

CM SKYE

CM Notes

ASSET PROTECTION: FRAUDULENT TRANSFER; AND RE THE PETITION OF CHRISTOPHER JOLLIAN HEGINBOTHAM 1999

OCCASIONAL PAPER, 1ST DECEMBER 1999

Summary

Following changes in the law of the Isle of Man, the Isle of Man has, since 1999, been one of the better jurisdictions for the establishment of structures for 'Asset Protection'.

We recommend that, for *Asset Protection*, there should be either a domestic trust in the USA, or an offshore trust in a suitable equitable jurisdiction, in which any necessary Estate tax planning is done, but with the assets held in a subsidiary LLC, established in the Isle of Man LLC, which provides the Asset Protection strength.

Where an offshore Trust is the preferred mechanism, we would normally use the Isle of Man, (or Gibraltar), depending on the preferences of the client, with an Isle of Man LLC underlying the trust.

We believe that LLCs are more certain in law, and much simpler in application, although it is not possible to build U.S. Estate Tax planning provisions into them. Combining an Asset Protection Trust with an underlying Asset Protection LLC creates a very powerful mechanism.

Trustee services are provided through a subsidiary, **CM Skye Grantees Limited**, in the Isle of Man.

Note. ¹ *Re the Petition of Christopher Jollian Heginbotham 1999* reported in the International Trust and Estate Law Reports 21TEL 95.

30TH SEPTEMBER 1999

ASSET PROTECTION:

THE ISLE OF MAN DECIDES - THE PRECEPTS OF THE STATUTE OF ELIZABETH

DO NOT APPLY!

- PROF. CHARLES A. CAIN MA FCIB TEP

There has for some time been an area of uncertainty relating to the law of fraudulent transfer in the Isle of Man. This arose because the Isle of Man, as a jurisdiction is, and always has been separate and distinct from that of England, and thus English law was never 'received' in the same way as, for example, it was received into former English colonies, including the USA. The infamous 'Statute of Elizabeth', or more properly, the *Fraudulent Conveyances Act 1571 (13 Eliz I Cap 5)* was never adopted in the Isle of Man. The earliest legislation on the subject is *Fraudulent Assignments Act 1736* of which, today, just one section remains in force. This reads as follows:

- (4) And that all fraudulent Assignments or Transfers [sic] of the Debtor's Goods or Effects shall be void and of no effect against his just Creditors, any Custom or Practice to the contrary notwithstanding.

The only other reference in Manx legislation is to found in the *The Bankruptcy Code 1892*.

Section 30 reads:

Avoidance of voluntary Settlements

- (1) Any Settlement of property, not being a settlement made before and in consideration of marriage, or made in favour of a purchaser or encumbrancer in good faith and for valuable consideration, or a settlement made on or for the wife and children of the settlor of property which has accrued to the settlor after marriage in right of his wife, shall, if the settlor becomes bankrupt within two years after the date of settlement, be void against the trustee, and shall if the settlor becomes bankrupt at any subsequent time within ten years after the date of the settlement, be void against the trustee unless the parties claiming under the settlement can prove that the settlor was at the time of making the settlement able to pay all his debts without the aid of the property comprised in the settlement, and that the interest of the settlor had passed to the trustee of such settlement on the execution thereof.

- (2) 'Settlement' shall for the purposes of this section, include any conveyance or transfer of property.

Thus the whole situation relating to future creditors, (i.e. creditors not existing or being ascertainable at the time of the settlement is effected and arising subsequent to such a settlement having been made) was unknown.

This is of great significance because the Isle of Man was one of the pioneer jurisdictions for asset protection trusts, but fell by the wayside because of uncertainty on this point. In addition, the Isle of Man turned its face against the type of 'debtor' protection legislation as was adopted in many

other jurisdictions, to the extent that the Isle of Man does not even feature on a list of jurisdictions favoured for asset protection work.

Of course, one of the results of this is that the establishment of a trust in the Isle of Man came to be regarded as a very 'clean' thing to do. Whereas the establishment of a trust in certain Pacific and Caribbean jurisdictions has become almost tantamount to a badge of fraud in itself, the same is palpably not true of the Isle of Man.

In the last few years, however, there has been a considerable amount of work put into designing the Isle of Man LLC for asset protection purposes, with considerable success. For a simple inexpensive and uncomplicated asset protection structure, the combination of an onshore trust (say in Delaware or Alaska) with an Isle of Man LLC has many attractions. The tax planning is done in the onshore trust, whose reporting requirements are much simpler than those of an offshore trust, whereas the Asset Protection planning is done through the offshore Isle of Man LLC.

However, in a recent judgement in the Isle of Man, the whole issue of fraudulent transfer has been resolved. *Re the Petition of Christopher Jollian Heginbotham 1999* is reported in the International Trust and Estate Law Reports 21TELRL 95⁵. The note of the Editor (Philip Baker) in that case notes:-

The issue decided by this case had not previously been settled in Isle of Man jurisprudence. The issue is of relevance because the Isle of Man has eschewed specific asset protection legislation. This case now establishes (subject to any contrary decision of a higher court) that a transfer of asset to a trust, for example, cannot be set aside at the instance of creditors whose debts were not known and ascertained at the time of the transfer. Thus so long as the transferor is not in a 'state of insolvency' at the time of the transfer - that is, he can pay all his known and ascertained debts, including those falling due on a future date - the transfer cannot be set aside.

This case also confirms the general principle that a trust, bona fide established by a person who is not insolvent, is a perfectly good asset protection arrangement. In some instances, the use of a trust in a territory with strong asset protection legislation - such as in the Cook islands - is an indication that the transferor was not bona fide or knew of future debts he wished to avoid. On the outcome of creating an asset protection trust under such a regime, see *ETC v Affordable Media* 21TELRL 73.

The case was a petition under the Fraudulent Assignments Act 1736 for an order that the petitioner could enforce a judgement against two Isle of Man companies. The Petitioner, a local Estate Agent (Realtor), Mr A, had sold out to a Purchaser, Mr W. The deal was structured so that the business was transferred to a new company, A Ltd, which was owned by Mr W. Because of local legislation, an Estate Agency business must have a qualified person in management. Mr A was so qualified. Mr W was not. Therefore, the services of Mr A were retained as a director of A Ltd.

There was a disagreement between Mr A and Mr W, and the terms of the agreement were not carried out. Mr W, needing a qualified person, did a deal with Mr M, who was so qualified. Part of the business was transferred into one of the companies; the other part, which required a qualified person to be involved, was transferred to the second company with which Mr M was associated.

Mr A obtained a judgement for specific performance of the agreement, but was unable to enforce it against A Ltd, since the asset had been transferred out of A Ltd to the two new companies. Mr A petitioned under the Fraudulent Assignments Act 1736 to have the transfers set aside as fraudulent transfers.

The Deemster (as a High Court Judge is called in the Isle of Man) rejected the Petition. HELD

- (1) For the 1736 Act to apply, there must be an intent to defraud creditors. This intent applies only to present debts, not contingent or future debts which may never materialise. Present debts include known and ascertained debts which are to fall due on a date in the future.
- (2) At the time of the transfers to the two companies, the petitioner had not yet served his defence and counterclaim to the action. The judgement debt was not therefore a present debt. The transfers were bona fide and not contrived to defraud creditors.

The Deemster considered the implications of the 'Statute of Elizabeth' and the Fraudulent Assignments Act 1736 at great length. This included a judgement of the Judicial Committee of the Privy Council of 1859. He also considered the 'obiter dicta' of Deemster Kneen in *Re Corrin's bankruptcy* (1912), which those who have followed the Isle of Man's law in this area will be aware of.

For the time being, therefore, the law in this area is clarified.

What does it mean in practice. It means that Asset Protection Trusts or LLCs established in the Isle of Man are now safe in Manx law, provided that, at the time of establishment, the Settlor was solvent, was able to meet all his known and ascertainable creditors, and had no intent to defraud creditors.

The Isle of Man must now be considered as one of the preferred jurisdictions for asset protection structures.

Notes:-

¹ Trustee in bankruptcy

² Published by Butterworths, London UK. In the USA available from Lexis Law Publishing, Charlottesville, Virginia ISSN 1464-7125.

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