



Asset Protection Planning: Why Go Offshore?

By: Jeffrey R. Matsen



I. Introduction

Asset protection planning has been practiced by attorneys, financial planners and accountants for several decades. Business persons have always had concerns over the exposure of their personal assets to claims against their business. The corporate form of business entity with its shield of limited liability has been invoked for centuries. Certainly, protecting one's assets from the myriad of risk involved in business and personal financial planning is not a novel objective or planning idea.

Since the 1970's, expanding theories of liability and the proliferation of litigation have given increased emphasis to asset protection planning to the extent that it is now a well recognized area of practice. It certainly comes within the concept of lifetime estate planning involving the protection and conservation of accumulated wealth or asset base.

II. Primary Goal of Asset Protection Planning

A major goal of asset protection planning is to substantially diminish and reduce your financial profile. If you can restructure your assets in such a way so as to place them beyond the reach of future potential creditors, while at the same time maintaining a beneficial interest in those assets, you have succeeded in substantially reducing your financial profile. Accordingly, you are a far less attractive target for litigation because of issues of doubt of collectability, thusly reducing the likelihood that you will be sued; or if you are sued, increasing the likelihood of a favorable settlement.

III. The Use of Trusts in Achieving Your Goal of Asset Protection Planning

A trust can be an effective foundation for your asset protection planning. Trusts have been utilized for centuries as a means of conserving and protecting property for the beneficiaries of the trust. However, most domestic trusts do not provide protection from creditors. The typical revocable

living trust, wherein the trustors are the lifetime beneficiaries and retain the power to revoke, amend and invade the principal of the trust, provides no protection whatsoever against the creditors of the trustors. Accordingly, absent specific legislation to the contrary, self created or self settled trusts are ineffective for asset protection planning purposes.

IV. Domestic Asset Protection Trusts

As was stated previously, most self settled trusts are not protected from creditors. However, recently, several states have provided various degrees of asset protection legislation for a self settled trust. The trust legislation in Alaska, Delaware, Missouri, Oklahoma, Nevada, Utah and Rhode Island is similar in many respects to the asset protection trust legislation found in several offshore jurisdictions. It should be noted, however, that the courts have not had an opportunity to pass muster on this type of legislation because of its recent enactment and because the statute of limitations in most cases has not expired. Depending on the timeline involved with respect to when the claim has arisen, these trusts can be and should be considered in appropriate circumstances, but only by an attorney who understands all of the ramifications.

V. Foreign Asset Protection Trusts ("FAPT")

A. Introduction and Overview

Offshore asset protection planning normally involves the utilization of offshore trusts and other entities. Offshore planning generally raises justifiable concerns with respect to asset security and tax issues. The most efficacious manner to address these concerns is to make certain that you are receiving the best advice and counsel from a qualified expert in the area. You must be sure that the attorney with whom you are dealing has expertise in the field and is recognized in this regard by his

Asset Protection Planning: Why Go Offshore?

By: Jeffrey R. Matsen

peers.

A FAPT is a trust that is set up in an offshore jurisdiction which has enabling trust legislation providing for substantial protection against creditors of the trustor. One of the greatest advantages of the FAPT is the fact that by its very nature any legal attacks against its assets are transferred abroad to a different legal system. The FAPT is generally much more expensive to set up and create than a domestic trust and requires a certain willingness on the part of the Trustor to deal with offshore jurisdictions and trust entities. The FAPTs' greatest value is for asset protection planning well in advance of any potential creditor problem. Moreover, many times FAPTs are only used when the client already has some international connections and networking. Recent cases have emphasized the need for careful planning in the structuring of the FAPT if it is to be legally efficacious and successful in meeting the purposes and objectives of the trustor.

B. The major advantages and purposes of the FAPT are set forth below:

1. No Comity of Law in Foreign Jurisdictions

Most foreign jurisdictions do not recognize US judgments. This may force a trial de novo on the merits under the laws of the foreign situs in order for the creditor to impose liability on the trustor and reach the assets of the FAPT. Obviously, the fees and expenses of this trial de novo and the burden of having to select offshore counsel can be substantial. Moreover, the FAPT jurisdiction, generally, requires plaintiffs to employ attorneys who are licensed in that jurisdiction.

2. More Favorable Law

Most foreign situs jurisdictions require that the burden of proof in challenging asset transfers to a FAPT is on the creditor and does not shift to the trustor. Moreover, many foreign jurisdictions impose a higher standard of proof upon civil litigation plaintiffs such as the "beyond

the reasonable doubt" standard. This is in sharp contrast to the "preponderance of the evidence" principle utilized in US domestic civil cases.

3. Statute of Limitations

The FAPT legislation of many jurisdictions establishes a statute of limitations for challenging asset transfers to a FAPT that begins to run on the date of transfer. This is contrary to US law where the statute may begin to run the date the transfer is "discovered" by someone with a claim against the trustor. Additionally, the statute of limitations of many FAPT jurisdictions is much shorter than the typical four year statute found under US law.

4. Fees and Expenses of Litigating in Foreign Jurisdictions

Manifestly, it is going to be much more expensive and inconvenient to prosecute a claim offshore. Think of the inconvenience of having to pursue a claim out of state and then multiply that by two to three times the cost to pursue the matter in a foreign jurisdiction. Many foreign jurisdictions prohibit contingency fee arrangements forcing the claimant to finance a litigation process entirely on his/her own. Creditors may think twice about having to deal with a completely different legal system out of the country. This unfamiliarity, plus the additional expenses and costs, and the entire uncertainty with respect to the process, adds a substantial element of protection to the FAPT.

C. Non Asset Protection Purposes

The FAPT may assist the trustor in achieving several other objectives and planning goals independent of asset protection planning. Traditional estate planning issues such as the orderly transfer of property at death, the avoidance of probate, the strengthening of spendthrift provisions, greater privacy w, the management of offshore assets and businesses and premarital planning can all be addressed by the FAPT.

Asset Protection Planning: Why Go Offshore?

By: Jeffrey R. Matsen

VI. How the FAPT Protects Your Assets

A. Liquid Assets

The easiest way to understand how a FAPT protects cash and securities is to focus on the process by which a claimant would try to reach trust assets. A claimant must either bring his case in a court that has jurisdiction over the trustee so that the court can order the trustee to give up the assets or initiate litigation in the court that has jurisdiction over the assets themselves so that the court can attach or seize the assets. However, if the client's offshore planning strategy is properly structured and implemented, no domestic court can successfully attack the plan because it would not have the ability to force the offshore trustee to expatriate or return the assets nor would it have the ability to levy on assets properly held outside of the United States.

B. Non Liquid Assets

Protecting non liquid assets like real estate, accounts receivable and business equipment involves the process of equity stripping. Although some of these assets can be put in charging order protected entities that may provide some limited protection, the most effective strategy available to protect a domestic illiquid asset is to strip that asset of its value by encumbering it as collateral for a loan and protecting the loan proceeds with your other liquid assets in the FAPT. Creditors are going to be very discouraged attempting to levy on an asset that may have substantial value, but has very little equity because of a loan encumbrance or lien.

VII. US Tax Consequences

Generally speaking, the establishment of the offshore asset protection plan will be tax neutral. The FAPT will either be a US grantor trust or a foreign grantor trust with a US grantor for US income tax purposes. It will be necessary to file various forms with the Internal Revenue Service in either case, but these forms will only demonstrate that the

taxpayer is a responsible and law abiding citizen.

VIII. Offshore Planning Structure

One very typical arrangement with respect to a possible offshore strategy would be for the client to establish the offshore asset protection trust utilizing an offshore trustee. The trust would then set up an offshore limited liability company which would be entirely owned by the offshore trust. You could be the manager of the LLC with direct signature control over bank accounts and securities accounts. In the event of a crisis, you would obviously resign as a manager and appoint a trusted friend, relative or a management company. There are modular variations to this strategy that can be worked out with your professional advisors.

IX. Conclusion

The proliferation of plaintiff lawsuits and the expanding concept of liability that has become second nature in our court system have engendered much concern and anxiety about the preservation of wealth in the United States. Many professionals like doctors and lawyers as well as business owners, corporate executives, real estate developers and investors, contractors and others operate in an environment of high risk. Many such people lack confidence that they will be treated fairly by the US legal system and are desirous of reducing their financial profile and eliminating their liability potential. For these individuals, the offshore planning alternative may very well be the best planning device available for maximum comfort and piece of mind.

Jeffrey R. Matsen provides sophisticated asset protection, estate and business planning services to affluent individuals and families, prestigious institutions and highly successful business owners. Matsen has been designated and honored by Worth Magazine as one of the nation's "Top 100 Attorneys".