

## Protecting Your Asset Portfolio from Legal Assault

A nanny who worked for a wealthy business owner was driving her employer's children to school, talking on her cell phone, when she ran a red light and crashed into another car, killing a family of three. State law stipulated that in such cases both the driver and the vehicle owner were liable. Both the business owner and his wife were named on the car's registration as they were on all of their personal and professional assets. Due to the lack of protection planning, the accident ultimately put all of the business owner's assets in jeopardy.

We spend most of our working lives building and trying to turn our small businesses into larger ones, but could you survive the cost of a catastrophic loss?

The United State is host to 95 percent of all lawsuits filed worldwide. A new lawsuit is filed every 30 seconds, and if you own your own business, you have a one in four chance of being sued this coming year.

What can you do to protect your personal and business assets from frivolous lawsuits, and the possibility of judgments?

The following are seven rules that help a small-business owner protect what they have:

- **Rule No. 1:** Protect your assets before the need for protection arises. Asset protection is the process of arranging your affairs so as to minimize the risk of your wealth being seized, whether by prospective litigants, future creditors, or some taxing authority.
- **Rule No. 2:** Use multiple safeguards, since no perfect structure exists that will protect all assets all the time. You'll need to look at a variety of tactics to protect all of your assets in all contingencies, such as maximizing your contributions to 401(k) plans, pensions or IRAs; and finding low-cost umbrella insurance. Besides protection, if litigation does arise, a plaintiff's attorney may well become fixated on hitting the umbrella insurance policy to the exclusion of other personal assets.

- **Rule No. 3:** One of the best asset protection strategies, and the simplest, is titling things appropriately. If you own your own office building and it's in your name, for instance, a victorious plaintiff can claim it. To forestall such a maneuver, create an entity such as a limited liability company to hold the title. Likewise, you could set up separate ownership vehicles for each rental property that you own. That way, if a tenant sues you, that plaintiff cannot go after any of your other buildings to satisfy a judgment.
- **Rule No. 4:** Make your home unattractive to creditors by mortgaging it to the hilt, or creating a qualified personal residence trust.
- **Rule No. 5:** Do not trust that a spouse defense will save your assets. Married business owners occasionally put all of their worldly goods in their spouse's names for safekeeping. The tactic may or may not work, depending on where you live. In many states, signing property over to a spouse is better than owning it together, because a creditor can force a couple to liquidate jointly held assets to collect the debtor's share.

Of course, letting a spouse own everything puts the other spouse in a vulnerable position if the couple later gets divorced. If the spouse is merely holding assets that the other spouse still controls by writing checks on a bank account, for example, a creditor still has a good shot at those assets. To qualify for protection, the transferred assets must truly become the spouse's property.

Shifting assets to a spouse may be in vain in states that have community-property laws, such as California, Washington, Arizona, Nevada, Oregon, Wisconsin, Louisiana, Idaho, and Texas. In these states, a married couple jointly owns all property that is acquired during marriage, even if the property is title in only one spouse's name.

- **Rule No. 6:** Educate yourself so that you can understand which asset-protection strategies work and which ones do not. Suppose your goals are to make your assets

creditor and judgment-proof, but you are conservative and do not want to invite future problems. As a general rule, stay away from traditional offshore protection trusts. Any asset-protection attorney will tell you that these are a target of the IRS. If you establish a trust, you are required to notify the IRS, and just by doing that, as you know, you may become a target for examination by the IRS. The IRS takes the position that any offshore asset-protection trust means that you are trying to hide something.

- **Rule No. 7:** Consider a private insurance portfolio. Life insurance is one of the very few forms of investment that's often inherently protected from creditor claims. As a private insurance portfolio, in particular, lends itself to asset-protection planning, and for many individuals that will be a principal motivation for the investment.

When properly structured and established in the right jurisdiction, private insurance portfolios ("PIP") enjoy legal protection from creditors. The use of a PIP has expanded from seeking investment growth free of federal income tax in a cash-value account to designing sophisticated estate planning solutions to mitigate estate taxes on the transfer of wealth using the death benefit. Now, PIP solutions support wealth transfer, wealth creation and philanthropic needs, by using the death benefit in tax-advantaged ways.

The interest in PIPs for asset protection has also increased. Asset protection in offshore insurance vehicles offers many additional advantages for high-net-worth clients. By using an offshore trust, you don't automatically eliminate federal income, since you still need to report worldwide income. However, if the offshore trust owns the private insurance portfolio, then those assets grow free of any federal income tax and free of predators after the client's estate. At the death of the insured, those assets can be distributed in a tax-advantaged way to the next generation.

To summarize, protect your assets with estate planning in mind. Experts say that this strategy has a better change of holding up in court because it won't look as if you are only trying to stiff creditors or avoid paying a possible judgment. The best defense is to use a variety of estate planning tactics and keep your assets out of reach of judgments before the need arises.