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The plight of the new poor

Once only a concern for physicians, asset protection planning is needed by builders, auto dealers

By Carol Lundberg

If Howard B. Young didn't read a single newspaper, he'd still know that something was terribly wrong with the economy.

He would know because the profile of his client is changing dramatically.

For decades, the asset-protection attorney has served a certain type of client: doctors, particularly obstetricians, who can get only about $200,000 worth of insurance coverage, not nearly enough to cover their massive exposure to catastrophic claims. Without some protection, each faces being wiped out by a single lawsuit.

During the past year, a new category of clients has been calling Young, of Weisman, Young & Ruemenapp PC in Bingham Farms. They are home builders and car-dealership owners hoping to salvage some of what they have earned.

Young specializes in structuring client assets and in setting up offshore and spendthrift accounts and trusts to keep creditors from cleaning out his clients' personal bank accounts. He helps them legally squirrel away protected assets in trusts in Delaware, Alaska, Missouri, Rhode Island and Montana. (See "Safe off shore," opposite.)

"Most people don't think at all about asset protection, especially when times are good," Young said. "But recently, I've been getting an onslaught of people who are in trouble. They've already been hit."

Everyone is vulnerable, said Geoffrey L. Silverman, of Silverman & Morris PLLC in West Bloomfield.

"Developments in the marketplace have upset everything," said Silverman, who specializes in bankruptcy and insolvency matters. "There is an increase in the type of clients who are now worried about if the sky falls."

One of Young's clients is the typical businessperson he has been seeing regularly.

The client is a successful home builder. His father also was a reputable and wealthy home builder now comfortably retired.

But houses aren't selling, nor are the lots in his company's holdings. And the client made the No. 1 mistake builders make: He personally guaranteed his business debt.

He fears ruin is imminent.

That personal guarantee means business creditors can come after family assets.

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"These are wealthy people who were well-respected. They were philanthropists. They had esteem in the community. And now they're going to be broke, really broke … They're facing the most emotionally difficult time in their lives, at least when it comes to their finances."

— Howard B. Young, Weisman, Young & Ruemenapp

Truth is, the client never thought much about personal guarantees. It's the way he had always done business; he thought he was safe, Young said.

"Even in 2006, before there were really big problems on the horizon, he got appraisals from the bank, and the banks valued his 15 active large subdivisions for $100 million," Young said.

He had loans that totaled $70 million.

"So then he could say that he has $30 million in equity, and has no risk."

But today, because the land is not selling, no one knows what it is worth. Some investors, known in real estate circles as "vultures," buy properties late in the foreclosure process, when their values are severely depressed. Even if such a buyer offers as much as $20 million, the gap between what the client owes and what the buyer will pay is $50 million, Young said.

"The lenders are saying there's no collateral, so pay up," Young said. (See "Looking for the nut the debtor squirreled away," next page.)

Most clients in the builder's shoes would work with bankruptcy attorneys to minimize the fallout, mainly because they're unaware that they could protect some of their assets, and partly because there are so few asset protection lawyers in Michigan.

Part of the reason so few seek out asset-protection lawyers, Young said, is that Michigan clients tend to be conservative in their finances. So they cringe when they hear about such options as offshore accounts.

"Somehow offshore accounts got a reputation for trying to sidestep the law, but that's not what they do, and that's not what they're for," Young said. "Their purpose is to keep people safe when everything goes bad in their businesses."

And, Silverman said, the increasing demand for asset protection has generated an increasing number of costly mistakes by both lawyers and clients. Some clients, he added, even try to save money by setting up their own asset-protection plans.

"Doing your own asset-protection planning is like being your own doctor," Silverman said. "You can make your situation a whole lot worse. You think you can pretty much do whatever you want if you're solvent. The problem is that many people, even many lawyers, don't understand insolvency. You can be insolvent and never have missed a payment."

The most common mistake a person makes, he said, is transferring the deed to the family home into a revocable trust in the name of one of the people on the deed. The goal is to insulate the home from creditors, but it can't be transferred for the purpose of evading debt.

Asset-protection plans are the most effective if they're established while clients' finances are healthy, Young said.

If his builder-client had come to him in

Demand for asset protection rising

Few lawyers in Michigan practice in the highly specialized niche of asset protection. Young said he thinks there are only four.

But there will probably be more, said Jeff Kirkey, director for partnership and certification programs at the Ann Arbor-based Institute of Continuing Legal Education (ICLE), a nonprofit co-sponsored by the State Bar of Michigan and law schools at the University of Michigan and Wayne State University, the Thomas M. Cooley Law School, University of Detroit Mercy School of Law and Ave Maria School of Law.

Kirkey has increasingly heard from lawyers seeking information for their asset-stressed clients.

"The clients often are small-business owners who want to know which of their assets are safe and which are not. And if they are not, they want to know how to make them more safe," he said.

He fields a growing number of requests from lawyers who ask if the institute soon will be dealing with the changing profile of the newly poor.

"I've gotten several requests recently for ICLE to hold a seminar on bankruptcy for high net-worth clients," Kirkey said. "That tells me that we're seeing a different kind of clientele that wasn't vulnerable in the past."

Safe off shore

Some asset-protection tools have a bad reputation, said Howard B. Young, of Weisman, Young & Ruemenapp in Bingham Farms. But, Young said, they are legal means of protecting his clients' cash.

"There is a big difference between asset protection and debt avoidance," Young said. These are a few of the ways he protects his clients' assets:

- **Offshore asset protection trusts:** Allowed in certain jurisdictions, such as the Cook Islands, the Caymans and the Bahamas, these arrangements allow the owner of an asset to pass legal ownership of the asset to a trustee. The trustee is usually a bank or trust company. Such trusts usually are established to protect assets, as they are not accessible to creditors. They are however subject to the same tax rules as assets that are domiciled in the United States.
- **Domestic Asset Protection Trusts:** "In 1996, Alaska woke up and said, 'Why can't we have the same situation'" as the islands have, Young said. The state soon after changed its laws to allow self-settled spendthrift trusts, which allow the beneficiary to establish an entity such as a bank to be the trustee. States which have followed Alaska to allow the establishment of these protected trusts: Delaware, Missouri, Nevada, Utah, Tennessee, South Dakota, New Hampshire and Rhode Island. The accounts can shield assets from creditors, so long as they are not established to defraud creditors.
- **Spendthrift trust:** Similar to a self-settled spendthrift trust, which can be established by the trust's beneficiary, a spendthrift trust can be established in any state on behalf of the beneficiary by someone else. Young said these types of trusts usually are established by parents for their children who are either unable to control their spending, or could put their assets in danger in other ways, such as by getting married without a prenuptial agreement.

2006, protecting more of his assets would have been possible. It was then that personal accounts could have been established in protected jurisdictions, such as the Cook Islands, Belize, Channel Islands and Switzerland.

Or a business owner's assets can be assigned to a spouse or parent or child, or placed in a spendthrift account, without the client's violating the Uniform Fraudulent Transfer Act.

For many of Young's new clients, it's too late. Sometimes all he can do is refer them to good bankruptcy lawyers to help them sort out their debts.

"These are wealthy people who were well-respected," Young said. "They were philanthropists. They had esteem in the community. And now they're going to be broke, really broke.

"They're facing ruin. They are facing the most emotionally difficult time in their lives, at least when it comes to their finances. They're frightened."

In the builder-client's case, he didn't have to go bankrupt. He has worked out a forbearance agreement with his creditors, who realized they had squeezed about as much out of him as they can.

The builder's wife hadn't personally guaranteed the business debt, so the couple's home was protected because she is one of the owners.

If Young's client's wife had a pension, that would have been safe as well. Other assets belong to the builder — for example, his 401(k) and profit-sharing accounts — also can't be touched by creditors.

Young told his client's retired father how to structure his will to best protect the builder-son's inheritance from creditors.

"The father will be leaving, let's say $15 million, to his three children. Because the builder-son's debt could linger for years, or decades, or possibly the rest of his life, the will had to be tweaked," Young said.

The father established for the son a discretionary spendthrift trust, to be held by a family member, a family friend or the bank. Creditors cannot collect from such a trust, but it will pay the son's expenses after his father dies.

Young had to walk his client through the range of future events, including what would happen to the family home, life insurance money and inheritance in the event that the builder outlives his wife. Every asset needed to be restructured and protected to keep the builder from a destitute future.

"These things have been done for years, but they were usually for irresponsible playboy sons, or wealthy sons and daughters who get into marriages that the parents felt were headed for disaster," Young said. "But not anymore."

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Looking for the nut the debtor squirreled away

When the calls came last week to attorney Gary D. Nitzkin, the chase was on.

Two companies need his help. They need their $75,000, owed them by a local furniture store.

Nitzkin is hoping the furniture store owners call him soon to discuss resolving their debt. He's hoping, he said, because if he has to look for the money the store owes, he will find it, and his method for collecting is going to be unpleasant.

Nitzkin, of Southfield-based debt-collection firm Nitzkin & Associates, is seeing a sharp rise in the number of commercial collections.

NITZKIN

"No one ever thought they would be in times that are this tough," Nitzkin said. "The economy is so upside-down right now. Debtors are trying to protect what little they have."

Unfortunately for them, debtors are going about protecting their cash and assets the wrong way, Nitzkin said. (See "The new poor," page 1.)

The biggest mistake Nitzkin sees is the usually inept shifting around of assets to hide them from creditors.

In one case, Nitzkin was trying to collect a debt from a physician who had been sued for malpractice. He owed his patient more than $2 million.

To hide his assets, the doctor transferred more than $1 million to his wife's and children's accounts. What astounded Nitzkin is that the doctor said he did so with the blessing of qualified counsel.

"He showed up in my office with four file boxes full of records," Nitzkin said, "and he was represented by three attorneys."

But Nitzkin figured out where he had shifted the assets in violation of the Uniform Fraudulent Transfer Act.

Nitzkin drafted a letter to the doctor and his attorneys, stating he was going to file suit against the wife and children.

"I basically told them I was on my way to file the suit in court," Nitzkin said. "He came in within a couple of days with a cashier's check for $1.6 million."

If the doctor had had an asset-protection plan in place, the debt probably would have been uncollectible, Nitzkin said.

"There is a fine line between asset protection and debt evasion," he said. "If you're on the right side of that line, there's nothing I can do."

Howard B. Young, of Weisman, Young & Ruemenapp PC in Bingham Farms, specializes in asset protection.

In a case in which a doctor knows he is going to be sued and is worried that he hasn't structured his assets properly, the first thing Young would do is to call upon independent counsel to evaluate the doctor's exposure to risk.

"Let's say that the independent counsel says that the doctor could be on the hook for $100,000, on top of the $200,000 in insurance coverage he already has," Young said. "What we would do is to put three times that amount — $300,000 — into escrow for the purposes of paying a possible judgment against the doctor."

Then his client would be able to set up protected accounts that can't be touched by creditors.

"No one can say we're trying to delay or defraud creditors by protecting those assets," Young said. "It's just the opposite; we put away three times what an independent consultant said we'd need. We set money aside for this very purpose. That's far from trying to get away from responsibility."

Certainly a plaintiff lawyer like Nitzkin could try. But Young said most don't.

"The plaintiff's lawyers have to win two lawsuits: first, the lawsuit regarding the malpractice, then the suit to collect more than the amount we're offering. They don't want to do that," Young said. "The point is that our philosophy is how we can position our clients in order to ensure they have minimum exposure and maximum leverage."

Nitzkin has never beaten Young in court. But he has beaten most of his other opponents, he said, because they haven't been as cautious about asset protection.

Nitzkin's firm employs two certified public accountants to follow debtors' money trails. When he finds the money, he says he's determined to collect on behalf of his clients, which brings him back to the unpleasantness of the collections process.

Last year, he had to collect a debt from two local jewelry stores. He went about collection the same way for both.

"I sent a court officer to clean out their inventory," he said.

The officer went to the stores during business hours, when customers could see what was happening.

"It was horrifying," Nitzkin said.

If the furniture store returns his calls and works out a plan with Nitzkin, he can spare its owner that kind of embarrassment.

"I suppose the fun is in the hunt," Nitzkin said, acknowledging his enthusiasm for his work.

To keep it interesting and sportsmanlike, he chases down, almost exclusively, commercial debtors. It wasn't much fun, nor was it profitable, to collect consumer debt such as credit-card debt. And since the mid-1990s he hasn't tried to collect a single debt for a hospital.

"I just can't do it. People don't choose to have hospital debts. The last one I did was a collection for Children's Hospital," he said. "It was too heartbreaking. I never touched another case like it after."

— CAROL LUNDBERG

The Collector's Creed

Choose your cases carefully. In Gary Nitzkin's case, he uses a complex network of Internet databases to research which cases will be collectible before deciding whether to take them.

The result is that in an industry in which the liquidation standard is 20 percent, his is between 70 and 80 percent said Nitzkin, of Southfield-based Nitzkin & Associates.

Here are few rules he lives by:

- Don't pursue people who have filed for bankruptcy. Their debts will not be collectible.
- Same goes for people involved in landlord-tenant disputes. When debtors are being evicted, their debts will not be collectible.
- Don't chase down people who rent apartments. They don't have the cash to be collected.
- Don't try to collect hospital debt. No one chooses to be in debt for something like that. "It does have to be done," Nitzkin said. "But I don't have to be the one to do it."
- Do look for signs that debtors had money and suddenly do not. That's a clue that they have violated the Uniform Fraudulent Transfer Act, he said, and the money can be found.