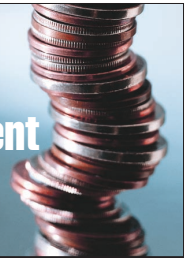


Keep Your Money Safe

Lawyers will get sued, and assets are best protected before claims.

Wealth Management

A Practice Focus



BY JAY D. ADKISSON

Attorneys, when it comes to asset protection, heal thyself: Consider our colleague, Philadelphia corporate lawyer H. Beatty Chadwick. Embroiled in a nasty divorce, Chadwick sent his money to Gibraltar, allegedly to keep it from his wife.

When he didn't bring the money back, Chadwick was ordered in 1995 to jail for contempt and has been there ever since—13 years now. He also received a five-year suspension from legal practice.

The point is this: If you are ever faced with a judgment, don't think that you can just hide money offshore and stiff your ex-spouse or creditors. Once you have a judgment entered against you, it is probably too late to do any effective planning. And planning that violates a law or court order can cause you to lose your ticket to practice law.

Should you even worry? Most lawyers don't think that they will be sued for malpractice, at least for amounts in excess of their errors and omissions coverage. That is probably right. Getting hit with a malpractice lawsuit in excess of your coverage limits is pretty rare.

But think that you will never get into a bad business deal? Think again. These days there are a lot of lawyers who invested in real estate and are starting to sense the harsher meaning of "personal guarantee." They join a sizeable number of lawyers who have discovered that the fruits of their careers can suddenly disappear because of anything from partnership disputes to sexual harassment claims to bad car accidents.

The truth is that lawyers do get sued—quite frequently it seems—but are less likely to protect assets against a judgment than are ordinary business people.

So what can you do to avoid ending up like our brother H. Beatty Chadwick?

• *Let's Talk Insurance:* We'll start out with the basics, which means your existing insurance coverages. Periodically review your limits to see if they are adequate. Just how long

do you think it would take the three injured passengers in the car you just hit to blow through \$100,000 in intensive care?

The best asset protection you can buy comes in the form of personal umbrella insurance. For only a few hundred dollars a year, you can purchase coverage into the millions against most unforeseen and otherwise uncovered events. Although this type of insurance will not protect you from professional negligence claims or contractual liability, it will pick up many other things.

• *Protecting Your Inheritances:* Another way to protect assets is to never receive them in your own name in the first place. Consider an inheritance: If you take the inheritance in your own name, those assets immediately become exposed to your creditors. But if those assets are given to you in a discretionary spendthrift trust, your creditors will have no rights to them, except possibly in some states for child support (which you should be paying anyhow).

And remember this for your kids, who probably still face the steep learning curves of marriages, business deals, and perhaps even safe driving. You are doing them a disservice if you give them large gifts outright, since those gifts will instantly become exposed to creditors.

• *Taking Chips Off the Table:* To be a winner, you have to walk away from the table a winner. Or so they say in Vegas. But this gambler's truism holds guidance for protecting wealth. Determine how much wealth that you really need for yourself, and transfer the rest to a trust for your children. That amount comes off your balance sheet where it is exposed to your creditors and moves the wealth into a place where it is protected.

Taking chips off the table is not a one-time transaction, either. It is a continuing pattern, where excess wealth is routinely moved into a protected environment.

If you are curious, the statute of limitations for a fraudulent transfer is four years. But it is very difficult for a creditor to establish that a gift was inappropriate if the person making it did not have any creditor problems at the time.

• *Prenuptial Agreements:* Where do lawyers (and doctors) lose the most wealth? It is not to verdicts in excess of insurance coverage, not by any stretch of the mathematical imagination. More money is probably lost by lawyers in divorces in a single year than in all the excess malpractice verdicts combined.

The reason for this loss is simple: Lack of planning, which means lack of a prenuptial agreement. Wealth losses because of divorce are easy to avoid by agreeing with your beloved beforehand as to how things will be split up, but hostile, drawn-out, and wasteful divorces are still the norm for lawyers. You would think that lawyers of all people would have prenuptials, but for whatever reason (probably the unconscious arrogance that they could “win” a divorce being the biggest one) lawyers almost never seem to get these agreements.

You can’t wait until you get into the divorce to start planning. Just ask our friend H. Beatty Chadwick.

• *Encapsulating Liability:* Own some rental properties? A car wash? Some other side business? These need to be operated from some sort of entity, such as a corporation or limited liability company, that will internalize the liabilities that they generate.

For this to be effective, you need to cede your day-to-day control to somebody else, such as a property management company. Otherwise, if something goes wrong, you will likely be sued along with the entity. Remember: An entity provides no defense for one’s personal acts or negligence.

But don’t think you can put purely personal assets into a corporation or LLC and they will be protected. The theory of “reverse alter ego” has been successfully used to disregard the entity where no bona fide commercial venture was being facilitated and it was clear that the entity was just the personal piggy bank of the debtor.

Personal assets go into trusts. Business assets go into business entities. When you start crossing these lines then you risk the court disregarding the structure.

Keep in mind that the term “Family Limited Partnership” is planner’s slang and that legally there is no such animal. Partnerships and LLCs provide asset protection only when they are used for the business purposes for which they were intended.

• *Don’t Give Up Control:* Many asset protection schemes require that you surrender your assets to somebody else, under the “If I don’t own it, you can’t have it” approach. Although this can work in many instances, the downside is that you really do have to surrender control for this to be effective, and when you do so, you place your assets at risk.

Now, if you put your assets with a large trust company, that is one thing. But other than that, problems can arise. Probably far more money has been lost by lawyers to their fiduciaries who dipped into the cookie jar than to excess legal negligence verdicts. And don’t think that just because you are a lawyer that the person you are trusting will be trustworthy: Once a person makes a decision to embezzle another’s assets, whether to fund their drug habit or whatever, it doesn’t seem to make a difference who their victim is.

• *Offshore? Think Again:* When most people think of

asset protection, they immediately think of keeping money in a Swiss bank account or having a Cook Islands trust. Indeed, an entire industry of banks and advisers exists to help you get your money offshore.

The obvious advantage to offshore planning is that it provides a level of deterrence, because most creditors will not want to spend the time and costs to make an international attempt to squeeze blood from the turnip.

But there are problems with offshore asset transfers. The most practical one is that although your assets may be offshore, your body will probably stay here and be subject to court orders. This means that you can be subject to what is known as a Repatriation Order essentially saying, “Bring the money back, or go sit in jail.” Courts routinely grant these orders, and debtors routinely go to jail when they refuse to comply.

Offshore transfer also can actually highlight what assets you have. You must report to the U.S. Treasury Department all your offshore financial accounts (liberally defined to include stock accounts, offshore life insurance, and offshore annuities) and all transfers out of the United States of \$10,000 or more. These filings can create road maps for creditors to identify your offshore assets.

• *What About Offshore Trusts?* Once upon a time, offshore trusts were sold to clients as that perfect castle that creditors could never successfully assault. You put your money in a trust in the Cook Islands or some other spit of land surrounded by reefs, and then when the collector man came around you would say, “I’m sorry, but I don’t own those assets anymore, and the trustee refuses to give them back to me.”

Judges started saying: “We do not believe that you would transfer all of your assets outside of the United States and not maintain control over them.” Thus, even if the trust documents demonstrated that the debtor had no control, the courts started throwing debtors in jail anyway until the assets came back. Moreover, the 2005 federal bankruptcy reforms created what amounts to a 10-year clawback for transfers to self-settled trusts (trusts that you create for yourself) that effectively guts the protections of offshore trusts, as well as the newer “domestic asset protection trusts” in such states as Alaska and Delaware.

• *Simply Stated:* Whatever you do needs to be explainable to your average jury and judge. If it is so complicated that you can’t explain it, it probably isn’t going to work. Likewise, you will need to be able to explain very simple things, such as where you are getting money to live on. If a judge gets a whiff that you are hiding assets, the breaks will start going against you.

So, keep your asset protection planning simple and explainable, but most of all, do it well in advance of problems.

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