



# Family Legacy Protection Planner

## THREE LIABILITY PLANNING TIPS FOR PHYSICIANS YOU CAN USE TOO

The practice of medicine is a profession fraught with liability. It's not just medical malpractice claims either – employment related issues (wrongful termination, sexual harassment, and discrimination), careless business partners and employees, and contractual obligations (personal guarantees, leases, business agreements, etc.), coupled with personal liabilities (divorce, vehicular accidents, rental real estate), add to the increased risk assumed by a physician in private practice. Unfortunately, in our litigious society, these liability risks are not unique to physicians. A broad range of people, including business owners, board members, real estate investors, and retirees, need to protect their hard earned assets from a variety of liabilities too. In this issue you will learn:

- Types of liability insurance you need to have in place;
- State exemptions that will protect certain assets from the claims of creditors; and
- The role of business entities in liability planning.

### **Tip #1 – Insurance is the First Line of Defense Against Liability**

Liability insurance is the first line of defense against a claim. Liability insurance provides a source of funds to pay legal fees as well as settlements or judgments. Types of insurance you should consider include (as applicable):

- Homeowner's insurance
- Property and casualty insurance
- Excess liability insurance (also known as "umbrella" insurance)
- Automobile and other vehicle (motorcycle, boat, airplane) insurance
- General business insurance
- Professional liability insurance
- Directors and officers insurance

*Planning Tip #1:* You should not rely on insurance as your sole means of liability protection since the cost of a comprehensive policy may be prohibitive, and each type of policy has numerous exceptions to coverage. Instead, insurance should be used as one of a multiple layer of

strategies designed to place a barrier between your business and personal assets and the claims of a plaintiff. In addition, you should work with an insurance professional who can explain the purpose of each type of coverage, make recommendations for liability limits and deductibles, and shop around for the best coverage on an annual basis.

### **Tip #2 – State Exemptions Protect a Variety of Personal Assets From Lawsuits**

Each state has a set of laws or constitutional provisions that partially or completely exempt certain types of assets owned by residents from the claims of creditors. While these laws vary widely from state to state, in general you may be able to protect the following types of assets from a creditor seeking to enforce a judgment:

- Primary residence (referred to as “homestead” protection in some states)
- Qualified retirement plans (401(k)s, profit sharing plans, money purchase plans, IRAs)
- Life insurance (cash value)
- Annuities
- Property co-owned with a spouse as “tenants by the entirety” (only available to married couples; and may only apply to real estate, not personal property, in some states)
- Wages
- Prepaid college plans
- Section 529 plans
- Disability insurance payments
- Social Security benefits

*Planning Tip #2:* You will need to consult with an experienced asset protection attorney in your state to determine which state exemptions are available to you and how much can be protected. It is also important to understand the pros and cons of each type of exemption. For example, while tenants by the entirety co-ownership between you and your spouse may make sense in the short term, in the long run it can become completely useless if you divorce or after one spouse dies. As with liability insurance, exemption planning is best used as one layer of an overall asset protection strategy.

### **Tip #3 – Business Entities Protect Business and Personal Assets From Lawsuits**

Business entities include partnerships, limited liability companies, and corporations. Just like physicians who own their practice, business owners need to mitigate the risks and liabilities associated with owning a business. Business entities can also help real estate investors mitigate the risks and liabilities associated with owning real estate. The right structure for your enterprise should take into consideration asset protection, income taxes, estate planning, retirement funding, and business succession goals.

Business entities can also be an effective tool for protecting your personal assets from lawsuits. In many states, assets held within a limited partnership or a limited liability company are protected from the personal creditors of an owner. Depending on the type of business entity and the state of formation, the personal creditors of an owner may be prevented from taking over control of the business. Instead, the creditor is limited to a “charging order” which only gives the creditor the rights of an assignee. This is beneficial to the owners, because an assignee generally only receives distributions from an entity if and when they are made.

An added benefit of using a limited partnership or limited liability company to protect your personal assets is the leverage that can be created for gifting and wealth transfer planning through the use of valuation discounts. With a properly structured limited liability entity, assets held within the entity will be entitled to a discounted valuation for tax purposes because of lack of control, lack of marketability of the interests in the entity, and the inability of owners to simply to walk away from the business and take their ownership interests with them. Discounts on the value of the entity’s underlying assets can range from 20% to over 50%. Valuation discounts allow you to gift entity interests for cents on the dollar and at a reduced use of the lifetime gift tax exemption.

*Planning Tip #3:* Creating a business entity that protects your assets from lawsuits involves much more than just filing some forms with the state and paying an annual fee. Business formalities must be observed and documented; otherwise a creditor can attack the entity through “veil piercing” or “alter ego” arguments. In addition, state laws governing business entities vary widely

and are constantly changing due to legislative action and court decisions. Therefore, it is important to work with an attorney to properly chronicle business activities and modify governing documents as applicable laws change. Finally, as with liability insurance and state exemptions, business entities should be used in conjunction with other asset protection strategies.

### **Final Advice for Protecting Your Assets**

Liability insurance, exemption planning, and business entities should be used together to create a multi-layered asset protection plan. We are experienced with helping physicians, business owners, real estate investors, board members, and retirees alike create and maintain effective liability protection plans. Please call us if you have any questions about this type of planning and to arrange for your liability protection consultation.

## **ENSURE YOUR FAMILY IS PROTECTED**

If you want to ensure that your family is protected, please schedule your complimentary Estate Planning Strategy Call with San Francisco's premier estate planning attorney, Matthew J. Tuller.

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