

Cook Islands Trust Corporation Ltd - Asset Protection Trusts

CIT EXPERIENCE: Cook Islands Trust Corporation Ltd. (CIT) was incorporated in the Cook Islands in 1988, and is licensed as a trustee company. The directors of CIT are Laveta Short and Reuben Tylor, the principals of Short & Tylor, the first law firm established in the Cook Islands, and Antony Will. Reuben Tylor was appointed as a principal of a trustee company in 1982 and has specialized in offshore work since that time. In 1989, he pioneered and developed the first asset protection legislation for which the Cook Islands is the dominant international jurisdiction. Laveta Short has had a distinguished international career as a lawyer, a Cabinet Minister, and foreign diplomat, and also played an important part in setting up the Cook Islands tax haven. In recognition of his services to the Cook Islands he was awarded an OBE from Her Majesty the Queen in 1998. Antony Will joined CIT in 2000 as in-house counsel, at the start of 2003 Antony was appointed as an Executive Director of the company.

Cook Islands Law

The Cook Islands is recognised as the world leader in formation of asset protection trusts, safeguarding the assets of high net worth clients. Cook Islands law contains a number of unique features that make the operation of an asset protection trust administratively friendly and highly protective.

The most important of these features relate to claims by creditors that a transfer of assets to the trust was fraudulent against them, and therefore void. This would enable a creditor to gain access to those assets. Therefore, provisions include:

- A time limit for any actions being brought against a Cook Islands trust alleging fraudulent transfer;
- No action can be brought for "future fraud" i.e.: if the transfer of assets to the trust occurs prior to a creditor's cause of action accruing;
- There is no bankruptcy law in the Cook Islands;
- The Cook Islands law of fraud is based on the old Eng-

lish law and requires proof by the creditor, of intent to defraud that particular creditor, to a criminal standard i.e.: beyond reasonable doubt; and

- Foreign judgements, negating a transfer of assets to a Cook Islands trust, based on foreign law, will not be recognised by a Cook Islands court.

In addition, there are numerous provisions that enable a Cook Islands trust to be administered without requiring the settlor to give up all control over the trust assets.

Basic Structure of the Asset Protection Trust

The trust structures that we recommend focus on ensuring that any challenge to the trust has little chance of succeeding. The way in which Cook Islands Trust Ltd (wholly owned subsidiary of CIT) operates and administers trusts in its role as trustee is also geared towards ensuring that the trust cannot be successfully challenged. A further, vital point is that CIT maintains no presence in the US and thus is not exposed to the exercise of jurisdiction by US courts.

The Parties

SETTLOR: The client, the person putting the assets into the trust.

TRUSTEES: Hold the title to the assets and administer the running of the trust.

PROTECTOR: Oversees the operation of the trust, as well as removes and appoints the trustees. Often the settlor, but can be settlor's attorney or family member.

BENEFICIARIES: Those who are to receive the benefits (income and capital payments) from the trust. Usually settlor plus family members. Can include any person or class of people that the client chooses.

The Structure

The US Asset Protection Trust

This is the most common structure and is adopted by a settlor who has no current concerns but is conscious that there may be some liability in the future and wishes to establish a basic structure as a safeguard.

Parties

Three trustees are appointed, Cook Islands Trust Ltd plus two US Domestic Trustees (can be settlor but preferably settlor's attorney or family member), and a protector. The Cook Islands trustee normally delegates its operating powers to the two US trustees. Essentially the two US trustees then exercise all powers relating to investment of trust assets and distributions to the beneficiaries according to the settlor's "wishes", and report back to the Cook Islands trustee at an annual meeting.

The protector oversees all decisions made by the trustees and retains the ability to veto any decision made by the trustees. The protector also has the power to remove and appoint trustees if they do not perform their duties as required by the settlor.

Assets

Assets are normally placed into a Family Limited Partnership (FLP). The settlor holds the general partners 1% share, but transfers the limited partners 99% share to the trustees. The settlor continues to control all investments by the FLP and the trustees are involved only for the purpose of:

- (a) Receiving annual reports from the General Partner; and
- (b) Distributing any profits passed to the trustees by the FLP.

Litigation

If there is a threat to the settlor (e.g. a pending law suit) then the trust structure is changed to become more like that of a foreign asset protection trust. The US trustees are removed, the FLP is liquidated, and any liquid assets are placed with a Swiss custodian bank. Investment is then continued under the direction of an Investment Adviser appointed by the settlor. The Cook Islands trustee becomes responsible for any decisions to distribute to beneficiaries. Under this structure, with no assets to attack, an attorney acting on a contingency fee for a plaintiff is much more likely to either abandon their claim or settle for significantly less than the amount claimed. Once settlement is achieved, the previous structure with the two US trustees can be reinstated.

While this is a common structure, there are variations that can be implemented to suit individual requirements. Some settlors like to transfer assets directly to the trustees. This is possible although the trustee itself must not be exposed to any potential liability. Some prefer to open an investment account with a Swiss Investment bank from the outset, so that if an emergency does arise then they already have the relationship in place. Some settlors decide at the outset not to appoint any US trustees and adopt a structure where the protector controls the Cook Islands trustee.

There is also variation in the amount of assets transferred into the trust. Some settlors like to transfer all their assets; others take a less aggressive stance and transfer only sufficient for a "nest egg" in the event of them losing the rest of their wealth.

The Foreign Asset Protection Trust

This structure is most commonly used for Nest Egg trusts and offers the best level of protection against threatened action by a creditor.

Parties

CIT Ltd is appointed as the sole trustee. The trust still has a protector who can veto any trustee actions and can remove the trustee at will. The trustee also normally appoints an Investment Adviser, (normally the settlor's existing financial planner), approved by the protector. A foreign custodian

bank is also involved.

Assets

The best level of protection is offered if persons outside of the US hold title to assets. For this reason assets are often held by a Swiss custodian bank, with the Investment Adviser directing all transactions. Funds may also be placed with the Swiss bank under discretionary management on terms approved by the protector.

Litigation

The structure is designed to withstand litigation without further changes.

Tax Implications

Offshore asset protection trusts should not be confused with offshore tax vehicles.

Both of the trust structures described above are designed as grantor trusts. They are tax transparent for income tax purposes, and the settlor continues to be personally liable for any income from the trust. In addition, the trusts are drafted so that all transfers to the trust are "incomplete" and therefore there are no gift tax, estate tax, or excise tax issues arising. The trust assets are included in the settlor's estate on his or her death. Both trusts also have US reporting requirements. The foreign asset protection trust has substantially more requirements to be met, than the US asset protection trust. ■