

Protecting Your Assets – Planning Beyond Insurance

As physicians, the number one concern should be how to better serve one's patient. In today's society, however, there are many other burdens on physicians that may be distracting and ultimately, a significant number of preventative measures are overlooked in the process. As a result, countless physicians are left vulnerable and looking back to what "should have" and not enough focus toward the future to what "could be".

The High Costs of Insurance

A common worry in most medical professionals' minds is the potential malpractice lawsuit. This worry has become a reality for some members of the medical community, as the number of medical malpractice claims have risen and the amounts awarded by juries has considerably increased. Traditionally, physicians have purchased malpractice-related liability insurance in order to cover the probability of litigation. Nevertheless, the risk of insuring doctors has caused insurance companies to significantly raise the cost of premiums. In many states the insurance cost to properly cover a physician is prohibitively expensive. This point is driven home by the fact that the national mean of medical malpractice awards has increased from \$4,090,751 in 2004 to more than double in 2005, \$10,370,637.¹ The highest award in 2005 was for \$212,580,000.²

Because of the likelihood of these claims, excessive jury awards, and unpredictability of the courts, physicians have needed to purchase additional coverage while medical malpractice insurance premiums have sharply increased. Some physicians are also discovering that the field in which they are practicing are such high-risk specialties that some insurance companies will not insure doctors in their industry.

Potentially Underinsured

Even with expensive insurance coverage, many physicians do not have the protection they require. In 2001, 52% of all awards exceeded \$1 million.³ In 2005, three of the top ten verdicts awarded in the nation—\$600 million, \$212.5 million, and \$36.5 million—were entered in malpractice lawsuits.⁴ The groundbreaking jury award for a Connecticut malpractice case The most shocking of those three verdicts was the \$36.5 million verdict, which was a case decided in Connecticut.⁵ Without the predictability of knowing how much coverage is sufficient, many physicians may be personally at risk. Insufficient coverage may result in the physician being held personally liable for the amount in excess of the insurance coverage. In that situation, the physician's house, bank accounts, and other valuable assets are subject to seizure. At that time, it is already too late to begin planning to protect one's assets.

¹ See Sarah Diamond, *Trial Trends*, VERDICTSEARCH.COM, 2006,

http://www.verdictsearch.com/jv3_news/trial_trends/index.jsp (last visited October 20, 2006).

² See VerdictSearch, *Top 100 Verdicts of 2005*, VERDICTSEARCH.COM, 2006,

http://www.verdictsearch.com/jv3_news/top100_2005/index.jsp (last visited October 23, 2006).

³ See Tanya Albert, *Malpractice Awards Hit the Jury Jackpot*, AMEDNEWS.COM, Feb. 3, 2003,

<http://www.ama-assn.org/amednews/2003/02/03/prsc0203.htm> (last visited October 18, 2006).

⁴ See VerdictSearch, *Top 100 Verdicts of 2005*, VERDICTSEARCH.COM, 2006,

http://www.verdictsearch.com/jv3_news/top100_2005/index.jsp (last visited October 23, 2006).

⁵ *Cowles v. Hartford Hospital*, No. CV-00-0168303-5 (X06), (Conn. Super. Ct. November 23, 2005).

Flying Under the Radar

There are other potential risks to personal assets other than malpractice lawsuits. One of these risks stems from the fact that many physicians enter marriage without consulting a legal professional beforehand. In many states, once a couple marries, the assets of each spouse become pooled together and divided in the event of a divorce. Physicians with significant asset holdings expose more if the marriage fails, even in the event where a pre-nuptial agreement was signed. Other risk factors include having a teenage driver in the family or owning a rental property unrelated to the profession. These scenarios are common to many individuals, but it is important for physicians to recognize that there are additional threats to their financial well-being other than the malpractice suit. These factors are prevalent to everyone with substantial assets and should be considered before simply purchasing additional malpractice insurance to cover a single risk. The solution should be perceived as less of a fix for the future and more of an asset management foresight.

Preventative Measures

The large expense of malpractice insurance, the risk of being insufficiently insured, and the exposure that many physicians face beyond malpractice litigation has led physicians to search for other solutions. Asset protection specialists recommend alternative, common structures as effective defensive techniques beyond insurance. These solutions will vary, depending on different levels of risk tolerance and various life situations.

One thing these solutions are not: fill-in-the-blank, one-package-fits-all, uniform answers. They are customized to the client and should be structured very cautiously with a well-seasoned legal professional. The most dangerous situation to be in is one in which a client pays a discounted price for an off-the-shelf product and later realizes that she is not as protected as she originally thought. This article will provide you with a brief summary introduction to several asset protection tools, their benefits, and some commonly asked questions that will prepare you to evaluate your vulnerability.

Domestic Structures

Moving assets out of one's own name or legally encumbering them is a typical first step to protecting one's financial health. The next step is to establish structures, or "barriers" against attacks by potential creditors. Examples of planning techniques include trusts, family owned entities, and equity stripping.

Domestic trusts are an excellent means to transfer wealth to other family members. A trust may be "settled" (formed and funded) during your lifetime or at death. If at death, the trust works in conjunction with your Will to determine how assets will be allocated to various individuals and provides control via provisions written into the Trust. Examples of control are: spendthrift provisions – preventing beneficiaries from pledging their share in the Trust to creditors – and discretionary provisions – where the trustee determines how much money to release to the beneficiary. The possible disadvantage of a domestic trust is that it is subject to the jurisdiction of the U.S. Courts, which may make the Trust an easy litigation target.

Family owned entities, such as the Family Limited Liability Company ("FLLC") provide significant asset protection as well as an orderly transition of wealth to one's family members. A physician can transfer her interest in properties, securities portfolio, practice ownership or any other interests she wishes to protect to the FLLC. The FLLC will transfer the FLLC ownership interest to the physician and members of her family, however she chooses the ownership structure. If a creditor wins a judgment against the physician, the creditor can only attach any capital distribution to the doctor's FLLC ownership interest, since the ownership interest itself cannot be transferred outside of the family. This powerful structure adds an extra layer of protection between the physician and the creditor,

leaving more bargaining leverage for the physician. This entity can also transition assets from parents to their children, having a strong estate planning element.

Equity-stripping is a means of protecting one's real estate. The more equity is in one's home, the more valuable the asset becomes for creditors. Properly stripping one's equity can allow a physician to have added protection because it dissuades creditors from attaching onto a property that has little to no equity. As an example, a home equity line can be used to encumber the equity in a property, using the cash available as an investment in a FLLC which holds an securities investment portfolio.

Foreign Structures

The Foreign Asset Protection Trust (FAPT) is an effective defensive technique for some professionals, including many physicians. It is a trust established in a friendly offshore jurisdiction, which does not recognize United States debtor-creditor laws or judgments rendered by United States courts. It provides the same benefits as the domestic trust structures, however, there are many added features.

Most FAPTs include "flee" clauses, which are provisions authorizing the Trustee to change the location of the Trust in the event there is a threat of legal action against the Trust, an impending change in jurisdiction's legislation or some cataclysmic occurrence such as a war or natural disaster. FAPTs also include "anti-duress" provisions, which prohibit the Trustee from making any distributions from the Trust to any creditor of the Settlor. The assets in a FAPT are generally held with a custodian such as a triple "A" rated international financial institution.

Another powerful feature of most FAPTs is the "spendthrift" provision. Under US laws, even if a trust contains a spendthrift provision, certain parties may obtain a court order attaching present or future distributions for the benefit of the beneficiary. These parties include a trust's beneficiary's child, spouse or former spouse who has a judgment or court order against the beneficiary for support or maintenance. The same is true for a judgment creditor who has provided services for the protection of a beneficiary's interest in the trust. However, under the laws of most FAPT jurisdictions, the Trustee is prohibited from making distributions from the Trust for the benefit of a judgment creditor of any beneficiary of the Trust, including beneficiaries who are the spouse or children of the Settlor ("Grantor").

FAPTs are also subject to the stricter secrecy laws of the foreign jurisdiction where they are created. Fiduciaries, financial institutions and local government authorities generally require disclosures of certain information about the trust and its participants prior to registration. Nevertheless, without evidence of fraud or other serious wrongdoing, the laws of offshore jurisdictions typically prohibit the disclosure of information related to FAPTs to creditors and other third parties.

One of the main advantages of an FAPT is that it forces a US creditor to travel to a foreign jurisdiction and file his or her claim there. Some offshore jurisdictions require potential judgment creditors to post a substantial bond before proceeding with the lawsuit. Additionally, most offshore jurisdictions do not allow for contingent fees, thus increasing the creditors' costs and risk. Finally, regulated by a defendant-friendly bar, many foreign attorneys are unwilling to take on cases without a substantial amount of money at stake. These and other characteristics of FAPTs encourage negotiations and settlement, almost always in an amount significantly smaller than the original claim.

Action Items

Everyone who owns anything of value is at risk of losing it to creditors. Nevertheless, these risks can generally be both identified and reduced, if not eliminated. Physicians in particular need to be cautious because of the litigious nature of our society and amount of personal liability at stake. Generally, the greater time that goes by between any transfer of assets into a plan, the less likely the transfer will be attacked. The key to protecting assets is to do it before any perceived threat might materialize. Remember that because proper preventative methods are necessary, one should first consult with professional experienced in asset protection, estate planning and taxation matters. A professional has the benefit of knowing the law, and what legal tools to use to safeguard your wealth. It is important to plan a protective measure that will provide you with the assurance that what you have worked hard to own remains with you for a long time.

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