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In Depth: Asset Protection Planning

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May 2009

Asset Protection involves a variety of legal techniques that can be used to protect assets of individuals and businesses. Asset protection planning is receiving increasing attention due to the great number of lawsuits filed each year in the United States; current economic conditions; recent high profile business failures; the recent wave of foreclosures; and the rising number of bankruptcy filings. Most of us spend a lot of time trying to accumulate assets but very little time protecting the assets we have. Here are a few standard asset protection strategies (most of which also make sense for general economic and tax reasons):

Maximize Contributions to IRAs and Qualified Plans

Assets in IRAs and qualified employee benefit plans are generally afforded special protection from creditors. Qualified plan assets are also protected in bankruptcy because they are not part of the bankruptcy estate. The Bankruptcy Act of 2005 protects IRA assets up to $1 million, adjusted for inflation.

Divide Assets Between Spouses

Simply dividing assets between spouses may offer some protection from creditors, and can also be important in some situations for estate planning reasons.

Life Insurance

Life insurance is frequently part of an asset protection plan. In many states life insurance death benefits and/or cash values are exempt in whole or in part from claims of creditors of the insured. In Ohio, for example, insurance death proceeds are exempt by statute if paid to the spouse, children, or certain other designated beneficiaries.

Trusts

Not all trusts provide asset protection; but some do. At least ten states have enacted asset protection trust legislation. These state statutes generally require that a trustee in that state have discretion in making payments to the person who established the trust. Most of this legislation has not yet been tested in the courts. We continue to monitor developments with respect to these so-called asset protection trusts.

Irrevocable life insurance trusts (ILITs) can be a great estate planning tool under the right circumstances, and they provide significant asset protection. Life insurance owned by an ILIT is not generally part of the insured's estate (for both federal and Ohio estate tax purposes). If the ILIT is formed properly, creditors of both the person who establishes the trust and the beneficiaries should have no rights in either the cash value or the death benefits of the insurance. Assets of an ILIT should also generally be immune from claims in a divorce.

So-called "dynasty" trusts are designed to maintain assets in trust through a number of generations. One of the advantages is that the assets in the trust are generally beyond the reach of creditors of the beneficiaries in the event of divorce, court judgments and other financial difficulties.

Many other types of trusts include so called "spendthrift" clauses which limit the rights of creditors to reach the assets of trust beneficiaries.

While there are more exotic asset protection alternatives (including offshore trusts), many basic strategies are relatively inexpensive and easy to implement. Your current will, trust and related estate planning documents should be reviewed periodically with a specific view toward asset protection considerations. While certain asset protection strategies can properly be utilized after a problem arises, it is far better to act before any claim is made.

For those interested in a more detailed discussion of asset protection strategies, please refer to the article on our website at www.ssrl.com. Click on "Library" and go to "2008 Business Presentation - Asset Protection".

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