PHYSICIANS PROTECT YOUR ASSETS

By William A. Ensing

Of growing concern in the medical community is the accelerating rate of malpractice claims against physicians and medical professionals. An additional concern is the rapidly increasing level of malpractice premiums levied by the insurance companies writing that coverage. In fact, the situation is out of control. A fact which every physicians must face at every level of practice is that at some point he or she will very likely become a defendant in a lawsuit, and some more than once. Without careful planning for that event, loss of accumulated wealth and assets can be instantaneous and unrecoverable.

Lawsuits can be filed almost immediately and sometimes for the most absurd and frivolous of reasons. One study estimated that 80 million lawsuits are filed in the United States each year - an average of 152 each minute the courthouses are open. Another study completed at the end of 1999, revealed that filing a lawsuit is viewed by many as the second fastest way to strike it rich today, second only to winning the lottery and far ahead of receiving an inheritance. The legal community has coined this trend “predatory litigation”, and it is rampant. It results in the view by most physicians that each person who comes into the office is no longer a patient, but a potential plaintiff seeking redress for some manufactured inconsequential, or worse, feigned injury. This is where asset protection planning will be of very valuable benefit.

A definition of asset protection planning would sound something like this: Asset protection planning is the process of organizing wealth, assets and affairs in such a manner, utilizing the most favorable entities, agreements and system of laws, so as to protect and shelter that wealth and those assets from lifetime risks to which they would otherwise be subject. Regardless of the definition used, the concept of lifetime protection of wealth and assets from risks associated with professional practice, avocational or occupational hazards, any activity with a higher than average degree of risk or, frankly, the unfortunate accidents which occur in daily life, should be an attractive concept worthy of exploration and serious consideration.

The need for wealth and asset protection planning developed as a direct response to the inability of the legal profession to offer and establish reasonable limits to legal damages. The fundamental concept of wealth and assets protection planning is to place accumulated wealth and assets out of harms way and in a protective structure that, if required, would shield them from creditor attack to the greatest extent possible. Wealth and asset protection planning specifically designs an environment which will cause a potential plaintiff to think far more deliberately about pursuing collection efforts through otherwise traditional litigation measures in the U.S.

Additionally, the law has established, and experience has shown, that the United States is, comparatively, a very plaintiff and creditor friendly environment. For example, the full faith and credit clause of the U.S. Constitution allows seizure of Florida assets in satisfaction of an Illinois judgement, and *vis versa*. Attorneys are readily available for fees contingent on recovery and the administrative fees required to file suit are minuscule. Additionally, Statutes of Limitations are designed to give the creditor longer periods of time within which to file suit. All of this has fueled the litigation explosion we are experiencing today.

Well, what can be done to accomplish current wealth and asset protection? Can assets and wealth be protected today from the risks, occupational or otherwise, during life so they can be enjoyed without the threat of a plaintiff creditor seizing those assets and wealth in satisfaction of a hastily entered judgement in favor of a predatory litigant? The answer is a resounding yes, and this is where careful wealth and asset protection planning can help.

The process begins with identification and measurement of the exposure to risk and the tolerance of it. For example, professional risks are rather easily defined and identifiable resulting from professional activities which put others at physical or financial risk. Practice in the medical and legal professions commonly present these readily apparent risks. Ownership of real estate, operation of manufacturing plants and retail establishments also carry their respective type of risk to be quantified.

But many other occupations, activities and ventures will also carry a large degree of risk as well. Daily activities outside of professional or vocational pursuits can also give rise to risk in a variety of situations. Any activity which carries a heightened level of risk has the ability to turn into an ugly and litigious situation which could have potentially devastating financial results to the unprotected. Driving a car or owning a particular asset capable of causing harm to others will expose the owner to a higher degree of liability. Motorcycle riding, auto racing, flying airplanes, and others each of which carries a greater level of risk to the participants, spectators and passengers which in turn results in a greater opportunity for suit against the operator, owners, their families or anyone associated those vehicles or activities. Additionally, the risk of increased and misplaced liability can arise in other settings such as divorce or bankruptcy which can place assets and wealth in jeopardy. Identification, insulation and protection of assets from these risks using every available tool is the goal of wealth and asset protection planning.

Insurance is not the complete answer either. While some level of insurance is important, the limitations of insurance must be recognized. For example, insurance policies have limits based upon the coverage purchased or available. Furthermore, policies are drafted with specific exclusions which limit coverage. And finally, the larger the policy, the greater the target.

Plaintiff's lawyers seek the largest money judgement or settlement they can obtain. The more they can recover for their client, the larger the contingency fee becomes. If one of several defendants has a large, juicy insurance policy, it is in the plaintiff's (and his lawyer's) best interest to work harder at tackling that defendant to get at that insurance policy; the proverbial deep pocket. Consequently, reliance upon this method to fully protect assets can prove not only insufficient but concentrate the plaintiff's litigation efforts toward that insurance pot of gold.

No one should be without some level of insurance coverage, nor would I recommend canceling a policy which can offer good coverage at prescribed levels. However, when foresight can never be good enough to indicate how much is enough, perhaps an alternative method of protecting wealth and assets is necessary given the particular circumstances. There is no sense in handing over all the marbles when sound asset and wealth protection can be designed and implemented for virtually every such risk.

How is comprehensive asset protection accomplished? The underlying principal of asset protection planning is the separation of asset ownership from control without deprivation of enjoyment. Several entities can be used to accomplish this separation. If an asset is owned directly, it appears on the judgement creditor's radar screen and can be taken to satisfy the judgement. However, the ownership of personal assets can be structured in such a way that future creditors, any future creditor, will have a very, very difficult time attaching and applying those assets in satisfaction of a judgement.

Once the risks are identified and quantified, design and construction of a wealth and asset protection structure begins with the formation of a domestic entity; either a family limited partnership or limited liability company. These entity forms are preferred since there are safeguards against creditors included in the enabling statutes and which can be drafted into the supporting agreements. The assets to be protected are transferred into the entity of choice by the owner in exchange for a corresponding interest in the entity. This entity would be designed to include all the protections and creditor disincentives afforded and permitted by state law against the seizure of assets by unfriendly third parties or potential creditors.

Without going into detail beyond the scope of this article, the selection of which state jurisdiction to use in the formation of the domestic entity becomes a very important analysis as well. Consider it sufficient to state that just as there are 50 states in the union, each has a slightly different slant on the creditor safeguards permitted. Most allow multiple remedies while some, coined single remedy states, will only allow the judgement creditor one bite at the remedy apple against properly formed limited partnerships or limited liability companies.

While we might stop at this point with some confidence that we have done enough using the available statutory protections which accompany the domestic entity, the real safeguards are afforded by creating a mechanism which removes the assets completely from the reach of creditors or the creditor friendly jurisdictions of the United States. Remember that the goal of wealth and asset protection planning is to protect accumulated wealth and assets applying the most favorable legal system which most effectively frustrates seizure by creditors. Statutory domestic entity safeguards notwithstanding, experience has shown that total reliance upon the U.S. statutory and common law framework may be ill placed. Consequently, to obtain the greatest protection of assets available, the next step should be carefully and fully considered.

Once the domestic entity is in place, a carefully designed asset protection trust should be drafted and funded with a large interest in the domestic entity previously formed plus any assets which by their character are not suited for ownership by the domestic entity. Initial control is retained by the party responsible for managing the domestic entity; the general partner of the limited partnership or the manager of the limited liability company, regardless of percentage ownership or ownership at all.

No physical relocation of assets is necessary at this point in the planning and implementation stage. The assets which are now titled in the name of the domestic entity are still in the local bank or brokerage house, perhaps even where they were located before planning began. The real estate is still located where you built or purchased it, although real estate protection presents its unique set of issues. What has been accomplished is a careful re-titling of assets such that the protective mechanism is in place to spring into effect when, if ever, that might become necessary. The trust just established is similar to a trust used in traditional estate planning contexts, but for the addition of several more bells and whistles and the inclusion of a foreign fiduciary who remains passive until needed.

Full protection of the assets is accomplished when a lawsuit threatens by the initiation of mechanisms within the documentation designed to sever all legal ties with the United States, dissolve the domestic entity, and place the assets in the structure under the control of the foreign trustee. For the duration of the threat, the assets are protected by the offshore trustee from attachment by creditors even if a U.S. court has issued a repatriation order as that court order has no effect against the foreign fiduciaries now in title. And, just as with any trust well designed for the benefit of the beneficiaries, the trustee is directed to continue making necessary distributions for the benefit of those beneficiaries. The trustee can pay the electric, gas and mortgage bill; medical and orthodontia bills, if required; and any others which are necessary for the beneficiaries benefit. After the threat subsides or is extinguished, the mechanisms are in place to reestablish the initial structure using the original design including a domestic entity for active domestic management and perhaps by the initial founding party.

Using the laws of a foreign jurisdiction in this context is no different in practical terms than a company operating in Illinois incorporating in Delaware. It is using laws available to it, even though outside its home jurisdiction, to accomplish the goals established for incorporation of the company and for the greatest obtainable benefit of the company. In wealth and asset protection planning, all available laws are considered, even though outside our domestic or home jurisdiction, to accomplish the most effective protection of wealth and assets and for the greatest obtainable benefit of the trust beneficiaries. In this context, we use the laws of the jurisdictions most favorable to accomplish the goal and which will result in the greatest wealth and asset protection available.

These jurisdictions have enacted legislation to fully support the wealth and asset protection industry. For example, the full faith and credit clause of the U.S. Constitution has no application outside the territory of the United States. Attorneys are not permitted by law in these jurisdictions to accept cases for contingent fees. To file a lawsuit in these jurisdictions, the courts require a bond of sufficient size to insure that if the plaintiff loses, it will pay the attorney's fees and costs of the defendant. The Statutes of Limitations are very short in comparison. And, as a significant additional benefit, by designing the wealth and asset protection structure utilizing these safeguards and enlisting the laws of these favorable jurisdictions, we have chosen the location of the final contest: the courts of that creditor unfriendly jurisdiction.

The actual structure used may vary widely with each specific situation and level of wealth protection desired or necessary as each planning opportunity will have a different threshold of risk endurance and degree of wealth protection desired. What may be an acceptable level of risk endurance in light of the profession or activities in which the individual is engaged will be quite different from someone wishing to protect different assets from a specific and unique range of risks. For that reason, the design and installation of a particular wealth protection structure may apply only for one situation and be completely inappropriate for another. It is an individual decision based upon entirely subjective criteria and after careful consultation with an appropriate and qualified professional advisor.

Also, it is an individual decision as to how much of currently owned assets should be sheltered using the methods described. Some seek and desire a complete shelter of all assets to safeguard as many assets and as much of the estate as possible, being careful to preserve the legal solvency of the client. Others will desire more of a nest egg, or rainy day, approach, setting aside only that amount which might be necessary to get through a difficult period. Again, it becomes a subjective decision considering all factors including the type of risk generating activity from which the individual is attempting to protect assets and the quantity of assets to be sheltered. While there are no absolute guarantees of a complete, ironclad and utterly failsafe method of protecting wealth against all creditors, despite the many sales efforts which claim so, the methods outlined here can add a level of protection which cannot be attained through even complex wealth transfer planning or any domestic structures.

Unlike estate and wealth transfer planning, wealth and asset protection planning falls into the category of planning it is hoped will never be needed. However, those engaging in riskier activities who are unprepared in this environment have a far greater degree of vulnerability and may get hurt, perhaps irreversibly so. The time to accomplish wealth and asset protection planning is as soon as possible and hopefully long before any accident or event occurs which may result in a lawsuit. Attempting to shelter wealth from current or potentially foreseeable creditors is fraudulent. Certainly, once the accident happens, the lawsuit is filed or a judgement follows, the planning opportunities are significantly reduced. Just as with insurance, the time to plan and purchase is exactly the same time that there are no needs or conflicts looming or foreseeable. Those who are prepared will weather the storm and carry on with a greater proportion of wealth and assets intact.

The first step of preparation in any planning context is assessment of the concerns, goals and objectives followed closely by education of alternatives and benefits. Together with a qualified professional, the applicability of wealth protection planning in the overall financial plan can be explored. Realizing what may be at stake and available to offer protection, the better educated can then be more fully prepared to make an informed decision to plan with the assistance of qualified professionals, or to endure the risks and concerns without it.

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