

## Fraudulent Conveyance to Avoid or Hinder the IRS

## Fraudulent Conveyance to Avoid or Hinder Creditors

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Think you can avoid paying the IRS by holding property and other assets in the names of your relatives, friends or business entities that you own? Think again

Under the law of fraudulent conveyance a transfer made by a debtor is fraud perpetrated against the creditor whether the claims of the creditor were made before or after the transfer if the debtor made the transfer in either of the following ways:

1. with actual intent to hinder, delay, or defraud any creditor, or
2. without receiving a reasonably equivalent value in exchange for the transfer of the asset and if either of the following applies:
  - (a) the debtor was engaged or was about to engage in a business or transaction for which the remaining assets of the debtor were unreasonably small in relation to the business or transaction; or
  - (b) the debtor intended to incur, or believed or reasonably should have believed that he would incur, debts beyond his ability to pay as they came due.

For example, we can all reasonably expect to owe income tax in the future. We are worried that one day the government could seize our property for back taxes so we set up trusts for our children or spouse or parents to hold our assets. We may now believe that the property is safely beyond the reach of the IRS in future years should we ever fall behind in paying our taxes. WRONG! And you can substitute the name of any creditor in place of the IRS in the example here, same rules apply.

No effort to hinder or delay creditors is more severely condemned by the law than an attempt by a debtor to place his property where he can still enjoy it and at the same time require his creditors to remain unsatisfied. Direct evidence of a party's fraudulent intent is not required in court because it is impossible to look into a debtor's mind for the purpose of ascertaining his intent, the court must consider the circumstances surrounding the fraudulent transfer to determine intent from what the debtor does or fails to do.

The court will look for badges of fraud which are circumstances surrounding the fraudulent transfer to determine intent from what the debtor does or fails to do.

The court will look for badges of fraud which are circumstances so frequently attending fraudulent transfers that an inference of fraud arises from them. The following

acts are considered strong evidence that you have committed fraud in transferring or attempting to hid assets to prevent losing them to pay a debt you owe:

1. Whether the transfer was to an insider (i.e. relative, friend, etc);
2. Whether the debtor retained possession or control of the property transferred after the transfer. Meaning that you really own it in all but legal title.
3. Whether the transfer was concealed or done “secretly” or whether it was disclosed and done openly in the “sunshine”.
4. Whether before the transfer was made or the obligation was incurred, the debtor had been sued or threatened with a suit. Whether you knew, or should have known, that you were going to incur a debt.
5. Whether substantially all of the debtor’s assets have been transferred to related parties to hide the true ownership.
6. Whether the debtors absconded;
7. Whether the debtor attempted to hide assets or remove them to a place where they could not be found.
8. Whether the dollar value the debtor received from the related party that he transferred the assets to approximated FMV. In such a case your relative simply becomes your nominee or “straw man” (i.e. “selling” the assets to your child for a very low price or selling at a fair price but taking a not in lieu of cash payment knowing the note will never be paid or “gifting the assets- which by the way triggers the federal gift tax);
9. Whether the transfer of assets caused the debtor to become insolvent shortly after the transfer of assets was made
10. Whether the transfer occurred shortly before or shortly after a substantial debt was incurred;

Although badges of fraud are not conclusive and are more or less strong or weak according to their nature and the number occurring in the same case, a concurrence of several badges will always make out a strong case against the debtor.

If the creditor is able to prove a sufficient number of badges, the burden of proof then falls on the debtor to prove that the transfer was not fraudulent.

The doctrine of “economic substance over legal form” applies here. No matter that you have all the legal documents prepared with the i’s dotted and the t’s crossed, this will not protect your assets if your actions and intent fail the badges of fraud test. The court will look to the reality, not the legal fiction, of what really is going on with those properties. If you continue to use, control, benefit from, and enjoy the properties then you are in fact still the legal owner, no matter whose name is on the deed.

If you hold these properties in the business entities, i.e. corporations for LLC’s, then you must strictly observe the formality of the “corporate veil” and never pierce it if you expect to benefit from the limited liability statutes of state law. Otherwise, your

company will be deemed to be your “alter ego” or “nominee” and this means that the entity is not the real owner but rather it is you. You will lose it all in court.

If you undertake to protect your assets be sure that your attorney is well versed in the statute of frauds and fraudulent conveyances.

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