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TRUSTS & ESTATES

Ethical Considerations in Asset Protection Planning

There's no reason to fear

Patricia Donlevy-Rosen

Sep 3, 2014

Today's clients are concerned with safeguarding their wealth during their lifetime. This concern for lifetime asset protection planning (APP)¹ goes beyond the traditional estate planning focus on minimizing estate and inheritance taxes, avoiding probate and providing for heirs. Consequently, estate planners are expected to have a working knowledge of available asset protection strategies, including the use of asset protection trusts (APTs). However, many practitioners avoid APP or try to dissuade their clients from using APTs, fearing that APP is unethical. That fear is usually based on a lack of knowledge of the area.

Is Conduct Professionally Ethical?

Whether conduct is professionally ethical is determined not by individual subjective feelings, but by standards adopted by members of a particular profession for conduct in that profession. Attorneys are governed by rules of professional conduct (RPC) adopted by the jurisdictions where they practice. These rules are based on the Model Rules of Professional Conduct (Model Rules)² adopted by the American Bar Association. Ethical standards for attorneys in the APP context are more specifically developed (through RPCs, bar opinions, case law and the commentaries of the American College of Trusts and Estate Counsel (ACTEC)) than those for CPAs³ and financial professionals. Because only an attorney should draft APP documents and oversee the entire process, I'll focus on ethics as applicable to attorneys.

While all RPCs require an attorney to zealously represent a client, individual states take slightly different approaches to what constitutes ethical representation; therefore, attorneys need to examine the cases and ethics opinions of the state in which they practice. All states have statutory provisions exempting certain assets from creditors' claims, and more than 15 states have enacted domestic asset protection trust (DAPT) legislation.⁴ This widespread legislative adoption supports the position that APP is ethical. Or at least it can be. It should be noted that some DAPT statutes, such as the one adopted by Ohio,⁵ specifically provide litigation protection for professionals assisting clients in APP. Although APP is basically ethical, it can be practiced unethically. The real question is: How does an attorney do APP ethically? This is when the applicable RPCs and best practices come into play.

Know Your Client

As a practitioner, you must "know" your client. Knowing your client entails obtaining basic information from him about his current financial and litigation status, foreseeable or expected changes to such status and information as to his source of funds, that is, how your client obtained his wealth. In addition, references from your client's banker, attorney and/or CPA should be obtained. If appropriate, obtain letters from other professionals representing your client as to particular issues: for example, on-going litigation, new or risky business ventures and family health issues. In addition, obtain and review income tax returns, financial statements and an accountant's letter (concerning businesses of the client) to verify that your client is, and after the proposed transfer will be, solvent under applicable law. The extent of existing, threatened or foreseeable claims (if any), must be considered; verification and evaluation from your client's counsel regarding such claims should be obtained.⁶

Can it be Done?

Determining whether you may ethically assist a particular client in APP will depend on the applicable state (of residence of the client) and federal fraudulent transfer (voidable transaction) laws. What can be effected ethically in one state may not be effected ethically in another. Also, what you can't effectively protect domestically, you may be able to effectively protect by using an offshore asset protection trust (OAPT), that is, one governed by the laws of a foreign jurisdiction.

Avoid Unreasonable Client Expectations

Once you've determined that a client may be represented in an APP matter, you must avoid another common ethical pitfall: communication failures, especially allowing unreasonable client expectations. It's imperative that your explanations of the planning be sufficiently detailed so as to allow a client to make informed decisions regarding what APP options are appropriate and may be undertaken for him.⁷ Domestic planning limitations, include, for example, differing statutes of limitations on fraudulent transfers, required location of (at least) some assets in the DAPT state and the possibility of the entire domestic APP structure being "undone" by a bankruptcy court for up to 10 years after it's created. On the other hand, you must explain that these limitations won't affect an OAPT that's been properly drafted and implemented (no U.S. court will have the power over the trustee of the OAPT). In addition, make clear to your client that the efficacy of protection varies from asset type to asset type. Your client should know about all these and other limitations before the APP is begun. Then, even if your client elects not to implement the advised APP or isn't an ideal candidate for the planning, you've met ethical obligations while avoiding malpractice exposure.

Once your client decides what he wants, it's recommended to have a retainer letter, signed by the client, clearly setting forth: (1) the parties' responsibilities; (2) fees and estimated costs, (3) the fact that APP services will be provided only if the client fulfills the disclosure requirements and passes the criteria deemed appropriate by applicable law and by the attorney; and (4) that the client will pay for the attorney's services in making such determination notwithstanding termination of representation, if facts or circumstances are disclosed which preclude representation.⁸

Outsource When Necessary

A basic rule of professional conduct is to provide competent representation.⁹ In addition to having thorough knowledge of the law, competent drafting to implement the plan is of utmost importance. For example, inexperienced drafters sometimes attempt to take advantage of a statutory provision merely by naming it, for example, "duress," but then fail to include a mechanism that will ensure that the provision will be effective when implemented. Competent drafting can come from working with

one who's already been effectively drafting the plan sought to be implemented. It makes no sense to re-invent the wheel or the planning document.

The Model Rules commentary strongly suggest that you work with an experienced professional to learn how to implement and draft a plan properly so that it accomplishes the goals sought.¹⁰ Attorneys hesitate to refer clients to another attorney for fear of losing the client. You can avoid this by contacting the expert and having a frank discussion about the extent of the participation and client contact of each attorney. Of course, it's imperative that the attorney to whom the work is outsourced has the requisite qualifications and experience. If you use an "of counsel" or ghost writer attorney, you may be liable for their work product. It may be preferable to refer the work directly to a practitioner focused in APP/APT planning. Before making a referral, establish a relationship with a qualified attorney, discuss the limited scope of his representation and finalize any co-counsel arrangement for shared projects. With an infrastructure already in place, prompt referrals and ethical representation of a client can be assured.

Don't Procrastinate

Finally, let's not forget that you "should act with reasonable diligence and promptness in representing a client."¹¹ A client's interests and your ability to ethically represent the client can be adversely affected by the passage of time or a change in conditions. Therefore, the sooner an APP is drafted and implemented, the better for the client.

Endnotes

1. APP is the adoption of advance planning strategies to place assets beyond the reach of future potential creditors. It's not based upon secrecy, hiding assets or dodging taxes. The effect of a proper plan is to lower a client's financial profile and discourage lawsuits.
2. To the extent that the Model Rules of Professional Conduct (Model Rules) focus on adversarial conduct, the American College of Trust and Estate Counsel (ACTEC) publishes a set of commentaries specifically designed to assist the estate planning attorney: ACTEC, Commentary on the Model Rules of Professional Conduct (4th ed.

2006)(the ACTEC Commentary). The ACTEC Commentary provides additional guidance to the asset protection planner, who generally renders estate-planning advice and may employ trusts in the implementation of an asset protection plan.

3. A CPA refers to his state board of accountancy, the AICPA Code of Professional Conduct, AICPA Statements on Responsibility in Tax Practice and the Treasury's Circular 230 for guidance.

4. Legislation by the states in doing so was initially spurred by the volume of U.S. persons taking advantage of protective trust legislation enacted by certain offshore jurisdictions (such as the Cook Islands and Nevis) in the 1980s and 1990s who moved liquid assets offshore out of local banks and trust companies.

5. Ohio Rev. Code Ann. Section 5816.07(D).

6. Model Rules, Rule 1.3.

7. *Ibid.*, Rule 1.4.

8. *Ibid.*, Rules 1.2 and 1.5.

9. *Ibid.*, Rule 1.1.

10. *Ibid.*, Rule 1.1 and commentary.

11. *Ibid.*, Rule 1.3 (see comment to Rule 1.3).