TALES FROM THE TRENCHES™
BY BARRY C. MCGUIRE

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ASSET PLANNING & PROTECTION – THE POWER OF TRUST

I've got a real bee in my bonnet about Asset Planning & Protection (APP). I have done Focus Workshops all about Legacy Planning, Asset/Corporate Structure, Insurance, and Tax Planning, but now it's time to bring this focus back to my blog and podcast. It's hugely important for all of us, but we are all so busy buying, selling, and managing real estate that APP always takes a back seat. I want you to have a much better general understanding of Asset Planning & Protection. Are we trying to turn you into lawyers, accountants, financial planners, or tax experts? No, absolutely not. But we are trying to help make you more informed and prepared!

Let's start with some basic considerations.

1. **Asset Planning & Protection is a legitimate, basic building block of finanacial life.**
   It is part of any complete business plan. Do not be thrown off track by those who refuse to plan, or see every plan as a scam.

"Asset and wealth protection should not be seen as the bailiwick of the unprincipled and desperate. Planning for the protection of our wealth and assets, modest or abundant, is prudent if we are to enjoy our lives, care for our families, contribute to the needs in our communities and contribute to meaningful change in our world."

(Asset and Wealth Protection by Kelly R. Doyle LEXIS-NEXIS 2009)

2. **Life is uncertain. Uncertainty accentuates the need to plan and protect.**
   For example there are numerous legal uncertainties arising from ongoing interpretation of law, the Charter of Rights and Freedoms, an increasingly litigious society, contracts, guarantees and indemnities, participation in businesses, joint ventures, matrimonial and family relationships, and limited insurance coverage. Tort legislation and class actions are more prominent, examples being various church abuse disgraces, the residential schools debacle, and the Red Cross tainted blood scandal. You just don't know what's coming.

Economic uncertainties are influential and happen even in our closely regulated, stable economies. Think of the oil price collapse, Bernie Madoff, subprime mortgages leading to world economic collapse, and everyone hates the oil sands. Climate change will be a huge driver of economic decisions. All these macro events have an effect on you. What about politics? We are relatively stable here in Canada but our neighbours to the south are big, pushy, and look out for themselves (e.g., Keystone). Think of the Trans-Pacific Partnership, the Patriot Act, and Arctic sovereignty. ISIS, the growing refugee crisis, and the rise of China and India as world powers are just a few of the issues that affect Canada and, ultimately, every one of you.

3. **Life is complicated, and growing ever more complicated**. As much as you would all like life to be simple, it is unlikely we are ever returning to simpler times. But, you might think your circumstances are simple. I can't say this enough, oversimplify at your peril. Your circumstances might be simple, but find out for sure. Each of your situations and facts are different. Every one of you needs to take professional advice before creating a plan to maximize and shelter your assets. Overly simplistic

plans or plans that step in the 'grey area' do not serve you or the public and could easily expose you to the very risk that you are trying to avoid. And, as much as every one of you needs a plan, remember this.

"There is no bulletproof theory, no impenetrable legal fortress. For asset protection to work for you, you must be able to look the judge in the eye and honestly proclaim confidence in the abilities of your planner who... gave you sound professional advice that you followed in the course of a perfectly legitimate personal, financial and business planning."

(Asset Protection: Concepts and Strategies for Protecting Your Wealth by Jay Adkisson and Christopher Riser, McGraw-Hill 2004).

We all need to be very clear on what assets we have, plan to have, the best way to protect those assets, pay appropriate tax on those assets, how to use assets for our own and family enjoyment, how to leave legacies for our loved ones, and how to contribute to our community. (Did I mention that I feel strongly about this?!) With that introduction and summary on the various aspects of APP, let's get on to a Tale that illustrates why a properly drafted asset plan always has elements of asset protection.

Now, as real estate investors we always seem to worry about our third-party liability in terms of a tenant slip and fall. Or, perhaps we worry about a joint venture partner suing us. In my experience, these two situations do not come up that often. So, yes we have to guard against these situations but there are so many more circumstances that could bite us.

In this Tale our client was a mid-level manager in a very successful employee owned company. He came to see us when his company was spending money and acquiring assets that would pay off big time down the road, say 7–10 years, and then for a period of 10 years. His payoff was going to be $1 million per year.

At the time our client was 50 years old with a daughter age 10 and a son 14 years old. He was worried that just when his share of the company's investment was starting to really generate some cash, his children would be roughly 20 and 24 years old. As we worked on his asset plan, he kept saying, "I know what I was like when I was in my early 20s. I'm surprised I survived till now!" Whatever else we did, the asset plan had to ensure that his children did not necessarily get big chunks of cash when they were too immature to manage that cash in a sensible way.

Of course, when you think about any asset plan, a review of tax reduction strategies is always a major consideration. And, of course, the more income or gains you are generating, the more important it is to reduce tax. With our client thinking that his income would be in the $1 million per year range, we are now talking substantial tax.

After much reflection and research, the answer was to create a Family Trust. Our client was the trustee and he, his wife, and their two children were the beneficiaries. The Trust was discretionary in that the trustee had the authority to distribute the income of the Trust as he saw fit. He was not bound to distribute evenly to each beneficiary or to any particular beneficiary at all.

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Fast forward 12 years. The first real test came when our client's daughter, now 22 years old, was off at University and fell in with the wrong crowd. She foolishly tried some OxyContin at a party and was soon hopelessly addicted. Like many addicts, she would do anything to feed her addiction. She cheated, lied, and stole from her parents, her friends, and brother, but she would not accept treatment.

She desperately wanted her usual distribution from the Trust, which was relatively small, enough to pay for University and living expenses. But, of course, she now wasn't going to school and all the money went into drugs.

Our client tried all the usual assistances and interventions, but, in the end, had to apply tough love. He completely cut off her distribution from the Trust and kept it that way even though it cut him like a knife to see his daughter living on skid row.

Distributions from the Trust now went to him, his wife, and their son with nothing to the daughter. Again, the ability of our client as trustee to vary distributions and protect against beneficiary claims was an immense benefit in this difficult situation. The good news is that the daughter fought back, is now clean, and has remained drug-free for three years. She is now participating again in the Trust distribution.

The second glitch came when our client's company hired a new CEO. The CEO thought of himself as the new broom sweeping clean. Our client had been with the company for 30 years but the new CEO saw him as baggage that was not contributing. And, worse than that, accused our client of making bad business decisions that enriched himself at the expense of the company.

The result was that the new CEO purported to fire our client for cause, in other words, they had good and valid reasons for firing. Our client sued for wrongful dismissal and the company counterclaimed for alleged negligence and harmful conduct committed by our client. The company claimed a huge sum of damages and, guess what, specifically named our client's Family Trust as where they thought our client held his ill-gotten gains.

This lawsuit never got to court as the CEO's lawyers advised him that, on further investigation, there was no proof that our client did anything wrong and, perhaps more importantly depending on how you look at it, that the company could not successfully attack the Family Trust. So, this was the first test of whether or not the asset plan contained in the Family Trust did something other than freeze our client's income at a point in time, and allow a much more tax friendly distribution of income.

When you think about guarding against liability, you can rest assured that our clients never contemplated being sued by his own company, which was the vehicle for generating the wealth in the Family Trust. The cool thing about a Trust is that no-one owns it—so by definition, it cannot be taken away by a third party.

Now, on the tax planning side, the Trust was working perfectly. Potential tax bills of $350,000 were reduced to $200,000 and the Trust was able to distribute Trust income in a way that best suited the tax circumstances and real life circumstances of the four beneficiaries.

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Family and Trust matters were all looking rosy until the now 26-year-old son discovered that his wife was cheating on him and his marriage collapsed. The cheating wife hired a very aggressive divorce lawyer and the fight was on.

Essentially the cheating ex said that she would disappear if she got a big payout from the Family Trust as part of their matrimonial property settlement. And, if they didn't want to just pay the money, then a lawsuit would commence to force our client to compensate his son's soon-to-be ex-wife. The lawsuit commenced.

In the usual exchange of documents between lawyers, the wife's lawyer was given a copy of the Family Trust. After not too much back and forth, the wife's lawyer advised her that they could not attack the Trust and she disappeared without very much more trouble. To be clear, the wife didn't just want a part of the assets owned by the Trust, but rather she wanted the income from the Trust to be included in calculating her spousal support. She failed in both regards!

So, there you are. This is a good example of how a properly drafted asset plan also has important elements of asset protection. N.B. that APP is never a cookie-cutter. Everyone's individual circumstances are, if not unique, at the very least substantially different from anyone else's individual circumstances.

Lessons Learned:

1. Everyone needs to consider Asset Planning & Protection (APP).
2. APP is not a cookie cutter.
3. An asset plan must include asset protection.

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