ASSET PROTECTION PLANNING – THE BASICS

Asset protection planning is an essential component of estate and financial planning. Forms of ownership of assets as well as the utilization of trust vehicles are often considered with each type of planning. Similar to traditional estate planning which may involve planning to protect achieved wealth from some form of taxation, the concept of asset protection planning involves the protection of property and wealth prior to a lawsuit or claim. Proper asset protection plans may even provide incentive for settlements of lawsuits and claims and may possibly deter expensive and stressful litigation.

If you have purchased a form of insurance such as automobile, homeowners, umbrella or malpractice insurance, you have implemented a form of protection planning. But your insurance may not cover a full claim or your carrier may decide to no longer provide the coverage if too many or substantial claims have been filed against you. Therefore, in addition to purchasing proper insurance policies, other forms of asset protection planning should be considered. These may include how certain assets are titled, doing business within a corporate or limited liability entity form and relying on state statutes for protection and exemption from enforcement of claims. For example, spouses may title property in Maryland as tenants by the entireties and if property is titled in this way, a creditor of only one spouse may not attach this property. But the tenancy ends at the death of the first spouse and the protection is then lost. Forming a business or limited liability entity to protect the business owner's other personal assets not involved with the operation of the business against potential claims by clients or customers of the business is usually advised. However, with respect to asset protection purposes, business entities should only be used when conducting some type of profit generation business and should not be counted on to simply protect personal assets that are transferred into some type of business entity. Finally, assets invested in certain retirement plans (such as certain Section 401 plans), certain forms of life insurance and annuity contracts and IRA's receive protection from claims per Maryland statute. However, with respect to IRA's, the Maryland statutory exemption may be limited to only $1,000,000.00 by federal bankruptcy law and there is a possibility that an IRA that was inherited by you as a beneficiary (as opposed to an IRA which has been funded entirely by you) may be subject to creditor claims and not protected by Maryland statute.

Certain irrevocable trusts may be used to protect assets from creditors. This involves creating an irrevocable trust (meaning the trust cannot be revoked by the creator) and transferring assets to the trust. The person creating the irrevocable trust should not be the beneficiary of the trust in Maryland because the law may allow creditors to be paid the distributions from the trust that otherwise could have been made to the creator of the trust. However, in many cases, the creator of the trust may still be the trustee who manages and oversees distributions from the trust.

Regardless of the reason for creating asset protection plans, the plan cannot be used to defraud creditors. The planning should occur prior to a claim being presented or even before a potential claim could be threatened. Therefore, asset protection planning is important and a great time for its discussion is when you are creating an estate plan.