

Asset Protection Strategies Beyond Insurance

You've worked hard to accumulate your assets and property; that's why it's so important to take measures to protect your wealth. Often, the simplest way to protect assets is by shifting the risk to an insurance company. But insurance may not provide all the protection you need or it might not be available, so you may need to consider other strategies.

These asset protection strategies generally involve transferring legal ownership of assets to other persons or entities, such as corporations, limited partnerships, and trusts. The logic behind shifting ownership of assets is fairly straightforward: your creditors can't reach assets you don't own.

Shifting assets to a C corporation

The law views a C corporation as a separate legal entity. As such, business assets owned by a C corporation are considered separate from your personal assets, which will generally not be at risk for the liabilities of the business.

However, protection from liability may be lost if the business does not act like a business, such as when the business acts in bad faith, fails to observe corporate formalities (e.g., organizational meetings), has its assets drained (e.g., unreasonably high salaries paid to shareholder-employees), is inadequately funded, or has its funds commingled with shareholders' funds.

Shifting assets to other entities

A limited liability company (LLC), limited liability partnership (LLP), or family limited partnership (FLP) is a legal entity that can be used to separate business assets from personal assets.

An LLC is generally taxed like a partnership with income and tax liabilities passing through to its members (and not double-taxed as a C corporation), but it is viewed as a separate legal entity and can be used to own business assets, protecting your personal assets from business claims against the LLC.

If you have business partners, an LLP may protect you from the professional mistakes of your partners. That is, if one of your partners is sued for negligence, and the LLP is also named in the lawsuit, the partner sued may be liable personally for any judgment, but the LLP should protect your personal assets from the reach of any judgment creditor of the LLP.

An FLP is a limited liability partnership formed by family members only. Generally, a creditor can only obtain a charging order against the FLP, which allows the creditor to receive any income distributed by the general partner (who is usually a family



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member). It does not allow the creditor access to the assets of the FLP. Although each of the entities discussed above are alike in that they can protect your personal assets, they are very different in other ways. Make sure the entity you choose satisfies all of your needs.

Shifting assets to a trust

There are many different types of trusts that can be used to protect assets. A protective trust may protect assets intended to eventually pass to another person. For example, you transfer assets to a protective trust naming yourself and another as beneficiaries. The trust allows you to receive only income from the trust, with no access to the trust principal. At your death, the assets are to pass to the other beneficiary. If you're sued, the creditor can only receive your right to trust income, but not the assets of the trust. These trusts usually contain a spendthrift provision that makes it difficult for creditors to reach trust assets to satisfy claims against trust beneficiaries.

The laws in a few states, such as Nevada, Alaska, and Delaware, enable you to set up a domestic self-settled trust. You can create this type of trust, transfer assets to the trust, and name yourself as beneficiary. The trust gives the trustee discretion over whether or when to distribute trust property or income to beneficiaries. Creditors can only reach property that the beneficiary has a legal right to receive. Therefore, the trust property will not be considered the beneficiary's property, and any creditors of the beneficiary, including yourself, will be unable to reach it.

Many foreign countries have laws that make it difficult for creditors to reach trust assets held in that foreign country. In order for a creditor to reach assets held in a foreign or offshore trust, a court must have jurisdiction over the trustee or the trust assets. Because the trust is properly established in a foreign country, obtaining jurisdiction over the trustee in a U.S. court action will not be possible. Thus, a U.S. court will be unable to exert any of its powers over the offshore trustee.

Protecting assets doesn't include fraud

Protecting your assets by legally repositioning them does not extend to actions intended to hide assets or defraud creditors. So, make sure you implement any asset protection strategy before there is any hint of trouble, and be sure to carefully document that you are doing so for sound business or other reasons.

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