There is a case study set out in Appendix 1 of this paper which sets out a typical client situation arising in the current climate where advice on asset protection is sought. There will be reference to this case study throughout the lecture.

1 Introduction

It has become very clear in recent times that clients are concerned with their borrowings and they want to be sure they will not lose 'the roof over their heads'. Practitioners are being asked as to how to go about protecting their client assets in the event of the clients becoming unable to meet their debts. The purpose of this paper is to outline how best to advise these clients - when they should start protecting the assets, how they should do it and what are the benefits and potential downsides to introducing such protection. Also today I would like to highlight other reasons behind why certain clients consider asset protection.

2 Why are assets protected?

While asset protection comes to mind most frequently these days in the context of insolvency, the use of asset protection measures is not confined to protecting assets from creditors in the face of impending insolvency.

Traditionally asset protection concerns have arisen in the following situations:

- Where there is a potential of insolvency based on existing borrowings taken out;
- Where traditional professions who were (or still are) not entitled to incorporate are concerned to protect their assets over and above their professional indemnity cover (e.g. solicitors, doctors, architects, accountants). This is likely to increase further with the considerable pressures being put on the professions by virtue of the increases in the professional indemnity cover. Many professionals may only be able to afford to take out minimum cover but are then more exposed to claims above that lower level of cover and wish to protect their personal assets from such claims. Indeed if the cover is so conditional and these conditions are not met, the professional client may find that in certain cases the cover will not apply and so his assets are fully vulnerable;

- Where a person is a member of a Lloyds' syndicate;
- Where a person, who is trading under the protection of limited liability through his company, has had to give personal guarantees e.g. for rent or company borrowings;
- The entrepreneur about to start out on a potentially hazardous business;
- The business person selling up who does not want to lose all that he made if any of the warranties given are ever called upon;
- Where a person is concerned about impending divorce/separation claims from a spouse;
- Where a person wishes to avoid 'forced heirship' provisions requiring him to transfer his assets on death to particular beneficiaries;
- In the case of the improvident or profligate beneficiary – where the client wishes to provide for assets to pass to a person, e.g. a child, who may not be able to manage financially yet the client wishes the child to be given some independence;
- Corporate clients concerned about the risk of expropriation or confiscation of corporate assets operated in 'risky' jurisdictions. This can be done by creating what is known as a "Philips Trust". However there are significant complexities inherent in creating an appropriate trust vehicle for a large corporate body with worldwide operations and assets. This topic is outside the scope of this talk today.

In all of these cases the client wishes to divest himself of his 'good' assets so that others cannot claim against those assets, yet at the same time the client wishes to retain the assets for his own use and enjoyment for his lifetime and have as much control as possible over them. Naturally the client also wishes to ensure the divesting of the assets and the ongoing management of the assets do not trigger significant taxes.

The client's creditors can fall into several time categories - present, potential and future -

- present creditors are those to whom liabilities are now due from past dealings, including cases where liability is admitted as well as where it is denied
- potential creditors are those to whom liabilities may become due from current dealings and;

- Future creditors are those to whom liabilities may become due from future dealings, where the client has current customers whom he thinks will come back to do business in the future as well as customers he does not have e.g. in a start up position[1].

The people who make claims against the trustees of trusts created for asset protection purposes by a client (who was the 'settlor' of the trust) include:

- The creditors of the settlor who claim that the trust assets are liable to be taken into account in satisfaction of their debts;

- Members of the settlor's family who claim indefeasible or discretionary matrimonial or succession rights;

- The Official Assignee in bankruptcy of the settlor who has been made bankrupt claiming to set aside transfers made into the trust;

- Public authorities who claim the assets disposed of are the proceeds of crime;

- In certain countries criminal prosecution authorities who claim that an offence has or may have been committed in setting up the trust;

- The settlor himself against the trustees if it should be determined that the trust is for some reason ineffective.

The creditor usually claims against the assets by stating either that the settlor retains a beneficial interest capable of being taken in the execution of the judgment (a 'sham trust argument') or that the transaction creating the trust is liable to be set aside in whole or in part as either a fraud on the creditors or made within a particular time frame that it can be set aside and thus the assets can be taken to satisfy judgment.

[1] Re Butterworth, ex p Russell (1882)19 ChD 588 held that, in determining whether a settlement was entered into to defraud creditors, the court should account for not just actual creditors and potential creditors (where the settlor was already dealing with them as customers) but also future creditors, where the settlor was proposing to embark on a hazardous activity, had not yet done and business and had no future creditors in view at all. The relevant legislation was section 172 Law of Property Act 1825

Claims can be made by family in relation to succession/matrimonial matters. For instance, in Ireland the following claims can be made by family members;

- The spouse of a deceased has a legal right share in the estate on the death of the Settlor to either a one third share of the estate or a one half share of the estate (depending on whether the deceased had children)[2]. If the asset protection structure has been created so as to defeat the amount available to pass under the Succession Act and therefore reduce the legal right share, this could be challenged under legislation that allows the court to add back assets divested within 3 years of a deceased's death if the transfer was done for the purposes of diminishing or defeating the claim of the spouse[3].

- Likewise the children of a deceased have a right to claim for proper provision to be made by the deceased[4] and if this right is reduced or diminished by the transfer of the deceased's assets within 3 years of his death to an asset protection structure, this can also be a basis for children to claim against the trust under similar grounds as that of the spouse's claim.

- Similar claims can be made by spouses and children whose rights under intestacy have been reduced by the transfer of the assets out of the name of the deceased into the asset protection structure, again within 3 years of death[5].

- Under matrimonial legislation[6] a transfer to an asset protection structure can be reviewed by the courts and set aside within 6 years[7] of the transfer if the disposition was made with the intention of defeating a claim for relief under the matrimonial legislation.

In addition these relatives could also claim that the transaction was a sham and accordingly the assets still form part of the settlor's estate on his death divorce separation.

---

[2] Section 111 Succession Act 1965
[3] Section 121 Succession Act 1965
[4] Section 117 Succession Act 1965
[5] Section 121 Succession Act 1965
[6] Section 74 Family Law Act 1995 and Section 75 Family law (Divorce) Act 1996
[7] If the transfer takes place within 3 years of the application for review of the disposition, the burden of proof is on the transferring spouse that the transfer was not made for the purpose of defeating a claim. If it takes place after 3 years, the burden shifts to the claiming spouse.

3 How assets are protected

There are different approaches to the way a person may wish to protect assets, ranging from the simple to very complicated.

3.1 Incorporation

Where a person incorporates his business into a limited liability company, he is protecting his personal assets from being attacked in the case of any insolvency of the business. The company becomes a separate legal entity from its members/shareholders so that creditors of that company cannot attack the assets of the owner of the company to recover debts owed to them to the extent that the shareholder has fully paid up the shares in the company.

Incorporation is highly recommended for businesses that may be subjected to claims against them in respect of the products of that company or by its own employees e.g. construction companies are vulnerable to claims against them by purchasers of houses in respect of a fault in the building of its houses and by its employees in the event of accidents on the worksite. Limited liability is very useful to protect the shareholder from such claims against him personally. The value the shareholder has put into the company will be lost if the company is liquidated on insolvency but at least the rest of the shareholder’s assets are not vulnerable to claims by creditors of the company.

There are however limitations to the benefit of incorporation such as the following:

- In cases where the company takes out borrowings for the business, usually the bank may require a personal guarantee from the directors/shareholders of the company thus defeating the benefit of the limited liability status in respect of those borrowings.
- If the owner has funded the company by way of an unsecured loan, it is unlikely that loan will be recovered on a liquidation of the company as it will rank lower than secured creditors.
- As mentioned above, many professional trades are not permitted by virtue of their governing bodies to incorporate in a limited liability fashion, e.g. in the case of solicitors, doctors, architects, accountants.

- Even when limited liability is achievable, it may not be suitable for the person to apply it from a marketing point of view. E.g. the introduction of limited liability beyond the required minimum professional indemnity cover for Irish solicitors has not been taken up widely in the profession to date.
- Where the courts or the legislature permits the lifting of the corporate veil. A company is a distinct legal entity separate from its members. A veil therefore separates the company from its members from the date of incorporation. However, the courts and the legislature in certain instances can lift the corporate veil and look through the separate legal entity of the company to its shareholders. If this happens, individual members can be held liable for the debts of the company itself. Instances of when the corporate veil can be pierced are set out in Appendix 2 below.

The effect of incorporation is therefore limited from a pure asset protection point of view.

In turn it is important to note that the transfer of 'healthy' assets into a limited company will not protect those assets from an attack by the creditors of the shareholder. If the shareholder himself is likely to become insolvent, the transfer of his assets in advance of insolvency into a corporate structure will not protect those assets from claims by his creditors. The shares of the bankrupt shareholder (and therefore the value of the company and the assets within that company) are available to the Official Assignee in Bankruptcy.

Therefore in the case study outlined in Appendix 1, although Joe has an incorporated business, Construct Ireland Limited, that company is not protected from claims by Joe's creditors. As it may in fact be one of the healthier of Joe's assets, it will be vulnerable to claims by the banks on foot of Joe's personal borrowings for the sites. The banks may seek to realise the value of Construct Ireland Limited by forcing a sale of Joe's shares in the company or by forcing the company into liquidation to realise the value of Joe's shares in the company.

On the other hand, if Construct Ireland Limited turns out to have bad debts and needs to be wound up, the debts of Construct Ireland Limited will not affect Joe's solvency status other than that he no longer holds any value in the shares (provided of course it cannot be said that he was involved in reckless trading, see Appendix 2).

3.2 Nomineeship or Bare Trust

Where a trust is created so that the person who owns the assets (the 'settlor') transfers the assets to another person (the 'trustee') for the trustee to hold the assets solely for the benefit of the settlor, a bare trust or nomineeship is created. Despite the fact that the legal ownership of the assets are transferred out of the settlor's name, creditors of the settlor could still look to these assets as they are held by the trustee beneficially for the settlor. Therefore the transfer of the assets is not an effective method of asset protection. At Appendix 3 there are examples of trust structures that may at first sight appear to be more than bare trusts but in fact the assets are still within the settlor's control and are in fact bare trusts.

In many cases, it is not obvious on the face of the document that the trust is a bare trust. If a trust is created that appears to be one of substance and therefore is not a bare trust but subsequently it is held that the trust form is a sham, it becomes a bare trust as, while the legal ownership is held by the trustees, the equitable ownership and control remains in the settlor. The crucial question to ask is whether the form of the trust instrument is such that the settlor retains equitable ownership in the capital so that the trustees hold the capital to his order without the settlor having to do something positive. If the trust is a sham, apparently having legal effect but not really intended by the parties to have any legal effect (the settlor having real control of the trust fund), then the trust is ineffective except in the nomineeship/bare trusteeship sense as the whole equitable ownership remains in the settlor.

The case of *Rahman -v- Chase Bank (CI) Trust Company Limited* [8] was a case where the trust was determined to be a sham. If the trust instrument, such as the one in *Rahman,* provides for many rights and powers to remain with the settlor then the easier it is for the trustees to let the settlor run the trust and the easier it becomes to attack the trust as a sham. If the transaction is shown to be a sham then the assets are treated as continuing to belong to the settlor and those assets can be taken to satisfy any creditor's judgment.

The difficulty for clients is that the client as settlor usually wants to keep control of his assets, particularly where the assets being transferred to the trust are business assets. There have been structures where the settlor transfers 98% of the business

[8] *Rahman -v- Chase Bank (CI) Trust Company Limited* (6 June 1991)

assets to the trustees to hold as limited partners and he retains the 2% of the asset himself subject to a Partnership Agreement where control is reserved to the 2% holder as the general (and managing) partner. In such a case a Partnership Agreement may satisfactorily explain the settlor's daily control of the business assets for partnership purposes but, if the settlor in turn seeks to control the disposition of the income and the capital benefits out of the trust to the beneficiaries, then the trust and perhaps the related partnership could be regarded as a sham.

If the truth is that the property continues to belong to the settlor and the transaction of creating the trust is merely a smoke screen, it is open to challenge.

A concern may also arise in the event that the trustee himself becomes a bankrupt and his creditors seek to take the trust property into account in meeting the trustee's own debts. While the creditors are not entitled to do so as it is not property beneficially owned by the trustee[9], the trustee[10] will have to prove the fact of the trust to ensure that the assets are protected. If this trust was set up to 'hide' the assets from the settlor's creditors, those creditors can find the assets all the more easily at that stage.

In the example given in Appendix 1, Joe could set up a bare trust himself as settlor transferring his assets into the name of Mary as trustee (or indeed say to his brother whom he trusts) to hold on trust for Joe as beneficiary. However, this would provide no protection as, were Joe to be made bankrupt, the trust would be fully available to Joe's creditors for the payment of their debts despite the fact that the assets would be in the name of another person (Mary or Joe's brother).

3.3 Life Interest or other Interest in Possession Trust

Where a trust is created so that the person who owns the assets (the 'settlor') transfers the assets to another person (the 'trustee') for the trustee to hold the assets solely for the benefit of the settlor for his lifetime and for the assets to pass on the settlor's death a certain way (e.g. to the spouse or children of the settlor), a life interest trust is created. This is a form of an interest in possession trust, other forms being trusts in favour of a person for a period shorter than the life of the beneficiary involved.

---

[9] Section 44(4)(a) Bankruptcy Act 1988
[10] Or rather the beneficiary on behalf of the trustee who has the interest in pursuing this!

The effect of such trusts is that the beneficiary of the interest in possession has the right to receive the income of the trust. Therefore, if such beneficiary were to become bankrupt, his creditors could require the trustees of the trust to pay that income to them to meet the debts incurred by the beneficiary.

While the trustees are generally given power under the terms of the trust to invest in assets which may or may not produce income (and therefore presumably weigh in favour of capital growth), the trustees are at all times bound by their fiduciary duty to balance the needs of the person holding the interest in possession against the needs of the persons entitled on the expiry of that interest in possession (the remaindermen). Therefore if the creditors believe that the trustees have not balanced the need for income for the life tenant (who as the bankrupt would have to pass on that income to his creditors) as against the need for capital growth for the remaindermen, they could sue the trustees for breach of their fiduciary duties.

Therefore the transfer of a client's assets into a life interest trust or other interest in possession trust will not give any protection to the income arising out of such assets and will not protect the assets from being converted into income producing assets, which income can be taken by the client's creditors to meet debts.

In the example given in Appendix 1, Joe could set up a life trust himself as settlor where he is a beneficiary so that the assets are held in the trust and any income out of these will be paid to Joe himself and that on his death Mary, Saoirse and Fintan would benefit. In such a case if Joe were to become bankrupt, all the income arising form the assets in the trust would be used to pay off his debts and the trustees would be obliged to ensure that the assets do produce a decent amount of income to do this. The capital of the trust however would be preserved for the benefit of Mary, Saoirse and Fintan on Joe's death.

3.4 Protective trust

The protective trust was originally a Dickensian style of trust whereby the benefactor sought to ensure that his dependant received a living from a trust through a life interest but, concerned that the dependant might squander what he would get from the trust in the future, the trust would automatically convert to deprive him of the interest in the trust on certain acts arising so that the beneficiary would not be guaranteed anything into the future (and so his creditors could not claim that interest from him). While it is still suitable for the improvident and the profligate, in more modern times with adjustments it has also become more fashionable for the risk taking entrepreneur.

A protective trust in modern times is a combination of a life interest and a discretionary trust. It is a trust which provides that the beneficiary, who may become vulnerable to creditor claims, receives all the income from the trust fund during his lifetime but, if anything happens or if the beneficiary himself commits any act which would, if he were entitled absolutely to the trust fund, have the effect of depriving him of it, his interest as a beneficiary would cease and determine immediately. In such a case, instead of the trustees holding the trust fund for the beneficiary for his lifetime, they would automatically hold the trust fund on discretionary trusts for a class of beneficiaries including the original beneficiary, his spouse and children and other extended family members if so desired. The discretionary trust would continue for the balance of the lifetime of the original beneficiary and if required[11] could automatically cease on the death of that beneficiary to pass on death to specific persons e.g. to his spouse and/or children.

The effect of this is that the funds would still be available to the beneficiary through payments to his family or on a discretionary basis to discharge outgoings actually incurred by him, yet he would not be automatically entitled to the assets in the event his creditors sought to recover from them.

In the example given in Appendix 1, Joe could set up a protective trust himself as settlor where he is a beneficiary so that the assets are held in the trust and any income out of these will be paid to Joe himself but that, were he to be made bankrupt, the trust would become discretionary with Joe, Mary, Saoirse and Fintan as potential beneficiaries, the discretionary element ceasing on Joe's death and then passing to Mary or, if she has also died, to Saoirse and Fintan equally.

3.5 Discretionary trust

A discretionary trust provides that trustees hold the trust fund on discretionary trusts for a class of beneficiaries including the 'intended' beneficiary, his spouse and

[11] Usually this would be done to avoid discretionary trust levies (see below)

children and other extended family members if so desired. The trustees are usually guided by a letter of wishes written by the settlor regarding how they might exercise their discretion. This letter is not legally binging on the trustees. The discretionary trust could continue for the lifetime of the 'intended' beneficiary and if required[12] could automatically cease on the death of that beneficiary to pass on death to specific persons e.g. to his spouse and/or children. The advantage to this trust over the protective trust is that the automatic change in status of the trust from a life interest trust to a discretionary trust would trigger capital gains tax (as outlined below) but if the trust is always discretionary such tax would not arise on the beneficiary becoming bankrupt. As with the protective trust however, CGT would still arise on the death of the beneficiary (if the discretionary element were to cease automatically on death) or on any payments out of capital from the trust.

It has become a trend that the creation of discretionary trusts for the purposes of protecting assets are made more 'awkward' to attack by creating blind trusts and/or locating such trusts offshore.

3.5.1 Blind Trust

To be valid a trust must have certain ascertainable beneficiaries. In many instances a trust is set up whereby the beneficiary is a charity, such as the Red Cross, and the trust is held for exclusively charitable purposes or such exclusively charitable purposes as the trustees may select from time to time. There is then power to add anyone in the world to the class of beneficiaries or a power to appoint to anyone in the world which power is to be restricted to persons nominated in writing by either the settlor, the protector or existing beneficiaries. This is done often for perception purposes, given that it would on the face of the trust appear that the settlor is not a beneficiary of the trust and therefore his creditors are less likely to seek to attack the trust. However if the settlor is subsequently added as a beneficiary of the trust and discovery proceedings are taken against the trustees, this mechanism of hiding the trust assets is defeated. If the settlor has been appointed the assets in the trust, such assets would be available to his creditors to meet payment of their judgements.

[12] Again usually this would be done to avoid discretionary trust levies (see below)

To ensure that this trust is not challenged as a sham, the trustees should not take literally the settlor's letter of wishes but should act independently of the settlor. In addition the letter of wishes should not indicate that the settlor would be of the view that the trustees should never actually benefit the charity.

The trustees will be subject to the rules regarding accountability which means that each beneficiary needs to know that he is a beneficiary so he can bring the trustees to account if necessary.[13] Therefore in a discretionary trust where the Red Cross are named as the charitable beneficiary, the Red Cross would need to be informed that they are the potential beneficiaries. The persons who are identifiable as merely contingent beneficiaries (e.g. the issue of the settlor unnamed) can also exercise their rights to see accounts and discover how the trust property is invested[14]. While there is no duty to inform the objects of discretionary powers (as opposed to discretionary trusts) the settlor may be uncomfortable with the objects of the discretionary trust having such information.

3.5.2 Offshore Asset Protection Trust

A typical asset protection trust is usually made totally offshore so that the trustees, the governing law and the situs of the assets are all out of the jurisdiction where the settlor carries on or has carried on his business. It is not necessary for this to happen, however the offshore element is usually included so as to provide obstacles to creditors and others in attacking the trust.

The offshore asset protection trust ('offshore APT') is designed to side step the insolvency law, the succession law and the matrimonial law of the jurisdiction local to the settlor. However it is not usually designed to be tax efficient.

Another typical feature of an offshore APT is that the settlor remains very much the principal beneficiary, if not the only beneficiary, during his lifetime. He may have a life interest or other interest in possession limited to come to an end in certain circumstances (such as bankruptcy) i.e. as a protective trust, but the settlor will

---

[13] *Brittle Bank -v- Goodwin 1864 LOR5 Eq 565, Spellson -v- George 1987, Scully -v- Southern Health Board 1991 4 All ER 563*

[14] *Chaine-Nixon -v- Bank of Ireland 1976 IR 393*

occupy a particular role in the control of the assets in question. This is the great attraction of the offshore APT for the settlor but can also be its downfall.

While the offshore element of the APT seeks to cause an obstacle to the creditor enforcing the judgment or the relative making the claim, it is not necessarily an insurmountable one. The Brussels Conventions[15] facilitate the creditor/spouse considerably in enforcing his claim if the creditor/spouse obtains a judgement in one of the EU states and the offshore APT is located in another EU state. Because of this, typically offshore APTs are located outside of the EU but this can introduce further taxation downsides. In other jurisdictions, the local legislation can ultimately provide comfort to the creditor so that the creditor's judgement for debt can be enforced in the country where the offshore APT is located and they can access the funds, however the cost and time spent in doing this can put off many creditors.

There is also the possibility of the situs of the offshore APT moving jurisdiction through provisions in the trust instrument so that the place of residence or business of the trustees (as opposed to the place where the assets are or indeed the governing/proper law of the trust) can change. Sometimes this can take place automatically or in consequence of an exercise of a power to do so whether exercised by the trustees, the settlor or someone else such as a protector. In such cases clauses known as "flee clauses" are inserted allowing for a trigger event where the jurisdiction of the situs can change. This is a favourite technique in asset protection planning where the trustees do not move but the assets within the APT do, leaving one trust and joining another. Sometimes 'pilot trusts' are set up with nominal value to allow for this. In this way there can be a chain of pilot trusts stretching from jurisdiction to jurisdiction so as to again provide obstacles for creditors in claiming against the assets of the trust.

Quite apart from the cost involved in going to such extremes in running away from creditors seeking to enforce judgements against the trust in various jurisdictions, the downside to this approach is that on the transfer of the trust to another jurisdiction the trust may not comply with the laws of that jurisdiction. If the trust is defeated by

[15] Brussels I – Council regulation (EC) No 44/2001 of 22 December 2000 on jurisdiction and the recognition and enforcement of judgements in civil and commercial matters (but does not apply to areas of civil law such as wills and succession). Brussels II and Brussels II bis– the Council regulations (EC) No 1347/00 of 1 March 2001 and 2201/2003 of 27 November 2003 on jurisdiction and the recognition and enforcement of judgements in matrimonial matters (Denmark excepted).

provisions within the legislation of that jurisdiction, the result will be that that jurisdiction would decide that the trustees hold the assets on resulting trust for the settlor himself thus unwinding the protection. Examples where this could arise is that the use of the protective trust where a life interest is determinable on bankruptcy is valid in one jurisdiction (e.g. Ireland) but void as against public policy in another jurisdiction (e.g. England and Wales[16]); also the trust must comply with the local rules against perpetuities and accumulations. This also ignores the significant tax implications that most likely could arise on a trust exiting one jurisdiction and entering another.

Certain jurisdictions, such as Belize (formerly British Honduras), have special legislative provisions concerning the rules of enforcement of judgments. For instance if the offshore APT is resident in Belize, the Belize courts will not recognise or enforce any judgment or order purporting to set aside a disposition to a Belize trust. Nor will the Belize court give effect to claims against Belize resident trustees. In addition it will not give any assistance to a trustee in bankruptcy appointed by a foreign court. In effect, the assets of a Belize trust cannot be attacked to satisfy the judgment of a foreign court based on any foreign law. This is so even if the transfer is done with the specific intention of defeating the claims of creditors, and whether the claim and/or the judgment arose before or after the trust was created.

Other jurisdictions attempt to deal with fraudulent conveyance claims by mandating a statutory limitation period and imposition of other procedural requirements for the prosecution of such claims. For instance the period is two years in the case jurisdictions such as Nevis, the Turks & Caicos and the Cook Islands. In effect, in these jurisdictions the law of fraudulent conveyances continues to apply to trusts created in the jurisdiction, subject however to time constraints

Such provisions however will only protect the trustee in the trustee's home jurisdiction. If he or the assets of the offshore APT should stray outside of that offshore nirvana or if the trustee himself holds assets in other countries, the trustee may find himself subject to legal proceedings, judgments and orders under a less kindly law. Therefore if the assets consist of Irish situate property and this property is transferred into an APT created in Belize, the creditors can still attack the assets in Ireland even though the Belize law does not recognise the attack on the trust itself.

[16] Underhill and Hayton Trusts and Trustees 14 Edn at pg 155, note it is trust law not insolvency law that strikes it down

The trustee therefore needs to bear in mind that the trust can be subject to claims within its home jurisdiction and more significantly claims within any jurisdiction where the trust assets are located.

3.6 Transfer to spouse

The simplest and most tax effective way of protecting assets is to transfer them to a spouse, provided of course the client is comfortable with the spouse owning the assets solely going forward.[17]

The complexities arising from this approach would be

- What types of assets are most suitable for transferring? It would be sensible to transfer only assets that have no borrowings secured against them;
- Would the spouse also be vulnerable to being made a bankrupt? If the spouse is also in a business that is exposed to claims, are the assets moving from the proverbial 'frying pan into the fire'?;
- If assets that are currently free of borrowings are transferred to the spouse, will these need to be used by the spouse to earn a living for the family and, if so, will the spouse have to enter into borrowings in her own right? There is a dilemma if a good trading asset is transferred to the spouse but later that trade needs finance and the spouse then also enters into the spiral of borrowing;
- What about future divorce or separation? Marriages are put to considerable tests when financial difficulties arise.

[17] There are widespread crude asset protection schemes such as the case in Canada where a husband, on the eve of bankruptcy, transferred his shares in the matrimonial home to his spouse alleging marital breakdown and thereupon obtaining a Family Court Order sanctioning the transfer. The next day he bankrupted himself, sure in the knowledge that the house was safe from his creditors! However since then the Canadian Courts have moved away from the protection from collateral attack of the Family Courts by the Bankruptcy Courts and have allowed for such a transaction to be set aside(1). The Australian courts however still appear to allow for such a method of protection. In Ireland this distinction does not arise as the fraudulent preference provisions of the Bankruptcy Act 1988(2) (which provisions will be dealt with in more detail in the later lecture by Dearbhla Cunningham) apply to transfers to spouses.(3)

1. Peake v Dashey #31/0434764 ON S.C. July 15 2009, also see STEP Journal Oct 2009
2. Section 59 Bankruptcy Act 1988
3. unless made before & in consideration of marriage, in which case separate provisions apply

Typically a client is usually comfortable in transferring the family home (or his undivided joint share in it) to his spouse provided he clears the borrowings off it in advance of the transfer. There is an element of resignation that in any future divorce the spouse would get the house anyhow!

In the case study Joe should consider with Mary using their savings (Joe in priority to Mary, leaving Mary with cash of €125,000) to discharge the borrowings on the family home (provided the family home is not used as collateral for any other borrowings). Then Joe could transfer the home to Mary free of tax. Mary has a share of the borrowing on site 2 but, as the security is recourse only to the land itself, although her credit rating would suffer if there was a default on the loan, the family home would not be able to be taken to meet that debt of hers. In any event, given the value decrease, it is likely the bank lending for site 2 would only agree to a transfer by Mary to Joe provided further security is furnished, which would not be appropriate for Mary to give.

3.7 Transfer to children

Another simple way to protect assets is to transfer them to a child or children (or in trust for them if they are under age 18).

The complexities arising from this approach would be

- The transfer will trigger taxes, unlike in the case of a transfer to a spouse;
- What types of assets are most suitable for transferring? It would be sensible to transfer only assets that have no borrowings secured against them;
- If assets that are currently free of borrowings are transferred to the child, will these need to be used by the child in a risky fashion to get their value worth and, if so, will the child have to enter into borrowings in his own right? There is the same dilemma that if a good trading asset is transferred to the child but later that trade needs finance and the child would also enter into the spiral of borrowing;
- Is the child capable of managing the asset? Coming into assets at a young age can be intimidating or could set a child off on a spending spree! While the client may be there to guide the child, at the end of the day it is the child's assets with which he can do what he pleases!

In the case study Joe and Mary might consider transferring their joint interest in site 2 to Saoirse if it is clear to them both that that site will be of considerable value in the future, it can currently of itself fund the borrowings and they do not want it to be lost in any bankruptcy of Joe's. However, given the value decrease, it is unlikely the bank lending for site 2 would agree to a transfer by Joe and Mary to Saoirse unless further security is furnished, which would not be appropriate for Mary to give (though maybe it would be possible for Joe to give personally if the bank thought him still to be a good call after Joe has already transferred the family home to Mary). Joe and Mary would be making a call on Saoirse having the good sense to ultimately manage the site once it shows promise. Giving the site to Saoirse who may need to borrow against it further if it were to be developed in the future would protect the family home still (as would not arise in the case of giving the site to Mary). However Saoirse may not appreciate in later years being saddled with the debt on this site, particularly if it turns out that it is not producing any income to meet the current borrowings.

4 Legal issues to consider

4.1 Declaration of Solvency

Before the transfer of any asset into a company or trust, or to a spouse or a child ('the assets protection structure'), the question of whether that transfer is valid or could be unwound needs to be addressed. I have referred briefly above to the fraudulent preference provisions of the Bankruptcy Act 1988[18] (which provisions will be dealt with in more detail in the later lecture by Dearbhla Cunningham). These provisions apply to any transfers made at an undervalue, i.e. by way of gift or partial gift, unless made before and in consideration of marriage, in which case separate provisions apply. If assets are transferred into any of the asset protection structures mentioned above, care must be taken to ensure the legislation will not apply to unwind the transfer and make it available to the Official Assignee in Bankruptcy of the client.

The legal practice to provide good title to the assets transferred is that the client must swear a declaration of solvency stating that he is solvent without recourse to the

[18] Section 59 Bankruptcy Act 1988

assets proposed to be transferred. However in addition it would appear sensible for the client to back up that declaration with a statement of net worth that has been prepared and analysed critically by professionals. While this would not protect the transfer until the 2 year cut off period has passed (during which time, if the client becomes bankrupt the transfer can be declared void whether or not the client was in fact insolvent at the time of the transfer), it will assist the transferee to resist a claim made if the client becomes bankrupt within 5 years of the transfer (but after the 2 years have passed).

There is no requirement for an Official Assignee to prove a fraudulent intention in these cases. If the bankruptcy occurs within 2 years, no proof is necessary regarding fraud or solvency. If the bankruptcy occurs between 2 and 5 years, the only proof required is that the settlor could not pay his debts at the date of the transfer without recourse to the property transferred.

Nevertheless, where there is a conveyance of property made with the intent to delay, hinder or defraud creditors and others of their just and lawful debts, rights and remedies, such a conveyance is voidable unless the conveyance is bona fide for full consideration to a person not having notice or knowledge of the intended fraud.[19] There is no time limit on this provision, albeit in this case the intent to defraud would have to be proved.

4.2 Joint assets

Where a person holds an asset in the joint names with another and that asset in itself is not subject to any debt, the share of the asset owned by the person, should he become bankrupt, is available to the Official Assignee in Bankruptcy. If the asset is held in joint ownership as tenants in common, it is usually clear who owns what share of the property so that the percentage open to attack is clear. In the case of joint tenancies, the presumption is that the asset is owned equally by the joint owners.

Where there is a debt on the jointly owned asset itself, the asset must be used to pay off the joint debt first. If that debt is paid off and there is still value in the asset, then the remaining share of the asset is available to meet the debts of the joint owner who has been made bankrupt. Where the debt on the joint property is greater than the

---

[19] Sections 10 and 14 Conveyancing Act 1634 which will be re-enacted with effect from 1 December 2009 in Section 74(3) Land and Conveyancing Law Reform Act 2009

value of the joint property, the balance of the joint debt should be paid out proportionally out of the separate assets of the joint owners.[20]

For example, in the case study Joe and Mary jointly own the family home with a small mortgage on it. If Joe was not to transfer the family home as suggested above and later Joe was to become bankrupt, his share of the home and its mortgage would be deemed to be 50%. The 50% share that Joe has in the home would be used to pay off his 50% share of the debt on the home. After that, the balance of his 50% of the house would be available to pay off his other debts. While Mary's own 50% of the home cannot be taken by the Official Assignee, the practical effect is that unless Mary can buy out Joe's share out of her own funds, she would have to sell her share also to let Joe meet his debts and use her net share to buy a smaller house.

If on the other hand the house mortgage was higher than the value of the house (e.g. the house was worth 1,500,000 but the mortgage was 2,000,000 then, on Joe's bankruptcy, the Official Assignee would sell Joe's share in the house receiving 750,000 to pay off Joe's loan of 1,000,000 and pay off the outstanding balance of Joe's loan of 250,000 as best he can out of other assets, bearing in mind Joe's other debts. Mary in turn would have to pay off her share of the loan of 1,000,000 out of her share of the house, 750,000, and other assets in her own name.

4.3 Charged assets

Dearbhla will deal with the effect of assets being charged and how this affects the priority of payment of debts. The purpose of mentioning charged assets at this point is to highlight that, if a client wishes to carry out asset protection planning, if he were to seek to transfer assets that are already subject to bank security, the transfer would generally be ineffective unless consent is obtained by the chargor, typically the bank. It is unlikely that such consent would be available as the purpose of the asset protection transfer is to remove those assets from being available to that bank to pay off its loan. Therefore in practice it is only assets that are already free of debt and security is available for transfer to an asset protection structure.

---

[20] Section 34 Bankruptcy Act 1988

4.4 Insolvency within the Asset Protection Trust

To what extent is a trustee bound to involve himself in the affairs of the underlying company? Caselaw[21] states that if the only reasonable way to protect and preserve the trust assets is to have an insolvency practitioner appointed to the trust assets then the trustee should do this. However, once an underlying company within the trust is insolvent, the trustee has the difficult problem that its duties as director will cease but his duties as trustee will not. The trustee therefore needs to protect the trust fund albeit by working with the insolvency practitioner. Steps that could be taken to ensure that the control is not lost would include monitoring the liquidator's conduct or indeed securing a place on the creditor committee.

In the case of the insolvency of the trustee himself, the general rule does not automatically mean that a trustee must vacate office although generally they would do so. However, given that the right of an indemnity in respect of trustee expenses reasonably incurred is a personal asset of the trustee, any creditor of that trustee can exercise a right of subrogation to the trustee's right of indemnity against the trust and get paid that way. However, the trustee must first discharge any prior indebtedness of his own to the trust before he can exercise his right to indemnity.

5 Taxation

The following is a note of the taxation considerations that could arise on the creation, running and ultimately disbanding each asset protection structures already discussed. This is not intended to be a comprehensive discussion as in many cases, for instance in the case of incorporation, whether a trade or an investment property should be incorporated or not are subjects worthy of a seminar in itself.

5.1 Creating the Asset Protection Structure

On the creation of an asset protection structure, the client is disposing of his assets and effectively putting them out of his (and his creditors') reach. This means that for tax purposes, he is disposing of his assets and, unless the disposal falls into any of the exemptions or reliefs or is a disposal of a non chargeable asset, CGT and Stamp Duty (SD) will arise on the creation of the asset protection structure.

[21] Bartlett v Barclays Bank Trust Company Limited [1980] Ch 515

For this reason, the client usually limits the amount and type of asset put into the trust to cash assets and assets that will not trigger a hefty tax charge; otherwise the creation of the asset protection structure will create a further debt for the client (a tax charge).

5.1.1 Incorporation

On the transfer of assets in a business from an individual to a company, specific reliefs are available under Sections 596 to 600 TCA 97 so as to defer any CGT arising until the shares in the new company are disposed of.

Stamp Duty will arise on the transfer of assets other than those that can pass by delivery[22] or where the transfer can 'rest in contract'. Thus stock in trade, plant and machinery (not fixed), cash, bank accounts can pass without documentation to avoid triggering a charge to Stamp Duty.

In the case of the transfer of non business assets from an individual to a company, CGT and Stamp Duty will arise in the normal course.

5.1.2 Bare Trust

As there is no change in the beneficial ownership of the assets passing from the client to the trustee/nominee of the bare trust, no taxes (CAT, CGT or SD) arise. However, as already highlighted, neither does any protection arise!

5.1.3 Interest in Possession Trust

On the transfer of assets from an individual client to a trust to hold on behalf of that individual for life or for any period certain, there is a deemed disposal for CGT, CAT and SD purposes. The disposal is deemed to have occurred at the open market value of the assets transferring.

For CGT purposes the charge arises in the hands of the client transferring the asset. For this reason, it is best to transfer assets that on disposal will produce no gain or

[22] Section 59 SDCA 99 provides that certain chattels are liable to SD at contract stage if included in a contract for sale.

indeed will produce a loss (which loss would be available for the client against any other gains).

For Stamp Duty purposes, even if the trustee is a relative of the client, the consanguinity relief[23] is not available as they are receiving the benefit in their capacity as trustees.

For CAT purposes, assuming the beneficiary of the interest in possession is in fact the disponer, no CAT will arise[24].

5.1.4 Protective Trust

On the transfer of assets from an individual client to a trust to hold on behalf of that individual for life or determinable on his bankruptcy, similar to the interest in possession trust, there is a deemed disposal for CGT, CAT and SD purposes. The disposal is deemed to have occurred at the open market value of the assets transferring.

For CGT purposes the charge arises in the hands of the client transferring the asset. For this reason, it is best to transfer assets that on disposal will produce no gain or indeed will produce a loss (which loss would be available for the client against any other gains).

For Stamp Duty purposes, even if the trustee is a relative of the client, the consanguinity relief[25] is not available as they are receiving the benefit in their capacity as trustees.

For CAT purposes, assuming the beneficiary of the interest in possession is in fact the disponer, no CAT will arise[26].

---

[23] Schedule 1 SDCA 99 Paragraph 15 of Head - conveyance or transfer on sale of any property other than stocks or marketable securities or a policy of insurance or a policy of life assurance
[24] Section 83(2) CATCA 03
[25] Schedule 1 SDCA 99 Paragraph 15 of Head - conveyance or transfer on sale of any property other than stocks or marketable securities or a policy of insurance or a policy of life assurance
[26] Section 83(2) CATCA 03

5.1.5 Discretionary Trust

Again on the transfer of assets from an individual client to a discretionary trust to hold on behalf of a class of beneficiaries including himself, similar to the interest in possession trust, there is a deemed disposal for CGT, CAT and SD purposes. The disposal is deemed to have occurred at the open market value of the assets transferring.

For CGT purposes the charge arises in the hands of the client transferring the asset. For this reason, it is best to transfer assets that on disposal will produce no gain or indeed will produce a loss (which loss would be available for the client against any other gains).

For Stamp Duty purposes, even if the trustee is a relative of the client, the consanguinity relief[27] is not available as they are receiving the benefit in their capacity as trustees.

For CAT purposes, CAT will arise only on the appointment out of assets from the trust and not on its creation. As the settlor is alive, no discretionary trust levies will arise.

5.1.6 Transfer to Spouse

On the transfer of assets from an individual client to his spouse, any CGT, CAT or Stamp Duty that would normally arise will be exempt[28].

5.1.7 Transfer to Child

On the transfer of assets from an individual client to a child (or to a trust for the absolute benefit of a minor child), there is a deemed disposal for CGT, CAT and SD purposes. The disposal is deemed to have occurred at the open market value of the assets transferring.

For CGT purposes the charge arises in the hands of the client transferring the asset. For this reason, it is best to transfer assets that on disposal will produce no gain or

[27] Schedule 1 SDCA 99 Paragraph 15 of Head - conveyance or transfer on sale of any property other than stocks or marketable securities or a policy of insurance or a policy of life assurance
[28] Stamp Duty (assuming not a sub sale) under section 96 SDCA 99; CGT provided the spouse is living with the client under s1028 TCA 99; CAT under s70 CATCA 03

indeed will produce a loss (which loss would be available for the client against any other gains).

For Stamp Duty purposes, as the child is a relative of the client, the consanguinity relief[29] is available so that where ad valorem rates apply; these are discounted by 50%.

For CAT purposes, CAT will arise based on the value of the asset passing and the extent of prior benefits that the child has already received[30].

5.2 Running the Asset Protection Structure

Once the asset protection structure is created, it is a different entity to that of the client and different taxes may arise in the new entity which taxes might not have been a concern when the client held them in his own name.

5.2.1 The Company

The income and gains arising from the assets are now in the regime of corporation tax and not income tax, including close company surcharges etc.

5.2.2 Bare Trust

As there was no change in the beneficial ownership of the assets passing from the client to the trustee/nominee of the bare trust, the same taxes arise in the hands of the client as when he owned the assets legally in his own name.

The trustees have power to recover from the trust assets if they are assessed to income tax[31]. This would normally arise in the case of the client becoming non resident and Irish source income arises[32].

---

[29] Schedule 1 SDCA 99 Paragraph 15 of Head - conveyance or transfer on sale of any property other than stocks or marketable securities or a policy of insurance or a policy of life assurance
[30] Assuming the child has received no prior benefits, he can receive €434,000 in value of assets before CAT at 25% will arise, (current rate and threshold, November 2009)
[31] Section 1046 TCA 99
[32] Section 890 TCA 99

5.2.3 Interest in Possession Trust

If the client life tenant is in receipt of income which is mandated to him, he will be assessed to income tax direct as before[33]. If not, the trustees should pay income tax at the standard rate and pass over the net income to the life tenant, providing him a certificate of income tax deducted[34]. The life tenant is then assessed to income tax on the income received from the trust as Schedule D Case IV income and is allowed a credit for the income tax paid by the trustees.

CGT on any gains arising in the trust is charged in the hands of the trustees with no annual exemption available to them.

5.2.4 Protective Trust

The client life tenant/ trustees are assessed to income in the manner of the interest in possession trust on the basis set out at 5.2.3 above but, once the trust is converted into a discretionary trust, the income is assessed as on the basis set out at 5.2.5 below and the levies may arise again as set out below.

If the trust is converted into a discretionary trust there is an automatic trigger of capital gains tax on any increase in the value of chargeable assets in the trust even though no assets have actually been disposed of[35]. The chargeable assets are deemed to be disposed of by the trustees for their market value and reacquired by them at that value. This is a principal drawback of the protective trust as against a discretionary trust.

5.2.5 Discretionary Trust

The trustees of a discretionary trust should pay income tax at the standard rate and pay an income tax surcharge of 20% on any income not paid out of the trust to a beneficiary within 18 months (the discretionary trust income surcharge). If the trustees do pass over the net income to a beneficiary they should provide him a certificate of income tax deducted[36]. The beneficiary is then assessed to income tax on the income received from the trust as Schedule D Case IV income and is allowed

[33] Williams v Singer 7 TC 411, but the trustee must file a return under section 890 TCA 99
[34] A Form R185 is furnished
[35] Section 577(3) TCA 99
[36] A Form R185 is furnished

a credit for the income tax paid by the trustees. If that income is paid over after the surcharge has arisen though, the surcharge is not available as a credit.

The trustees need to take care in deciding to pay over the income on a regular basis to a beneficiary as, if it appears that the trustees are automatically treating a beneficiary as being entitled to the income, the Revenue (or indeed other creditors) may seek to claim the trust is not in fact discretionary. However where the beneficiary is the original settlor, there is no advantage to the Revenue to argue this as no CAT arises.

CGT on any gains arising in the trust is charged in the hands of the trustees with no annual exemption available to them. On the appointment of any capital to a beneficiary in the form of an asset, a charge to CGT could arise as there would be a deemed disposal for CGT purposes. If the trust is held offshore[37] where gains are made by the trustees when managing the trust, anti avoidance legislation can trigger CGT in the hands of an Irish beneficiary[38] whether he receives benefits or not (in the case where there has been an Irish settlor[39]) and otherwise on the payment of capital benefits to that beneficiary[40].

The advantage to this trust over the protective trust is that the automatic change in status of the trust from a life interest trust to a discretionary trust would trigger capital gains tax (as outlined above) but where the trust is always discretionary such tax would not arise on the beneficiary becoming bankrupt.

If the settlor dies, discretionary trust levies may arise, depending on the trust documentation and who are the beneficiaries. If the discretionary element of the trust ceases on the death of the settlor (which can be written into the trust), the levies will not arise. Assuming the concern for protection was merely for the settlor himself, there seems little need to continue the discretionary element of the trust beyond his death. However if the settlor's family are young at the time he creates the trust he may wish to keep the trust discretionary beyond his death to ensure his children do not come into assets at too young an age.

---

[37] The trustees are not resident or ordinarily resident in the State
[38] Beneficiary must be domiciled and either resident or ordinarily resident in the State
[39] Settlor must be domiciled and either resident or ordinarily resident in the State at the time of the creation of the settlement or in the year of the gain
[40] Sections 579 and 579A TCA 99

If the discretionary element of the trust does not cease on the death of the settlor, if the trust does not include principal objects[41] of the settlor, a 6 % initial levy[42] will arise together with an annual 1% levy as long as the trusts remains discretionary.

5.2.6 Transfer to Spouse

The same taxes arise in the hands of the spouse as had arisen in the hands of the client when he had owned the assets.

5.2.7 Transfer to Child

The same taxes arise in the hands of the child as had arisen in the hands of the client when he had owned the assets.

5.3 Winding Up the Asset Protection Structure

Times may come good again for the client or the threats he had perceived may have dissipated and the client may then wish to unwind the asset protection structure and get it back into his own hands. Even though this is something the client wants however he is not entitled to demand it and he will have to persuade the trustees/his spouse/his children to get it back as the asset is no longer in his control. Assuming he is successful in persuading the relevant party, taxes can arise on the undoing of the structure.

5.3.1 The Company

Here the client does have the control as shareholder to wind up the company. Assuming there is an uplift in value in the company on assets in the company (e.g. a property gain), if the client wishes as shareholder to take back out the property he will be subject to the double charge to CGT (the gain on the property in the hands of the company and the gain on the shares in the hands of the shareholder).

Unless the assets are distributed in specie to the client, Stamp Duty will arise on the taking out of the assets from the company.

[41] See definition in section 14 CATCA 03
[42] Reduced to 3% if the trust is wound up within 5 years, see Section 18(3) CATCA 03

5.3.2 Bare Trust

As there was no change in the beneficial ownership of the assets passing from the client to the trustee/nominee of the bare trust, there is no change in getting it back into his own name and no taxes arise.

5.3.3 Interest in Possession Trust

On the winding up of a life interest trust, the trustees would need to ensure they have been given power to appoint all of the capital back to the life tenant. In such a case no CAT should arise as the disposal is made to the original disponer. However CGT and Stamp Duty will arise.

For CGT purposes, the trustees are deemed to dispose of the chargeable assets in the trust for their market value[43] and so CGT may arise.

The disposal of the assets to the client also triggers Stamp Duty and, even if the assets include shares which are normally subject to the 1% rate, in this case it is a disposal of trust assets, all therefore coming under the ad valorem rates. Again no consanguinity relief will be available as it is a disposal from persons in their capacity as trustees even if they are relatives of the client.

5.3.4 Protective Trust

On the winding up of the protective trust while it is still in the form of a life interest trust, the trustees would need to ensure they have been given power to appoint all of the capital back to the life tenant. In such a case the provisions outlined in paragraph 5.3.3 above would apply.

On the winding up of the protective trust while it is still in the form of a discretionary trust, the provisions outlined in paragraph 5.3.5 below would apply.

If the trust has already become discretionary, the death of the beneficiary who was the original life tenant does not trigger a charge to CGT if the discretionary element continues beyond the death of the client. However if the trust deed provides that the discretionary element ceases automatically on the death of the original life tenant,

---

[43] Section 576 TCA 99 applies as it is an enlargement of a life interest and not a termination of a life interest, see also Revenue CGT manual paragraph 19.3.5.8(c)

CGT would arise on a deemed disposal by the trustees as they would then hold the assets absolutely for named individuals e.g. the spouse and children[44].

5.3.5 Discretionary Trust

On the appointment out of all the assets in a discretionary trust to the beneficiary, CGT and Stamp Duty arises.

For CGT purposes, the trustees are deemed to dispose of the chargeable assets in the trust for their market value[45] and so CGT may arise.

The disposal of the assets to the client also triggers Stamp Duty and, even if the assets include shares which are normally subject to the 1% rate, in this case it is a disposal of trust assets, all therefore coming under the ad valorem rates. Again no consanguinity relief will be available as it is a disposal from persons in their capacity as trustees even if they are relatives of the client.

As with the protective trust however, if the trust deed provides that the discretionary element ceases automatically on the death of the original life tenant, CGT would arise on a deemed disposal by the trustees as they would then hold the assets absolutely for named individuals e.g. the spouse and children[46].

5.3.6 Transfer to Spouse

On the transfer back of assets from the spouse to the client, any CGT, CAT or Stamp Duty that would normally arise, will be exempt[47].

5.3.7 Transfer to Child

On the transfer back of assets from the child to the client, there is a deemed disposal for CGT, CAT and SD purposes. The disposal is deemed to have occurred at the open market value of the assets transferring.

---

[44] Section 576 and the exemption under Section 577(3) are not available as the interest that expires is not a life interest.

[45] Section 576 TCA 99 applies as it is an enlargement of a life interest and not a termination of a life interest, see also Revenue CGT manual paragraph 19.3.5.8(c)

[46] Section 576 and the exemption under Section 577(3) are not available as the interest that expires is not a life interest.

[47] Stamp Duty (assuming not a sub sale) under section 96 SDCA 99; CGT provided the spouse is living with the client under s1028 TCA 99; CAT under s70 CATCA 03

For CGT purposes the charge arises in the hands of the child transferring the asset.

For Stamp Duty purposes, as the client is a relative of the child, the consanguinity relief[48] is available so that, where ad valorem rates apply, these are discounted by 50%.

For CAT purposes, CAT will arise based on the value of the asset passing and the extent of prior benefits that the client has already received within the Group B threshold[49].

6 Conclusion

The main difficulty for a settlor is that under any effective asset protection structure, such as a discretionary trust, by and large he as provider of the funds expects to be the principal beneficiary and controller of what goes on in the trust. He is used to giving instructions and being in charge. The very idea that he has to appoint somebody else (and indeed pay them) to take charge of his assets and who could ignore his instructions is not something that he can easily accept. In addition the idea that there are other beneficiaries who might have rights under the trust might not sit well with him. However the more the settlor controls the less likely the trust is to be genuine whatever type of trust and whatever jurisdiction is chosen as it will be a sham and liable to be set aside.

In addition if the settlor does become insolvent how does he access monies in the trust so that then those monies are themselves not subject to a claim by his creditors? It is not easy to benefit an insolvent beneficiary! It may be that the trustees will have to pay for out of pocket expenses of the settlor (beneficiary), assuming he can get credit to pay those expenses in the first place.

There is also question as to what type of trustee should get involved in cases such as this. The trustees themselves are very vulnerable to cases taken against them if they seek to make any remedies charged against the trust assets difficult to enforce.

---

[48] Schedule 1 SDCA 99 Paragraph 15 of Head - conveyance or transfer on sale of any property other than stocks or marketable securities or a policy of insurance or a policy of life assurance

[49] Assuming the client has received no prior benefits, he can only receive €43,400 in value of assets before CAT at 25% will arise, (current rate and threshold, November 2009)

Given the fact that these structures are intended to protect and not to be tax efficient, it is crucial the client is aware of what he is getting into. Is it worth running the risk that he might not become insolvent in the next 2 (or 5) years as against running a structure knowing it is not the most tax efficient way to deal with his assets?

Finally the time limits imposed by legislation which seeks to unwind the transfer of assets into protective structures means that this sort of planning is not something that can be done on the eve of bankruptcy. Careful planning is required.

7 Disclaimer

The material contained in this paper and related slides is for general information purposes only and does not constitute legal, taxation or other professional advice. While every care has been taken to ensure that the information in this paper and related slides is accurate and up to date, you should seek specific legal and/or taxation advice in relation to any decision or course of action. No liability whatsoever is accepted by Aileen Keogan, Solicitor & Tax Consultant for any action taken in reliance on the information on this site.

Appendix 1 Case Study

Joe and Mary have been happily married for 20 years with two children, a daughter, Saoirse, aged 19 and a son, Fintan, aged 14. Joe is a builder and developer who had been very successful over recent years but is finding it difficult to keep trading since the downturn.

Joe was originally an electrician by trade and has pared back the building business to provide electrician services through his construction company ‘Construct Ireland Limited’ and has, with difficulty, kept things going. He is however concerned with the number of sites that he had bought over the last few years, some in his own name, some in the joint names of his wife and himself and some in the joint names of himself and a friend of his, Patrick, who was a developer and builder also. There are borrowings on the sites in each case and some personal guarantees against some, but not all, of the borrowings. His family home is in the joint names of himself and Mary and he has small savings – he had considered that his savings and pension were the development sites that have now gone sour.

Joe is not in arrears in relation to any of his borrowings. Joe has to date successfully renegotiated the loans on the sites so that he can manage to pay the interest or it had previously been on an interest roll up basis. The banks to date have been willing to continue this but he is unsure of their attitude going forward on the borrowings eventually being moved into NAMA.

Mary is very conscious of the dangers of the downturn on their personal circumstances and main concern is to protect the family home. As she cannot recall ever signing documents on security in relation to the family home itself, she believes that it will be protected but needs reassurance on this. She recalls that, when Joe persuaded her to buy the site with him in their joint names, she was reassured at the time that the family home would not be vulnerable. Their eldest child appreciates the difficulties and has a sensible attitude but their youngest child is somewhat wayward and it is the hope that he will settle as he reaches maturity. Patrick has his own financial difficulties and, while he and Joe are still friends, Joe is of the view that it ‘being business’ Patrick will be very careful to protect his own position ahead of Joe’s, even if that does mean Joe could be put under more pressure. Joe is not aware of Patrick’s financial situation but is concerned that Patrick may default on the joint borrowings in an effort to pay off his sole borrowings, leaving Joe with the entire of the borrowings to meet.

Mary has recently received a lump sum from her mother's estate and is concerned to keep this as a nest egg for education and household expenses going forward as she is conscious that the income for the house has reduced considerably. She is also considering taking up work herself now that the children are reared and there is a need for money but she is conscious she will not find a job very easily.

Joe and Mary's assets and liabilities are summarised as follows. While the values are currently conservatively low, there is always the risk they could decline further:

Family Home - joint names	1,500,000
Joint Mortgage on family Home	(200,000)
2 shares in Joe Construction Ltd (100% owned by Joe)	100,000
Cash in bank (Mary – inheritance)	250,000
Joe's cash savings	75,000

Site 1 – Joe's sole name
Purchase price 5,000,000
Borrowings 2,000,000
Current market value unknown, possibly 2,500,000
Security - the land itself and a personal guarantee by Joe
Net value assuming valuation can stand 500,000

Site 2 – Joe's and Mary's joint names
Purchase price 2,000,000
Borrowings 1,100,000
Current market value unknown, possibly 1,000,000
Security - the land itself only
Net value assuming valuation can stand (100,000)

Site 3 – Joe's and Patrick's joint names (50:50)
This site is already partially built
Purchase price of one half share 2,000,000
Borrowings on one half share 1,100,000
Current market value of one half share unknown possibly 1,000,000

Security - the land itself; and	
- joint and several personal guarantees by Joe and Patrick	
Net value of one half share assuming valuation can stand	(100,000)
Total net joint assets of Joe and Mary	2,025,000

Appendix 2 Piercing the Corporate Veil

1. Intervention by the Courts

While there are no set criteria as to when the veil of incorporation will be lifted by the courts, the following therefore constitutes a list of loosely defined categories in which the courts have lifted the veil.

- Just and Equitable Grounds - Section 213(f) of the 1963 Companies Act provides the court authority to wind up a company if it is just and equitable to do so.

- Fraud and Misconduct - The winding up of a company may also take place where truly oppressive conduct (as opposed to manifestly unlawful conduct) has occurred.

2. Intervention by the Legislature

Legislation also provides circumstances where the veil of incorporation can be lifted. The Companies Acts, 1963-2009 contain a number of provisions enabling the veil to be lifted as set out below.

- Section 138 of the Companies Act, 1990 (the "1990 Act") provides that an officer of a company such as a director can be declared to be personally responsible, without limitation of liability, for all or part of the debts of the company where it appears that, while he was an officer of the company he was knowingly a party to the carrying on of the company's business in a reckless manner. Additionally, any person, whether an officer or not, can be made similarly liable if he was knowingly a party to the carrying on of any business of the company with intent to defraud its creditors or for any fraudulent purpose. This provision extends the concept of fraudulent trading previously contained in section 297 of the 1963 Act.
- Section 140 of the 1990 Act enables a court to make an order that any company that is or has been related to a company being wound up will pay an amount equivalent to the whole or part of all of the debts of the company being wound up, if the court is satisfied that it is just and equitable to make such an order.

- Section 141 of the 1990 Act empowers a court to make an order for the pooling of the assets of related companies where two or more related companies are being wound up. Any such order by the court will be made if the court is satisfied that it is just and equitable to do so.
- By virtue of section 36 of the 1963 Act any member who knew that the company was carrying on business with less than the statutory minimum number of members for more than six months will be held severally liable for the company's debts contracted during that time.
- In accordance with section 114 of the 1963 Act any officer or any person on its behalf responsible for the company failing to exhibit its name in its correct form on any relevant document will be liable to a fine and will be held personally liable to the creditor who holds a bill of exchange, promissory note, cheque or order for money or goods for an amount which has not been paid by the company.
- There are other situations contained in legislation under which the veil of incorporation is lifted, examples of which are the Consumer Information Act, 1978 and the Land Act, 1965.

Appendix 3 Examples of Potential Bare Trust Structures

Are these bare trusts?

- A trust provides that the Trustees hold the assets on trust for the Settlor's lifetime to pay the income or capital to him or at his discretion and after his death to hold the capital equally for such of his children as are then alive or for such persons as the Settlor may designate in writing in his lifetime or by Will.

  This is a bare trust as the Settlor retains full equitable ownership. The purported disposition on death to his children is testamentary and must comply with the form of Wills under the Succession Act 1965.

- A trust provides that the Trustees hold the assets on trust for the Settlor for life with remainder equally to such of his children as are still alive at his death or to such persons as the Settlor may designate in writing in his lifetime or by his Will but with the power for his Trustees in his lifetime to appoint such capital to him as they see fit or to such other persons designated in writing by the Settlor as they see fit and with power for the Settlor to revoke the trust wholly or partly.

  This is an interest in possession trust as the children have a contingent defeasible interest in remainder. The Settlor is therefore only entitled to the life interest unless and until the Trustees appoint capital to him.

- A trust provides that the Trustees hold the assets on trust to accumulate income in the Settlor's lifetime, the capital to pass on his death to X absolutely but with power for the Settlor in his lifetime to appoint income or capital to himself or anyone else.

  This is an interest in possession trust as X has a vested defeasible interest, the Trustees being under a duty to hold to the Settlor's Order only if the Settlor orders it whilst in the example at (1) above the Trustees have an immediate duty to hold it to the Settlor's Order.

26 November 2009
Aileen Keogan
Solicitor & Tax Consultant
www.aileenkeogan.ie