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A common misconception is that a living trust will provide creditor protection for families facing bankruptcy, foreclosure, lawsuits etc.. Unfortunately, while a living trust does provide important benefits after the owner's death, such as avoiding probate and reduction of estate taxes, it does not provide creditor protection. If you are interested in asset protection, there are other trusts and methods available, which are considered "advanced" planning techniques, which will provide creditor protection if used properly and maintained.

Some time ago, Mr. G contacted us. He had run a successful retail business for many years. Due to the financial crisis, however, he had lost a lot of money and was forced to close his business. He was aware that nothing could be done to save his business, and his main concern was to protect his home from business creditors.

Most asset protection methods involve a separation of the asset from the control of the person who may be sued (owner). In order to be effective, most asset protection methods must be used **before** the liability arises. Mr. G wanted to protect his personal assets, i.e. his house, from his business creditors. One option would have been to set up a corporation or a limited liability corporation ("LLC") for the business. Both corporations and LLCs protect its owners from being personally liable in the event that the company is sued. However, there are different tax treatments, benefits, and filing requirements. A consultation with an attorney would have determined which was best suited for Mr. G's business.

Another option would have been to set up a Qualified Personal Residence Trust ("QPRT") to shield his home from creditors.

The QPRT is a trust technique used to permanently transfer either a principal residence or a vacation home to your children while you are still living. Because you have already given your home to your children irrevocably in the trust, and it no longer belongs to you, your creditors cannot go after the house because technically the house is no longer owned by you. A QPRT is irrevocable and cannot be changed once it is set up. Even after you set up a QPRT, you can sell your current home and replace it with a new home, and many of the tax advantages of home ownership are still available to you. However, you cannot later choose to give your home to other people.

Unlike an outright gift directly to the children, however, by putting the gift into a QPRT you have a legal right to continue living in the home. The QPRT will set a number of years for which you have the right to occupy the house and retain all income-tax benefits of home ownership (“term”). After the term expires, you will have the right to continue occupying the house in exchange for rent, which will be paid to your children. For example, a client can set up the QPRT term for ten years, then after ten years if they want to continue to live in the house, they can pay reasonable rent to their children. **The QPRT is one of the few methods available which can provide some protection for licensed professionals such as doctors, lawyers, dentists, architects, engineers, etc., who are normally unable to use most asset protection methods to avoid professional liability.**

The QPRT also provides additional tax benefits. Transfers made during your lifetime are subject to gift taxes, and transfers made after you die are subject to estate taxes. With a QPRT, your children will be able to get a substantial discount on gift taxes owed. In addition, all future appreciation will be excluded from your estate, and it will not be subject to estate tax upon your passing.

A key point to remember is that most of these techniques must be used BEFORE the possibility of a creditor claim or lawsuit occurs. For example, Mr. G was already facing financial difficulty in his business, and so he would not be able to set up a QPRT at this time. If he had set up the QPRT earlier, then he may have been able to protect his home. For those engaged in professions that are likely to be sued, it is very important that the QPRT planning is done before problems arise.

There are many additional techniques that can provide creditor protection, as well as tax benefits. Please contact our offices if you wish to get a more detailed review of your assets and the techniques that would allow greater creditor protection for those assets. The QPRT is an advanced estate planning technique, and there are many other factors to consider before creating one. If you have questions about the QPRT or other techniques, please call our office.