



# ASSET PROTECTION

## for High-Risk Professionals

Much has been written about asset protection strategies, such as offshore trusts, limited liability companies (LLCs), insurance, and exemption planning. The focus of this article is to identify which of those strategies are best suited to high-risk professionals, whose risk exposure derives from the provision of professional services (as opposed to risky investments or predators who target the megawealthy). Some of the strategies discussed below reflect ways to reduce a professional's financial profile and accordingly, the size of the targets on their backs.

### EXEMPTION PLANNING

We first address the most basic technique, which involves safeguarding assets from creditor attachments using protections available under applicable federal and state laws. Exemption planning is an important asset protection tool, as this type of planning takes advantage of categories of assets that are legally exempt from attachment by judgment creditors.

Exemptions exist under both state and federal law and may apply in either a bankruptcy or nonbankruptcy context. If an exemption is available for specific property, the debtor retains all rights of ownership and enjoyment of the property free from creditor interference.

Federal exemptions exist under the US Bankruptcy Code,<sup>1</sup> the Employee Retirement Income Security Act of 1974,<sup>2</sup> the Social Security Act,<sup>3</sup> and the Consumer Credit Protection Act.<sup>4</sup> Many states have statutes that provide more liberal exemptions related to (1) homestead, (2) life insurance or annuity contracts, (3) wages and earnings (or at least a portion thereof), (4) nonwage income, (5) personal, household, and other possessions, and (6) retirement benefits. As such, in some states, a professional could claim the more liberal state exemption in bankruptcy matters as opposed to the stricter federal exemption.

The homestead exemption represents one of the most significant protections under the law and can be extremely beneficial for high-risk professionals. However, state laws generally impose some type of limitation on the homestead exemption. For example, while Florida and Texas have unlimited dollar-amount exemptions, both states limit the homestead exemption to a maximum specified amount of land.<sup>5</sup> Other states have adopted a monetary limitation, which varies dramatically by state: coverage is as high as \$605,000 in Nevada and as low as \$2,500 in Arkansas (with an accompanying acreage limitation).<sup>6</sup>

## INSURANCE

Insurance can be an important component of asset protection planning. However, insurance may not be able to cover all liability risk, and policies typically have exclusions that may limit their usefulness. Many high-risk professionals, such as doctors and lawyers, utilize malpractice insurance but also hold general business insurance policies and personal liability insurance policies (such as car insurance, homeowner's insurance, and umbrella policies). Malpractice policies typically have numerous exclusions that may limit their effectiveness, for example, for intentional or grossly negligent conduct.<sup>7</sup> Furthermore, professionals who primarily serve wealthy clients may not be able

to purchase sufficient coverage to protect themselves against all risks at a reasonable cost. Thus, while insurance is an important aspect of any asset protection plan, other strategies must also be employed to offer the maximum protection possible.

## LIMITED LIABILITY COMPANIES

The LLC has proven to be a highly effective asset protection tool because it traps liability at the entity level similar to a corporation. It also provides what many consider to be the added advantage of being taxed as a partnership or disregarded entity unless an election to be taxed as a corporation is made. LLCs preclude an LLC member's creditor from accessing LLC assets to satisfy the member's personal debt. Further, they protect the member from liability that may arise from the assets held in the LLC (e.g., liability due to a slip-and-fall accident at a rental property owned by the LLC), as only assets owned by the LLC are exposed to such liability, not the member's personal assets. As discussed below, multiple LLCs can be formed to separate *hot assets* (i.e., assets such as the aforementioned rental property that could be a source of liability)<sup>8</sup> from *cold assets* (i.e., assets that do not expose the member to liability).<sup>9</sup>

Transferring assets into an LLC provides asset protection for an LLC member because their personal creditors may be limited to obtaining a charging order for debts that arise after the formation of the LLC.<sup>10</sup> A charging order is a statutorily created means for a creditor to reach a debtor's beneficial interest in an LLC. This charging order protection also shields the interests of other LLC members by preventing the debtor member's creditor from reaching the LLC's assets to satisfy their claim. A charging order functions similarly to an assignment of income: future distributions from the LLC that would otherwise be made to the debtor are instead made to the creditor who obtained the charging order until the debt is paid. Thus, the creditor is unable to reach an LLC's assets except for

---

1 11 U.S.C. §§ 101–1532.

2 29 U.S.C. §§ 1001–1461.

3 42 U.S.C. §§ 301–1305.

4 15 U.S.C. §§ 1601–1693r.

5 Fla. Const. art X, § 4(a)(1) (160 acres outside municipality, one-half acre inside municipality); Tex. Const. art. XVI, § 51 (200 acres outside municipality, 10 acres inside municipality).

6 Nev. Rev. Stat. §§ 21.090(1)(l)–(m), 115.010 (2022); Ark. Code Ann. § 16-66-210(c) (2024).

7 See Barry S. Engel, *Asset Protection Planning Guide* 125–26 (3d ed. 2013).

8 In addition to rental properties, other examples of hot assets include aircrafts, boats, vehicles, stock in a corporation that is vulnerable to a piercing-the-corporate-veil ruling, a personal residence, and a general partner interest in a limited partnership that owns hot assets or that engages in activities that could cause liability.

9 Cold assets are assets that are not an inherent source of liability, for example, a treasury bond, which by its nature does not cause liability.

10 In some jurisdictions, charging orders are not the exclusive remedy for the personal creditors of LLC members that look to the LLC to satisfy their claim, particularly in the context of single-member LLCs. See *infra* note 14. Some states also allow creditors to seek a court order directing the foreclosure sale of a debtor member's ownership interest to the judgment debtor, but the creditor is not permitted to exercise the member's managerial rights.

distributions made to the debtor. If the debtor member is also the LLC's manager, the debtor member may, in some circumstances, remain in control of when (and if) such a distribution is ever made.<sup>11</sup>

Foreign LLCs may offer stronger protections than their domestic counterparts and make it more expensive for a creditor to pursue a charging order against a debtor.<sup>12</sup> Using a foreign LLC in jurisdictions such as Nevis, the Cook Islands, and Belize offer the following advantages:

### Nevis

- The plaintiff/creditor may need to first provide a bond to proceed with any legal action against an LLC's assets.<sup>13</sup>
- A charging order expires after three years and is nonrenewable.<sup>14</sup>
- The charging order is the sole remedy available to any creditor to satisfy a debt or judgment from a member's interest, even if the LLC has only one member.<sup>15</sup>
- If an individual creates and funds a Nevis LLC, it is very difficult to demonstrate that a fraudulent transfer has taken place because the value of the LLC interest received in exchange for the assets contributed to the LLC is deemed to be of equal value under Nevis law, which by definition precludes the transfer from being a fraudulent transfer.<sup>16</sup>
- No judgment obtained in a foreign domicile will be recognized or enforced.<sup>17</sup>

### Cook Islands

- The charging order is the sole remedy available to any creditor to satisfy a debt or judgment from a member's interest.<sup>18</sup>

- No member's rights or interest is capable of being seized, charged, or levied upon or taken in execution by or under any form of judicial process.<sup>19</sup>
- No judgment obtained in a foreign domicile will be recognized or enforced.<sup>20</sup>
- Cook Islands LLC law maintains the confidentiality of member and manager information.<sup>21</sup>

### Belize

- Before a plaintiff can pursue assets, the plaintiff must deposit cash in the amount of the greater of \$50,000 and one-half of the amount of the claim being sought with the Belize Supreme Court Registry.<sup>22</sup> This is a deterrent to suit.
- Belize has a duress provision that shifts control away from any manager or member of an LLC who is being coerced to act against their free will.<sup>23</sup>

## HOLDING COMPANIES

While individual LLCs can have significant asset protection benefits, using multiple LLCs in a holding company structure can provide additional protection for the owners while also isolating high-risk assets from both other high-risk assets and low-risk assets. Holding company structures are most commonly used by clients who have operating entities or hold numerous high-risk assets and want to isolate the risk of those businesses and assets. They can be implemented using domestic LLCs or foreign LLCs.

In a typical holding company structure, one overarching LLC is formed as the holding company. This holding company is normally held by the individual owners of the structure or through a trust. The holding company in turn owns numerous other LLCs, each of which owns a separate business or asset.

11 Charging order protection may not be available for single-member LLCs (SMLLCs). Unless applicable state law provides that a charging order is the exclusive remedy for an SMLLC, which is the case in a few states including Alaska, Delaware, Nevada, South Dakota, Texas, and Wyoming, the creditor may be able to force a distribution in the case of an SMLLC.

12 Some types of claims will likely be brought in the United States despite the formation of the LLC in a foreign jurisdiction. For example, for slip-and-fall liability involving an LLC holding real estate located in the United States or some other product-type liability, the lawsuit would be filed in the state where the event or accident occurred. In the context of contracted debt, there is almost always jurisdictional language in the debt instrument.

13 Nevis Limited Liability Company Ordinance § 62 (2017).

14 *Id.* § 60(15).

15 *Id.* § 60(5).

16 *Id.* § 61(2) and (3).

17 *Id.* § 61(11).

18 Cook Islands Limited Liability Companies Act 2008 § 45(6).

19 *Id.* § 45(2).

20 *Id.* § 45(14).

21 *Id.* § 72.

22 See Belize International Limited Liability Companies Act § 37(7) (2011).

23 *Id.* § 64(3)–(4).

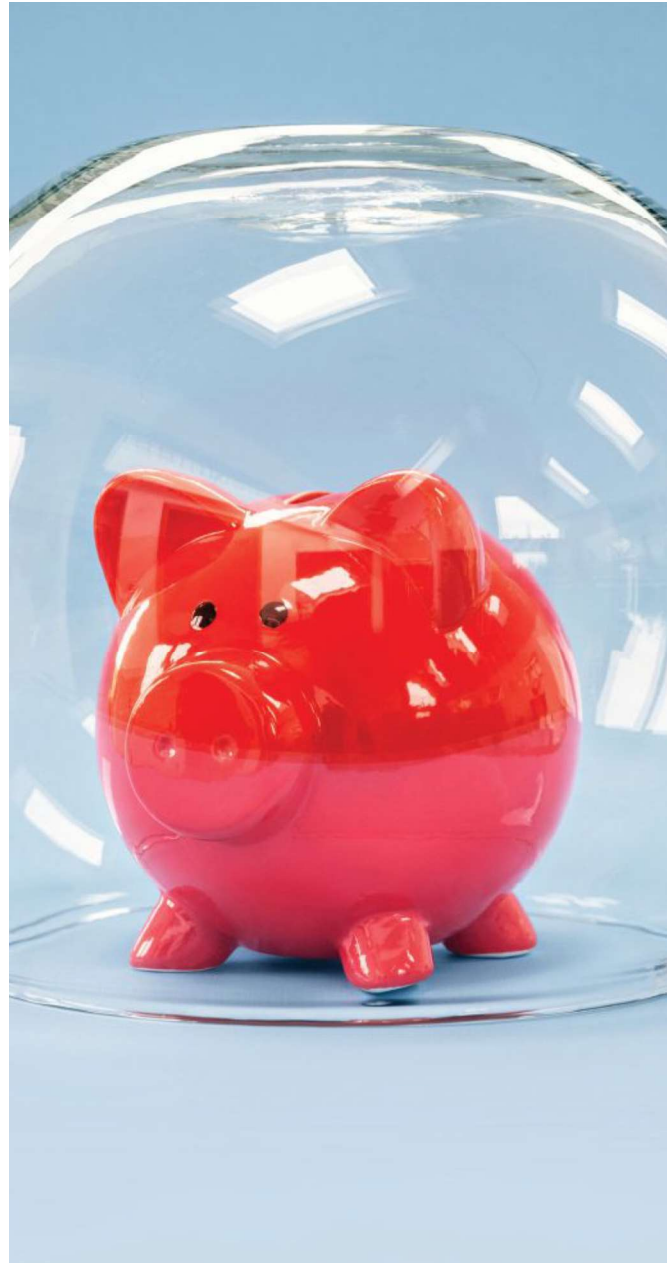
For example, for a physician client who owns five separate medical practices,<sup>24</sup> one holding company could be set up to be owned directly by the physician. The holding company could own five separate LLCs, each of which owns one of the medical practices. Each separate LLC, including the holding company, should open a separate bank account. In addition, all employment contracts and other contracts should only be entered into by the LLC that owns the applicable practice.

A holding company structure enables the ultimate owner's personal assets to be insulated from creditor claims through the use of multiple layers of limited liability entities: the risk associated with each entity's assets (or group of assets) is isolated into separate limited liability entities. Returning to the medical practice example, if there is a malpractice claim against one of the practices, the entity that owns that practice may ultimately be liable for damages, and all assets owned by that entity can be attached by the creditor suing the entity. However, the other four practices held by the other LLCs should not be subject to liability because the liability for the malpractice claim is limited to the LLC that owned the specific practice at issue. If all of the practices were held by one LLC, all five of the practices' assets could be reached by the creditor. This exposure could mean that a significant lawsuit could cause the client to lose or be forced to sell multiple medical practices, whereas the holding company structure could limit the risk to a single practice.

However, when utilizing a holding company structure, it is extremely important that all companies involved strictly follow company formalities. This means that expenses of the entities cannot be commingled, contracts must be executed by the appropriate parties, etc. If these formalities are not followed, the structure may be disregarded, and a creditor may be able to pierce the veil to reach the assets of the owners and of the other LLCs.<sup>25</sup> Thus, when setting up a holding company structure, attorneys should weigh the benefits of the structure against the administrative burden of following all of the necessary formalities.

## TRUSTS

Trusts, particularly when used together with limited liability companies, are strong asset protection vehicles. Trusts are also commonly used in conjunction with a client's overall estate plan as vehicles to reduce estate taxes and to ensure that assets



are available to benefit future generations, among other reasons.<sup>26</sup> Thus, trusts can provide numerous benefits independent of any asset protection that they may also provide. The main types of trusts used for asset protection purposes are domestic asset protection trusts (DAPTs), offshore asset protection trusts, and third-party trusts (TPTs), each of which is discussed

<sup>24</sup> For example, (1) a physician's office for treating patients, (2) a sleep clinic, (3) an eating disorder clinic, (4) a surgery center, (5) a vendor of medical supplies or equipment, and (6) the owner (landlord) of the office building where the doctor's offices are located.

<sup>25</sup> These formalities include but are not limited to (1) making annual filings and paying annual fees, (2) keeping proper documentation of business decisions, (3) not commingling business and personal assets, and (4) ensuring that the business is not undercapitalized.

<sup>26</sup> Trusts can provide additional benefits such as planning for incapacity, planning for surviving spouses, and financially protecting beneficiaries.

separately below. Keep in mind, however, that depending on state law, there may be restrictions on whether a professional practice (such as a medical professional corporation) can be owned by a trust.

### Domestic Asset Protection Trusts

In some jurisdictions, a settlor can establish a spendthrift trust **for their own benefit** as well as for other beneficiaries.<sup>27</sup> Such a trust is categorized as a self-settled spendthrift trust or DAPT, which is a common trust formed for asset protection purposes. The weight of authority is that self-settled spendthrift trusts are indeed valid trusts; however, the level of protection afforded to the settlor of a DAPT varies depending on the applicable state law. If the trust does not provide protection against all of the settlor's creditors, this lack of protection would not only apply to the settlor's present creditors but also to future potential creditors and for as long as the trust is in existence. Thus, at least in some jurisdictions, the "door to trust assets" remains open to creditors of clients who create a self-settled spendthrift trust. Therefore, in contrast to jurisdictions that recognize creditor protection for settlors of DAPTs, a judgment creditor would not need to resort to a fraudulent transfer (also known as a voidable transaction) theory or other claim to gain access to trust assets.

### Offshore Asset Protection Trusts

An offshore asset protection trust is designed to utilize a favorable foreign jurisdiction's statutes. It enjoys a well-established history of success and is typically harder for a creditor to breach than a DAPT. An offshore asset protection trust offers the following advantages:

- Increased ability for the settlor to retain benefit and control
- Lower likelihood of being an automatic target in litigation against the settlor
- Practical barriers such as the following that do not exist with domestic trusts will likely impact a creditor's decision about whether to pursue assets in foreign jurisdictions:
  - Lack of comity (meaning that a foreign court will not give force or effect to a United States court's proceedings and rulings that are contrary to the foreign jurisdiction's laws)
  - Heightened burden of proof required by the creditor

- Stricter and shorter statutes of limitations compared to most domestic jurisdictions
- Increased costs
- Legal counsel's unfamiliarity with offshore laws


### Third-Party Trusts

A TPT is a spendthrift trust created by a settlor for the benefit of an individual other than the settlor. Because TPTs are not self-settled trusts, TPTs are typically more straightforward and are often also used for other estate planning purposes, such as utilizing a client's gift and estate tax exemption. Numerous types of trusts are TPTs, including trusts created for children, grandchildren, and other relatives, but the type of TPT commonly used by high-risk professionals for asset protection is a spousal lifetime access trust (SLAT).

A SLAT is a trust—often a completed gift trust—that a settlor creates for the benefit of their spouse, with the remainder after the spouse's death typically held for the settlor's children and other descendants. Because SLATs are not self-settled, it is not necessary to form them in specific jurisdictions, which provides the settlor with additional flexibility when determining whom to name as the trustee.<sup>28</sup> A SLAT should not direct any mandatory distributions to any beneficiary; rather, a SLAT should provide the trustee with broad discretionary distribution powers to maximize the asset protection it offers. When these trusts are structured properly, the assets held in the trust are protected from the creditors of the settlor and the settlor's spouse, but the spouse can still receive distributions or benefit from trust assets if necessary.

SLATs are popular when creating a TPT for asset protection purposes, but most types of TPTs, if structured properly, offer significant asset protection. Thus, trusts created by a settlor for their children can provide asset protection benefits for both the settlor and their children, regardless of whether the trust is formed for that purpose.

### CONCLUSION

The asset protection strategies described above are not mutually exclusive. A carefully created and monitored asset protection plan may involve the use of several of these techniques. No one asset protection plan is optimal for all situations. Rather, an asset protection plan must be tailored to fit your client's particular profession and needs. 

27 As of the date of publication, less than half of US states have DAPT statutes, with Alaska, Delaware, Nevada, and South Dakota traditionally viewed as having particularly robust protections.

28 See, e.g., Colo. Rev. Stat. § 15-5-502 (2024) (detailing when spendthrift clauses are valid in the state of Colorado, which does not allow for self-settled spendthrift trusts).