Asset Protection

Asset Protection For the Dental Practice

Dental practice owners are among those professionals who should provide that the accumulation of assets created by the practice are insulated from claims of creditors if there are successful business or other claims against the dentists which are not covered by insurance. It is for this reason that asset protection devices such as family limited partnerships, family trusts, or transfers of titles should be created to protect assets from those creditors.

A family limited partnership allows a parent or husband and wife as general partners in a family limited partnership to transfer assets to family members who are limited partners in the partnership to both save money on taxes and protect assets from claims of creditors. The limited partners would be in a lower tax bracket than the general partners and those assets are not included in the parents’ gross estate for federal tax purposes. Also, the transfer can be considered a gift to the children, and allow for the federal gift tax exclusion to come into effect.

The general partners in a family limited partnership can still have control over the assets even if they hold a minority interest in the partnership (even as low as say 5%). A creditor of a general partner, although it may obtain a charging order trying to take the assets of the general partner, cannot take direction and control of the partnership and cannot reach assets which are transferred by the general partner to the limited partner. The profits distributed to the general partners are allowed to be reached by the creditors, but a provision can be inserted into the partnership arrangement so that the partners are not required to make profit distributions to the general partnerships and can reinvest any profits into the partnership. There is a possibility that a state wage law exemption can allow for earnings to be distributed to a general partnership as wages as long as there is a reasonable management fee paid by the limited partnership to the general partnership.

When the creditor of a general partner obtains a claim over income distributed to it by a limited partner it must pay taxes on that distribution. It is thus to the creditor’s advantage to negotiate a settlement which is more advantageous to the partnership.

Another asset protection device is to transfer all assets to another person or entity without retaining any type of interest in the assets. A transfer to title to the assets can be made to a spouse less vulnerable to creditors, or a revocable trust can be created to allow for presumption of ownership of those assets to be in the less vulnerable spouse without control that comes with ownership. Also transfer can be made to a family limited partnership or children’s trust, and the parents can then borrow cash or assets from the trust or family limited partnership. In the case of a children’s trust, though, assets do belong to the children and would be ultimately distributed to the children. An irrevocable life insurance trust can be created which cannot be amended and which is beyond the reach of creditors. The premiums can be paid without gift tax liability.

A corporation may be set up to prevent creditors to reach the assets of the corporation that are in the form of stock that has been transferred to a trust. Maintaining the corporation does have the necessity of filing additional documents such as an annual report and keeping corporate minutes of actions such as payment of dividends, election of directors and officers’ bonuses.

It must be noted that in any asset protection move, there is the possibility of a transfer being struck down as a sham or fraud if it is too broad, such as in the case of a limited partnership agreement. The timing of the transfer is a major consideration in this kind of ruling, with a longer time before any legal claim that is established being of primary importance. Because of this, a transfer to a corporation or living trust may be preferable than to a family limited partnership. Judges are inclined to find reasons to get around statutes or rules that protect asset protection devices, and thus any transfer must be carefully drafted.