

12-1-1998

Caribbean Asset Protection Trust: Here Comes The Sun: Dispelling The Dark Clouds Of Controversy

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Recommended Citation

Denise C. Brown, *Caribbean Asset Protection Trust: Here Comes The Sun: Dispelling The Dark Clouds Of Controversy*, 7 U. Miami Bus. L. Rev. 113 (1999)

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CARIBBEAN ASSET PROTECTION TRUST: HERE COMES THE SUN—DISPELLING THE DARK CLOUDS OF CONTROVERSY

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I. INTRODUCTION

The legends of offshore banking in the Caribbean have become a modern story of reverse piracy. Instead of bounty found, the tales are of money hidden. Unfortunately, the perceptions of Caribbean offshore banking, in particular offshore trusts, as nothing more than hidden treasure, are inaccurate and fail to recognize the value of this asset protection device as a legal, smart wealth shield.

In attempting to redeem the offshore trust as a legitimate planning instrument for asset protection, this comment will examine the concept of the offshore trust, describe how a site for offshore trusts is selected, focus on the popularity of the Caribbean region for establishing offshore trusts,

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explore prudent implementations of the Caribbean offshore trust, and discuss the various causes for the misconceptions regarding offshore trusts in the Caribbean.

II. THE CONCEPT OF AN ASSET PROTECTION TRUST: THE ABCS OF APTS

An offshore asset protection trust ("APT") is a potent mechanism for the preservation of wealth. Some practitioners are billing the APT as the ultimate method of asset protection available,¹ since its creative structure enables the trust to legally withstand judgments from U.S. courts.

The premise behind the APT is "an English common law based on non-U.S. jurisdictions with favorable trust protection laws."² That is, a grantor transfers assets to a foreign trust administered by at least one foreign institutional trustee.³ The APT is generally arranged as a discretionary trust, permitting the trustee to distribute income according to his discretion.⁴ However, the trust is often governed by a "letter of wishes," indicating the grantor's preferences regarding disbursement.⁵ Since the foreign trustee's "discretion" ultimately prevails in disbursement of APT income, the foreign trustee may deny creditors' requests for distribution from the trust to satisfy a debt of the grantor.⁶

The basic premise behind an APT is removal. One commentator noted

Removal of one's assets from the jurisdiction of the court is a time-honored strategy for defeating one's liability. Upon removal, the principle of territoriality takes effect; to recover, the creditor must sue in the foreign legal system where the assets are located.

¹ Philip R. Rupprecht, *The Increasing Use of International Trusts*, 34 ARIZ. ATT'Y 22, 22 (Nov. 1997); see also Jonathon L. Mezrich, *It's Better in the Bahamas: Asset Protection Trusts for the Pennsylvania Lawyer*, 98 DICK L. REV. 657, 658-59 (1994) (touting APTs as the most "foolproof" method of asset protection available).

² Howard S. Rosen, *Offshore Trusts: A Closer Look*, IV THE ASSET PROTECTION NEWS 2 (Feb. 1995) <<http://www.protectyou.com/apn4-2-fr.html>>. See Milton Grundy, *GRUNDY'S TAX HAVENS* 147 (1993) (discussing historical connection between numerous offshore business centers and the United Kingdom).

³ David D. Beazer, *The Mystique of "Going Offshore"*, 9 UTAH B.J. 19, 21 (1996); see also Howard D. Rosen, *Tax Management Portfolios*, ASSET PROTECTION PLANNING A16 (1994) (defining an "offshore trust" as one under which at least one trustee is resident outside of the United States); Rick J. Taylor, *Offshore Trusts Offer Asset Protections*, 78 A.B.A. J. 84, 84 (1992).

⁴ Ruben Diaz, Jr., *Foreign Trusts and Other Offshore Planning Opportunities*, SB10 ALI-ABA 587, 608 (1996).

⁵ Diaz, *supra* note 4.

⁶ *Id.*

If the foreign legal system will not enforce liability against the assets of the debtor, removal achieves more than hindrance and delay; it bars recovery.⁷

Thus, where an APT is properly established in a foreign country, obtaining jurisdiction over the trustee through a U.S. court action will be impossible,⁸ forcing creditors to pursue litigation in the foreign jurisdiction in their attempt to attach the assets.⁹

III. SELECTING AN APT JURISDICTION: WHICH BASKET FOR THE EGGS?

The selection of the most beneficial foreign jurisdiction for an APT involves consideration of several important factors. Primarily, a grantor will seek "a jurisdiction in which the enforcement of a foreign judgment against a trustee will be, at least, sufficiently difficult to discourage claimants from bringing actions in such courts."¹⁰ In addition, grantors should consider foreign business operations, banking and investment infrastructure, language, political stability, "health" of the economic environment, telecommunication capabilities, access to qualified trustees, specific trust laws, time zones, and set-up and maintenance costs in selecting a jurisdiction for an APT.¹¹

Currently, there are a number of different worldwide jurisdictions regarded as suitable sites for APTs.¹² The most popular jurisdictions used

⁷ Lynn M. Lopucki, *The Death of Liability*, 106 YALE L.J. 1, 32 (1996).

⁸ Howard D. Rosen, *The How's and Why's of Offshore Trusts in Asset Protection Planning*, TAX MANAGEMENT'S ESTATES, GIFTS, AND TRUSTS J. (May 1996) <http://www.protectyou.com/OFFSH_TR-fr.html>.

⁹ Rosen, *supra* note 8.

¹⁰ Diaz, *supra* note 4, at 609.

¹¹ See generally Beazer, *supra* note 3, at 20, 22 (listing key considerations for choosing an APT jurisdiction); Elena Marty-Nelson, *Domestic and International Asset Protection Planning*, 45 CATH. U. L. REV. 1269, 1278 (1996) (book review) (emphasizing the importance of considering political stability and qualified local professionals when choosing an APT jurisdiction); Gideon Rothschild, *Establishing and Drafting Offshore Asset Protection Trusts*, 23 EST. PLAN. 65, 65 (1996) (suggesting consideration of the specific trust law of a jurisdiction in deciding where to locate an APT); Rosen, *supra* note 3, at A17-A18, A20 (discussing critical factors in selecting an appropriate jurisdiction for an APT); Grundy, *supra* note 2, at 156 (discussing the practicality of establishing an offshore trust within the same time zone as the grantor).

¹² See generally Diaz, *supra* note 4, at 609 (listing jurisdictions that have adopted asset protection trust legislation, including the Bahamas, Belize, Bermuda, the Cayman Islands, the Cook Islands, Cyprus, Gibraltar, Mauritius, the Turks and Caicos, and Nevis); Mezrich, *supra* note 1, at 666 (citing the Bahamas, the Cayman Islands, the British West Indies, the Cook Islands, and Gibraltar as popular jurisdictions for APTs); THE COMPARATIVE LAW YEARBOOK OF INTERNATIONAL BUSINESS ix (Dennis Campbell & Susan Cotter eds., Special Edition 1995) (Addressing 13 common jurisdictions for offshore trusts).

by U.S. citizens include the Bahamas, Bermuda, the British Virgin Islands, the Cayman Islands, the Cook Islands, the Isle of Man, Switzerland, the Turks and Caicos, and St. Kitts and Nevis.¹³ Five of these nine most popular jurisdictions are located in the Caribbean. Add to that list Barbados and Anguilla¹⁴ and the result is at least seven attractive APT locations in the Caribbean region.

IV. FOCUS ON THE CARIBBEAN: A POPULAR DESTINATION FOR APTS

U.S. citizens tend to favor Caribbean jurisdictions for several reasons, including proximity to the eastern coast of the U.S., a resort atmosphere that permits a mixing of business with pleasure, and the fact that these countries generally conduct business in the English language.¹⁵ One author suggests that with beautiful beaches, crystal clear waters, and great golf courses, the quality of life in the Bahamas for investing clients' funds offshore is pretty good.¹⁶

At any rate, Caribbean APTs are gaining popularity. Walter Diamond, a noted economist and author, estimates that more than five trillion dollars pass through offshore financial centers in general each year, representing nearly half of the world's funds.¹⁷ Of that, an estimated one trillion dollars are held specifically in APTs.¹⁸ As of 1996, the U.S. Treasury believed that at least \$650 billion of U.S. investments in APTs are held in the Bahamas and the Cayman Islands.¹⁹ These statistics indicate that U.S.

¹³ Beazer, *supra* note 3, at 19.

¹⁴ See Howard S. Rosen, *Review of Offshore Jurisdictions: Jurisdiction 2: Anguilla*, VI THE ASSET PROTECTION NEWS 2 (July/Aug. 1996) <<http://www.protectyou.com/apn6-1-fr.html>> (discussing the viability of Anguilla as a jurisdiction for APTs); Howard S. Rosen, *Review of Offshore Jurisdictions: Jurisdiction 3: Barbados*, VI THE ASSET PROTECTION NEWS 1 (Mar. 1997) <<http://www.protectyou.com/apn6-1-fr.html>> (discussing the viability of Barbados as a jurisdiction for APTs).

¹⁵ Mezrich, *supra* note 1, at 666 (elaborating on the popularity of certain jurisdictions for the establishment of APTs, including the Bahamas, and the Cayman Islands). See generally Rosen (both citations), *supra* note 14 (discussing attributes of Anguilla and Barbados as sites for APTs, emphasizing their accessibility to U.S. citizens and the use of English as the official language); Howard S. Rosen, *Review of Offshore Jurisdictions: Jurisdiction 4: Bahamas*, VI THE ASSET PROTECTION NEWS 3 (Aug. 1997) <<http://www.protectyou.com/apn6-3-fr.html>> (discussing the proximity of the Bahamas to Florida and noting its English-speaking common law jurisdiction).

¹⁶ Beverly Helm, *Tax Planning Offshore... Is It Better in the Bahamas?*, 13 NO. 2 COMPLEAT LAW. 62, 62 (1996); see also Mezrich, *supra* note 1, at 667 (citing one reason for establishing a foreign situs trust in the Bahamas is that it is "frequented as a 'tourist paradise'").

¹⁷ Beazer, *supra* note 3.

¹⁸ Elena Marty-Nelson, *Offshore Asset Protection Trusts: Having Your Cake and Eating It Too*, 47 RUTGERS L. REV. 11, 14 (1994).

¹⁹ Helm, *supra* note 16, at 63. See also Barbara Hauser, *International Legal Developments in Review: 1996 Business Transactions and Disputes*, 31 INT'L LAW. 355, 355 (1997) (suggesting that at

citizens are indeed favoring Caribbean jurisdictions when establishing APTs.

An increasing number of U.S. citizens are investigating APTs in the Caribbean. Once perceived as only serving the "super-rich,"²⁰ APTs now appeal to a wide range of people, including professionals, business owners, small businesses, officers and directors of companies, as well as high-income individual clients.²¹

V. POSITIVE USES OF CARIBBEAN APTs: NO MORE TROUBLE IN PARADISE

Although the Caribbean APT has received bad press in the past, it remains a legitimate asset protection and estate planning tool.²² Essentially, creating an APT is based on the same wisdom a U.S. citizen exercises in consulting an accountant for tax savings or an attorney to proactively limit risk.²³ A prospective grantor may consult an attorney to determine the most prudent means of asset protection, considering the worst-case scenarios of the future in order to make the wisest decisions in the present.

A Caribbean APT is just one response to the increase in litigation the U.S. has experienced in recent decades. Indeed, the popularity of APTs has been attributed to the litigiousness U.S. society and to the uncertainties to which an individual is subjected by the legal system.²⁴ One proponent suggests that APTs are merely a reaction to today's "court-happy" society, and should be permitted until frivolous lawsuits and litigiousness are

least \$644 billion has been transferred by U.S. persons to the Bahamas, the Cayman Islands, and a European jurisdiction in APTs).

²⁰ Marty-Nelson, *supra* note 18. See also Beazer, *supra* note 3 (indicating that references to the Bahamas, the Cayman Islands, or similar jurisdictions will conjure images of the ultrarich).

²¹ See Rupprecht, *supra*, note 1, at 24, 34 (suggesting there are a host of potential clients of relatively modest means who could consider at APT); see also Helm, *supra* note 16 (suggesting investing offshore in the Bahamas may be beneficial for small business in addition to high-income individuals); Marty-Nelson, *supra* note 18 (noting that APTs may be an appropriate way to insulate officers and directors of companies that face potential tort liability).

²² Rupprecht, *supra* note 1; see also Beazer, *supra* note 3, at 19 (indicating the offshore financial centers are "no longer just sunny places for shady people").

²³ Beazer, *supra* note 3, at 19.

²⁴ Rothschild, *supra* note 11, at 65 (noting that result-oriented judges increase uncertainties of the domestic legal system for an individual); see also Marty-Nelson, *supra* note 11, at 1271 (citing unrestrained growth in litigation and the corresponding increase in plaintiff's judgments as fueling the phenomenon of asset protection).

substantially curbed.²⁵ Until this happens, "asset protection is really just fair play."²⁶

APTs in the Caribbean serve myriad functions. In addition to asset protection, which should not be the sole stated purpose of the trust under certain state laws,²⁷ there are a number of other beneficial uses of APTs. Besides functioning as a traditional estate planning tool,²⁸ APTs can also serve as a prudent negotiating mechanism, a method of preserving anonymity of wealth, a means of achieving economic diversification, a tool to provide prenuptial or antenuptial protection, and a forerunner to change of domicile or citizenship.²⁹ Other less common functions include transferring assets to beneficiaries no longer residing in the U.S., purchasing unregistered foreign securities that are not offered in the U.S., or holding title to foreign property.³⁰ These less common uses have particular application to Caribbean APTs, as many U.S. citizens seek to acquire property, from time-shares to boats, in one of the many resort locations of the Caribbean. Thus, a Caribbean APT is a convenient way to hold title to this property, which is already located offshore.

The following sections will examine positive uses for the Caribbean APT such as a prudent negotiating tool and an effective planning device.

A. *The Ultimate Bargaining Chip*

In today's world, few can hide from litigation. Those with significant assets become targets for lawsuits.³¹ Sophisticated asset protection planning

²⁵ Mezrich, *supra* note 1, at 675 (placing responsibility on the U.S. judiciary or legal community to reign-in damaging lawsuits).

²⁶ *Id.* at 675.

²⁷ *Id.* at 659 (referring to 12 PA.CON.S.TAT.ANN. §5104(a)(1) (1994)).

²⁸ Rupperecht, *supra* note 1, at 24; *see* Mezrich, *supra* note 1, at 659.

²⁹ *See generally* Beazer, *supra* note 3 (suggesting nine specific applications of APTs, including: (1) protection against malpractice suits and as a supplement to insurance; (2) protection from investment activities outside of the client's main area of work; (3) a stop-loss where an institution requires an open-ended personal guaranty; (4) an alternative to premarital agreements, or for a spouse concerned with the financial risks or imprudence of the other spouse; (5) a method to reduce one's financial profile and segregate a portion of one's assets for future ventures; (6) additional protection for retirement benefits; (7) a strategic positioning tool for current problems [cautioned]; (8) protection of inheritance or proceeds from the sale of a business; and (9) a method to limit toxic waste liability exposure); *see also* Howard B. Young, *Asset Protection Planning With the Use of Foreign Situs Trusts*, 73 MICH. B.J. 446, 446 (1994)(considering various objectives of asset protection, including litigation deterrence, creating a strong inducement for early and cheap settlement, avoiding the necessity of entering into a prenuptial agreement, and establishing a substitute or supplement for liability insurance which may be prohibitively expensive or unavailable); Mezrich, *supra* note 1.

³⁰ Taylor, *supra* note 3.

³¹ Jon Newberry, *Protect Assets Before Lawsuit Arises*, 82 A.B.A. J. 89, 89 (1996) (declaring that wealth itself often prompts claimants to pursue litigation).

through Caribbean APTs will make the grantor of an APT an unattractive target for the contingency-fee litigator, as a creditor's ability to collect a judgment against the grantor is severely diminished by the structure of an APT.³² One attorney specializing in the creation of APTs admits that clients can either choose to be passive, hoping to avoid ever being ensnared in legal controversy, or they can be proactive and implement planning strategies.³³ The attorney views the former approach as denial, and the latter approach as asset protection planning.³⁴

The leverage provided by an APT in the Caribbean allows grantors to resolve disputes on more favorable terms than would be available under more traditional methods of planning,³⁵ when creditors realize that Caribbean APTs are established under laws that provide, in part, for nonrecognition of U.S. judgments and other roadblocks, the proven result is a cost-effective settlement in favor of the defendant.³⁶ Proponents of the APT advocate complex asset protection strategies as the antidote to the "unpredictability of a tort system run amok."³⁷

1. PROTECTION AGAINST PROFESSIONAL LIABILITY

Professionals who recognize the high risk of malpractice lawsuits are taking advantage of Caribbean APTs to protect themselves and their practice from financial ruin.³⁸ Any professional at risk of suit for tort liability can use a Caribbean APT as a supplement or backstop to malpractice coverage.³⁹ Most liability insurance policies do not cover

³² Howard S. Rosen, *Selected Questions Concerning Asset Protection* (visited Mar. 3, 1998) <<http://www.protectyou.com>>.

³³ Newberry, *supra* note 31.

³⁴ *Id.*

³⁵ Rothschild, *supra* note 11; *see* Newberry, *supra* note 31.

³⁶ Rothschild, *supra* note 11; *see also* Young, *supra* note 29, at 446-47 (The author portrays a likely scenario where a wealthy physician has a judgment entered against him: since he does not have adequate assets to satisfy the judgment, other than an APT, the creditor will look to the APT to satisfy the judgment. Once the creditor realizes the terms and implications of the APT, it is likely that the judgment will be settled for pennies on the dollar) (emphasis added).

³⁷ Marty-Nelson, *supra* note 11, at 1269; *see also* Young, *supra* note 29 (asserting that a primary objective of asset protection is litigation deterrence).

³⁸ *See generally* Newberry, *supra* note 31 (relaying that many attorneys come to establish an APT saying "I don't want someone to do to me what I do to people all day in court."); Beazer, *supra* note 3; Helm, *supra* note 16, at 63; Marty-Nelson, *supra* note 18 (noting that many newcomers to APTs are those whose professions or businesses leave them vulnerable to potentially devastating liability risks and who want to shield their assets from runaway malpractice claims); Alson R. Martin, Nancy Schmidt Roush, and John T. Thomas, *Protecting the Assets of a Professional or Other Closely Held Business Owner from Creditors*, C796 ALI-ABA 639, 650 (1993) (recognizing that a professional is always subject to liability from professional negligence or "malpractice" claims).

³⁹ Rupprecht, *supra* note 1, at 34-35 (noting that an APT allows physicians, surgeons, and

awards of or associated with punitive damages or intentional wrongdoing, and there generally is a limit to coverage.⁴⁰ Prudent planning with a Caribbean APT will aid in circumventing these shortcomings of insurance.

Some professionals are unable to insure themselves or their practice, or find the costs prohibitive.⁴¹ In these cases, a Caribbean APT becomes insurance for such a professional. In fact, in certain instances, establishing an APT may actually cause insurance savings,⁴² making professional insurance affordable after all.

2. PROTECTION AGAINST CORPORATE OR BUSINESS LIABILITY

On a similar note, officers and directors of certain companies face potential liability for the actions of the business or its agents.⁴³ Even officers of charitable businesses are subject to potential individual lawsuits as a representative of the charity.⁴⁴ Anyone involved in a business operating as a general partnership is particularly subject to risk and may stand to benefit from an APT.⁴⁵

There are at least three types of liability for officers and directors: (1) Liability stemming from a profession itself; (2) Liability stemming from another tort; and (3) Liability stemming from a debt or a contract.⁴⁶ The first type of liability, that of malpractice related to a specific profession, is addressed in the preceding section.

others at risk an opportunity to reduce malpractice coverage while maintaining financial security).

⁴⁰ Rosen, *supra* note 32 (discussing why asset protection is still appropriate, even if a client has liability insurance); *see also* Martin, et al, *supra* note 38 (noting that large punitive damage awards are a concern).

⁴¹ Beazer, *supra* note 3 (giving the example of an appropriate candidate for an APT an architect/structural engineer who cannot obtain liability insurance at a reasonable cost and is concerned about the possibility of a large lawsuit); *see also* Mezrich, *supra* note 1 (recognizing that in the U.S. many insurance companies are not willing to insure higher-risk practices, and some practitioners are unable to afford such insurance, if available).

⁴² Rosen, *supra* note 32 (indicating that insurance savings available from asset protection planning can pay for its full cost in some cases, sometimes even in the first year alone by reducing or eliminating the umbrella coverage most professionals carry over and above minimum liability insurance).

⁴³ Marty-Nelson, *supra* note 11, at 1271 (blaming the extension of corporate liability to officers and directors as necessitating their focus on asset protection planning).

⁴⁴ Beazer, *supra* note 3 (giving a hypothetical example of a potential APT client as a member of the board of directors of a local charity who risks being named individually as a defendant in lawsuits).

⁴⁵ Rupperecht, *supra* note 1, at 24 (exemplifying the partnerships of Laventhal & Horwath, Gaston & Snow, among others, where one office of a national partnership brought upon the financial collapse of all partners).

⁴⁶ Martin, et al, *supra* note 38, at 650-51.

The second type of liability, that of "other torts," includes libel, personal injury, products liability, hazardous waste, and other environmental tort liability, depending on the nature of the business.⁴⁷ Often, heavy insurance is not available for such torts, making a Caribbean APT a way for officers and directors of companies to insure against unforeseen liability.⁴⁸

The third type of liability for this sector, that of a debt or a contract, poses significant risks for businesspeople. Debt liability, while predictable, may come directly or through a guaranty and is generally not insurable.⁴⁹ This often means officers and directors of companies are held personally responsible for the debts of the business, indebtedness not always dischargeable through bankruptcy.⁵⁰ One observer uses the example of Arizona real estate developers to advocate for asset protection planning in light of exposure to debt or contract liability.⁵¹ He notes that in the "heyday of real estate development," no one feared personal liability.⁵² However, when the market turned, the once successful businesspeople found their entire net worth at risk because they either guaranteed substantial bank debt for the business or they were general partners in insolvent partnerships.⁵³

B. A Little Foresight

1. PREMARITAL PROTECTIONS

A popular new trend is the use of Caribbean APTs in lieu of premarital agreements.⁵⁴ One advocate of the APT touts the device as an "attractive and unfrontational alternative" to traditional prenuptial agreements,⁵⁵ since no agreement must be made per se. Rather, the assets of the concerned spouse are safely guarded should an unfortunate intra-family lawsuit arise in the future. A Caribbean APT can also be a good asset

⁴⁷ *Id.* at 651; *see also* Marty-Nelson, *supra* note 18 (suggesting the use of APTs to insulate officers and directors that face potential environmental tort liability).

⁴⁸ *See* Martin, et al, *supra* note 38 (suggesting that while many of these potential torts can be insured, the amount is unpredictable).

⁴⁹ *Id.* at 651.

⁵⁰ Martin, et al, *supra* note 38, at 651 (noting that when business owners secure debt for which they are personally liable there is an increase in the likelihood of payback, but there is also a high, uninsurable risk which cannot be discharged in bankruptcy in the cases of certain corporations, according to 11 U.S.C. § 101 et. seq.).

⁵¹ Rupprecht, *supra* note 1.

⁵² *Id.*

⁵³ *Id.* at 22.

⁵⁴ Mezrich, *supra* note 1.

⁵⁵ Rupprecht, *supra* note 1, at 35.

planning strategy for an individual concerned about the financial risks or imprudence of a current spouse.⁵⁶ Use of a Caribbean APT as an alternative to a prenuptial agreement allows other parties to have control in the matter of asset protection from a potential spouse. For example, a parent, concerned that his child's spouse may sue for divorce, can still provide funds for his child and grandchildren without risking loss to the divorcing spouse.⁵⁷

2. CASHING IN ON A BUSINESS

Business owners selling their enterprises often look to a Caribbean APT as protection for their cash bounty. In so doing, businesspeople may be able to shield themselves from "buyer's remorse,"⁵⁸ where the purchaser of a business sues the previous owner in an attempt to reach his "deep pockets."⁵⁹ By arranging an APT in the Caribbean, a seller of a business can protect his proceeds from such attacks.

IV. NEGATIVE STIGMA OF CARIBBEAN APTs: SUNSHINE IS THE BEST DISINFECTANT

Despite the popularity of APTs, their inventive structure lends itself to abuse.⁶⁰ As one author has observed, "the potential for exploitation and abuse by both practitioners and unsavory characters is a very real one."⁶¹ Another author suggests that APTs are the one mutation of the once staid spendthrift trust that has become controversial.⁶² Indeed, exploitation and abuse has occurred, staining the reputation of a perfectly legitimate asset planning tool.⁶³

In recent years, the negative stigma associated with APTs has gained congressional attention.⁶⁴ This negativity stems from illegal uses of an

⁵⁶ Beazer, *supra* note 3.

⁵⁷ *Id.*

⁵⁸ Rupprecht, *supra* note 1, at 35.

⁵⁹ Beazer, *supra* note 3 (giving as an example of a good candidate for an APT a seller of a business who is to realize several million dollars and is concerned that the buyer may sue her for subsequently arising problems, including environmental contamination).

⁶⁰ See Newberry, *supra* note 31 (indicating that the mere thought of shielding assets and offshore trusts raises ethical concerns).

⁶¹ Beazer, *supra* note 3; see Newberry, *supra* note 31.

⁶² Marty-Nelson, *supra* note 18, at 12.

⁶³ See Beazer, *supra* note 3 (suggesting the notoriety associated with APTs and other offshore financial activity as a way to avoid taxes and launder unclean funds is warranted). See also Rupprecht, *supra* note 1, at 24 (recognizing that grantors of offshore trusts are often perceived as "cleverly corrupt").

⁶⁴ Hauser, *supra* note 19 (noting that in 1995 Representative Gibbons focused attention on "the billionaire's expatriation loophole").

APT, such as tax evasion or fraudulent conveyance, as well as misunderstood legal applications of an APT, such as shielding assets from liability.

A. Tax Evasion

Perhaps the most publicized abuse of the APT is tax evasion. Even casual references to the more familiar Caribbean jurisdictions, such as the Bahamas and the Cayman Islands, often conjure up images of wealthy U.S. citizens hiding money away to avoid U.S. income taxes.⁶⁵ In 1995 Representative Gibbons reported to the U.S. Congress that “many . . . wealthy individuals, while retaining their citizenship in this country, are abusing our tax laws by hiding their assets in offshore trusts.”⁶⁶ According to Gibbons’ estimate, \$644 billion was transferred by Americans to the Bahamas, the Cayman Islands, and a European jurisdiction; only \$1.5 billion was reported to the IRS.⁶⁷

The notion that a Caribbean APT provides tax savings is a misnomer. The goal of an APT is asset protection, not the minimization of taxes.⁶⁸ Rather, the APT is generally “tax neutral”⁶⁹ in that the offshore jurisdiction will usually not impose taxes, but U.S. income rules still apply.⁷⁰ In other words, an investor’s income, estate, and gift tax picture remain the same as before the creation of the APT.⁷¹

Despite the fact that APTs are tax neutral for U.S. citizens, some unethical promoters have been claiming that moving assets offshore in the Caribbean offers certain tax advantages.⁷² This type of misinformation leads to the skepticism associated with APTs, as unethical manipulations of APTs for tax evasion are publicized, minimizing the legitimacy of the APT as an asset protection device.

In response to the abuses of APTs for tax evasion purposes, the IRS has promulgated specific requirements for the establishment and reporting of an APT.⁷³ The current reporting requirements under I.R.C. § 6048 mandate

⁶⁵ Beazer, *supra* note 3.

⁶⁶ Hauser, *supra* note 19.

⁶⁷ *Id.*

⁶⁸ Rothschild, *supra* note 11, at 66 (asserting that offshore trusts created by U.S. persons are not intended to avoid income taxes).

⁶⁹ Mezrich, *supra* note 1, at 668-69. *See also* Helm, *supra* note 16, at 63 (indicating that the establishment of an APT is a tax-neutral transaction); Marty-Nelson, *supra* note 11, at 1277.

⁷⁰ Helm, *supra* note 16, at 63.

⁷¹ Rosen, *supra* note 2.

⁷² *Id.* (asserting the opinion that those who promote APTs as offering certain tax advantages are either ignorant of the law, or just don’t care what it says).

⁷³ Mezrich, *supra* note 1, at 670 (noting that the IRS is so concerned that foreign transfers not be used to evade U.S. income taxes that through their compliance forms they have practically “blue-

the filing of an information return within 90 days of (1) the creation of a foreign trust by a U.S. person, or (2) the transfer of any money or property to a foreign trust by a foreign person.⁷⁴ The information return is required from the grantor of the foreign trust or fiduciary or other person creating the foreign trust.⁷⁵ Furthermore, every taxpayer subject to tax under the provisions of I.R.C. § 679, regarding a United States person who directly or indirectly transfer property to a foreign trust, is required to file a return with respect to such trust and the income received from it.⁷⁶

Attempts such as these by the IRS and the current administration seek to heighten the level of reporting responsibility for the creators of APTs.⁷⁷ If followed properly, perhaps they will ensure the more favorable press the APT deserves.

B. *Fraudulent Conveyance*

A second common abuse of the Caribbean APT is fraudulent conveyance. Here is a potential vulnerability for the Caribbean APT, since nearly every creditor attack on an APT is predicated by a fraudulent transfer allegation.⁷⁸ Critics, in fact, view the APT merely as a method to carry out what would otherwise be fraudulent transfers under a "banner of legitimacy."⁷⁹

APTs should not be designed to avoid existing creditors, including vested creditors, tort claimants in matters where a cause of action has already arisen or where suits are pending at the time of conveyance, or anyone else who is a reasonably foreseeable claimant.⁸⁰ Any transfer to an APT under these circumstances is fraudulent and illegal.⁸¹ U.S. courts may

printed" how to establish an APT).

⁷⁴ I.R.C. § 6048(a); *see* Diaz, *supra* note 4, at 613.

⁷⁵ I.R.C. § 6048(a); *see* Diaz, *supra* note 4, at 613.

⁷⁶ I.R.C. § 6048(c); *see* Diaz, *supra* note 4, at 613.

⁷⁷ *See* Helm, *supra* note 16, at 63.

⁷⁸ Rosen, *supra* note 8. *See* Rothschild, *supra* note 11 (a creditor seeking to enforce a U.S. judgment offshore will attempt to set aside a transfer to an APT on fraudulent conveyance grounds).

⁷⁹ Marty-Nelson, *supra* note 11, at 1269.

⁸⁰ Mezrich, *supra* note 1, at 660; *see also* Newberry, *supra* note 31 (the key in determining whether fraudulent conveyance laws have been violated is whether a claim is "pending, threatened, or expected"); Rothschild, *supra* note 11, at 67 (warning that when a client intends to hinder existing creditors, asset protection becomes controversial and may lead to adverse criminal or civil exposure); Young, *supra* note 29, at 448 (noting that present creditors generally also include those with contingent and unmatured claims, not only those with liquidated claims, thus, a bank holding a personal guaranty of a client is a present creditor for fraudulent conveyance purposes even though no default has occurred with respect to the underlying obligation).

⁸¹ Mezrich, *supra* note 1, at 660.

consider a number of factors in determining whether the debtor intended to “. . . hinder, delay, or defeat the claim of a creditor.”⁸²

Waiting for exposure to litigation is not the proper way to establish an APT. In order to avoid impropriety, or the appearance of impropriety, planning must occur before protection is anticipated or needed.⁸³ Planners must ensure that clients merely wish to protect themselves from the future, unforeseeable creditor or claimant, and are not seeking to defraud someone with an existing claim.⁸⁴ In fact, the American Bar Association Model Rules of Professional Conduct prohibit attorneys from assisting a client in a transfer the attorney knows is fraudulent.⁸⁵ This proactive ethical approach lives up to the name “asset protection” rather than the notion of “hiding assets.”⁸⁶

In addition to advance planning, a grantor must also select a proper jurisdiction to avoid findings of fraudulent transfer. This involves an analysis of the Statute of Elizabeth, an old English law that serves as the

⁸² Rosen, *supra* note 8 (listing possible factors a U.S. court may consider, including whether: (1) the transfer or obligation was to an insider; (2) the debtor retained possession or control of the property transferred after the transfer; (3) the transfer or obligation was disclosed or concealed; (4) before the transfer was made or obligation was incurred, the debtor had been sued or threatened with suit; (5) the transfer was of substantially all of the debtor's assets; (6) the debtor absconded; (7) the debtor removed or concealed assets; (8) the value of the consideration received by the debtor was reasonably equivalent to the value of the asset transferred or the amount of the obligation incurred; (9) the debtor was insolvent or became insolvent shortly after the transfer was made or the obligation was incurred; (10) the transfer occurred shortly before or shortly after a substantial debt was incurred; and (11) the debtor transferred the essential assets of the business to a lienor who transferred the assets to an insider of the debtor.)

⁸³ Beazer, *supra* note 3; *see* Rosen, *supra* note 2 (noting that advance planning is crucial to effective utilization of the APT); Rosen, *supra* note 32 (calling asset protection a vaccine, not a cure, best viewed as preventive medicine); Marty-Nelson, *supra* note 11, at 1269 (indicating that practitioners who tout the offshore trust as a panacea for virtually all creditor-related ills has fueled the perception of an unjust system).

⁸⁴ Mezrich, *supra* note 1, at 660; *see also* Rothschild, *supra* note 11, at 66-67 (cautioning practitioners to carefully evaluate a client's financial condition to avoid possible ethical, civil, or criminal liability to the client and practitioner when creating APTs).

⁸⁵ MODEL RULES OF PROFESSIONAL CONDUCT RULE 1.2(d); *see* Beazer, *supra* note 3 (discussing practitioners' liability and warning advisors to consider RICO, bankruptcy crime laws, tax crimes, conspiracy to defraud the U.S., the Crime Control Act of 1990, the Money Laundering Control Act, mail fraud, aiding and abetting, securities crimes and penalties, joint tortfeasor laws, fraudulent conveyance statutes, IRS penalties, and malpractice claims when advising clients); Rupprecht, *supra* note 1, at 36 (recognizing that attorneys must ensure that international trusts are established at a time when the grantor's legal difficulties can be accounted for in the planning or risk personal exposure); Marty-Nelson, *supra* note 11, at 1273 (admonishing attorneys to accurately characterize and evaluate a client's circumstances and motivation before implementing asset protection offshore).

⁸⁶ Rosen, *supra* note 32 (noting that the key to asset protection planning is the word “advance,” not transfers made “at the eleventh hour”).

basis for the fraudulent transfer laws of much of the world⁸⁷ and is the forerunner of the U.S. Uniform Fraudulent Transfer Act and Uniform Fraudulent Conveyance Act.⁸⁸ The purpose of the Statute of Elizabeth is the protection of creditors through the voiding of any conveyance made with the purpose or intent of defrauding creditors.⁸⁹ However, numerous jurisdictions, including several in the Caribbean, are taking a more modern approach to the Statute of Elizabeth.⁹⁰ While these jurisdictions have instituted “debtor- friendly” fraudulent conveyance laws,⁹¹ they do not sanction or encourage fraudulent conveyances.⁹² Rather, in an attempt to maintain credibility as lawful societies, these Caribbean nations “generally require assurances that the trust settlor does not intend to avoid legitimate creditors or engage in unlawful activity.”⁹³ These measures by host jurisdictions, coupled with honest effort on the part of practitioners to avoid fraud, should assist in cleaning up the reputation of Caribbean APTs as simply a venue for fraudulent conveyances.

C. *International Investment Scams*

Another abuse of the APT relates to international investment scams.⁹⁴ One estimate puts the cost to U.S. citizens of these phony investment programs at over \$1.1 billion per year.⁹⁵ Although no specific information is available regarding investment scams in the Caribbean, exploitation of novice investors is likely. Multiple trusts often provide the venue for bogus transactions, as clients “give away” assets and live tax free on “borrowed” income.⁹⁶ Bad publicity of past scams such as these contribute to the skepticism associated with APTs, as potential investors are scared away by the horror stories of previous victims. The good news is that the U.S. is trying to curb these activities by imposing strong civil and criminal penalties.⁹⁷

⁸⁷ Rosen, *supra* note 3, at A17.

⁸⁸ Rothschild, *supra* note 11.

⁸⁹ *Id.*

⁹⁰ Diaz, *supra* note 4, at 609.

⁹¹ *Id.* at 609 (suggesting a key consideration in choosing a jurisdiction for an APT is the level of protection afforded the debtor from a judgment against him on fraudulent conveyance grounds).

⁹² *Id.* (asserting that “debtor-friendly” jurisdictions find transfers made in trust “unassailable” after the passage of a specified period of time); see also Rothschild, *supra* note 11;.

⁹³ Rothschild, *supra* note 11.

⁹⁴ Beazer, *supra* note 3.

⁹⁵ F. Bentley Mooney Jr., PRESERVING YOUR WEALTH 212 (1993); see Beazer, *supra* note 3, at 21.

⁹⁶ Beazer, *supra* note 3.

⁹⁷ *Id.*

D. *Difficulty with the Fundamental Concept Behind APTs*

Much of the disapproving sentiment surrounding APTs stems from fundamental difficulties with the concept of allowing protection against liability.⁹⁸ There is indeed a discrepancy between APTs and deep-seated precepts of U.S. trust law,⁹⁹ the former reserving far greater protection against creditors than tolerated under the latter.¹⁰⁰ The contradiction between APTs and U.S. trust law raises some eyebrows and is responsible for generating negative publicity for the APT as a legitimate asset protection device.

The fact that APTs differ in premise from precepts of U.S. trust law does not make APTs illegal—it makes them smart.¹⁰¹ Opponents of APTs object to their attempt to place assets beyond the reach of future creditors who may have bona fide claims and no alternative recourse.¹⁰² However, as one promoter of APTs notes, this may be a better argument in a more conservative, less litigious world,¹⁰³ suggesting the increase of frivolous lawsuits has mandated asset protection strategy.

One author, in noting the difference between APTs and U.S. trust law, critiques the right of an owner of liquid wealth to move it to any nation that offers a better compromise.¹⁰⁴ The beauty of the APT is found in precisely the mobility this author criticizes, for it is the mobility of liquid wealth that enables competition in asset protection planning. In considering the appropriateness of the premise underlying the APT, consider analogous applications of foreign or nondomiciliary law, such as the use of Delaware law for corporate purposes despite the fact that no corporate activity is to be conducted in Delaware, or the use of generation-skipping trusts established under South Dakota law to avoid the rule against perpetuities.¹⁰⁵

With a Caribbean APT, laws of various Caribbean nations are used to provide the most advantageous asset protection for a grantor.

The fundamental misconception of the APT as a slap in the face of U.S. trust law has prompted some to urge for sanctions against the jurisdictions permitting APTs.¹⁰⁶ At the extreme, critics have postulated that APTs are

⁹⁸ See Marty-Nelson, *supra* note 11, at 1269 (discussing critics' regard of APTs as merely a way for clients to avoid their just debts).

⁹⁹ Marty-Nelson, *supra* note 18, at 15.

¹⁰⁰ *Id.*

¹⁰¹ Rosen, *supra* note 32 (asserting that asset protection planning is based upon a proven, sophisticated combination of business and estate planning).

¹⁰² Mezrich, *supra* note 1, at 675.

¹⁰³ *Id.*

¹⁰⁴ Lopucki, *supra* note 7, at 38.

¹⁰⁵ Rothschild, *supra* note 11, at 65.

¹⁰⁶ Lopucki, *supra* note 7, at 38.

contributing to the ultimate demise of liability.¹⁰⁷ However, as the preceding section of this article demonstrates, Caribbean APTs are a valid tool for the preservation of wealth, and should not be written off simply because of their novel approach to asset protection.

VII. CONCLUSION

Though once raising eyebrows because of past abuses, Caribbean APTs remain a viable, legal method of asset protection. With the continuing surge of litigation, practitioners should be aware of the hidden treasure a Caribbean APT can offer anyone searching for a prudent planning device.¹⁰⁸ Used ethically and with foresight, a Caribbean APT can be a method of saving for a sunny day.

¹⁰⁷ Lopucki, *supra* note 7, at 38 (suggesting that unless sanctions are imposed against nations offering APTs, strategists will have the means to defeat liability in individual cases, demoralize nonstrategists, and contribute to the death of liability.)

¹⁰⁸ Young, *supra* note 29, at 449.