

Core & Advanced Asset Protection Planning (Part One)

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James M. Duggan is a principal of DUGGAN BERTSCH, LLC, a Chicago-based business, tax, estate and wealth planning firm comprised of attorneys and accountants. Jim's practice has concentrated principally on business and corporate law, and estate and wealth planning, primarily as they relate to closely held business interests and high net worth families. Jim's experience in the structuring and implementation of Family Offices, sophisticated tax planning, and asset protection planning strategies is nationally recognized, as is his role in the firm's development of a leading multidisciplinary planning protocol. In addition to giving frequent lectures and authoring articles in his areas of concentration, Jim also serves as a director on numerous for-profit and not-for-profit organizations.

Jim's educational background includes attaining a Bachelor of Science in Marketing from the College of Commerce and Business Administration at the University of Illinois at Urbana-Champaign (*Magna Cum Laude*), a Masters in Business Administration in Finance from the DePaul University Graduate School of Business (*Summa Cum Laude*), and a Juris Doctor from the DePaul University College of Law, where he was awarded positions on both the *DePaul Law Review* and *DePaul Business Law Journal*.

The Real Threat of Litigation



The Top 10 jury verdicts of the last few years are not only staggering in amounts, but also show that private clients are exposed:

- **2009 – Choi v. Marciano (July 28, 2009)** \$370M defamation verdict - A Los Angeles jury awarded a record defamation verdict of \$370 million, including \$25 million in punitive damages, to five former employees of Guess Jeans mogul Georges Marciano.
- **2008 - Cantu v. Flanigan, United States District Court for the Eastern District of New York, Case no. CV 05-3580** \$188M defamation suit - A New York City jury awarded \$188 million to a Mexican contractor who claimed the words of an American businessman severely damaged his reputation.
- **2007 – Barrak v. Report Investment Corporation (Nov. 28, 2007)** \$102.7 million negligent security case - A man was shot and paralyzed in the parking lot of a Miami strip club.

The Real Threat of Litigation (cont.)



- **2006 - Navarro v. Carrollwood Emergency Physicians – Florida** \$216.7 million in medical malpractice - A man suffered severe brain damage after an unlicensed emergency physician's assistant misdiagnosed his stroke as a sinus infection.
- **2005 - McKinney v. Bob's Barricades** \$164 Million negligence claim - Plaintiff was critically injured when hit by a car while walking his bike home. His mother sued the company that barricaded the sidewalk, thereby forcing him to walk along the road's shoulder.
- **2004 - Poliner v. Texas Health Systems - Texas (Aug. 27, 2004)** \$366 Million tortious interference – The plaintiff, a cardiologist, claimed his practice was ruined when three fellow doctors and a hospital worked together to suspend his privileges to perform heart procedures.

Role of Asset Protection in Estate Planning



- Asset Protection Planning is a critical component of estate planning.
- A new standard of care is emerging – may be malpractice not to inform clients of asset protection options.

Asset Protection Planning Process



Aside from acting in a manner that will avoid lawsuits, and carrying sufficient insurance, personal asset protection optimization has two principal components:

- 1) Maximizing Exempt Assets
- 2) Transferring Non-Exempt Assets to Asset Protection Vehicles

Exempt Asset Planning



Step #1:

Identify Exempt Assets in Your State and Maximize Those Assets

- Homestead Exemption
- Tenancy by the Entirety
- Qualified/Retirement Plans
- Insurance
- Annuities
- 529 Plans
- Etc.

Exempt Assets Planning – State Comparison



To receive a list of the laws for each state, please e-mail info@thewpi.org

	TENANCY BY THE ENTIRETY	HOMESTEAD EXEMPTION	IRA	ROTH IRA	STATUTE AND SPECIAL PROVISIONS	LIFE INSURANCE CASH VALUE	LIFE INSURANCE PROCEEDS	ANNUITY CASH VALUE and/or PAYMENTS	529 Plan
AL	NO	\$5,000 Ala. Code § 6-10-2.	YES	NO	Ala. Code § 19-3-1 100% for assets held in “qualified trusts.”	100% for insurance on self or spouse payable to self, spouse, or children. Ala. Code §§ 6-10-8, 27-14-29, 27-14-30	100% for insurance on self or spouse payable to self, spouse, or children. Ala. Code §§ 6-10-8, 27-14-29, 27-14-30	\$250/mo annuity payments in the aggregate. Ala. Code §§ 27-14-30, 27-14-32	NO
AK	YES	\$54,000 Alaska Stat. § 09.38.010	YES	YES	Alaska Stat. § 09.38.017	\$10,000 Alaska Stat. § 09.38.025	Up to wage exemption if beneficiary is insured’s spouse or dependent. Alaska Stat. § 09.38.030(e)(4)	\$10,000 cash value. Alaska Stat. § 09.38.025	YES
AZ	NO	\$150,000 Ariz. Rev. Stat. Ann. § 33-1101(A)	YES	YES	Ariz. Rev. Stat. Ann. § 33-1126	100% Ariz. Rev. Stat. § 33-1126A6	Up to \$20,000 if payable to surviving spouse or child. Ariz. Rev. Stat. § 33-1126(A)(1)	100% Ariz. Rev. Stat. § 33-1126A7	NO
AR	YES	UNLIMITED Ark. Code Ann. § 16-66-210 and Ark. Const. art. 9	YES	YES	Ark. Code Ann. § 16-66-220 In re Holt, 894 F.2d 1005 (8th Cir. 1990) holding that Arkansas statutory exemptions are invalid as they violate the Arkansas Constitution.	To the extent permitted by the Arkansas constitution (\$500). Ark. Code Ann. § 16-66-209; Ark. Const. Art. 9 § 2; In re Hudspeth, 92 Bankr. 827 1988; Federal Sav. & Loan Ins. Co. v. Holt, 894 F.2d 1005 (8th Cir. 1990)	Same as life insurance cash value	100% Ark. Code Ann. § 23-79-134; Walker v. Walker, 303 Ark. 34, 791 S.W.2d 710 (1990)	YES
CA	NO	\$50,000(Single) \$75,000(Family) \$150,000(65 or older) Cal. Civ. Proc. Code. § 704.730	NO	NO	Cal. Code of Civ. Proc. §704.115 Limited to the extent reasonably necessary for support.	\$9,700 single / \$19,400 married Cal. Civ. Proc. Code § 704.100	Death benefits exempt to extent reasonably necessary for support of debtor, spouse and dependents. Cal. Civ. Proc. Code § 704.100	Same as life insurance cash value if annuity contract considered “life insurance” and not “investment” In re Payne, 323 B.R. 723 (9th Cir. BAP 2005)	NO

Exempt Assets – State Law vs. Federal Law



Federal - Bankruptcy Code, 11 U.S.C. § 522, provides for the following exempt assets:

- ERISA Plans – 100% protected (§522(d)(12))
- SEP-IRA/Simple IRA – 100% protected (§522(d)(12))
- IRAs/Roth IRAs – protected up to \$1,000,000 (§522(d)(12))
- Homestead Exemption - \$20,200 (§522(d)(1))
- Life Insurance Cash Value - \$10,775 (§522(d)(8))
- Annuity Cash Value – exempt to the extent reasonably necessary for support of debtor/dependants (§522(d)(10)(E))

State - State exemptions will apply in a federal bankruptcy case if the state has “opted out” of the federal exemptions.

Exempt Assets - Inconsistencies



Due to inconsistencies between federal law and the various states laws, forum selection must be considered. Examples include:

- a) 529 Plans -
 - Federal (§541(b)) - \$5,000 protected if given within 2 years of filing; rest is protected.
 - Nevada (Nev. Rev. Stat. §21.090(a)) – fully protected.
 - Illinois – not protected.
- b) IRAs -
 - Federal (Bankruptcy Code §522(n)) - \$1,000,000 limit.
 - Illinois (735 ILCS 5/12-1006) – fully protected.
 - Maine – not protected.

Planning for Non-Exempt Assets



STEP #2:

When exempt asset planning is either a) not available, or b) not desirable, the remaining assets (the non-exempt assets) must seek protection from asset protection vehicles:

- Limited Liability Entities – LLCs, LLPs, LPs
- Asset Protection Trusts

(*Note: transferring assets to another person (e.g., spouse) is not a real option)

The LLC Advantage



LLCs are preferred over other entity choices for the following reasons:

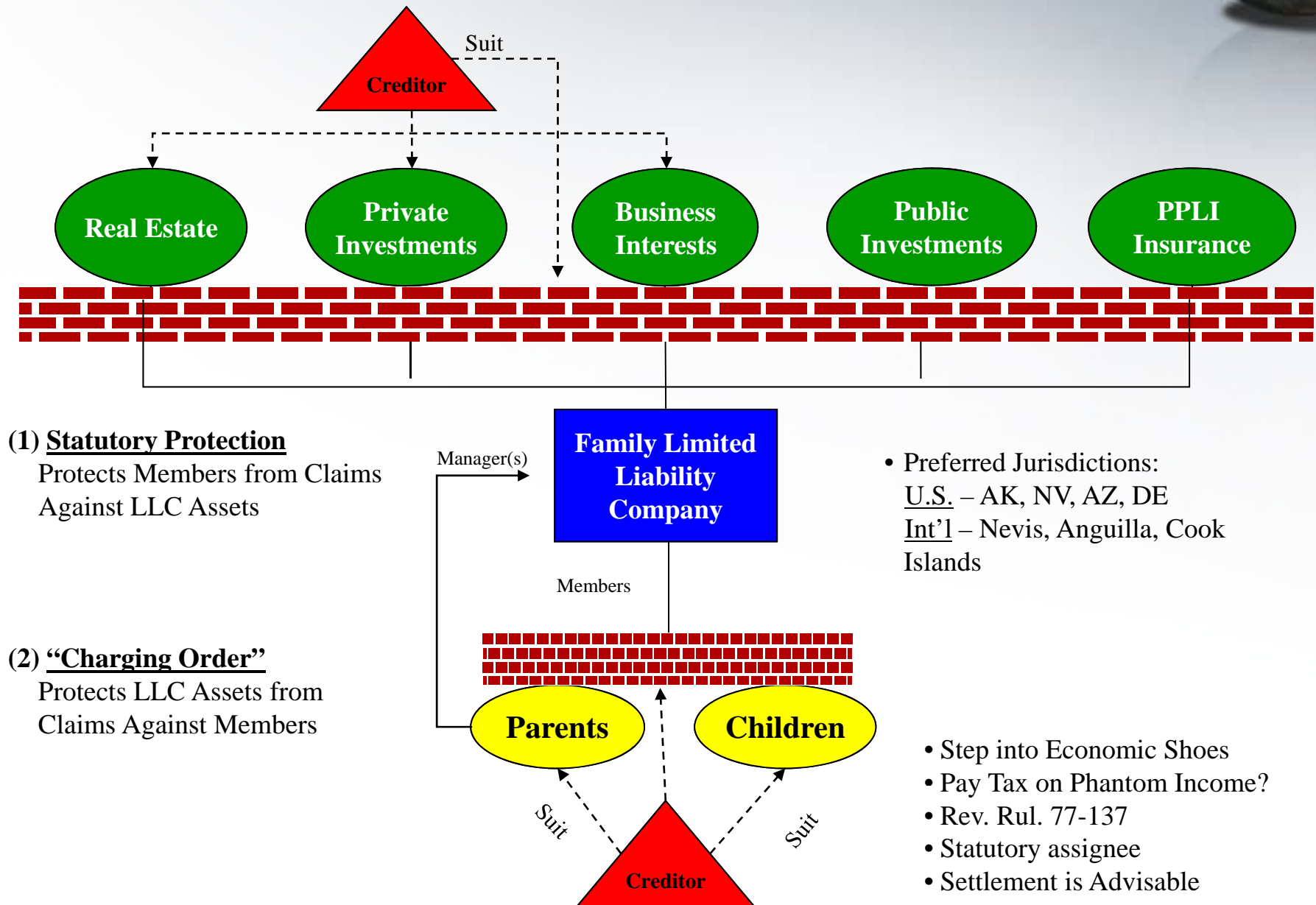
1) Greater Flexibility

- a) Drafting Options – e.g., limiting fiduciary duties
- b) Tax Treatment – “Check-the-Box”
- c) Allocations – income, loss, tax, etc.

2) Greater Asset Protection

- a) Charging Orders – a second level of asset protection
- b) Phantom Income Potential – Rev. Rul. 77-137; statutory assignee of full economic interest

Asset Protection with LLCs



Charging Order Statutes



1. Non-Exclusive Remedy Statutes – e.g., MI, CO
 - a) A court “**may**” charge the membership interest of a member
 - b) Either **allows other remedies or is silent** on the matter – e.g., judicial dissolution, judicial foreclosures, equitable remedies, etc.
2. Exclusive Remedy Statutes – e.g., AK, NV, Nevis, Cook Islands
 - a) A court “**may**” charge the membership interest of a member, plus,
 - b) This is the “**sole remedy**” available to creditors of a member

Charging Order Statutes - Michigan



Mich. Comp. Laws § 450.4507 (2009)

- On application to a court of competent jurisdiction by any judgment creditor of a member, the court **may** charge the membership interest of the member with payment of the unsatisfied amount of judgment with interest.
 - To the extent the membership interest is so charged, the judgment creditor has only the rights of an assignee of the membership interest.
 - This act does not deprive any member of the benefit of any exemption laws applicable to his or her membership interest.
- * No limitation on other remedies.**

Charging Order Provisions - Colorado



Colo. Rev. Stat. § 7-80-703 (2010)

- On application to a court of competent jurisdiction by any judgment creditor of a member, the court **may** charge the membership interest of the member with payment of the unsatisfied amount of the judgment with interest thereon and may then or later appoint a receiver of the member's share of the profits and of any other money due or to become due to the member in respect of the limited liability company and make all other orders, directions, accounts, and inquiries that the debtor member might have made, or that the circumstances of the case may require.
 - To the extent so charged, except as provided in this section, the judgment creditor has only the rights of an assignee or transferee of the membership interest.
- * No limitation on other remedies.**

Charging Order Provisions - Nevada



Nev. Rev. Stat. § 86.401 (2010) Rights and remedies of creditor of member

1. On application to a court of competent jurisdiction by a judgment creditor or a member, the court may charge the member's interest with payment of the unsatisfied amount of the judgment with interest. To the extent so charged, the judgment creditor has only the rights of an assignee of the member's interest.
2. This section provides:
 - a) the **exclusive remedy** by which a judgment creditor of a member of an assignee of a member may satisfy a judgment out of the member's interest of the judgment debtor.
 - b) Does not deprive any member of the benefit of any exemption applicable to his or her interest.

*** Charging Order is exclusive remedy.**

Charging Order Provisions - Delaware



Del. Code. Ann. Tit. 6, § 18-703 (2010)

1. On application by a judgment creditor of a member or of a member's assignee, a court having jurisdiction **may** charge the limited liability company interest of the judgment debtor to satisfy the judgment. To the extent so charged, the judgment creditor has only the right to receive any distribution or distributions to which the judgment debtor would otherwise have been entitled in respect of such limited liability company interest.
2. A charging order constitutes a lien on the judgment debtor's limited liability company interest.
3. This chapter does not deprive a member or member's assignee of a right under exemption laws with respect to the judgment debtor's limited liability company interest.
4. The entry of a charging order is the **exclusive remedy** by which a judgment creditor or a member or of a member's assignee may satisfy a judgment out of the judgment debtor's limited liability company interest.
5. The Court of Chancery shall have jurisdiction to hear and determine any matter relating to any such charging order.

* **Charging Order is exclusive remedy.**

Charging Order Provisions - Alaska



Alaska Stat. § 10.50.380: Rights of Judgment Creditor

1. If a judgment creditor of a limited liability company member applies to a court of competent jurisdiction, the court **may** charge the member's limited liability company interest for payment of the unsatisfied amount of the judgment.
2. To the extent a limited liability company interest is charged under (1) of this section, the judgment creditor has only the rights of an assignee of the member's interest.
3. This section provides the **exclusive remedy** that a judgment creditor of a member or a member's assignee may use to satisfy a judgment out of the judgment debtor's interest in the limited liability company. **Other remedies**, including foreclosure on the member's limited liability company interest and a court order for directions, accounts, and inquiries that the debtor member might have made, **are not available** to the judgment creditor attempting to satisfy a judgment out of the judgment debtor's interest in the limited liability company and may not be ordered by a court.
4. This section does not deprive a member of the benefit of an exemption applicable to the member's membership interest.

*** Charging Order is exclusive remedy plus other remedies are prohibited.**

Charging Order Provisions - Nevis



Nevis Limited Liability Company Ordinance, 1995, Part 7, § 43: Rights of Judgment Creditor

1. On application to a court of competent jurisdiction by any judgment creditor of a member of a limited liability company, the court **may** charge the member's interest with payment of the unsatisfied amount of the judgment with interest. To the extent so charged, the judgment creditor has only the rights of an assignee of the member's interest.
2. **Notwithstanding any other law the remedies provided by subsection (1) shall be the sole remedies available to any creditor of a member's interest.**
3. This Ordinance does not deprive any member of the benefit of any exemption laws applicable to his interest in the limited liability company.

*** Charging Order is exclusive remedy.**

Charging Order Provisions - Anguilla



Limited Liability Act, Interim Revised Statutes of Anguilla, Chapter 6, Part 7, § 47: Right of Judgment Creditor

1. On application to the Court by any judgment creditor of a member, the Court **may** charge the economic interest of the member with payment of the unsatisfied amount of the judgment.
2. To the extent so charged, the judgment creditor has only the rights of an assignee of the **economic interest**.
3. This Act does not deprive any member of the benefit of any exemption laws applicable to his member's interest.

*** Charging Order not exclusive, but limited expressly to “economic interest.”**

LLCs – Charging Order Case Law



For a comprehensive survey of case law applying charging orders in each of the 50 states, *see*:

Fifty State Series: LLC Charging Order Case Table (Dec. 2010)

Carter G. Bishop

Professor of Law, Suffolk University Law School

http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1565595

Single-Member LLCs – Case Law



- In re: Ashley Albright, 291 B.R. 538 (Bankr. D. Colo. 2003) – In the first SMLLC case, the Bankruptcy Court held that “in a single-member LLC, there are no non-debtor members to protect.”
- In re: A-Z Electronics, LLC, 350 B.R. 886 (Bankr. D. Idaho 2006) – “Debtor’s bankruptcy filing effectively assigned her entire membership interest to the bankruptcy estate, and the Trustee obtained all her rights, including the right to control...including decisions regarding liquidation of the entity’s assets.”

Single-Member LLCs – Case Law



- Cognex Corp. v. VCode Holdings, Inc. 2006 WL 3043129 (D.Minn., Oct 24, 2006) – court held that LLC was alter ego of parent and allowed suit against parents’ assets.
 - Dismissed application of traditional corporate alter ego analysis (e.g., corporate formalities, record keeping, commingling, etc.), stating, “Unlike a corporation, an Illinois LLC does not issue stock, does not appoint officers, and is not required to issues annual reports.”
 - It further noted that there was “no reasonable way” to distinguish between actions by officer/managers for the benefit of the single-member LLC or its parent.
- * Note: statements regarding Illinois law are actually incorrect.

Single-Member LLCs – Case Law



- Shaun Olmstead vs. federal Trade Commission, No. SC08-1009, June 24, 2010 –

In deciding not to issue a charging order, the court noted that:

- “[Florida’s] charging order provision established a nonexclusive remedial mechanism,” and,
- “there is no express provision in the statutory text providing that the charging order is the only remedy that can be utilized.

Lessons from SMLLC Cases



With much more case law to come, early lessons of SMLLC cases are:

- 1) Bankruptcy Courts will not issue charging orders with SMLLCs – a transfer to a BK trustee is a transfer of all rights;
- 2) Beware of a new and different application of the “alter ego” theory in each state; and,
- 3) Statutory language matters – and not just for SMLLCs (Olmstead is a call for legislatures to respond with express SMLLC exclusivity language).

SMLLC Statutes - Wyoming



Wyo. Stat. Amn. § 17-209-503 (2010)

1. This section provides the **exclusive remedy** by which a person seeking to enforce a judgment against a judgment debtor, **including any judgment debtor who may be the sole member**, dissociated member or transferee, may, in the capacity of the judgment creditor, satisfy the judgment from the judgment debtor's transferable interest or from the assets of the limited liability company.
 2. **Other remedies**, including foreclosure on the judgment debtor's limited liability interest and a court order for directions, accounts and inquiries that the judgment debtor might have made **are not available** to the judgment creditor attempting to satisfy a judgment out of the judgment debtor's interest in the limited liability company and may not be ordered by the court.
- * **Exclusive remedy; specifically prohibits other remedies; specifically includes SMLLCs.**

SMLLC Legislation – Cook Islands



Cook Islands Limited Liability Companies Act 2008, § 45: Rights of Creditor against a member

6. The charging order remedy given by this section shall be the **sole and exclusive remedy** available to a Creditor in respect of a member's membership rights.
7. For the avoidance of doubt and without limiting the generality of subsection (6):
...(d) **subsection (6) shall apply whether the limited liability company has a single member or multiple members.**

* **Sole and Exclusive remedy; specifically includes SMLLCs.**

SMLLCs – Dead or Alive?



- Not Dead, **developing**;
- Still appropriate as a **substitute for a sole proprietorship** (has nothing to do with charging orders);
- Use SMLLC **exclusive remedy** statutes only;
- Consider legitimate **grantor trust as second legal member**, but only one tax member;
- Consider **MMLLC owning multiple SMLLCs**; and,
- New **Proposed Regulations re: Series LLCs** make Holdco with SMLLC subsidiaries more likely.

SMLLC Statutes – Florida?



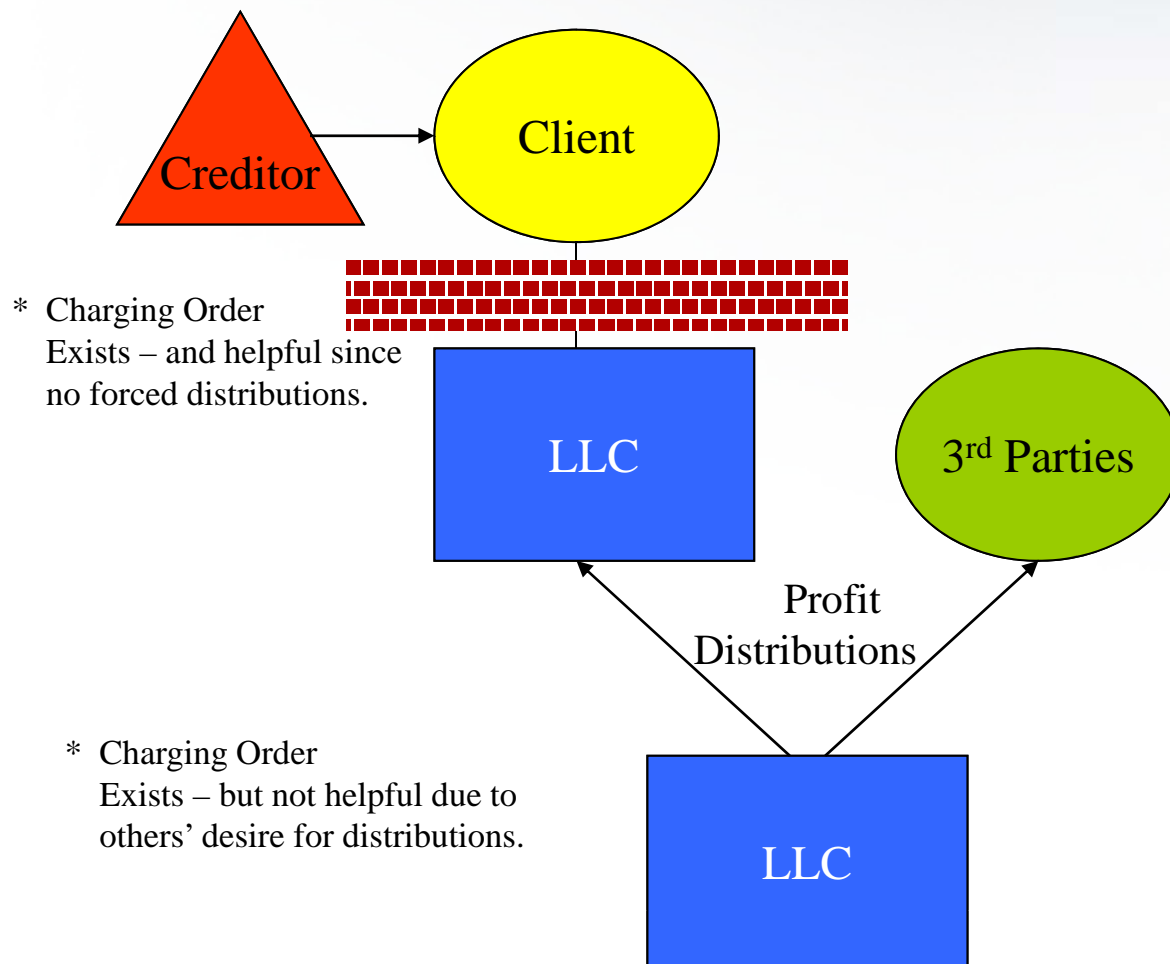
In response to Olmstead, Florida House Bill 253, which overwhelmingly passed both the House and Senate, has just been sent to the Governor. HB 253 provides, in pertinent part:

- 1) Charging orders are the “sole and exclusive remedy”;
- 2) Solely with respect to an SMLLC, a charging order is not the sole and exclusive remedy if anticipated distributions will not satisfy judgment within a reasonable time; and,
- 3) If foreclosure is ordered of an SMLLC, full membership interest is transferred and debtor is no longer a member.

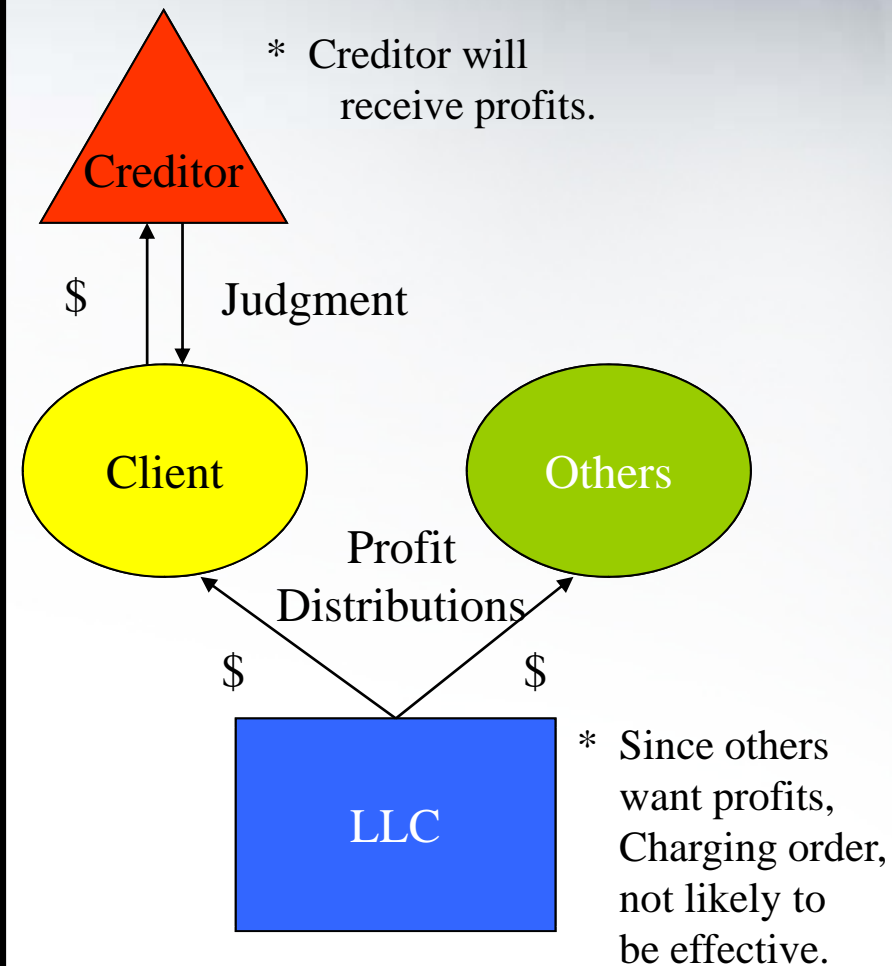
Sample LLC Planning Structures



“The Investment Holdco”



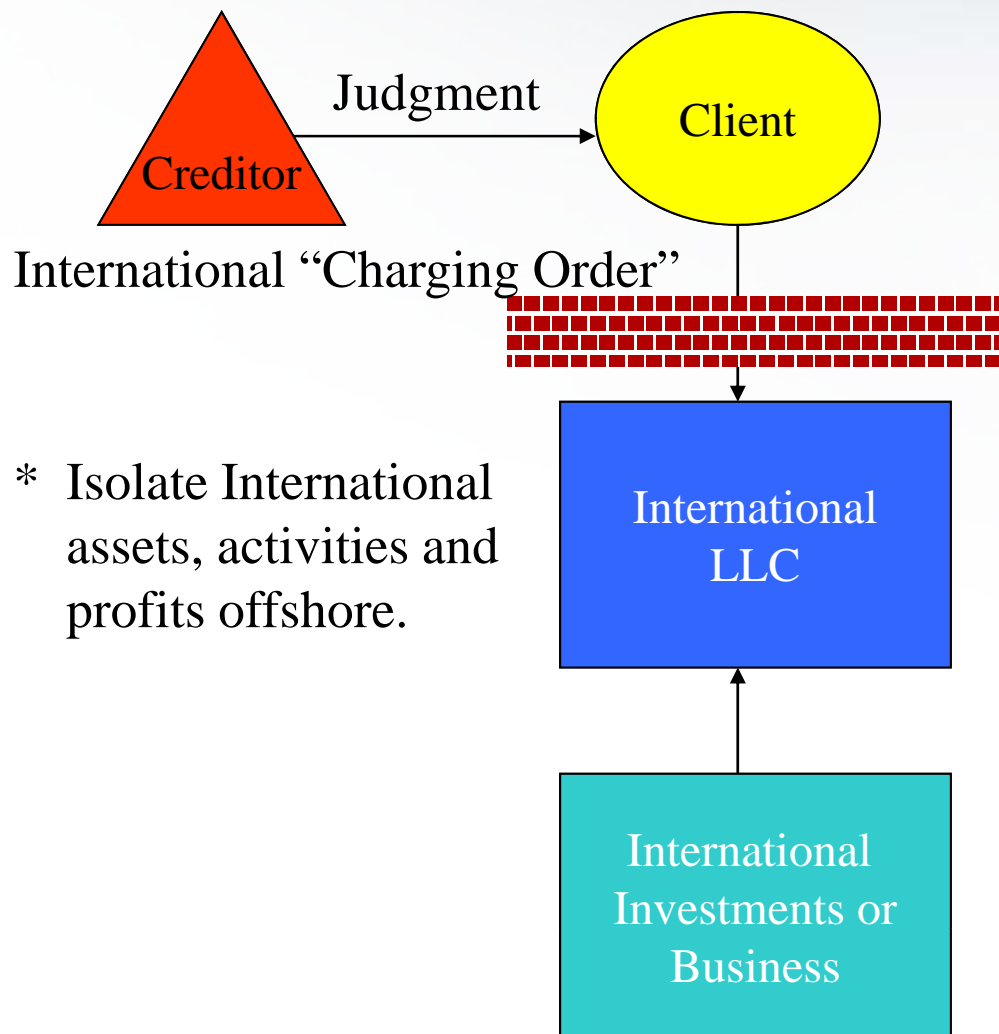
...without Holdco



LLC Planning Structures



“The Wholly International LLC”



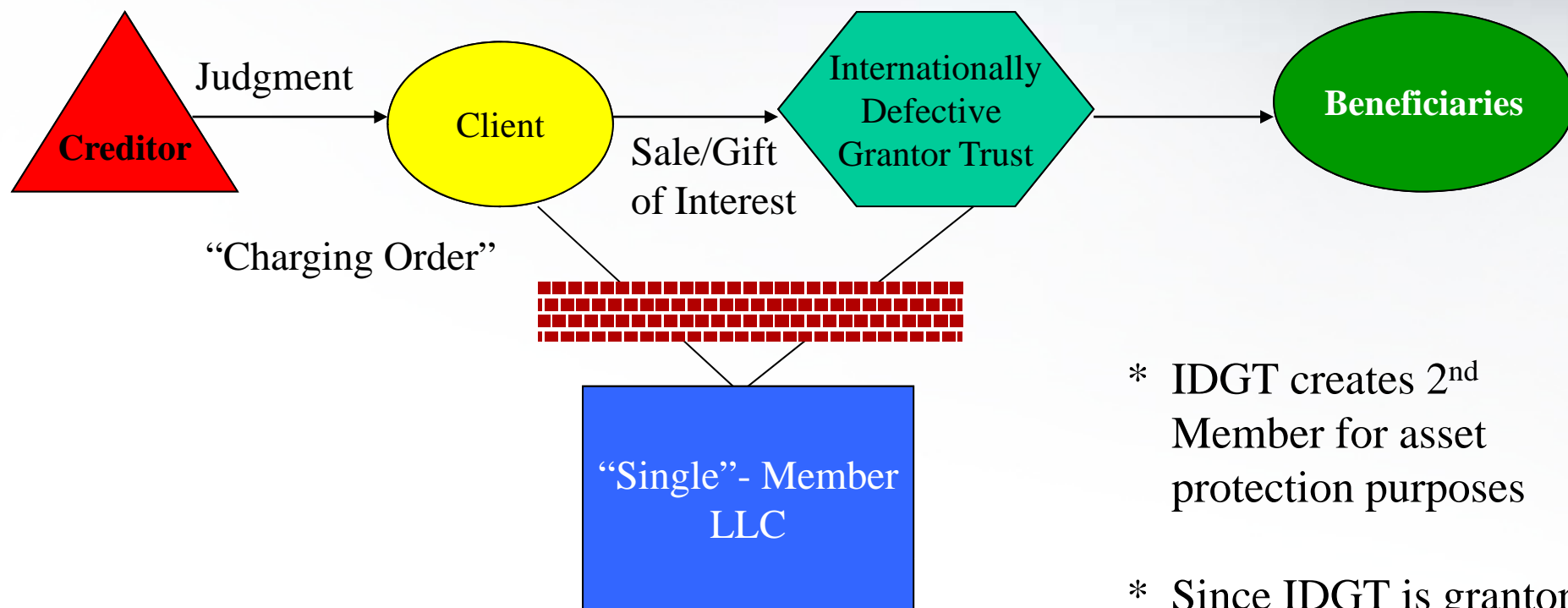
Avoid:

- a) International LLC owning U.S. attached assets
- b) U.S. LLC owning International assets

LLC Planning Structures



“The Multi-Member/Single-Member LLC”



- * IDGT creates 2nd Member for asset protection purposes
- * Since IDGT is grantor trust and treated as “the client” for tax purposes, LLC is taxed as SMLLC

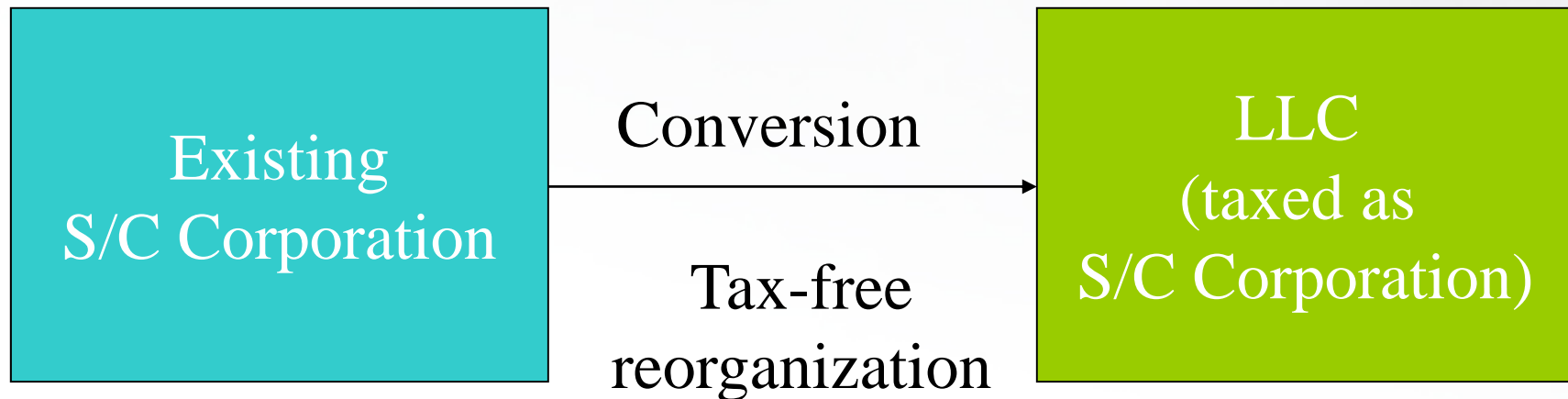
LLC Planning Structures



A) Corporate Conversions – Convert Corporation into LLC

* No Charging Order Protection

* Charging Order Protections

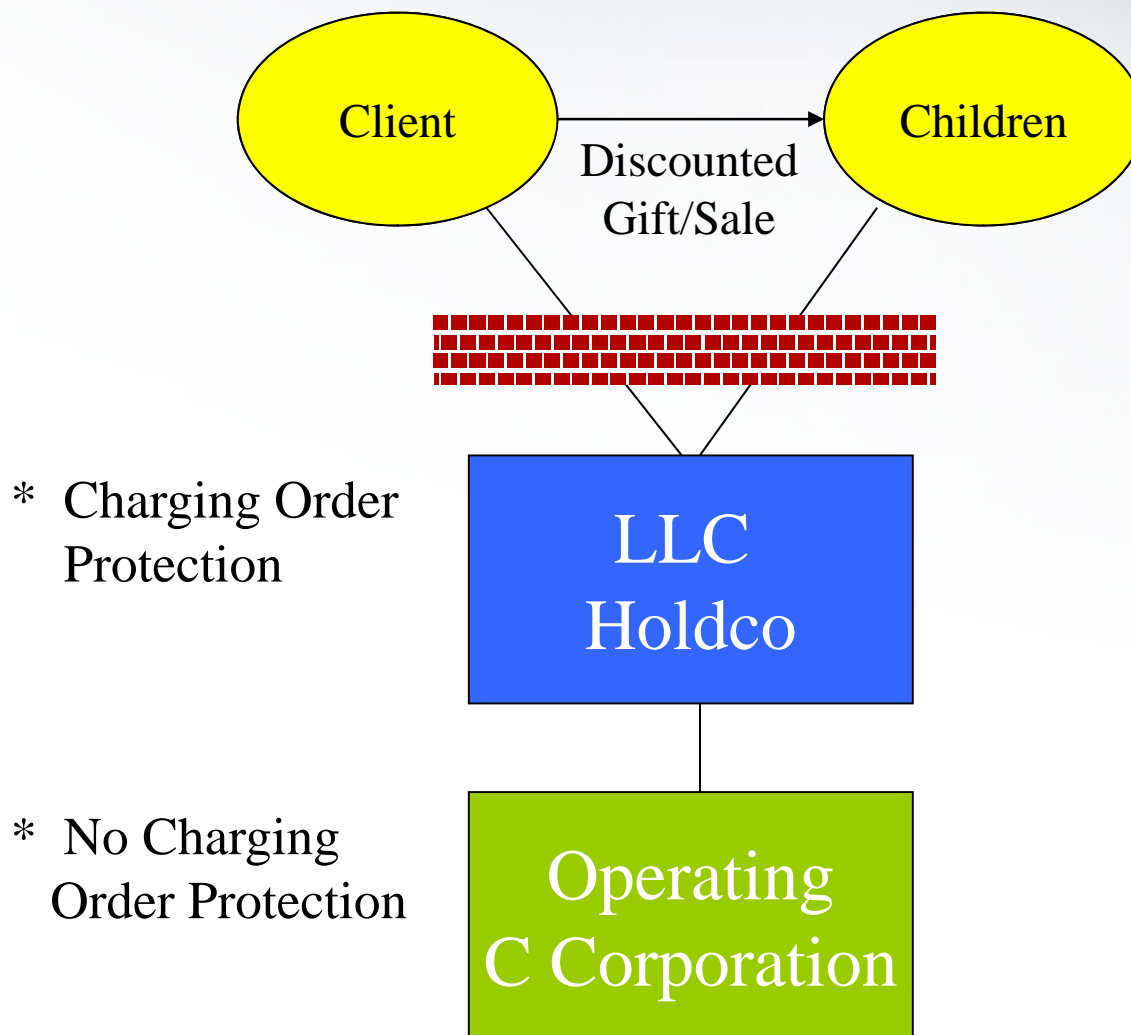


if maintain same tax status.

LLC Planning Structures



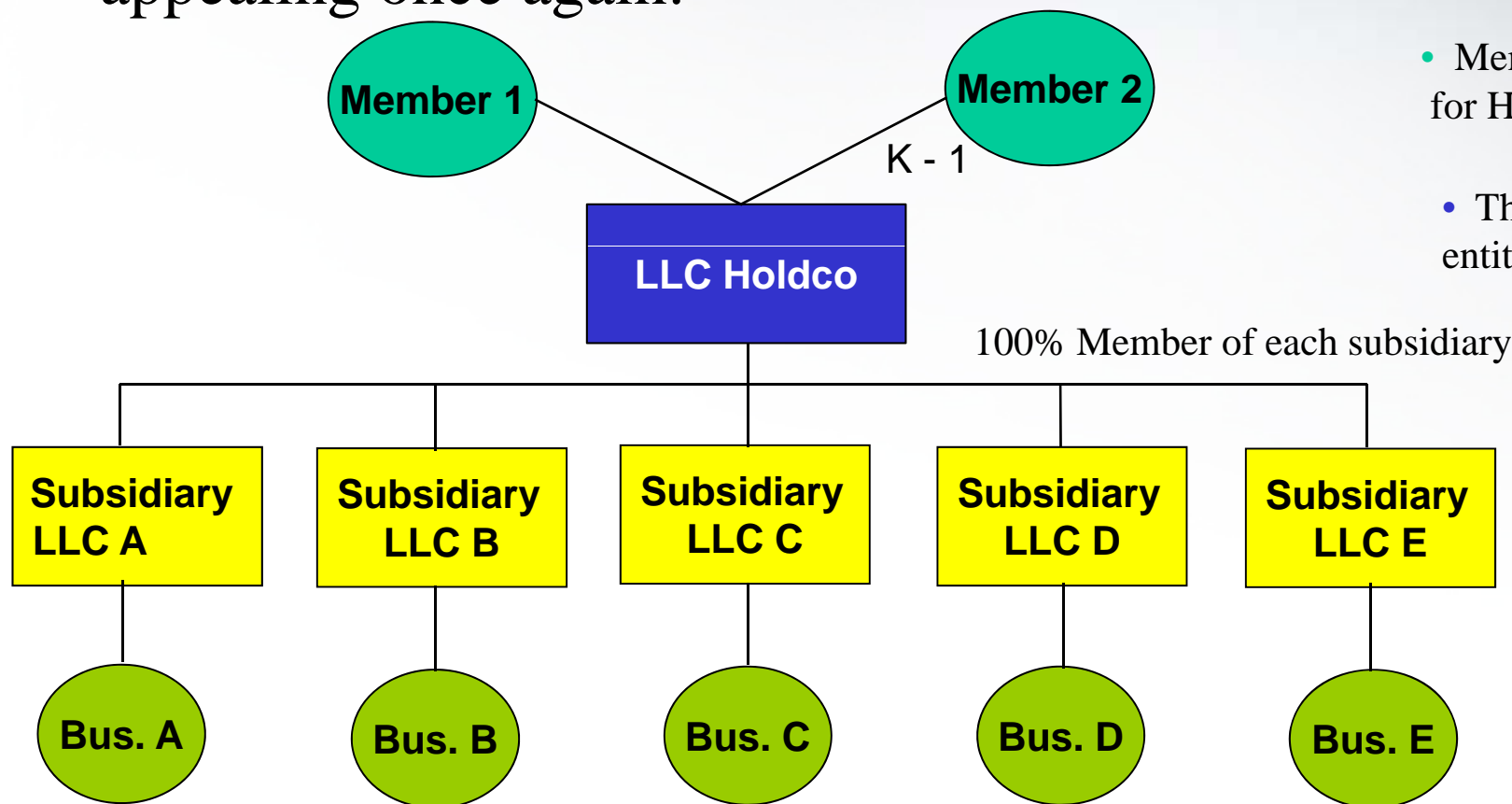
B) Corporate Conversions – Layer in LLC over Corporation



Series LLC/SMLLC Alternative – New Reporting Requirements



Proposed regulations make conventional LLC Holdco structure appealing once again:



- Members only get K-1s for Holdco

- This would be the only entity required to file

- Disregarded entities
- No tax reporting required

Questions?



- For general asset protection questions, please contact:
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 - Jim Duggan - jduggan@dugganbertsch.com