American Bankruptcy Institute

2017 Alexander L. Paskay Memorial Bankruptcy Seminar

Covering Your Assets!! The Ethics of Asset Protection

Hon. Cynthia C. Jackson, Moderator
U.S. Bankruptcy Court (M.D. Fla.); Orlando

John A. Anthony
Anthony & Partners; Tampa

Alan S. Gassman
Gassman, Crotty & Denicolo, P.A.; Clearwater

Michael C. Markham
Johnson Pope Bokor Ruppel & Burns, LLP; Tampa

Prepared by: Alan S. Gassman and Michael C. Markham

The authors thank Judge Alexander Paskay, Jonathan Gopman, Denis Kleinfeld and Jonathan Alper for their previous writings, including those quoted extensively in this article.

American Bankruptcy Institute Presentation:

ETHICAL AND LIABILITY EXPOSURE OF LAWYERS WHO ADVISE DEBTORS OF THEIR LEGAL RIGHTS WHEN A JUDGMENT EXISTS OR MAY BE IMMINENT

In some states, such as California and Connecticut, it is a breach of the rules of professional conduct and in some cases a tort for a lawyer to advise a client to engage in a "fraudulent transfer", or to assist a client in effectuating such a transfer, notwithstanding the significant difference that exists between committing "fraud" and making a transfer that may be for the purpose of avoiding a creditor. This can also violate Federal law, such as when there is an attempt to evade paying the Internal Revenue Service or certain other Federal agencies. *See* 18 U.S.C. §1032 (criminal penalties for concealing assets from the FDIC, any conservator appointed by the Comptroller of the Currency, or the National Credit Union Administration Board); IRC §7206(4) (criminal penalties for evading or defeating the collection of a tax; IRC §7212(a) (criminal penalties for corruptly interfering with the due administration of the Internal Revenue Code.)

The authors have found that many good Florida lawyers believe that a lawyer is not permitted to assist a client in engaging in a fraudulent transfer, as if a fraudulent transfer were the equivalent of committing fraud, which is not the case.

The below discussion should be of assistance to those Florida lawyers who represent debtors or potential debtors in situations where allegations of the making of a "fraudulent transfer" might be possible based upon future conduct. The authors thank Denis Kleinfeld and Jonathan Alper for writing the June 2004 Florida Bar Journal Article entitled "The Florida Supreme Court Finds No

Liability for Aiding or Abetting a Fraudulent Transfer", which is quoted in several places below where indicated, and encourage that advisors who work in this area actually read the cases herein discussed, which provide not only law but also the flavor that we have attempted to describe in this article.[1]

Common law and statutory fraud consists of conduct which constitutes the misleading of a third party. For example, the most prevalent definition provided by Black's Law Dictionary is as follows:

> "A knowing misrepresentation of the truth or concealment of a material fact to induce another to act to his or her detriment."[2]

In *Sheridan v. Rennhack*, 200 So. 3d 255, 258 (Fla. 1st DCA 2016), the Florida Supreme Court confirmed that a finding of fraud requires all four of the following elements exist: (1) A false statement concerning a specific material fact; (2) the makers knowledge that the representation is false; (3) an intention that the representation induces another's reliance; and (4) consequent injury by the other party acting in reliance on the representation.

Under Florida Statute Section 726.105, a fraudulent transfer occurs when a debtor:

> (a) With actual intent to hinder, delay, or defraud any creditor of the debtor; or
> (b) without receiving a reasonably equivalent value in exchange for the transfer or obligation, and the debtor

---

[1] Nevertheless, in the words of Jimmy Buffett, "You had to be there" - don't miss his double album live performance recordings from 1978 if you have not heard them. Pirates were early role models for aggressive debtors. *See also* footnote 30.

[2] Misrepresentation is an affirmative declaration contrary to fact. Concealment of a material fact is a failure to disclose or an omission of relevant information that can be critical to the decision making process. Moreover, "knowing" means that the misrepresentation or concealment must be intentional. In a decision regarding one's finances, misrepresentation of the truth or concealment of material fact must be done with knowledge of substantial certainty or purpose that the misrepresentation or concealment is to the other party's financial detriment.

> (1) was engaged or about to engage in a business or a transaction which the remaining assets of the debtor were unreasonably small in relation to the business or transacting; or
>
> (2) intended to incur, or believed or reasonably should have believed that he or she would incur, debts beyond his or her ability to pay as they became due.

Committing a fraudulent transfer is therefore much different than committing "fraud", although it is possible that both could occur simultaneously in certain situations. Hence the difference in the terms "hinder, delay or defraud" as used in the statute. Obviously, an act to hinder or delay is not an act to defraud. See In re Ellison, 2016 WL 5349715 (Bankr. C.D. Cal. 2016)(The dictionary definitions of these words reinforce these observations. The word "hinder" has been defined as a transitive verb: "1. To be or get in the way of. 2. To obstruct or delay the progress of." The American Heritage Dictionary of the English Language at 830 (4th ed. 2006). The word "delay" has been defined as a transitive verb: "1. To postpone until a later time; defer. 2. To cause to be later or slower than expected or desired." The word "defraud" has been defined as a transitive verb: "To take something by fraud; swindle.")

This is further evidenced by the passage by many states of the Uniform Voidable Transfer Act, which is replacing the Uniform Fraudulent Transfer Act, and is for the most part identical to the Uniform Fraudulent Transfer Act, with the notable change of the words "fraudulent transfer" to "voidable transfer", although commentators have voiced concern that the new official comments to the Act may impact its effect in situations where (1) transactions or transitions convert easily accessible assets that are illiquid and more difficult to seize and sell for cash, (2) entities or assets may be converted into limited partnerships or LLCs that are more difficult for a creditor to pierce, (3) with respect to the choice of law to apply when an asset protection trust is formed by a debtor residing in a non-asset protection trust jurisdiction, and (4) in other instances.[3]

---

[3] Estate Planning & Taxation by George D. Karibjanian, Trust and Estates, May 2016.

Florida Bar Disciplinary Rule 4-8.4(c) provides that a lawyer is not to "engage in conduct involving dishonesty, fraud, deceit, or misrepresentation" and Rule 4-8.4(d) prohibits "conduct in connection with the practice of law which is prejudicial to the administration of justice. The commentary to Rule 4-8.4 provides a good-faith exception when a "lawyer may refuse to comply with an obligation imposed by law upon a good faith belief that no valid obligation exists." There is also a well-known saying that "Justice depends on whose ox is being gored."[4] Further discussion of Rule 4-8.4 and a 2015 Florida Supreme Court Referee's decision with respect thereto is discussed below.

In the 2003 Fifth District Court of Appeal case of *Bankfirst v. UBS Paine Webber, Inc*., 842 So. 2d 155 (Fla. 5th DCA 2003), which is further described below, the dissenting judge, C. Harris*,* concluded that where lawyers and financial consultants actively advise and assist a debtor to transfer assets with the intent to defeat legitimate creditor rights, a valid cause of action for civil conspiracy, and assessment of damages against the advisors would apply, while the other two judges concluded in the majority decision that no such cause of action would exist absent the elements further described below. Judge Harris's dissenting opinion indicated that the fraudulent transfer law is applied by a Court of Equity and that Section 726.108(1)(c)3 enables the court to apply "any other relief the circumstances may require...subject to applicable principles of equity" and noted that the Fourth District Court of Appeal in the 2001 opinion of *Hansard Construction Corporation v. Rite Aid of Florida, Inc.*, 783 So.2d 307 (Fla. 4th DCA 2004), held that a plaintiff may recover money damages against the transferor under the "any other relief" provision.[5]

The following excerpt is from the Kleinfeld Alpert article which notes and cites a number of cases that we discuss after the below quotation:

[4] Derived from the Book of Exodus and interpreted by Martin Luther at Diet of Worms in 1521.

[5] *See also Profeta v Lombardo,* 75 Ohio App. 3d 621 (1991).

Ethical Issues

Prior to the Florida Supreme Court's decision in *Freeman v. First Union National Bank*, 329 So. 2d 1272 (Fla. 2004), some commentators argued that it was unethical in some circumstances for an attorney to assist a client's property transfer which was subsequently found to be a fraudulent conveyance. The most prevalent arguments were, one, that attorneys had a duty as an "officer of the court" not to impair the collection of a court's money judgment, or two, that assisting a client's fraudulent conveyance constituted the assistance of "fraud." Both ethical positions are inconsistent with the Florida Supreme Court's interpretation of the FUFTA.

To begin with, the Florida Bar Model Rules of Conduct (the "Rules") provides in the preamble that, "A lawyer is a representative of clients, an officer of the legal system and a public citizen having special responsibility of the quality of justice." The concept of lawyer as "an officer of the court" suggests the close working relationship between judges and traditional courtroom practitioners. The phrase "an officer of the court" is relevant primarily to representation involving work in a courtroom. The Florida Supreme Court has explained that an attorney's role as "officer of the court" is to work with the court system, for example, by improving the Bar admissions process, serving on disciplinary committees, and representing indigents.[6] This Court has never used the term "officer of the court" to impose on attorneys additional duties that could create conflict with or diminish the attorney's ethical responsibilities to diligently advocate on his client's behalf.[7] Any other meaning would place the attorney in the role of being an ombudsman rather than a zealous advocate.[8]

It is well settled that because of the adversarial nature of litigation and the duty for attorneys to zealously represent their clients with total loyalty and confidentiality, a lawyer lawfully providing services to a client has no legal liability to any third party in

[6] *In re: Petition for Advisory Opinion Concerning Applicability of Chapter*, 316 So. 2d 45 (Fla. 1975)

[7] The Rules, 4-1.3

[8] Standard of care for an attorney-client relationship is a duty to exercise the degree of reasonable knowledge and skill that lawyers of ordinary ability and skill possess and exercise. *See Rowell v. Holt*, 850 So. 2d 474, 484 (Fla. 2003).

contract, tort or for a fiduciary duty because of a client's conduct.[9] More specifically, the general principle is that an attorney has no legal duty to a third party adversary of his client's interest, including a client's potential creditors.

Secondly, there is an important ethical distinction between assisting actual common law fraud and assisting a fraudulent conveyance. Under Rule 4-1.2(d), Scope of Representation, "A lawyer shall not counsel a client to engage, or assist a client, in conduct that the lawyer knows is criminal or fraudulent". (Rule 4-8.4(c) defines professional misconduct to include "engage[ing] in conduct involving dishonesty, fraud, deceit or misrepresentation"). Rules 4-1.2(d) and 4-8.4(c) are the only references in the Model Rules to conduct of the attorney or client which involve fraud. The term "fraud" or "fraudulent" is specifically defined by the Rules[10] as denoting "conduct having a purpose to deceive and not merely negligent misrepresentation or failure to apprise another of relevant information." This definition makes no reference to a fraudulent conveyance or fraudulent transfer as under the Uniform Fraudulent Transfer Act, Uniform Fraudulent Conveyance Act or similar statute. "Fraud" does not include conduct which, although characterized as "fraudulent" by statute or administrative rule, lacks an element of scienter,[11] deceit, intent to mislead, or knowing failure to correct misrepresentations which can be reasonably expected to induce detrimental reliance by another.

Florida's Supreme Court and appellate courts have clearly elucidated this distinction between the intentional tort of common law fraud and deceit, on one hand, and remedies under the FUFTA, on the other. By specifically rejecting the notion that the FUFTA creates an independent tort for damages, the Supreme Court in *Freeman* distinguished fraudulent transfers from the common law tort of fraud and deceit of which damage is an essential ingredient. The Court recognized that despite the FUFTA's archaic language including the word "fraud," the statute does nothing more than create a creditor remedy similar to replevin or other equitable remedies. Such equitable remedies are different than

---

[9] Limited exceptions have been curved out in probate on the theory of a fiduciary duty involving wills and trusts cases in relation to deemed or intended third party beneficiaries. *See also* footnote 14.

[10] Terminology (4-8.4(c))

[11] Requires that intent, a state of mind requiring knowledge, or *mens rea*, simultaneously occur with a bad act, or *actus reus*.

damages awarded to remedy the intentional tort of common law fraud and deceit which requires all of the elements of misrepresentation, reasonable detrimental reliance, and proximate cause as well as damages.

The Florida Supreme Court also differentiated fraudulent transfers from common law fraud in *Havoco of America, Ltd. v. Hill*.[12] In *Havoco*, the Court focused on exemption of a Florida homestead from remedies under the fraudulent asset conversion provisions of the Florida Statutes and the Uniform Fraudulent Transfer Act. The Court concluded that homestead property is protected from the FUFTA's equitable remedies except where funds were obtained through fraud or egregious conduct. In sum, the Court held that a fraudulent conveyance is not fraud and not egregious conduct.

As previously discussed, several recent Florida appellate court decisions contrasted tortious fraud and fraudulent conveyance. The Third District Court of Appeal has twice stated that a fraudulent transfer is not a tort, and therefore unrelated to the intentional tort of common law fraud. Though not addressing the issue directly, the Fifth District Court of Appeal, in its *BankFirst* decision, cited several federal appellate cases to support its holding, including the Ninth Circuit decision of *Elliott v. Glushon*,[13] which held that fraudulent transfers in the context of bankruptcy include a great variety of actions which are not common law fraud. Thus, the Florida Supreme Court and Florida appellate courts have made clear that a fraudulent transfer falls outside the definition of fraud, under the law of deceit, proscribed by Florida's ethical rules, and is not otherwise considered egregious conduct. *See also Burris v. Green*, 2016 WL 5844165 (M.D. Fla. 2016)(fraudulent transfer claim is not a "tort" for purposes of personal jurisdiction or a "tortious act" under Florida's long-arm statute); *In re Wiand Receivership Cases*, 2007 WL 963165 (M.D. Fla. 2007)(fraudulent transfer is not a tort for purposes of *in pari delicto*).

---

[12] 790 So. 2d 1018, 1028 (Fla. 2001).
[13] 390 F.2d 514 (9th Cir. 1967).

The American Debtor/Creditor justice system clearly provides, with few exceptions, that a debtor has complete and uninterrupted ownership, possession, and control of his or her assets until there has been a judgment and legally permitted action to attach the assets once a judgment has been received. The colonial states were settled in large part by those escaping debtor prisons in Europe in the 1600's and 1700's. For example, the State of Georgia was initially populated by penal prisoners from debtor's prisons under the auspices of James Oglethorpe to create a "debtors colony."[14]

While there are limited mechanisms under the law for prejudgment injunctions that enable creditors to "lock down" on a debtor's assets before a judgment has been levied upon, the statutes permitting this will rarely be used because of the requirements that exist for the exercise thereof.

Florida Statute, Chapter 76 provides creditors with attachment rights. Specifically, Section 76.01, Right of attachment, reads as follows:

> Right to attachment.—Any creditor may have an attachment at law against the goods and chattels, lands, and tenements of his or her debtor under the circumstances and in the manner hereinafter provided.

Section 76.03, Courts from which attachments shall issue, reads as follows:

> Courts from which attachments shall issue.—Attachments shall be issued by a judge of the court which has jurisdiction of the amount claimed by the creditor, but if the property to be attached is being actually removed from the state and the creditor is unable to obtain process from the proper court in time to prevent such removal, any judge may issue the writ, making it returnable to the proper court and immediately sending all papers in the action to the clerk of the court to which the writ is returnable.

[14] Ekirch, A. Roger (1987), Bound For America: The Transportation of British Convicts to the Colonies, 1718–1775, Oxford University Press.

The Third DCA case of *Cerna v. Swiss Bank Corp. (Overseas), S.A.*, 503 So.2d 1297 (Fla. 3rd DCA 1987), concluded that a creditor could not obtain a prejudgment order to seize assets on the basis that the debtor was "fraudulently disposing of ... property" which was titled under the name of a shill.[15]

It is noteworthy that the United States Justice Department can use 18 U.S.C § 1963[16] to enforce prejudgment injunctions against those who have committed fraudulent[17] criminal acts.[18] Pursuant to subsection (d) paragraph (2) of 18 U.S.C § 1963, the United States can apply for a temporary order when an information or indictment has not been filed yet, "if the United States demonstrates that there is probable cause to believe that the property with respect to which the order is sought would, in the event of conviction, be subject to forfeiture under this section." The United States may also apply 28 U.S.C. § 3001 to garnish wages or obtain assets prior to a judgment for any outstanding debts owed to the United States.

Many authors refer to the 1999 U.S. Supreme Court case of *Grupo Mexicano de Desarrollo S.A. v. Alliance Bond Fund, Inc.*, 527 U.S. 308 (1999), where Justice Scalia, on behalf of himself and four other members of the Supreme Court, decided that a federal Court of Equity does not have

---

[15] 503 So.2d at 1299 (explaining that the debtor was not fraudulently disposing of property that remained in her name, and stated that "In sum, while we hold that property purportedly owned by Cerna may not be properly attached prejudgment, we do not agree that debts allegedly owed to Cerna by someone else, such as the sums in her bank and stockbroker accounts, may be garnished until her own liability to the plaintiff has been established by judgment.")

[16] Criminal Penalties for a violation of the Racketeering Influenced and Corrupt Organizations statute, prohibited activities. *See* 18 U.S.C. § 1962.

[17] "Common-law meaning of 'fraud' required a misrepresentation or concealment of material fact. Thus, this Court cannot infer from the absence of a specific reference to materiality that Congress intended to drop that element from the fraud statutes and must presume that Congress intended to incorporate materiality unless the statutes otherwise dictate." *Neder v. United States*, 527 U.S. 1, 3 (stating that materiality is an element of a scheme or artifice to defraud under the Federal mail fraud, wire fraud and bank fraud statutes.); Specific-intent requires willfulness in committing a particular proscribed act.

[18] RICO's prohibited activities of a "pattern or practice" are a criminal act usually based on predicate mail fraud or wire fraud violations. A fraudulent criminal act against the United States is utilizing the United States Postal Service or any electronic or wire broadcasting communication service with an intent to devise a scheme or artifice to defraud. *See* 18 U.S.C. §§ 1341, 1343.

the power to authorize a creditor to attach the assets of a debtor before receiving a judgment, unless a federal or state statute applies which would explicitly allow a pre-judgment attachment order. Judge Scalia noted that Federal courts of equity are limited to those powers provided to the English Court of Chancery at the time that the United States became independent, meaning that because courts of equity in England in 1776 did not have the power to grant pre-judgment attachment orders, these will not be permitted now in the absence of statutory authority.

Justice Ginsberg, joined by Justices Stevens, Souter and Breyer, noted that the Court of Equity under The Judiciary Act of 1789 probably did not need to issue pre-judgment injunctions because things moved slower and it was probably more likely that a judgment creditor would be able to find and attach assets post-judgment in the 1700s than is now the case, noting that "increasingly sophisticated foreign-haven judgment proofing strategies, coupled with technology that permits the nearly instantaneous transfer of assets abroad, suggests that defendants may succeed in avoiding meritorious claims in ways unimaginable before the merger of law and equity."

This case has been cited in a number of other decisions and articles for the proposition that debtors have the right to remain in control of, and to decide what to do with their assets until a judgment is being enforced. As Judge Scalia wrote in the opinion, "The requirement that the creditor obtain a prior judgment is a fundamental protection in a debtor-creditor law."[19] Justice Scalia further stated that by allowing federal courts to issue such injunctions for creditors "could radically alter the balance between debtors' and creditors' rights and might induce creditors to engage in a race to the courthouse…which might prove financially fatal to the struggling debtor."

Kleinfeld and Alper say the following about this case in the article cited:

[19] *Id* at 330.

> The U.S. Supreme Court in *Grupo*, solidified a property owner's right to freely transfer his property prior to judgment subject to subsequent equitable remedies under fraudulent conveyance statutes. This case involved an action for money damages where the creditor sought a preliminary injunction in federal court to prevent a defendant from transferring its assets prior to judgment being entered. The majority opinion pointed out prerequisites for equitable remedies as well as the general availability of injunctive relief against asset transfers depend on common law principles of equity. The Supreme Court stated, "It was well established, however, that, as a general rule, a creditor's bill could be brought only by a creditor who had already obtained a judgment establishing the debt." The Court reiterated its understanding of the well-established general rule, "that a judgment establishing the debt was necessary before a Court of Equity would interfere with the debtor's use of his property."[20] In other words, under common law a creditor has no property interest in the assets of a debtor prior to the creditor obtaining a judgment, and before judgment, a debtor's property is freely alienable.
>
> The point is that all people, even potential debtors, have fundamental rights to protect and control their property. The transfer of freely alienable property is not unlawful and cannot be restrained by a creditor, absent obtaining remedies allowed under other statutory law such as bankruptcy, even if the transfer could subsequently be challenged under fraudulent transfer statutes.

In many instances, estate planning or asset protection involves converting non-exempt assets into exempt assets so as to take full advantage of available exemptions, i.e. homestead, retirement assets, annuities, life insurance, entireties property. Many bankruptcy decisions in Florida, particularly authored by Judge Paskay, expressly hold that "Congress intended to permit Debtors to take full advantage of the exemptions available under applicable law."[21]

---

[20] *Grupo,* 527 U.S. 308 at 1969 (1999)
[21] *In re Russell*, 1982 WL 19332 (Bankr. M.D. Fla. 1982)

For at least ten years, Judge Paskay repeatedly cited to the legislative history of Section 522 of the Bankruptcy Code and expressly indicating that it was not fraudulent to take full advantage of exemptions on the eve of bankruptcy. *Matter of Rowe*, 46 B.R. 34 (Bankr. M.D. Fla. 1984*); In re Decker*, 105 B.R. 79 (Bankr. M.D. Fla. 1989*); In re Horath*, 116 B.R. 835 (Bankr. M.D. Fla. 1990*); In re Levine*, 139 B.R. 551 (Bankr. M.D. Fla. 1992). The oft-cited legislative history quote reads as follows:

> As under current law, the debtor will be permitted to convert nonexempt property into exempt property before filing a bankruptcy petition…the practice is not fraudulent as to creditors, and permits the debtor to make full use of the exemptions to which he is entitled. H.R. No. 595, 95th Cong., 1st Sess., 361 (1977), U.S. Code Cong. & Admin. News 1978, pp. 5787, 6317.

In *Decker*, Judge Paskay cited to the Fifth Circuit's decision in *Matter of Reed*, 700 F. 2d 986 (5th Cir. 1983).and stated:

> "The fact that the net effect of these transactions did, in fact, put under the exemption substantial assets is of no consequence. The Debtor merely attempted to do that which the function of exemptions was meant to do, and that is to put the property beyond the reach of creditors."

In *Horath*, Judge Paskay cited to numerous cases, including the Eighth Circuit's decision in *Norwest Bank Nebraska, N.A., v. Tveten*, 848 F. 2d 871 (8th Cir. 1988), and drew a distinction between an objection to exemptions and an objection to discharge. Judge Paskay further stated that:

> "This Court is unaware of any provision in the Bankruptcy Code which condemns the conversion of non-exempt property into exempt property

> and which would operate as a forfeiture of right to claim an exemption otherwise available to Debtors."

In *Levine*, Judge Paskay expressly held that the legislative history "leaves no doubt" that the conversion of non-exempt property into exempt property is "not per se fraudulent, and it permits a debtor to make full use of the exemptions to which the debtor is entitled." Judge Paskay further stated:

> "This Court's opinion should not be construed to be an approval of such 'pre-bankruptcy planning' or conversion of nonexempt assets into exempt assets, which might in some cases, be grounds to bar a debtor's discharge."

Then, Judge Paskay shifted his thinking in *In re Schwarb*, 150 B.R. 470 (Bankr. M.D. Fla. 1992), wherein he receded in part from *Levine* without mentioning his other published decisions on the issue. "After further research and consideration" of the oft-cited legislative history, Judge Paskay discounted the above quote and held that an exemption could be disallowed if property was converted "for the specific purpose of placing the asset out of the reach of creditors."

Perhaps Judge Paskay was clairvoyant as the Florida Legislature enacted Florida Statutes §§222.29 and 222.30 in 1993 specifically making a conversion to exempt with the specific intent to hinder, delay or defraud a creditor a "fraudulent asset conversion." *See Havoco of America, Ltd. v. Hill*, 197 F.3d 1135 (11th Cir. 1999).

Notwithstanding his decision in *Schwarb* and the change in chapter 222, Judge Paskay continued to cite to the legislative history and held yet again that conversion of non-exempt property into exempt is permitted. In *In re Snape*, 166 B.R. 184 (Bankr. M.D. Fla. 1994), Judge Paskay concluded that the evidence did not support a disallowance of the claim exemption where the debtors had embarked on “an elaborate strategy” to avoid a creditor because the debtors “believed” that the claim had been satisfactorily resolved.

The debtor-friendly rule pronounced by Judge Paskay many times and set forth by the Eighth Circuit in *Tveten* has continued to be cited in more recent cases. Twenty years later, the Tenth Circuit in *In re Warren*, 512 F. 3d 1241 (10th Cir. 2008), noted that the “very purpose of having exemptions is to permit a debtor to retain certain [assets]…without fear of creditors taking them.” The Tenth Circuit further noted that bankruptcy lawyers can face a dilemma in advising clients whether to acquire exempt assets stating:

> As one commentator observed, “[T]he same conduct can be malpractice not to advise in one jurisdiction, but voidable and grounds for denial of discharge and possibly for disbarment in another…”[22]

> At the end of the day, “[T]he cases…are peculiarly fact specific, and the activity in each situation must be viewed individually.”[23]

As recently as last year, at least one bankruptcy court expressly held that “as courts have held in connection with exemption planning, simply doing what the law allows you to do is not, in and of itself, bad faith.” *In re Portell*, 557 B.R. 161, 170 (Bankr. W.D. Mo. 2016).

In *In re Arends*, 506 B.R. 516, 523 (Bankr. N.D. Iowa 2014), the court held:

> “It is well settled that the mere conversion of non-exempt assets to exempt assets is not in itself fraudulent.”

[22] John D. Ayer, *How to Think About Bankruptcy Ethics*, 60 Am. Bankr. L.J. 355, 374 (1986).
[23] *Warren*, 512 F. 3d at 1250.

The Iowa Bankruptcy Court went on to state the colloquial phrase "pigs get fat; hogs get slaughtered."

Against this backdrop of legislative history and case law, query whether a lawyer could or should be attacked for assisting a client with asset protection through a conversion of non-exempt assets to exempt assets.

ADVISOR LIABILITY FOR FRAUDULENT TRANSFERS

Freeman v. First Union Nat'l Bank

In 2004, The Florida Supreme Court held that the Florida Uniform Fraudulent Transfers Act (FUFTA) does not give a cause of action against third parties who actively aid and abet a fraudulent transfer, notwithstanding the "catch all" phrase in the statute which permits a court to award "any other relief the circumstances may require." [24] In *Freeman*, victims of a $90,000,000 international Ponzi scheme sued First Union National Bank for "aiding and abetting" Unique Gems International Corp., which allegedly defrauded approximately 16,000 people who were led to pay money as a "deposit" in connection with the assembly of necklaces. The Court concluded that "FUFTA was not intended to serve as a vehicle by which a creditor may bring a suit against a non-transferee party (like First Union in this case) for monetary damages arising from the non-transferee party's alleged aiding-abetting of a fraudulent money transfer."[25]

Bankfirst v. UBS Paine Webber, Inc.

The Florida Supreme Court in the *Freeman* case described above made mention of the Florida 5th District Court of Appeals case of *Bankfirst v. UBS Paine Webber, Inc.*, 842 So.2d 155, 156

---

[24] *Freeman v. First Union Nat'l Bank*, 865 So. 2d 1272, 1277 (Fla. 2004).
[25] *Id.*

(Fla. 5th DCA 2003), where two of the three judges on the panel held that there is no cause of action for civil conspiracy where a professional actively assists a client in making a "fraudulent transfer." In that case, attorney Jonathan Alper, who co-authored the Kleinfeld Alper article that is extensively quoted herein, actively assisted a client who had a judgment against him in funding a Bahamian Asset Protection Trust after being introduced to this lawyer by PaineWebber. (Check out Mr. Alper's excellent web-site at alperlaw.com.) Mr. Alper and PaineWebber were sued by Bankfirst, and reportedly the bank had to pay their attorney's fees after losing the appeal. The majority stated that "neither Section 222.30 nor Chapter 726 of the Florida Statutes creates a cause of action against a party who allegedly assists a debtor in a fraudulent conversion or transfer of property, where the person does not come into possession of the property." In the dissent, however, Judge Harris stated that "[w]hile I agree that extreme caution should be taken before holding an attorney liable in civil conspiracy for a wrong committed by a client, still if a conspiracy is properly proved and the lawyer is shown to have willingly and knowingly participated in it, there is no immunity."[26]

Does Judge Harris' dissent and potential future "bad facts cases" leave the door open for activist courts to eventually find a way to punish lawyers who actively assist debtors in the avoidance of creditors? The *Harwell* bankruptcy case in Tampa should certainly give practitioners some pause.

In *In re Harwell*, 8:08-mp-0002-MGW (Doc. 73), aff'd 414 B.R. 770 (M.D. Fla. 2009), rev'd 628 F.2d 1312 (11th Cir. 2010), a well-respected Sarasota litigation lawyer permitted a debtor to have proceeds from the sale of a business pass through the lawyer's trust account, and from there to several different individuals in an apparent attempt to avoid a judgment creditor's active attempts to collect on the judgment. On summary judgment Bankruptcy Judge Michael Williamson found that there was no cause of action for aiding and abetting a fraudulent transfer under the above-referenced Freeman case, assuming that the lawyer was not considered to be an "initial transferee" under Bankruptcy Code Section 550(a)(1), which empowers a trustee in bankruptcy to recover property from "the initial transferee" of a fraudulent transfer under certain circumstances. District Judge James Moody affirmed on appeal. *In re Harwell*, 414 B.R. 770 (M.D. Fla. 2009). Hutton was later determined to be liable as an initial transferee by the

[26] *Id.*

bankruptcy court in a subsequent opinion, after remand on appeal based upon an updated definition of "initial transferee" that was provided by the Eleventh Circuit. *In re Harwell*, 2011 WL 4566443 (Bankr. M.D. Fla. 2011). There was no further discussion of whether the Freeman case would apply, which was presumably because Hutton was found to owe the money to the trustee under the above-referenced Bankruptcy Code provision, so Florida law was no longer relevant. Judge Moody's August 31, 2009 opinion also discussed whether Florida law recognizes a cause of action for civil conspiracy to commit a fraudulent transfer, and noted that one element of a civil conspiracy is "an unlawful act is that the conspirator must "do an unlawful act or ... do a lawful act by unlawful means", in addition to (1) the act being overt, (2) the act being in the pursuance of the conspiracy, and (3) the act causing damage to the plaintiff.[27]

Judge Moody noted that Judge Harris' dissent in the *BankFirst* case indicated that "there should be no policy reason to immunize someone who knowingly and willingly makes it possible for the transferor to commit a fraud."[28]

Despite affirming the summary judgment in the attorney's favor, Judge Moody's "shot over the bow" to "asset preservation" lawyers[29] which reads as follows:

> "Like the Florida Supreme Court, this Court is reluctant to say there is no set of facts under which a party who assists a fraud might be liable under a civil conspiracy theory. For example, had Hutton, the lawyer in this case, assisted Debtor in falsely answering the collection interrogatories, or had he violated the Colorado state court turnover order requiring the debtor to turn over settlement proceeds to the creditor, such an act might well be considered in furtherance of a conspiracy to commit fraud."[30]
>
> In saying that, this Court does not hold that such an action for civil conspiracy exists for aiding a fraudulent transfer. It is not required to reach that issue since there were no

[27] *Harwell*, 414 B.R. at 786
[28] *BankFirst*, 842 So. 2d at 157
[29] Jimmy Buffet song Pirate Looks at 40 lyrics, "Mother, mother ocean, after all the years I've found, my occupational hazard being my occupation's just not around, I feel like I've drowned, gonna head uptown, I feel like I've drowned, gonna head uptown."; *See also* footnote 2.
[30] *Harwell*, 414 B.R. at 787

> "wrongs" committed by the lawyer in this case. This issue is best left for another day, but, at least, a warning bell has sounded for parties involved in "asset preservation." [30]

If and when a lawyer actively assists a client in making a "fraudulent" transfer, and also assists that client in misleading a creditor in a way that causes violation of law, such as under the Federal Wire Fraud Act where untruthful information is communicated by mail or internet,[31] then the Civil Conspiracy Law may be found to apply, and the advisor or advisors may find themselves to be jointly and severally liable for the value of assets transferred and damages, including attorneys' fees and costs.

HARWELL - LAWYERS AS TARGETS IF THEY HAVE RECEIVED ACTUAL OR CONSTRUCTIVE RECEIPT OF A BANKRUPTCY DEBTOR'S ASSETS BY COOPERATING IN A FRAUDULENT TRANSFER OR SIMILAR CONDUCT.

The Eleventh Circuit Court of Appeals decision issued in *Harwell* reversed the lower court's finding that the attorney was an "initial transferee" and noting that the lawyer in this case may have gone beyond being an agent or conduit for the client under Bankruptcy Code Section 550(a)(1), and concluded that the "party must have acted in 'good faith' with respect to the relevant transaction in order to be spared the effects of Section 550(a)(1) by establishing that (1) they did not have control over the assets received i.e., that they merely served as a conduit for the assets that were under the actual control of the debtor-transferor *and* (2) that they acted in good faith and as an innocent participant in the fraudulent transfer.[32]

Footnote 10 of the opinion indicates that "We now explicitly hold that good faith is a requirement under this Circuit's mere conduit or control test."

The Court further stated that "in the vast majority of cases, a client's settlement funds transferred in and out of a lawyer's trust account will be just like bank transfers, and lawyers as intermediaries will be entitled to mere conduit status because they lack control over the funds. Mere conduits, such as lawyers and banks, do not have an affirmative duty to investigate the

[31] *See* 18 U.S.C. §§ 1341, 1343

[32] *See also Harwell*, 628 F .3d at 1323.

underlying actions or intentions of the transferor. However, under the particular circumstances of this case and given the bankruptcy court's assumptions about Hutton's major role in the fraudulent transfer of these funds at issue, Hutton is not entitled to summary judgment in his favor based on the mere conduit or control test.[33]

After this Eleventh Circuit opinion, Bankruptcy Judge Michael Williamson found that the lawyer was subject to liability under Section 550(a)(1), and there was no further mention of aiding and abetting or civil conspiracy, given that the Bankruptcy Code liability was apparently sufficient for the trustee's purposes. The attorney's liability in *Harwell* was linked to his actual possession of the funds. Counsel should think long and hard before taking clients funds into their trust account.

Section 550(a) provides that[34]:

> Except as otherwise provided in this section, to the extent that a transfer is avoided under section 544, 545, 547, 548, 549, 553(b), or 724(a) of this title, the trustee may recover, for the benefit of the estate, the property transferred, or, if the court so orders, the value of such property, from--
>
> (1) the initial transferee of such transfer or the entity for whose benefit such transfer was made; or
>
> (2) any immediate or mediate transferee of such initial transferee

It is noteworthy that the 11th Circuit's opinion made mention of the following:

> "The bankruptcy court also addressed whether Trustee Martinez had cognizable claims against Hutton, under Florida law, for (1) aiding and abetting a fraudulent transfer or (2) civil conspiracy to effect a fraudulent transfer. Citing *Freeman v. First Union National Bank,* 865 So.2d 1272, 1277 (Fla.2004), the bankruptcy

---

[33] *Id*.
[34] 11 U.S.C. § 550

> court determined that the Florida Uniform Fraudulent Transfer Act did not allow Trustee Martinez to assert a cause of action against Hutton for either aiding and abetting or civil conspiracy if Hutton was not an "initial transferee" of the money within the meaning of the Bankruptcy Code. The district court affirmed. *Martinez v. Hutton (In re Harwell),* 414 B.R. 770, (M.D.Fla. 2009)."

This language seems to imply that being an "initial transferee" under the Bankruptcy Code could cause liability for aiding and abetting or civil conspiracy. Would this be the case needed outside of bankruptcy?

Kleinfeld and Alper describe the above two cases and other Florida cases as follows:

Freeman v. First Union Nat'l Bank

In *Freeman*, the State of Florida filed a lawsuit in the U.S. District Court for the Southern District of Florida alleging that a company called Unique Gems ran a "Ponzi scheme." Unique Gems maintained bank accounts at First Union National Bank. In the course of litigation, Lewis B. Freeman was appointed receiver over the company. Plaintiff receiver's second amended complaint claimed that First Union National Bank was liable to the receiver for money damages on the grounds that it aided and abetted a fraudulent transfer by allowing Unique Gems to wire transfer money to Liechtenstein even after the state filed the lawsuit. The complaint alleged that although First Union informed Unique Gems in a letter dated February 21, 1997, that it would close its account in 10 days, the bank did not close the account. Subsequently, a court-ordered injunction was entered on March 5, 1997, freezing the Unique Gems account. Presumably, while the motion to freeze its assets was pending, Unique Gems transferred a total of $6.6 million from its First Union account to Liechtenstein. Even after the injunction was entered, and after First Union told Unique Gems that its account would be closed 30 days thereafter, First Union still allowed Unique Gems to wire transfer an additional $2 million to Liechtenstein. Finally, First Union closed the Unique Gems account on July 24, 1997. These facts represent an exceptional and excellent context to analyze the interrelationship between Florida's fraudulent transfer statutes and the common law tort of aiding and abetting by a third party nontransferee.

The district court dismissed the receiver's aiding and abetting claim against First Union with prejudice because it did not state a cause of action under Florida law. The district court held that the FUFTA allows creditors only to set aside fraudulent transfers. The court considered the FUFTA to be similar to the fraudulent transfer provisions of the Bankruptcy Code[34] and held that neither provides for aider and abettor liability. The district court noted that while the receiver cited cases recognizing aiding and abetting as common law fraud, or another cause of action, none of the cases related to the Uniform Fraudulent Transfer Act.

On appeal, the 11th Circuit Court of Appeals noted that the FUFTA remedies for fraudulent conveyance are different and possibly broader than those of the Bankruptcy Code. The appeals court said that, "While the Bankruptcy Code limits remedies to the recovery of transferred property or its value . . . the FUFTA clearly provides additionally for 'any other relief the circumstances may require.'" Thus, the issue before the 11th Circuit was whether the FUFTA remedies, like bankruptcy remedies, include only equitable powers to cancel a fraudulent transfer, or whether the FUFTA's "catch-all" phrase of "any other relief the circumstances may require" gives rise to common law theories for damages against third party nontransferees. The 11th Circuit felt it could not predict how the Florida Supreme Court would rule on the issue.[35] Specifically, the 11th Circuit asked the Florida Supreme Court, "Under Florida law is there a cause of action for aiding and abetting a fraudulent transfer when the alleged aider-abettor is not a transferee?" [36]

The Florida Supreme Court began its own analysis by reviewing the meaning of the wording "any other relief the circumstances may require" in F.S. §726.108(1)(c)(3). The court concluded that, "We believe that the Legislature intended it to facilitate the use of other remedies provided in the statute, rather than creating new and independent causes of action such as aider-abettor liability . . . ."[37] After further considering legislative intent,

---

[35] The appeals Court believed there was conflicting guidance from Florida's intermediate appellate courts on the nature of Florida's Uniform Fraudulent Transfer Act, its remedies, and its relationship to the Bankruptcy Code and therefore it certified this question to the Florida Supreme Court.
[36] *Freeman*, 329 F. 3d at 1234.
[37] *Id*. at 1276

the Supreme Court stated, "There is simply no language in the FUFTA that suggests the creation of a distinct cause of action for aiding-abetting claims against nontransferees. Rather, it appears that the FUFTA was intended to codify an existing but imprecise system whereby transfers that were intended to defraud creditors were to be set aside."[38] The court stated, "We simply can see no language in FUFTA that suggests intent to create an independent tort for damages."[39] The Supreme Court explained that "[t]o adopt the appellants' position in this case would be to expand the FUFTA beyond its facial application and in a manner that is outside the purpose and plain language of the statute. Consistent with this analysis we conclude that the FUFTA was not intended to serve as a vehicle by which a creditor may bring a suit against a nontransferee party (like First Union in this case) for monetary damages arising from the nontransferee party's alleged aiding and abetting of a fraudulent money transfer."[40] In *Freeman*, the Florida Supreme Court strictly interpreted the Florida Uniform Fraudulent Transfer Act and circumscribed the statute's remedies. The Supreme Court's unanimous decision is a remarkably clear and unequivocal rejection of the plaintiff/receiver/appellant's position.

The court's decision in *Freeman* is in keeping with a series of recent Florida appellate decisions concerning fraudulent conveyance law. In *Yusem v. South Fla. Water Mgmt. Dist.*, 770 So. 2d 746 (Fla. 3d DCA 2000), the Fourth District Court of Appeal reviewed an alleged fraudulent transfer of funds to an offshore account. The holding provides a clear definition of a fraudulent conveyance action. The court stated, "A fraudulent conveyance action is simply another creditor's remedy."[41] The court proceeded to define the nature of this remedy as "either an action by a creditor against a transferee directed against a particular transaction, which, if declared fraudulent, is set aside thus leaving the creditor free to pursue the asset, or it is an action against a transferee who has received an asset by means of a fraudulent conveyance and should be required to either return the asset or pay for the asset (by way of a judgment and execution)."[42] The Fourth District

[38] The Court cited its recent decision in *Friedman v. Heart Institute of Port St. Lucie, Inc.*, 863 So. 2d 189 (Fla. 2003) to illustrate the FUFTA's narrow focus. *Id*. at 1277.
[39] *Id*. at 1277
[40] *Id*.
[41] *Yusem*, 770 So. 2d at 749
[42] *Id*.

Court of Appeal emphasized that a fraudulent conveyance action is not an action against the debtor for failure to pay an amount owing from a prior judgment and does not warrant an additional judgment against the same debtor because of the fraudulent transfer. A fraudulent conveyance action is not a lawsuit against a transferor/debtor, but it is an action against the property or the transferee holding the property.

In *Beta Real Corporation, etc. v. Lawrence Graham*, 839 So. 2d 890 (Fla. 3d DCA 2003), the Third District Court of Appeal reviewed a situation where a partner in a British law firm allegedly stole $9 million, of which $1.4 million wound up in a Florida bank in the name of a BVI corporation and $675,000 was spent acquiring a Florida condominium. The plaintiff's only argument for in personam jurisdiction in Florida was that the defendant had committed a tortious act, specifically a fraudulent transfer, within this state. The appellate court held that a fraudulent conveyance is not a tortious act, and therefore not a basis for jurisdiction. However, the court did leave open further proceedings, including assertions of in rem or quasi in rem jurisdiction, by imposing a constructive trust, equitable lien, or similar remedy even though the damages could not exceed the amounts which have been traced to the theft and thus recoverable in rem or quasi in rem.

In *BankFirst v. UBS Paine Webber, Inc.*, 842 So. 2d 155 (Fla. 5th DCA 2003), the Fifth District Court of Appeal reviewed an asset protection plan where Bankfirst sued a debtor's lawyers and financial advisers for damages on the theory of common law civil conspiracy to make a fraudulent conveyance. The Fifth District, in what is probably one of its most concise decisions, upheld the trial court's dismissal of Bankfirst's civil conspiracy action based on the "conclusion that neither §222.30 nor chapter 726, Florida Statutes, creates a cause of action against the party who allegedly assists a debtor in a fraudulent conversion or transfer of property, where the person does not come into possession of the property."[43] Interestingly, the legal basis for the relatively lengthy dissenting opinion in that case is now completely refuted by *Freeman*.

---

[43] *Id*.

The Third District Court of Appeal, in *Danzas Taiwan, Ltd. v. Freeman*, 868 So.2d 537 (Fla. 3rd DCA 2004), again reviewed the argument that a fraudulent transfer was a tortious act that gave rise to personal jurisdiction within the State of Florida and reviewed an allegation of conspiracy. There was no allegation that the alleged tortfeasor, Danzas Taiwan, received fraudulently conveyed assets, only that it was paid fees for services rendered to facilitate the physical transfer of assets. The appellate court, citing the decisions of both *Bankfirst* and *Beta Real*, held that there could be no jurisdiction over Danzas Taiwan for commission of a tortious act in Florida "because there is no cause of action against Danzas Taiwan for conspiracy to engage in fraudulent transfers."[44] Thus, Freeman and its predecessors in Florida's appellate courts unequivocally and unanimously define an action under Florida's Uniform Fraudulent Transfer Act as a creditor's equitable remedy, and they further agree this statute gives creditors no cause of action in tort against nontransferees for aiding and abetting or civil conspiracy.

The Client's Right to Convey Assets

The Florida courts' characterization of fraudulent transfers as reversible acts, but not tortious acts, is important for the protection of a person's assets from creditor attack. Otherwise, it would be difficult and risky for people to design their business ownership and to arrange personal assets defensively if any asset transfer later cancelled as a violation of the FUFTA exposed the transferor and their professional advisors to additional civil damages based on theories of tort liability. Moreover, according to both the Florida Constitution and the U.S. Supreme Court, people have a basic right to both protect and freely transfer their property. The Florida Constitution refers specifically to the protection of citizens' property. Art. I, §2, Basic Rights, provides that "[a]ll natural persons, female and male alike, are equal before the law and have inalienable rights, among which are . . . to acquire, possess and protect property." It is clear that constitutional rights are accorded broad interpretation. While there are yet no cases which have asserted the constitutional right to protect property against creditor legal attack, this issue, no doubt, will arise and be examined by the courts.

[44] *Id*.

The case of *In re Harwell*[45] mentioned above makes clear that lawyers who possess funds and actively assist debtors in making fraudulent transfers to avoid creditors will have liability exposure if the debtor ends up in bankruptcy.

Gosman and Rosen–Exposure of lawyers for allegedly participating in fraud upon creditors, malpractice in failing to properly advise a debtor, or unjust enrichment.

In the below discussed cases of Gosman and Rosen bankruptcy, trustees pursued lawyers for acts that included (in one case or the other) allegedly conspiring with clients to mislead creditors, over charging for services not needed or called for (like $41,000 for an offshore trust when the court indicated that the client would have been better served by buying a larger homestead than placing assets offshore), or when the debtor lost assets to the creditor that might have been saved if the lawyer had done a better job at asset protection. It is ironic that a creditor who is able to seize assets that would have otherwise been unavailable may be able to "double dip" by stepping into the debtors's shoes, via a bankruptcy trustee, and pursuing a malpractice claim against the lawyer, with the active assistance of the ex client, who may have turned against the lawyer and assigned all rights to malpractice suite recovery as part of the settlement with the creditor. More discussion of these 2 cases now follows:

Abraham D. Gosman v. Peabody & Arnold, LLP and Joel Reinstein, P.A

In the 1999 Bankruptcy Court case of *Abraham D. Gosman v. Peabody & Arnold, LLP and Joel Reinstein, P.A.*, 382 B.R. 826 (Bankr. S.D. Fla. Dec. 13, 2007), the Bankruptcy Trustee brought claims against the law firm that had represented Mr. Gosman to recover damages on behalf of the bankruptcy estate for having cooperated and provided guidance for what the Bankruptcy Court had found to be fraudulent transfers under the guise of compensating Mrs. Gosman for alleged breaches of a pre-existing Prenuptial Agreement that was amended in conjunction with her receipt of assets in what the Court found to be a ruse for the purpose of avoiding creditors. The Court found that the doctrine of *in pari delicto* applied to prevent the trustee from having any viable cause of action against the law firm where the previous pleadings of the trustee have

[45] *In re Harwell*, 2011 WL 456643, *8 (Bankr. M.D. Fla. Sept. 30. 2011)

stated that Mr. Gosman's actions were intentional, and that the law firm was merely negligent in its representation.

> The opinion included the following:
>
> Furthermore, "[e]ven if the parties did not participate in the *same* wrongdoing, Florida also follows a general principle that no one shall be permitted to profit by his own fraud, or take advantage of his own wrong, or found any claim upon his own iniquity, or profit by his own crime." *May,* 2007 WL 2120269, at *4 (emphasis in original). In determining whether *in pari delicto* applies, "a court first determines whether the plaintiff's *13 guilt is far less in degree than defendant's, so as to make the doctrine inapplicable. If plaintiff's guilt is not far less, the court inquires if applying the doctrine would be contrary to public policy." *Id.* (Quoting *Turner*, 704 So. 2d at 750).
>
> Here, the Trustee alleges in its Second Amended Complaint that the Debtor, Mr. Gosman, was found to have acted with actual intent to defraud his creditors when he transferred assets to Mrs. Gosman. Therefore, Mr. Gosman's fraud appears on the face of the complaint. Because the Trustee stands in the shoes of the Debtor, I must determine whether this fraud would bar a claim by the Debtor against Peabody for negligence.
>
> In determining whether the doctrine of *in pari delicto* applies under Florida law, I first determine whether the Debtor's guilt is far less in degree than Peabody's, based on the allegations in the Second Amended Complaint. According to the allegations, the Debtor acted with actual intent to defraud while Peabody was only negligent, and therefore I find that the Debtor's guilt is not far less than Peabody's. Second, I find no reason why applying the doctrine of *in pari delicto* in this case would be contrary to public policy.
>
> Based on the allegations in the Second Amended Complaint, the Debtor's guilt is clearly at least as great as Peabody's, and therefore this can be resolved on a motion to dismiss.

The Court noted that the Trustee stands in the shoes of the debtor, and that any affirmative defenses that could be asserted against the debtor may also be asserted against the Trustee.

In the 2012 Bankruptcy Court cases captioned *In re Akram Niroomand, Debtor, Alan L. Goldberg, Plaintiff v. Howard D. Rosen, Donlevy-Rosen & Rosen, P.A.*,[46] the trustee in bankruptcy filed an action against the law firm that represented a debtor and had established an offshore asset protection trust that was apparently funded during the time that a creditor's claim was well developed and expected to cause possible insolvency.

The trustee sued for malpractice, and unjust enrichment, claiming that the law firm should not have charged $47,000 to establish an offshore trust and to provide other advice and services when the debtor was insolvent. While the debtor testified that she was insolvent at the time of the transfer of assets to the offshore trust, she had executed an Affidavit of Solvency, and had apparently assured the law firm that she was solvent.

The case against the lawyer was dismissed, based upon the Bankruptcy Court's conclusion that there was no evidence of legal malpractice or unjust enrichment, and that there was credible evidence to support a finding that the debtor was solvent at the time she made the transfer. The decision of the Bankruptcy Court was appealed and affirmed by both the District Court and the Eleventh Circuit Court of Appeals (493 Fed.Appx. 11).

Much has been written about this case, with commentators noting the importance of making sure that clients are solvent when they enter into offshore trust or associated planning.

One author of this paper discussed this case with Mr. Rosen, who confirmed that it should not have made a difference as to result if the court had found that the debtor was insolvent at the time that she funded the offshore trust. If the court had determined that she was insolvent then the authors believe that it would have had to find that the Florida case law described above would not make the lawyer responsible to creditors as the result of actively assisting and advising with respect to what is defined as a "fraudulent transfer" under Florida Statute Section 726, absent other facts that were apparently not existent in this case. No law was apparently broken, and no creditor was apparently misled by the conduct of the debtor and her legal counsel. The offshore trust protected the assets conveyed to it until eventually used to purchase a

[46] 2013 Bankr. LEXIS 383, *6-10 (Bankr. S.D. Fla. Jan. 30, 2013)

homestead. Mr. Rosen also pointed out that the trust had been dissolved long before the bankruptcy proceeding was commenced.

Naples attorney and offshore trust expert, Jonathan Gopman, has written the following with respect to this case.

> *Niroomand* illustrates several important points that should be considered as part of the asset protection planning process. The following are also tips to live by when counseling clients on asset protection strategies.
>
> First, timing is a critical aspect of effective asset protection planning. Given the existence of a claim, the creation and funding of an offshore trust was not appropriate. Clients should plan only at appropriate times and under appropriate circumstances and attorneys should only assist clients under such conditions. Many people seek advice about wealth protection strategies because they are involved or concerned that they are about to become involved in serious litigation. This may be the wrong time to plan or valuable opportunities may be foreclosed without raising serious fraudulent transfer issues.
>
> As a general rule, if assisting a client with a particular strategy raises an issue as to a fraudulent transfer do not proceed or proceed with a great caution. Bad things can happen to good people if planning is done under inappropriate circumstances. This does not mean that we cannot ethically assist clients who are involved in litigation (or concerned that litigation is imminent). However, it does mean exercise discretion. Contrary to Rosen's stated practice, *Grupo Mexicano* should not be interpreted as providing an attorney and his or her client the ability to engage in aggressive planning so long as its completed before judgment.
>
> Second, as a result of the jurisdiction where a client resides or may want to reside, the manner in which a client owns certain property interests (for example, homestead or tenancy by the entirety), it may be possible to achieve significant wealth protection for a client involved in litigation or concerned that litigation is imminent. In *Niroomand*, it was only after tens of thousands of dollars were wasted on an offshore trust structure that D eventually followed advice to pay down her mortgage – which ultimately may have

been a much safer strategy for D and a far less expansive. Nonetheless, D would have also most likely found it necessary to avoid finding herself in a bankruptcy proceeding for many years following the payment of the mortgages on her primary residence.

Third, carefully consider the consequences of using a "Jones Clause" in an asset protection trust. If the clause is substantially similar to the one used in the Trust, that is, it creates substantial hurdles for a creditor, it probably will not work to protect the client (or the attorney).

Fourth, following the creation and funding of a foreign trust or any other wealth protection strategy, filing bankruptcy should be viewed as an option of last resort notwithstanding that the planning may have been completed under appropriate circumstances. This is not to say that a properly implemented foreign trust structure or other wealth protection strategy cannot survive a challenge in a bankruptcy proceeding. Nonetheless, it is clear from a few bad fact cases that the present environment in the Bankruptcy Court system is hostile toward certain wealth protection strategies. Unfortunately, bankruptcy judges typically have the pleasure of reviewing bad fact cases involving foreign trusts. Experience demonstrates that judges in bad fact cases usually reach the proper result; however, the legal analysis is faulty. This faulty analysis has significantly damaged public perception regarding legitimate wealth protection planning. It is clear, however, that §548(e)(1) of the Bankruptcy Code (that is, the ten (10) year fraudulent transfer rule that applies to self-settled or classic asset protection trusts) mandates that bankruptcy courts respect the validity of such trust structures. Gone are the days when bankruptcy judges could wrongfully dismiss such trust structures as shams. Instead, the court must now engage in an analysis of whether a debtor's transfer of assets to such a trust constituted a fraudulent transfer. *See e.g.*, *Battley v. Mortensen, et al., (In re Mortensen),* 2011 WL 5025249 (Bankr. D. Alaska). For an excellent discussion of Mortensen see Shaftel, "Court Finds Fraudulent Transfer to Alaska Asset Protection Trust," 39 EP 15 (April 2012); Sulivan, Merric, Gillen, Bove & Nenno, "Fraudulent Transfer Claims," 150 Trusts & Estates 43 (Dec. 2011); and "Gopman & Rubin: Further Analysis on *In re Mortensen*," LISI Asset Protection Planning Newsletter #187 (November 7, 2011) at http://www.leimbergservices.com. See also, "Oshins & Keebler on Mortensen: No, the Sky Isn't Falling for DAPTs!," LISI Asset Protection Planning

Newsletter #186 (October 31, 2011) at http://www.leimbergservices.com and "Adkisson & Riser on Mortensen: Alaska Asset Protection Trust Fails To Protect Future Assets in Bankruptcy under New Section 548(e) Against Future Creditors," LISI Asset Protection Planning Newsletter #185 (October 20, 2011) at http://www.leimbergservices.com. The importance of obtaining an affidavit of solvency should not be ignored in this context. If a debtor's financial situation and affidavit is such that a transfer would not render the debtor insolvent, it would seem difficult for a creditor to argue that a debtor possesses the *actual* intent to hinder, delay or defraud such creditor from collecting on its judgment.

Fifth, reliance on *Grupo Mexicano*, for the proposition that a creditor has no pre-judgment remedies seems misplaced. Clearly, a creditor does have pre-judgment rights and can exercise such rights to a client's detriment. These rights should be disclosed to a client prior to assisting a client with making any transfers. Additionally, the issue of civil contempt should be discussed in these situations emphasizing that a judge may order incarceration in certain circumstances. It is important to advise a client in the context of using a foreign trust that it is likely that the client will remain in the United States within the jurisdiction of a court here.

It is just as important, however, to recognize that honest people seek legitimate wealth protection by using foreign trusts that are created and funded under appropriate circumstances. When properly structured and established under appropriate circumstances, foreign trusts are one of the most (if not the most) effective wealth protection strategies available. It is also important to recognize that the law permits individuals, businesses and other organizations to plan to protect assets and income from the claims of future unforeseen creditors. It is equally important to recognize that lawyers have a duty to zealously represent their clients, including lawyers who practice in the estate planning area. Zealous representation mandates that practitioners discuss all available planning wealth protection strategies and convey sufficient accurate information regarding such strategies so clients can make informed decisions.

Finally, collection of due diligence should never be viewed primarily as a method of impeaching a client's testimony as addressed by the court. Properly collecting due diligence to ensure that an attorney is not assisting a client with a fraudulent transfer should not only protect the attorney by proving the planning was done under appropriate circumstances, it should also protect the client by enabling the attorney, as the client's advocate, to prove to the court that such planning should be respected and accepted by the court.

FLORIDA BAR ACTION AGAINST LAWYER FOR ALLEGED FRAUDULENT TRANSFER ACTIVITY TO AVOID PAYING MONEYS TO HIS EX CLIENT.

In December of 2015, a Florida Supreme Court appointed referee determined that a lawyer who formed a new professional association in an attempt to avoid paying a judgment owed by his older professional association, did not violate Florida's Rules of Professional Conduct.[47] Initially, the Florida Bar sued the lawyer[48]claiming two separate violations. First, that the new professional association he created was a mere continuation of the prior one and had been formed with the intent to hinder, delay, or defraud collection action, which the Bar alleged to be in violation of Rule 4-8.4, and, second, that the lawyer diverted monies belonging to the first professional association to a bank account owned by the second professional association with the intent to hinder, delay, or defraud the creditor.

As indicated above, Rule 4-8.4(c)-d), titled "Misconduct," states that "a lawyer shall not engage in conduct involving dishonesty, fraud, deceit, or misrepresentation, (d) a lawyer shall not engage in conduct in connection with the practice of law that is prejudicial to the administration of justice."

The Referee found that the lawyer did not transfer tangible assets or accounts receivable from the first professional association to the second, and that there was no transfer of goodwill to the second professional association. The Referee also found that the lawyer's long standing practice

[47] When violations of the Florida Rules of Professional Conduct occur, the complaint is first brought before the Florida Bar Committee on Professional Ethics, once a decision is rendered at that level, an appeal to the Florida Supreme Court may be filed. Upon the Florida Supreme Court receiving the case, a "Referee" is assigned to the case to determine the final holding.

[48] *The Florida Bar v. Jefferson Riddell*, SC 15-1288, 2016 WL 1597199 (Fla. 2016).

of paying personal expenses from the business operating account of the professional association "is more than norm for small business than the exception," and that every year his CPA sorted out personal and business expenses so that "nothing was hidden. Nothing was 'laundered.'" The referee further noted that the Respondent did not commit fraud, deceit, or misrepresentation.

The Referee indicated that the evidence was not clear and convincing such that it could be proven that the lawyer acted in an unlawful or contrary manner to honesty and justice.

It would have been nice if the Referee had further pointed out that even if this lawyer had committed a "fraudulent transfer" to avoid a creditor, this would not be considered as conduct involving dishonesty, fraud, deceit, or misrepresentation. Nor, by our view, would this be considered to be "prejudicial to the administration of justice". The Referee was well aware that the lawyer shut down his practice entity to avoid making payment, but did not find this to be in violation of these ethical rules.

This case does point out that the Florida Bar may pursue lawyers who engage in aggressive transfers to avoid creditors and that it is important to confirm that no such transfer involves dishonesty, fraud, deceit, or misrepresentation.

Notwithstanding the above decisions, creditors, and sometimes debtors who have become cooperative with creditors after the fact, will continue to attempt to pursue causes of action against lawyers who assist in fraudulent transfers, and in particular this will occur when the conduct has been extremely aggressive, or on the edge of fraud.

Florida lawyers must therefore be careful to assure that their conduct is above reproach from an ethical and professional standpoint when advising debtors, given the high degree of past and expected future criticism that can apply in this arena.

Further, lawyers advising debtors in situations where the creditors consist of certain U.S. government agencies or where the debtors or contemplated actions are controlled by the laws of States that have "outlawed" transfers to avoid creditors must be especially careful.

REVISED HYPOTHETICALS - 1-31-17

Michael Markham's Hypothetical:

A new client comes in for asset protection advice the day after he is involved in a car accident. He is single and has approximately $800,000 in fairly liquid assets that are non-exempt. He currently rents but has been looking for a good deal on a house. He has $300,000 in liability insurance and does not believe that he was at fault in the accident, but advises that the other driver's injuries are significant. He wants to know if he should buy a house or something.

WHAT ADVICE CAN YOU PROVIDE?

ARE YOU CONCERNED THAT THERE IS A "KNOWN" CREDITOR?

ARE YOU CONCERNED THAT IF YOU DON'T TELL HIM TO BUY A HOMESTEAD THAT YOU COULD BE COMMITTING MALPRACTICE?

WHAT IF HE TOLD YOU THAT HE WAS DEFINITELY AT FAULT IN THE ACCIDENT? DOES THAT CHANGE YOUR ANALYSIS?

AFTER DISCUSSION, POLL THE AUDIENCE.

What if he came to you the day after the trial which resulted in a $1 million jury verdict against him? The client advises that his defense counsel was provided by his insurance company and that he did a horrible job. He did not have separate counsel advising him. Further investigation may reveal a bad faith claim against his carrier but current facts are very limited. Defense counsel has recommended a JNOV motion and an appeal. The client also advises that the judge was biased against him. The client wants to know what to do.

DOES THIS CHANGE YOUR VIEW?

ARE YOU COMFORTED BY THE DECISION IN *HAVOCO v. HILL*?

WOULD YOU ADVISE ANY EXEMPT ASSET OTHER THAN HOMESTEAD?

POLL THE AUDIENCE AGAIN.

What if the client came to you two years after the judgment was entered and advises that he just inherited $800,000? He advises that he's heard nothing from the creditor in over a year, but wants to know if he should buy a house.

DOES THIS CHANGE YOUR VIEW?

POLL THE AUDIENCE AGAIN.

WHERE IS THE LINE? IS THERE A LINE?

IS THERE ANY ISSUE WITH CONVERTING NON-EXEMPT ASSETS INTO EXEMPT ASSETS?

Alan Gassman's Hypothetical:

John Smith has a house worth $500,000 on 1/4-acre, 100% ownership of an LLC that employs he and his sister in a printing business, a girlfriend who he has promised to marry for the last 3 to 4 years, and stock and bond investments worth approximately $1,000,000.

He has negotiated with his next door neighbor, who has a $1,000,000 home on a quarter acre next to his property.

His sister would like to buy into the business, which does need a capital infusion.

He also has an offshore asset protection trust that holds $500,000 worth of gold coins in Switzerland that he set up in the 1990s that is irrevocable and for the benefit of himself and his children by a prior marriage. He and his lawyer are the Trust Protectors of this trust with the power to replace the Nevis trust company with an alternate trust company. The trustee has the power to make discretionary distributions for he and his children.

Mr. Smith was in a car accident and found to be 80% at fault by a jury who awarded the plaintiff, who was found to be 20% at fault, $800,000.

Mr. Smith only had $100,000 in coverage.

Mr. Smith's defense lawyer believes that there is a good chance of getting a new trial and proving that the plaintiff was much more at fault, so an appeal is underway.

There may also be a cause of action against the defense lawyer for not having worked harder to get the matter settled within policy limits when the plaintiff lawyer might have been willing to do so early in the case.

Mr. Smith wants to marry his long-time girlfriend, who has threatened to leave him if he doesn't.

In fact, they are now working to have a baby.

This will necessitate a need for more space, and he is therefore more motivated to buy the neighbor's house.

He comes to you for estate planning and business advice, and is interested in the following:

1. Assistance in putting together an offer to buy the house next door to make for a larger half acre homestead.

2. Review and offer from his sister's lawyer to have her buy into the LLC.

3. His fiancée is willing to waive all alimony rights and rights to his business if he will place $400,000 of his investments into a tenancy by the entireties account within 30 days after the marriage and allow her to save $30,000 per year so long as he is working.

4. He would like to amend and restate the offshore trust agreement and resign from being a Trust Protector.

5. He would like to pursue a cause of action against his defense lawyer, and possibly against the carrier for failing to make greater efforts to settle the case, and for failure to refer him to an independent lawyer when the plaintiff had offered to settle for $200,000 at mediation that took place months before trial.

Alternatively, the lawsuit is only against Mr. Smith's company, because a car being driven by one of his delivery people struck a pedestrian.

Mr. Smith was advised by his brother-in-law, who went to law school, but doesn't practice, to take all of the assets out of the company, sell them, and buy the house next to his house to have a larger homestead so that his brother-in-law can visit him and stay for longer periods of time.

J:\G\Gassman\SEMINARS\2017\February 2-4, 2017 - ABI Conference\Hypotheticals.1.wpd
:dlg 1/31/17

PASKAY SEMINAR HYPOTHETICAL – JOHN ANTHONY

Ms. Jane Doe is a guarantor of a commercial business loan from Bank of USA for her company, Doe International. The loan went into default after its largest account receivable filed Chapter 7; however, prior to the Chapter 7 filing, Doe International's revenue had been steadily declining and Ms. Doe was concerned about its future ability to make the required payments on the Bank of USA loan. It was during that time that Ms. Doe first consulted with her attorney, John Thinline, regarding taking precautions to ensure that her personal assets were protected against her business failing.

In connection with her consultation with Attorney Thinline, Ms. Doe transferred $400,000 in assets to Attorney Thinline's trust account. Attorney Thinline thereafter set up a revocable trust for the benefit of Ms. Doe's husband, and two children, and transferred the assets to the trust.

Thereafter, Ms. Doe became aware that the business's account receivable filed Chapter 7. Three (3) months later, shortly after receiving notice of Bank of USA's suit against Doe International and her individually, Ms. Doe transferred an additional $500,000 to Attorney Thinline's trust account. From those funds, $300,000 was used to purchase a parcel of non-homestead land held tenants by entireties with her husband. $200,000 was transferred to a limited liability company in Wyoming contemporaneously formed on Ms. Doe's behalf by Attorney Thinline. Bank of USA obtained a judgment against Ms. Doe and Doe International six (6) months later.

Bank of USA is now seeking to execute on its judgment against Ms. Doe and is alleging that all of the preceding transfers are fraudulent transfers under Florida Statutes § 726 or 11 U.S.C. § 548 in the event Ms. Doe files for bankruptcy. Bank of USA has served a subpoena to Attorney Thinline, seeking to obtain all documents evidencing the alleged fraudulent transfers, including communications between Ms. Doe and Attorney Thinline relating to the transfers. Attorney Thinline and Ms. Doe have objected to the subpoena, invoking the attorney-client privilege. Bank of USA has filed a motion to compel, seeking to invoke the crime-fraud exception.

1. WHAT FACTS SHOULD BANK OF USA RELY UPON TO SUPPORT THE CRIME-FRAUD EXCEPTION ARGUMENT?

2. WHAT FACTS SHOULD ATTORNEY THINLINE RELY UPON TO REBUT ANY PRESUMPTION OF FRAUD?

3. IS THERE ANY DISTINCTION BETWEEN THE SETS OF TRANSFERS FOR PURPOSES OF MEETING THE STANDARD FOR A CRIME-FRAUD EXCEPTION?

4. AT WHAT POINT DO ATTORNEYS PROVIDING ASSET PROTECTION ADVICE CROSS THE "CLOSE LINE BETWEEN PRE-BANKRUPTCY

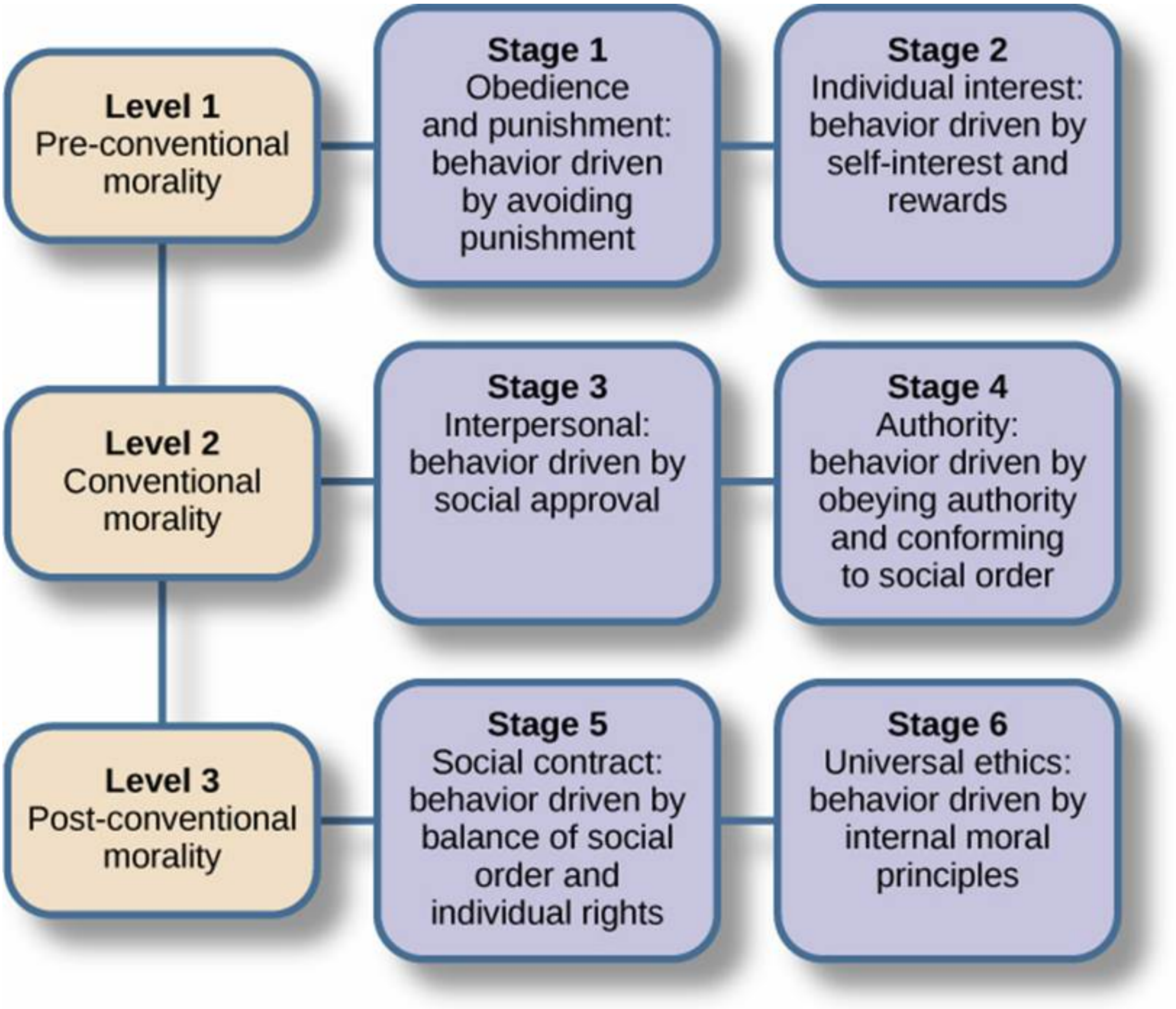
PLANNING AND THE INTENT TO HINDER, DELAY, OR DEFRAUD CREDITORS" AS REFERENCED BY JUDGE ISICOFF IN THE SIERVO CASE, OPENING THEIR ADVICE UP TO DISCOVERY UNDER THE CRIME-FRAUD EXCEPTION?

5. IS THERE ANY ARGUMENT THAT FRAUDULENT TRANSFER UNDER 11 U.S.C. § 548 OR FLORIDA STATUTES § 726 IS NOT CONSIDERED FRAUD FOR THE PURPOSES OF INVOKING THE CRIME-FRAUD EXCEPTION TO THE ATTORNEY-CLIENT PRIVILEGE?

6. IS THERE ANY LIABILITY FOR THE ATTORNEY FOR THE TRANSFERS AS AN INITIAL TRANSFEREE?

STAGES OF MORAL DEVELOPMENT

Lawrence Kohlberg's *From Is to Ought: How to Commit the Naturalistic Fallacy and Get Away with It in the Study of Moral Development*. 1971.



THREE FORMULATIONS OF THE CATEGORICAL IMPERATIVE

Immanuel Kant's *Groundwork of the Metaphysics of Morals*. 1785.

1. **The First Formulation: The Formula of Universality and the Law of Nature.**

   a. **The Universability Principle**:

   "Act only according to that maxim whereby you can at the same time will that it should become a universal law."

   b. **The Law of Nature Formulation**:

   "Act as if the maxims of your action were to become through your will a universal law of nature."

2. **The Second Formulation: The Formula of Humanity.**

   "Act in such a way that you treat humanity, whether in your own person or in the person of any other, never merely as a means to an end, but always at the same time as an end."

3. **The Third Formulation: The Formula of Autonomy.**

   "Thus the third practical principle follows [from the first two] as the ultimate condition of their harmony with practical reason: the idea of the will of every rational being as a universally legislating will."