



## **Worksheet Summarizing Asset Protection Techniques at the Practice Level**

This Worksheet is designed to provide an overview of the methods of protecting the assets owned by your medical practice (See the companion worksheet if you want more information on protecting your personal assets). It is intended to be used in conjunction with my book "The Asset Protection Guide for Florida Physicians" which provides a more detailed explanation of each technique, the upsides and downsides of each, and many traps for the unwary which are not presented in the overview chart below. The book is available for purchase at <http://www.KirwanLawFirm.com>. The chart set forth below gives a brief overview of the most common strategies used to protect practice assets, each strategy's primary upsides and downsides, and the price range you should expect to implement it. It is important to understand that the chart only provides a summary and should not be relied on alone. Remember that the asset protection techniques described below may not be effective if the creditor you wish to protect against has already been identified.

The process described below is designed to help you determine the most appropriate means of protecting your practice assets by first classifying each asset as either "Movable" or "Immovable." Next, you will examine the various means of protecting these assets paying close attention to each technique's upsides and, more importantly, downsides. Finally, you will examine the cost of each technique. Following these steps will give you a significantly better understanding of your options with respect to this important area of your comprehensive life planning.

### **Step 1 - Identify The Practice Assets.**

The obvious beginning point is to identify what assets are owned by your medical practice (for simplicity's sake I will refer to the legal entity housing the medical practice as the "PA"). It is recommended that you do this in writing. Once the list is complete, you will then go back over the list and classify each asset as either "Movable" or "Immovable." Movable Assets are simply assets that can be retitled (or "moved") to a person or entity other than the PA. Examples of Movable Assets are a building that houses the medical practice, medical equipment, furniture, computers, etc. Immovable Assets are assets that are difficult to move to another legal entity such as accounts receivable (I will refer to Accounts Receivable as "ARs"). I recommend placing the letter "M" in the margin next to each Movable Asset and the letter "I" in the margin next to each Immovable Asset.

**Step 2 - Consider Moving Movable Assets to a Separate Company.** The primary technique for protecting Movable Assets, is (as the name implies) simply to move the assets out of the PA to another legal entity (I'll refer to this as an "MA Company"). If this is done at a time when no creditor has been identified and no fraudulent transfer issues exist (see Chapter 5 of the "The Asset Protection Guide for Florida Physicians" for a discussion of the fraudulent transfer laws), if the PA is ever sued, the moved assets will not be subject to a judgement of the PA (since they are not owned by the PA). As mentioned in the chart below, there are usually costs associated with moving assets from one entity to another. If real estate is transferred, (i) documentary stamp tax is typically required to be paid (at the cost of \$7 per thousand dollars of fair market value of the transferred property), (ii) sales tax on the lease payments from the PA to the MA Company must be paid, and (iii) if the property was subject to a mortgage, the transfer must be approved by the lender and sometimes the property will need to be refinanced. This is why it is always best to purchase the property in an MA Company to begin with. If the PA has valuable movable assets (i.e., expensive medical equipment, etc.), then transferring them to an MA Company will usually make sense. If the movable assets are low enough in value (i.e., typical office furniture, computers, etc.) it often time does not make economic sense to create an MA Company to protect them unless an MA Company has already been established to protect other assets. Determine which assets (if any) are best suited to be transferred to an MA Company and circle them on your list.

### **Step 3 - Examine Other Available Techniques.**

The techniques other than creating an MA Company work by (i) creating liens on PA assets and/or (ii) creating the ability to remove assets from the PA leaving it valueless to a judgement creditor. The second option (discussed in more detail below and in the book) is oftentimes the best solution, since the creditor can be left with a judgement against an assetless entity and will then be left with the difficult task of having to try and collect from a new entity. This being said, the next step is to look at the upsides and downsides associated with each technique listed on the chart entitled Overview of Primary Asset Protection Techniques set forth below. I also recommend reading Chapter 20 of the "The Asset Protection Guide for Florida Physicians" in order to get a complete picture of the upsides and downsides associated with each technique since the chart simply is too small to give a complete understanding of everything you may want to know. After you have done this, cross out each technique that you feel has too many downsides (or even one big downside you feel is very distasteful).

### **Step 4 - Consider the Cost of Each Asset Protection Technique.**

Although cost is really just another downside associated with each technique, I feel it is important to address the issue of cost separately, mainly because some techniques have hidden costs that are not immediately apparent. You should focus on three separate cost elements; namely: (i) the initial cost of implementing the technique (e.g., legal expenses, etc.), (ii) the underlying cost of any "pieces" of the technique (e.g., interest cost associated with any loans, expenses associated with any insurance products, etc.), and (iii) the ongoing expense of maintaining the plan (e.g., sales tax on lease payments, additional legal expenses, costs, etc.). For example, if you decide to implement a technique that involves the use of insurance products to protect assets (which may make imminent sense under certain circumstances), make sure you understand the actual cost of doing so. The underlying mortality and administrative expenses associated with life insurance and annuity products typically range from 1% to 3% each year above and beyond what you would pay if those assets were invested outside the insurance product. That can equate to an additional annual cost of \$10,000 to \$30,000 for every \$1 million protected every year and there may be additional penalties if you wish to withdraw assets from the policy. Just make sure that you understand the underlying costs and penalties since they are oftentimes not readily apparent.

**Conclusion.**

After completing these four steps, you will be left with the asset protection techniques that have the greatest likelihood of balancing your desire for asset protection with your need for planning that takes into consideration the asset structure of your practice, the personal preferences of the practice owners, the practice owners' personal sensitivity as to cost, and the practice owners' personal view as to each technique's downsides. More importantly, you will understand why these techniques are best suited for your practice and you will be armed with sufficient information to intelligently discuss asset protection planning with your attorney. You will also want to incorporate each practice owners' personal asset protection planning into your practice plan to ensure that all the owners' needs are being adequately met and will continue to be met over time.

**Overview of Primary Asset Protection Techniques**

	#1	#2	#3	#4	#5	#6	#7	#8	#9	#10	#11	#12
	Move Assets to MA Company	Straight Bank Loan	Bank Loan to Shareholders	Bank Loan / Insurance Structure	Factoring Account Receivables	Immovable Assets Pledged as Collateral for Building Loan	Secured Lease Agreement with MA Company	Secured Severance Pay Package	Convertible Deferred Compensation Plan	Fund Pension Plan in Arrears	Establish a Management Company	Partner Loans
<b>General Explanation</b>	Movable Assets can be moved to another legal entity (e.g., an LLC, LLP, etc.) and placed outside the reach of the PA's creditors.	Money is borrowed by the PA from a bank and the PA's assets (including the ARs) are pledged as collateral for the loan. Loan proceeds are then paid to shareholders in the form of salary or distributions.	Money is borrowed directly by the shareholders from a bank and the PA's assets (including the ARs) are pledged as collateral for the loan as an employee benefit.	See explanation below.  <b>THIS IS NOT A TECHNIQUE I RECOMMEND</b>	The PA's ARs are sold to a factoring company or bank in exchange for cash which is then distributed to shareholders.	If building housing medical practice is held in a separate entity, the PA would pledge ARs and other PA assets as primary collateral under existing building mortgage.	If building housing medical practice is held in a separate entity, the lease between the PA and the MA Company can be drafted to create a lien on the ARs in the event the PA ever defaults on the lease.	Each physician owner of the PA has an employment agreement that provides for a severance package equal to a formula determined by the PA owners secured by the PA's assets.	A loan is secured by the PA and the loan proceeds are held in a special type of deferred compensation plan established by the PA. If the PA is sued, the plan converts to a protective type of retirement plan.	If the PA has an established retirement plan, the PA can wait to make its annual contribution until after the end of the tax year. If the PA is sued, the PA can use practice assets to pay this legal obligation.	The PA establishes a separate management company that leases employees and provides other services to the PA. The agreement between the PA and the management company is secured by the PA's assets.	If the PA needs additional capital, have the owner make secured loans to the PA rather than make capital contributions.
<b>Primary Upsides</b>	Assets can be leased to PA and are, therefore, available for use by PA but beyond a creditor's reach.	Very Protective because third party has a valid lien on the PA assets. Loan proceeds can be protected in the physicians' personal asset protection plan.	Very Protective because third party has a valid lien on the PA assets. Loan proceeds can be protected in the physicians' personal asset protection plan.	Very few. The asset protection offered by this technique is marginal at best.	Accelerates the collection of ARs.	No additional cost since interest expense under building loan is already being paid and lien encumbers PA's assets.	If properly structured, protection offered is relatively strong. Offers a method to remove assets from PA once law suit is brought.	If properly structured, protection offered is relatively strong. Offers a method to remove assets from PA once law suit is brought.	If properly structured, protection offered is relatively strong. Relies on protection offered by certain retirement plans.	No additional cost to the PA. Very protective.	If properly structured, protection offered is relatively strong. Offers a method to remove assets from PA once law suit is brought. Can strengthen the argument that a judgement against the PA cannot be enforced against a new medical practice for reasons discussed in the book.	Asset protection is low to moderate depending on when and how the PA is dissolved and the loans are paid off by the PA. Offers a method to remove assets from PA once law suit is brought.

	#1	#2	#3	#4	#5	#6	#7	#8	#9	#10	#11	#12
	Move Assets to MA Company	Straight Bank Loan	Bank Loan to Shareholders	Bank Loan / Insurance Structure	Factoring Account Receivables	Immovable Assets Pledged as Collateral for Building Loan	Secured Lease Agreement with MA Company	Secured Severance Pay Package	Convertible Deferred Compensation Plan	Fund Pension Plan in Arrears	Establish a Management Company	Partner Loans
<b>Primary Downsides</b>	Cost to establish new entity. Possible documentary stamp tax on transfer of real estate. Sales tax on lease payments between the PA and the MA Company.	Potential negative tax consequences on distribution of loan proceeds. Banks will not loan full value of receivables. Valuation of the practice is a must since a distribution to owners that render the PA insolvent could create liability to the owners under a corporate "claw-back" law and/or under the fraudulent transfer laws.	Potential negative tax consequences due to pledge of PA's assets as collateral for physician's personal loan. Banks will not loan full value of receivables. Potential for economic loss to PA if physician leaves and does not pay off personal loan.	Numerous downsides, including: (i) very expensive when all costs are considered, (ii) asset protection is poor, (iii) potential negative tax consequences, and (iv) the "claw-back" problem mentioned under #2.	Not very protective since new ARs must be continually sold. The distribution of cash from the PA after a law suit could be considered a fraudulent transfer. Cost of factoring ARs can be expensive.	Moderate protection since the mortgage holder will most likely have collateral in excess of the loan amount. In this case, the court may order the mortgage holder to foreclose on the real estate before going after the ARs or other collateral. Only protects assets up to the amount of the mortgage.	The technique can only protect a defined amount of assets. If the ownership of the Leasing Company and the PA are identical, the level of protection is lessened.	The secured person is an owner of the PA which raises fraudulent transfer issues, however, at least one case has held that the payment of a prenegotiated severance package is not a preferential payment under bankruptcy laws.	The technique is sophisticated and must be implemented by attorneys with a keen understanding of the laws governing pension plans.	The technique can only protect a defined amount of assets.	Cost to establish new entity. Sales tax on lease payments between the PA and the MA Company. Certain complexities associated with employee leasing.	Paying back loans after a law suit is brought may be considered fraudulent transfers. Interest on loan(s) is a cost to the PA and will economically benefit owners making the loan(s) to the exclusion of those owners who do not.
<b>Type of Asset Protected</b>	Movable Assets	Movable and Immovable Assets	Movable and Immovable Assets	Movable and Immovable Assets	Movable and Immovable Assets	Movable and Immovable Assets	Movable and Immovable Assets	Movable and Immovable Assets	Movable and Immovable Assets	Movable and Immovable Assets	Movable and Immovable Assets	Movable and Immovable Assets
<b>Cost Range (the price range is an average and may be more or less based on complexity of planning).</b>	Cost for new entity: \$2,000 to \$4,000	Moderate to Expensive. Interest cost. If the net rate is 5%, then the cost is \$50,000 per million dollars protected, EACH YEAR. Tax cost on distributions or compensation.	Moderate to Expensive. Interest Cost. If the net rate is 5%, then the cost is \$50,000 per million dollars protected, EACH YEAR. Potential tax cost on distributions or compensation.	Expensive. Set up fee by company offering this "service." Interest costs. Potential tax costs. Insurance costs.	Expensive unless the practice has a legitimate need for accelerating the collection of ARs.	Inexpensive since the mortgage interest is already an expense of the leasing company.	Inexpensive. The only real cost is the modification of the lease agreement.	Inexpensive. The only real cost is the modification of the employment agreements.	Moderately expensive. Price will range based on various factors unique to the PA.	Inexpensive.	Moderately expensive.	Moderately Inexpensive. Legal costs to draft secured notes and interest costs.

The above chart is designed to give an overview of many, but not all, methods of protecting medical practice assets from the claims of judgement creditors. Greater asset protection is oftentimes obtained by combining techniques and/or using techniques beyond the scope of this Worksheet. In addition, much of a plan's overall effectiveness stems from the manner in which the documents are drafted, how the plan is implemented, and post-law suit decisions made by the practice owners. Many legal documents I have reviewed offer very little protection because the attorney or planner did not fully understand the nuances of the technique or the oftentimes hidden traps for the unwary. Please ensure the person you choose to implement your practice's asset protection plan can fully explain the upsides and downsides of the recommendations they are making (and there is always a downside) and intelligently integrates it with the owners' asset protection, estate, and financial planning. If you do not understand a technique's downsides, you should not implement it as part of your planning.

**ADDITIONAL NOTES AND CONSIDERATIONS.**

**The Option of Creating a New Practice.**

Many of the techniques described above will be most effective if the existing PA is wound down and liquidated before a final judgement is handed down against the PA and then having the physicians form a new PA to practice medicine. Below is an example from my book.

Assume Dr. Jones, Dr. Smith, Dr. Anderson, and Dr. Geidvilaićiai, are all partners in Advanced Medical Specialists, PA (“AMS”). Dr. Smith is named in a medical malpractice law suit together with AMS due to alleged medical malpractice with respect to Patient X. AMS’ only real assets are furniture and computers with nominal value, patient records, and accounts receivable. The average collectable accounts receivable are \$500,000.

In the event Patient X is successful in obtaining a judgement against AMS, he will be able to reach AMS’ assets in satisfaction of the judgement, including the accounts receivable. If the judgement was significant enough, for all practicable purposes, AMS would be put out of business.

Assume further that the physician owners of AMS have consulted with their attorney and feel that there is a substantial risk that they could lose the law suit and that if they did, the judgement could easily exceed \$1,000,000.

The four physicians have used some of the techniques discussed above and decide the best course of action is to wind down the business of AMS before Patient X obtains a judgement and remove the assets of AMS using the chosen asset protection techniques. Patient X will then be left with a judgement against AMS which by then has no assets. If AMS is properly liquidated and a new medical practice is created, the judgement will be difficult to impossible to enforce against the new medical practice.

I want to point out that when a business is wound down like this, there are different means of removing value from the business. Some of them are legally defensible and others are not. The issues the business owners will face are based on a combination of the corporate laws, fraudulent transfer laws, and bankruptcy laws, all of which will be very technical in nature. That being said, this endeavor is not something that anyone should attempt without the aid of competent legal counsel. This typically will mean involving an asset protection attorney, a corporate attorney, a tax attorney, and a bankruptcy attorney. Anyone who attempts an undertaking like this on their own will almost always end up with substantial negative results. If you are ever faced with a situation like this, do yourself a favor and utilize professionals who understand these areas of the law.

**Problems With the Bank Loan / Insurance Structure.** There is an “accounts receivable protection strategy” utilizing a bank loan and life insurance products that is being heavily marketed to physicians. It is my opinion that this strategy will most likely not be protective and has many potential downsides which are not being adequately explained by its promoters.

The technique starts with a bank lending money to a medical practice with the medical practice pledging their accounts receivable as collateral for the loan. As mentioned above, one of the problems facing a medical practice using a bank loan to lien accounts receivable will be how to get the money out to the PA’s owners without causing the amount distributed to be subject to federal income tax. This technique attempts to solve that problem by having the physicians establish a deferred compensation plan. After the medical practice receives the loan proceeds from the bank, it purchases life insurance or annuity products (I will call these the “Insurance Products”) and then distributes these Insurance Products to the physicians as part of the deferred compensation plan. The cash value in the Insurance Products are pledged to the bank as additional collateral for the loan it made to the medical practice. This is a down and dirty explanation of the technique and there are several variations being promoted. All of them, however, have the same significant downsides.

First, from an asset protection standpoint, you have an over collateralized creditor (i.e., the bank) so it is very likely that a judge would order the bank to collect its loan against the Insurance Products rather than the accounts receivable. Second, if that does happen, it is likely to trigger surrender penalties in the Insurance Products resulting in an economic loss to the physicians. Even if you are told that the Insurance Products have low or no surrender penalties, since a commission is being paid to the person selling the Insurance Products and all insurance policies and annuities have internal expenses, it is not possible to get back all of the money placed in these Insurance Products until several years down the road and then only if the investments in the Insurance Products perform admirably (which they may not). Third, and of significant importance, is the fact that the non-taxability of the Insurance Products distributed under the deferred compensation plan is based on something called a “significant risk of forfeiture.” I do not want to get into a long discussion of the tax rules that apply to deferred compensation plans, however, the “significant risk of forfeiture” that this technique depends on to keep the distributed Insurance Products from being taxable is not directly supported by the Internal Revenue Code but rather by an aggressive interpretation of a “catch all” provision. If the promoters are wrong in their interpretation, all of the money in the Insurance Products will be taxable to the physicians receiving them. The physicians will then have to come up with the money to pay the tax, but wait, the money is all tied up in the Insurance Products. Once again, we are back to the surrender penalty problems. Finally, as mentioned above, unless the loan proceeds are properly removed from the PA, the corporate “claw-back” laws could leave the PA owners personally liable for a judgement against the PA.

In short, this technique is great if you are the one collecting the commission on the sale of the Insurance Products, but for the physicians involved it is a losing proposition. Note that some promoters are telling physicians that the plan has been tested and has passed IRS scrutiny. They are referring to one small aspect of the plan, however, the real issue (i.e., the “significant risk of forfeiture”) has not been tested to the best of my knowledge. If someone tells you that it has, I would verify their alleged success directly with the IRS.

**Problems with the Line of Credit Strategy.** Many physicians are under the false impression that they can obtain a line of credit secured by the accounts receivable of their medical practice and that this will protect the assets of the practice. This is simply not the case. Since the balance due on an unexercised line of credit (i.e., a line of credit that the medical practice has yet to use to borrow money) is zero, none of the collateral (i.e., the accounts receivable) are subject to a true lien. If the line of credit is exercised after the creditor is identified (which a bank may not be willing to do if it knows of the law suit or potential creditor, which you typically have a legal obligation to disclose), the money will be paid to the practice and, therefore, will still be subject to the claims of the creditor. If the money is paid to the owners (i) there will be income tax implications, and (ii) the transfer of money to the owners will most likely be considered a fraudulent transfer. If that is the case and the transfers are “unwound”, the physicians’ income tax liability will most likely not disappear. Therefore, the physicians will have personal tax liability and a balance due and owing under the line of credit which the physicians will most assuredly be personally liable for under the personal guarantees the bank typically asks for.