IN FACT AND IN LAW

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Setting Up A Trust: An Attractive Solution For Your Asset Protection Needs

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Today, it is easy to find examples where individuals' assets are threatened due to their professional activities or personal situation. Our governments have also given themselves effective means of tapping into the personal assets of individuals, mainly through the imposition of various directors' liabilities.

Personal liability is also a major concern for anyone who practises a profession where such liability cannot be limited. Insurance coverage is not always adequate and parties who feel wronged seldom hesitate to claim damages from those they consider liable. In such a context, individuals at risk would want to protect their personal assets from any claims that may be asserted against them.

For these purposes, a trust is a legal vehicle that provides asset protection for individuals at risk from a personal or professional perspective. Such protection usually aims to ensure that a person's assets are not threatened at the whim of anyone who rightly or wrongly believes that he or she can take an action against that person. This protection affords a position of strength – and some security – to individuals who adequately plan ahead.

The Various Structures

Many asset-holding structures may be considered by an individual who wishes to protect his assets. For instance, that person's spouse – to the extent that he or she is not at risk of being subject to proceedings – may hold all the assets of the family unit. However, such a solution involves considerable risk in view of the current fragility of matrimonial ties.

Conversely, an individual may choose to implement a complex structure involving the holding of assets through entities that do not reside in Canada. While such structures may prove efficient, they are complex, cumbersome and costly to set up and maintain. They are generally used in situations involving considerable fortunes or by individuals whose assets are already situated in several jurisdictions.

The use of trusts residing in Canada is often the most flexible and least costly solution to enable an individual to realize his or her asset protection goals, especially in light of the 1994 reform of the *Civil Code of Québec*, which clarified the basic legal rules that apply to trusts.

Asset Protection Trust

The implementation of an asset protection trust can be relatively simple. One merely has to establish its operating rules and specify the identity of the settlor and the beneficiaries. A trust deed formalizes the decisions that were made and, upon its execution, a separate patrimony by appropriation is created.

Things may not be as simple as they appear, however. Transferring assets from an individual to a newly created protection trust without adequate planning may well result in significant tax problems, usually involving the GST/QST, transfer duties and income tax.

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These problems can generally be avoided, though, as tax legislation provides for exemptions allowing the transfer of assets without penalty. In some cases, creative planning is the only way to avoid the tax bite when transferring assets. In the normal course of events, an asset protection trust does not provide any tax advantage with respect to taxation of the return on the assets that have been transferred to it. There are, however, several exceptions to this rule that apply in specific situations.

Rules to Remember

To achieve one's asset protection goals, trust planning must comply with certain rules. For instance, it is more prudent to specify many beneficiaries or categories of beneficiaries whose rights in respect of the trust capital and income are subject to the discretion of the trustees.

The moment at which an individual's assets are transferred to a trust is also important. It is most desirable that such a structure be implemented while the individual is solvent, even without the assets transferred to the trust. It can then be clearly established that the transfer of assets was not made to the detriment of the current creditors of the individual.

Conclusion

In short, a trust is a legal vehicle that can be used to protect the personal assets of individuals at risk from a personal and/or professional point of view. It can also sometimes be used for implementing financial and estate planning, provided that the tax savings outweigh the costs of setting up and maintaining the structure.

The legal and tax rules governing the implementation and maintenance of such structures are, however, very complex. They require special attention in order to avoid creating bigger problems than those you are seeking to avoid.

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