ascertainable) distribution standard
- Trustee can add and remove beneficiaries
- Redomiciliation permitted
- Independent investment advice the norm

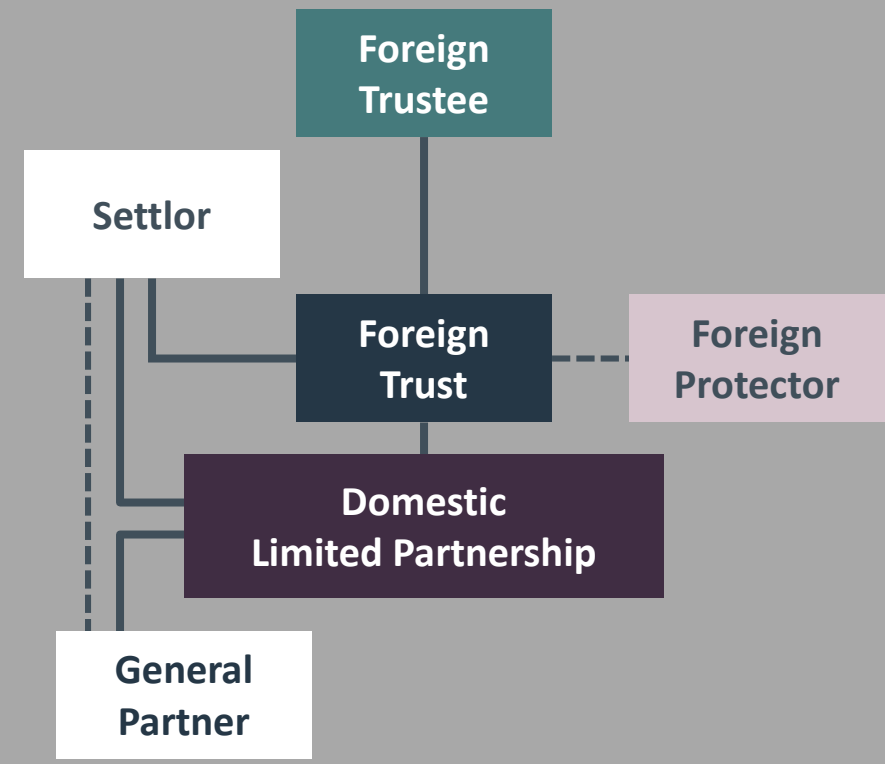
# Two Fundamentally Different Offshore Strategies

## EXPORT THE ASSETS



*Jurisdictionally Severed*

## IMPORT THE LAW

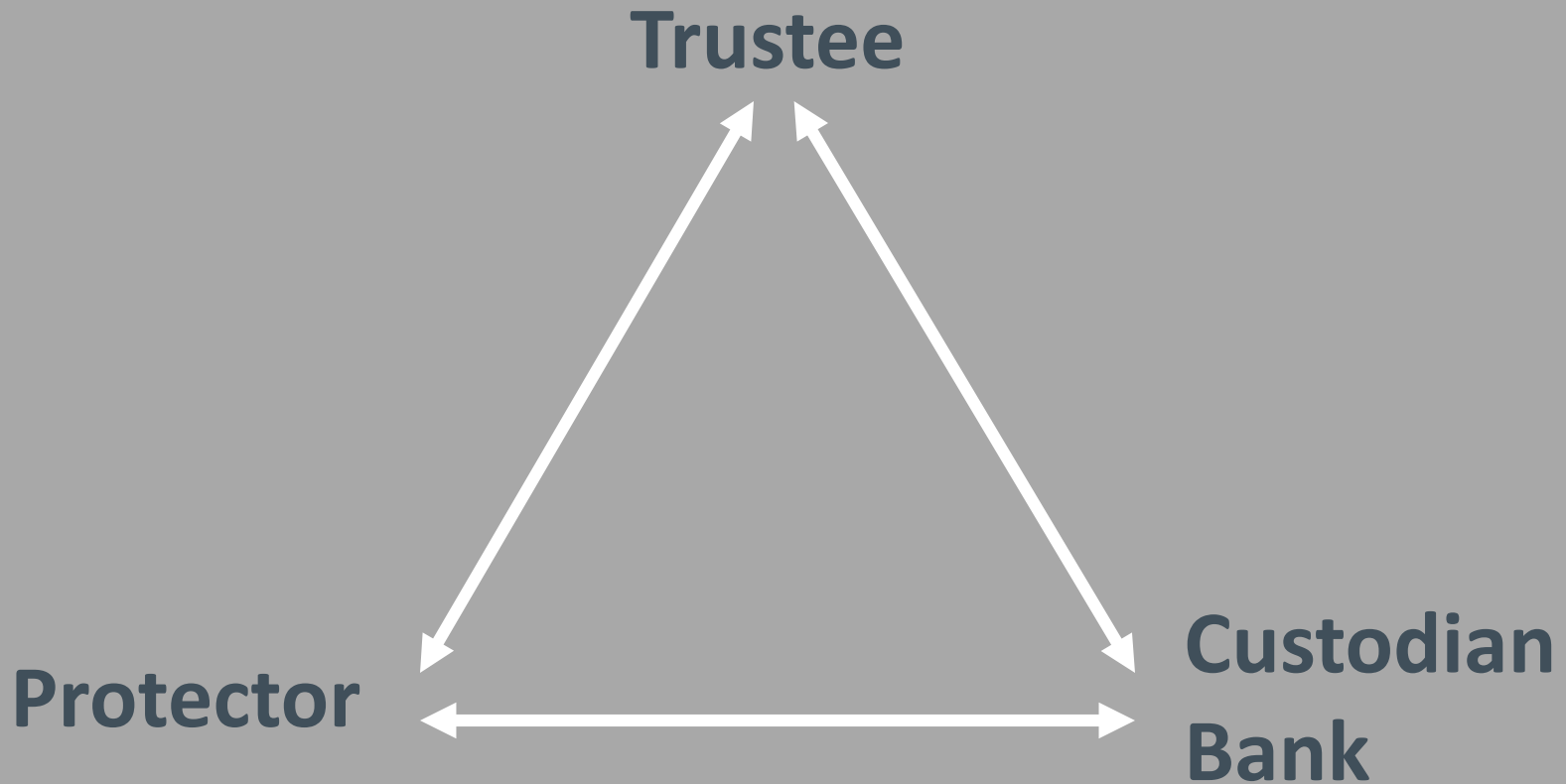


*Jurisdictionally Connected*



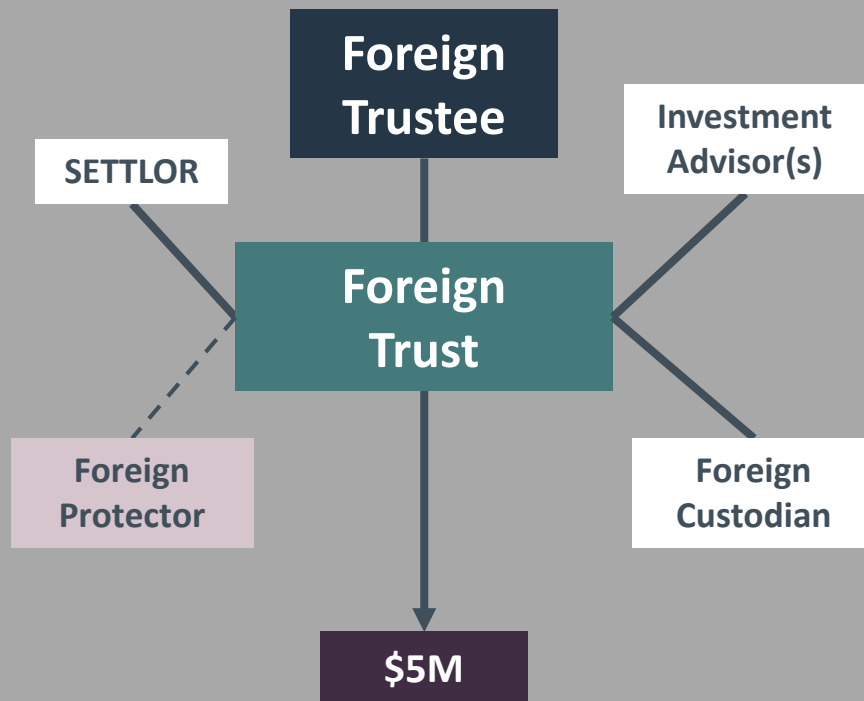
# Check and Balance System

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# Nest Egg Trust



## EXAMPLE

- Settlor has \$20M total assets
- Settlor has \$10M investment assets
- Settlor retains \$5M of investment assets personally and funds trust with \$5M
- Investment advice to Settlor and to Trustee may be provided by pre-selected investment advisor
- Contributions to trust are not subject to gift tax
- Settlor is subject to income tax on all earnings of the trust
- Trust assets are includible in settlor's estate for estate tax purposes

# Trust Implementation



# Selection of Jurisdiction

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- **Traditional Jurisdictions**
  - Jersey
  - Guernsey
  - Liechtenstein
  - Isle of Man
  - Bermuda

# Selection of Jurisdiction *(continued)*

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- **Established “Asset Protection” Jurisdictions**
  - Cayman Islands
  - Bahamas
  - Gibraltar
  - Belize

# Selection of Jurisdiction *(continued)*

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- **New “Asset Protection” Jurisdictions**
  - Cook Islands
  - Nevis
  - Turks & Caicos
  - Mauritius
  - Niue
  - St. Lucia
  - Antigua

# Negotiation of Fees

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- **Start-up**

- Legal fees
- Trustee fees
- Foreign taxes/duties

- **On-going**

- Legal fees
- Accounting fees
- Trustee fees
- Protector fees
- Custodial fees
- Money management fees
- Foreign taxes



# Taxation – Typically Tax Neutral

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- **Capital Gain Tax:** no tax on transfer of appreciated assets when trust is a Grantor Trust (*IRC §684*)
- **Gift Tax:** gifts can be either complete (*gift tax due on transfers*) or incomplete (*no gift tax due on transfers*); incomplete gift requires retention by grantor of special power of appointment
- **Estate Tax:** assets not includible in estate for federal estate tax purposes if there was a completed gift made at time of transfer, but are included if there was an incomplete gift made at time of transfer
- **Income Tax:** taxed as Grantor Trust if Settlor and at least one beneficiary are, or could be, U.S. persons (*IRC §679*)
  - All items of income, deduction, and credit flow through to Grantor



# Primary Foreign Trust

## *Filing Requirements*

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- **Form 3520:** Annual Return to Report Transactions with Foreign Trusts
- **Form 3520-A:** Annual Information Return of Foreign Trust with U.S. Owner
- **Form 1041:** U.S. Income Tax Return for Estates and Trusts (*prepare as Grantor Trust Information Letter*)





# Primary Foreign Trust

## *Filing Requirements (continued)*

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- TDF 90-22.1: Report of Foreign Bank and Financial Accounts
- Form 709: United States Gift (*and Generation-Skipping Transfer*) Tax Return “*Disclosure only*”





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