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ESTATE PLANNING MEMORANDUM

TO: **CPAs, Clients & Associates**

FROM: **David L. Silverman, Esq.**
Shirlee Aminoff, Esq.

DATE: **April 2, 2010**

RE: **Asset Protection: Ethical Considerations**

New York County Surrogates Court, in In re Joseph Heller Inter Vivos Trust, 613 N.Y.S.2d 809 (1994), approving a trustee's application to sever an inter vivos trust to "insulate[] the trust's substantial cash and securities from potential creditor's claims that could arise from the trust's real property, observed that "New York law recognizes the right of individuals to arrange their affairs so as to limited their liability to creditors, including the holding of assets in corporate form . . . making irrevocable transfers of their assets, outright or in trust, as long as such transfers are not in fraud of existing creditors."

Operating a business in corporate form, entering into a prenuptial agreement, executing a disclaimer, or even giving effect to a trust spendthrift provision, are common examples of asset protection which present few ethical issues, primarily because such transfers do not defeat rights of known creditors. However, transferring assets into a corporation solely to avoid a personal money judgment, or utilizing an offshore trust solely to avoid alimony or child support payments, would defeat the rights of legitimate creditors, and would thereby constitute fraudulent transfers.

The ABA's Model Code of Professional Conduct, DR 7-102, "Representing a Client Within the Bounds of the Law," provides that "[a] lawyer shall not . . . [c]ounsel or assist his client in conduct that the lawyer knows to be illegal or fraudulent." Although the Model Code does not define

"fraud," New York, a Model Code jurisdiction, has provided that the term "does not include conduct, although characterized as fraudulent by statute or administrative rule, which lacks an element of scienter, deceit, intent to mislead, or knowing failure to correct misrepresentations which can be reasonably expected to induce detrimental reliance by another." Therefore, in New York, the prohibition against counseling a client in perpetrating a "fraud" would apparently not prohibit an attorney from assisting a client in transferring property because of the possibility that the transfer might, in hindsight, be determined to have constituted a "fraudulent conveyance".

Model Rule 8.4 of the ABA's Model Rule of Professional Conduct provides that it is professional misconduct for a lawyer to "engage in conduct involving dishonesty, fraud, deceit or misrepresentation." Model Rule 4.4 provides that "a lawyer shall not use means that have no substantial purpose other than to embarrass, delay, or burden a third person." Conduct involving dishonesty or an attempt to deceive appears to be a readily determinable question of fact. However, conduct employing means having no substantial purpose other than to delay or burden third parties may be a more difficult factual determination.

Connecticut Informal Opinion 91-23 states that "[f]raudulent transfers delay and burden those creditors who would be inclined to try and satisfy their unpaid debts from property of the debtor. It forces them to choose either not to challenge the transfer and suffer the loss of an uncollected debt or to file an action to set aside the transfer. . . If there is no other substantial purpose, Rule 4.4 applies. Where there is another substantial purpose, Rule 4.4 does not apply. For example, where there is a demonstrable and lawful estate planning purpose to the transfer Rule 4.4 would not, in out view apply."

To minimize risk, the attorney should be careful in performing due diligence prior to engaging in asset protection. Specifically, the attorney should determine (i) the source of the client's wealth; (ii) the client's reason for seeking advice concerning asset protection; and (iii) whether the client has any current creditor issues or is merely insuring against as yet unknown future creditor risks. The attorney should also obtain a sworn statement affirming that the client (i) has no pending or threatened claims; (ii) is not under investigation by the government; (iii) will remain solvent following any intended transfers; and (iv) has not derived from unlawful activities any of the assets to be transferred. Since most prohibitions on attorneys involve the attorney having acted "knowingly," due diligence is the best insurance against future ethical or legal problems.