

# Asset Protection for Physicians and High-Risk Business Owners

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## **CHAPTER EIGHT**

### **The Privacy Trust**

#### **The Privacy Trust**

The Privacy Trust is a descriptive name for the legal strategies designed to achieve financial privacy goals—a legitimate concern for many individuals. The Privacy Trust successfully conceals ownership of bank and brokerage accounts, the family home, rental properties, and interests in other entities. If you have established a corporation, Family Limited Partnership, or Limited Liability Company for business or asset protection purposes, the Privacy Trust adds a desirable level of confidentiality to your personal affairs. Depending upon the particular features included in the trust—in addition to the privacy advantages—formidable asset protection and estate planning benefits can be created.

#### **Creating Legal Privacy**

Legal privacy for financial matters is a scarce and valuable commodity. As we have discussed, developments in technology now allow powerful search engines to sort through billions of records stored in vast interconnected databases. These programs are capable of locating and assembling disparate facts about your life into a comprehensive personal information report with detailed background, credit, employment, and financial information. The ready availability of bank and brokerage account balances and real estate ownership provides a potential adversary with an accurate picture of sensitive personal matters that you would choose not to disclose.

The full extent of the dangers associated with these privacy intrusions is only now becoming apparent. The Federal Bureau of Investigation reports that identity theft is the fastest growing crime in the nation. Easy access to personal identifying information such as name, address, birth date, Social Security number, and driver's license number allows a third party to pose as the victim, run up credit card bills, take out loans and mortgages, and open fraudulent bank accounts. An enterprising individual or an organized ring using hundreds of stolen identities can make millions of dollars within a few months and then disappear before the victims have even learned of the crime. The victims are left with collection actions, judgments, and devastated credit that may be impossible to repair. Congress has responded to these particular abuses with the Identity Theft and Deterrence Act of 1998, which provides criminal penalties for identity theft and gives victims the right to seek restitution from the perpetrators.

Identity theft is an easy and profitable crime, and the threat of prosecution is not likely to discourage these types of activities. Your key personal identifying information—such as Social Security number, date and place of birth, and mother’s maiden name—has already been distributed so widely that it cannot be retrieved. Privacy rights groups will advise you not to give out this information anymore, but it is too late for that. If you tear up your credit cards, refuse to fill out surveys, hang up on telephone solicitors and keep out of the newspapers, your information may eventually fade from view. As your name appears less frequently on the computer generated lists of affluent, creditworthy individuals, you might decrease your chances of being noticed and selected by an identity thief. But there is no practical way to remove yourself from the system. The volumes of information about you in the databases of the credit reporting agencies, public records, and information vendors don’t belong to you. They belong to the companies that compile the information, and you can’t restrict the flow of what is already out there.

It is possible and advisable to limit the availability of certain types of financial information about yourself. Although a variety of regulatory and reporting requirements create obstacles, the ownership of assets can be shielded from public disclosure. As long as taxes are paid on the income earned and the techniques are not used to conceal the proceeds of criminal activities, anonymous ownership can be legal and effective. Dangers associated with predatory lawsuits and threats from potential adversaries can be successfully combated by adopting strategies which defeat the information gathering processes.

### *Limiting the Supply of Personal Information*

The success of a strategy to keep your financial assets secret depends upon the same premise as the rest of your secrets in life. The fewer people that know something about you—the better. And those few people who know should be very good at keeping it to themselves.

Let’s see how this principle applies when you open a bank account. You would like to keep the existence of the account, your balances, and your transactions confidential. The representative who opens your account assures you that the bank maintains strict privacy standards and would never disclose customer information to anyone. The account opening agreement requests your name, address, date and place of birth, driver’s license number, and your Social Security number. This information is entered into the bank’s computer and an account number is assigned. What level of privacy should you now expect?

The account information in the bank computer is now available throughout all of the bank branches to virtually every employee. Account information is maintained centrally and is accessed through the terminals of every teller, loan officer, and customer service representative by a search under your name, account number, or Social Security number. The merger trend in the financial services industry makes ever larger quantities of customer information available to a greater number of people. Bank of America recently completed a merger with Nationsbank to create the largest bank in the country with 4,854 branches, 30 million customers, and 200,000 employees.

With access to personal account information available to so many employees, the financial institutions cannot control the flow of customer information from the bank to the outside. The investigators and information brokers who seek account information for clients on a regular basis pay bank employees to supply individual accounts records. So the first problem you have with your account secrecy is that even if the bank wanted to protect your privacy, it would have a difficult time preventing disclosure by its employees.

Your second problem is that when your bank tells you that it values your privacy, that doesn’t mean what you think it does. It really means that the information about your account is *valuable to the bank*. Sophisticated databases allow financial firms to create intimate profiles of customer portfolios, savings, and spending habits. This information is then used by the firm—or an outside marketing company—to create highly selective and targeted presentations to sell you services and products. Information about you and your account activity is a prime source of revenue for the firm, and it is exploited, traded, and sold like any other asset.

The recent merger between Citicorp and Travelers Group Inc., (now called Citigroup) illustrates this point. The plan is intended to create the world's largest "financial supermarket" with nearly 700 billion dollars in assets. Products would be cross-sold to what were, previously, each other's customers based upon the information gathered by each division. The combined company includes 10,300 stockbrokers at the Salomon Smith Barney subsidiary and 180,000 full- and part-time insurance salespeople. Detailed account information and behavioral analyses of bank customers will allow the new sales force to individually tailor each pitch for annuities, mutual funds, and insurance products.

Imagine the potential. A broker from the Salomon Smith Barney division of Citigroup calls Mrs. Wilson about her \$100,000 certificate of deposit at Citicorp which is about to come due. Although the two have had no previous business relationship, he tells her that he is calling from her bank and, as a service to its valued customers, has been asked to perform a thorough financial analysis of her account. After weighing the available investment options, his recommendation is that she purchase a Citigroup variable annuity with her \$100,000 savings. Or he might suggest putting her savings in the stock market, or in a mutual fund—anything to shift her out of the low margin CD and into a high profit, big commission investment product.

Citicorp lures the customers with the convenience of thousands of branch offices, ATMs, and online banking. It might even be willing to pay higher interest rates on CDs and deposits—a loss leader—simply to attract additional accounts. Once you are a customer, your individual customer data is gathered, spending and saving patterns and available cash are processed and analyzed, and the information is turned over to the sales force. Then the real money is made by selling investments and products loaded with fat fees and commissions.

This example is an accurate portrayal of the tactics that are used by the financial firms. NationsBank (now merged with Bank of America) signed a consent decree with the Securities and Exchange Commission agreeing to stop misrepresenting the safety of certain investments offered to its customers. The bank had provided its sales force with customer lists of maturing CDs—together with financial statements and account balances for likely prospects. The customers—many of whom had never invested in anything other than CDs—were told to switch their money into an investment called a "Term Trust," which "were as safe as CDs but better because they paid more." In reality, these Term Trusts were pools of funds that were invested in high risk derivatives and which proceeded to lose much of the customer's money. The consent decree does not bar the company from using customer account information to sell products, it merely prohibits misleading statements about the products.

The use of account information to sell products is not limited to these examples. Every company in the industry has recognized the effectiveness of the strategy and is scrambling to create marketing alliances, joint ventures, and mergers with others to acquire product lines and sales forces. The days of the small, independent local bank are gone forever. The little guys cannot remain competitive without large capital investments in technology and marketing, and so they are gobbled up by the regional and national firms. In San Diego, where we live, only one independent bank remains. Union Bank, Wells Fargo, Bank of America, and Washington Mutual have acquired every other local bank.

Now that you have the broad picture about how the financial firms operate, what conclusions can we reach about the secrecy of your account? We know that the information is widely available to employees and is traded and distributed by the firm to inside and outside sales forces. If you hope to accomplish secrecy by restricting access to particular information, it is easy to see that this ambition will be defeated from the very instant that the account is opened. As your account information is keyed into the computer, it is turned into a digital packet and shipped into the stream of commerce. To state the matter most directly, you can expect that all information in the possession of the financial firm will be available to anyone who wants it, for whatever reason.

## *What the Privacy Trust Achieves*

The approach we have developed is to hold all financial accounts within the Privacy Trust. This legal arrangement prevents the firm from acquiring any useful personal information. Since financial firms are not good at keeping secrets, we just won't tell them anything. The Privacy Trust acts as an intermediary to remove the connection between you and the account. Neither your name, nor your Social Security number, nor any other personal identifying information appears in any records related to your account. No employees of the firm are aware of your relationship to the account, and the bank can't sell information that it doesn't have. That's the proper model for creating financial privacy.

Information about your real estate assets—your home and other property can also be shielded from public disclosure. Since these records are publicly recorded and can be gathered through a database search—privacy means severing the connection between you and the property. When the records are searched under your name or identifying information, you do not want your home and other properties to appear on the list. If you hold real estate in a corporation, FLP, or LLC, your ownership of these entities must be concealed as part of any privacy strategy. Locating your property and determining its value is the easiest and most popular technique for measuring your attractiveness as a potential target for litigation or any other type of claim.

The Privacy Trust can be created in a simple and straightforward manner to accomplish most privacy, asset protection, and estate planning objectives. Progressive levels of sophistication can be added as the complexity of the financial circumstances increase. Advanced planning strategies may include a variety of domestic or offshore options, depending upon the particular results to be accomplished. For descriptive purposes, we can divide the Privacy Trust into Plan #1 and Plan #2, which we will discuss in this chapter. We base the distinctions upon the key privacy and asset protection feature of each.

### **Privacy Trust—Plan #1**

The Privacy Trust—Plan #1 is a convenient and flexible arrangement that successfully conceals ownership of a variety of assets. As its name clearly states, it is used specifically for the purpose of avoiding public disclosure of real estate, financial accounts, and personal property. This trust is commonly used by celebrities and public figures to hold title to the family residence, vacation homes, and investment accounts.

#### *The Role of the Trustee*

The feature that creates the ability to achieve privacy for these assets is the use of a special type of corporate trustee—whose duties are to carry out your instructions. The corporate trustee does not invest or manage trust assets. His role is strictly limited to acting as your agent and nominee and executing documents as you request.

This role differs significantly from that of a typical trustee. The responsibilities are, likewise, dissimilar from the traditional responsibilities assumed by a trustee. Most trust companies are in business to manage assets—and they charge substantial fees for performing these services. The company makes investment decisions for the trust and distributes funds according to the terms of the trust agreement. Specific requests by the settlor or the beneficiaries must be reviewed by trust officers and their counsel to make sure that legal responsibilities and fiduciary duties are satisfied. Within this bureaucratic structure, even relatively simple matters are time consuming and expensive to accomplish. Although these traditional trust services can be useful for a client who needs extensive independent asset management for an elderly or minor beneficiary, that is not the type of arrangement that most of our clients prefer.

Instead, our clients who create a Privacy Trust generally want to maintain control and authority over their property—while using the trust company only for the limited purpose of holding legal title and executing necessary documents as instructed. The requirements for the trust company are:

1. It must be adequately capitalized and bonded to assure the safety of trust assets.
2. It must be licensed and regulated by state banking authorities.
3. Trust officers at the company must have authority to respond quickly and efficiently to all instructions from the settlor.

When the proper precautions are taken to guarantee the safety of the property and we are satisfied that the trust company will carry out directions in a timely manner, the Privacy Trust can be created.

### *Why This Plan Works*

In the typical arrangement, the trust agreement specifies that you—as the settlor—have the right to revoke the trust at any time and that the trustee will perform only those activities specifically directed by you. Real estate is acquired or transferred into the name of the trust and financial accounts are opened at the bank or brokerage firm you choose.

The name on the property and the accounts is changed from your name to the name of the trust. For example, if we use the ABC Trust Company, the name of the trust could be ABC Trust #4006. Title to your home or other real estate is removed from your name and simply reads ABC Trust #4006. The trustee acts on your behalf for executing purchase or loan documents. Many lenders are familiar with these types of trusts and are comfortable with a mortgage loan in the name of the trust. You are required to maintain and manage the property in the trust. The trustee holds legal title for your benefit, but your responsibilities are not diminished.

An account at a bank or brokerage firm can also be opened in the name of ABC Trust #4006. The account opening agreement and the signature card are signed by the Trust Company. The tax identification number of the Trust Company is furnished. Your name and identifying information are not supplied to the financial firm—there is no visible connection between you and the trust.

This arrangement creates a true model for privacy because the financial firm and its employees *do not know* that you are the true owner of the account. Any inquiries regarding an account under your name or Social Security number will come up empty. They can't give away secrets they don't know. Your name is not in the computer and, as far as they know, you don't exist. The computer can apply sophisticated software analysis to the account to track savings and investment activity, and the firm can devise perfect product fits based upon the patterns evidenced in your account. But the firm can't sell your information, or give it to its sales force because the firm doesn't have a name behind the account. Now you control access to your personal information. It belongs to you and not the bank, and you can control what you supply to the outside world.

Sam, a private investigator, is contacted by attorney Aardvark who wants to know if you have enough assets to make it worthwhile to sue you. Sam flips on his computer, pours a cup of coffee, and dials into the database service that searches nationwide for real estate ownership. He keys in your name and Social Security number, but the screen says "No Matching Files Were Found." Your home and vacation house in the name of ABC Trust #4006 are not located in the search. Next, Sam contacts the agency that provides searches for bank and brokerage accounts and again—no luck. Since there is no record linking you to the trust account, a computer search of the customer accounts at every firm will produce no successful hits. At this point—with no real estate or financial accounts—he calls the attorney and tells him to find a better lawsuit prospect.

This strategy successfully protects the privacy of your sensitive financial information by strictly limiting the access. The information is secure because it is not made available to the bank, its thousands of employees, and its sales force. In contrast to your bank, the trust company has a legal and contractual obligation to maintain the confidentiality of the trust. It is in the business of providing fiduciary services and cannot breach the trust agreement without serious legal ramifications. It is certainly true that if somebody wants information badly enough they can penetrate any source. But a trust company with the proper safeguards in place will seriously reduce the risk of unauthorized disclosure.

In addition to the privacy benefits, all of the typical estate planning advantages can be achieved. The trust will perform the same role as a living trust to avoid probate, minimize estate taxes, and pass your property according to your wishes.

In the Privacy Trust–Plan #1, assets are owned directly by the trust as diagrammed in figure 8-1.

### *Who Should Use This Plan*

This arrangement is used most often by individuals who are primarily concerned with financial privacy issues. A client of ours had an elderly mother whose assets consisted of \$200,000 in savings at a brokerage firm. We put the funds in a Privacy Trust specifically for the purpose of eliminating high pressure telemarketing pitches for investment products and phony investment schemes. Our client wanted to protect against the risk that his mother would lose her money to a scam artist using account information to victimize the elderly.

We also have created this type of Privacy Trust for several clients in law enforcement—police officers and federal agents—who want to avoid privacy intrusions from dangerous individuals they have dealt with in their line of work. Similarly, for entertainers and public officials, who are well known by the public, we are often asked to conceal ownership of their homes and financial holdings with the use of this particular technique.

The Privacy Trust–Plan #1 is not designed to protect the assets of the trust from a judgment or a claim against you. Since the trust is revocable, the law provides that property in the trust can be reached in a collection proceeding. Although most lawsuits will be discouraged by the secrecy attributes, if you own Dangerous Assets or have substantial liability risks from your business you should consider a strategy which combines asset protection features with the Privacy Trust.

## **Privacy Trust–Plan #2**

The Privacy Trust–Plan #2 adds the asset protection benefits to the plan which we have just described. When we supplement the trust with an entity such as a corporation, Family Limited Partnership, or Limited Liability Company, we can insulate and shield assets from the risks of potential liability. Rather than holding property directly in the trust, we hold assets within entities that are designed to accomplish asset protection purposes. The interests in those entities are owned by the trust.

### *How to Use Plan–#2*

Here's an illustration of a typical plan. Our client, Henry, is married with three small children. He owns a dry cleaning business and a four-unit apartment building. These assets represent his lifetime savings. Henry and his wife want a plan to achieve three major goals:

1. Privacy—An important goal is anonymous ownership of the business and the real estate. During the previous ten years, Henry has been named in six frivolous lawsuits from customers, employees, and tenants. Although he won in court each time, the legal fees and the worry associated with the litigation have taken a financial and emotional toll.
2. Protecting Family Savings—The business and the real estate are both Dangerous Assets. A liability produced by either could wipe out all of the equity in the other. Henry wants a plan to ensure that if something goes wrong with the business or the property, he will not lose all of his savings.
3. Estate Planning—Avoiding probate, minimizing taxes, and providing for the care and support of his minor children are the remaining objectives of Henry's overall plan.

Each of Henry's concerns can be addressed within the convenient strategy of the Privacy Trust—Plan #2.

Let's see how this plan, depicted in figure 8-2, accomplishes Henry's goals.

We transferred the dry cleaning business into a Limited Liability Company (LLC #1) and gave the trust 100 percent of the interests in the LLC. Henry's name no longer appears as the owner. Licenses and permits are in the name of the company, and the public filing shows that the LLC is the owner of the business. The Articles of Organization for the LLC list the name of the trust—but not Henry's name. The same plan was followed for the apartment building. A deed transferred title to the apartment building into LLC #2. Anyone attempting to discern the owner of the LLC would find only the name of the trust. Important privacy goals have been achieved.

This strategy also provides a high level of asset protection. The LLC creates a legal shield, which protects each asset from a liability generated by the other. Henry can operate the dry cleaning business in LLC #1 without concern about being named in a lawsuit and without jeopardizing the apartment building. Similarly, liability from the property will be contained in LLC #2 without risk to the business.

Additional protection is furnished because a judgment creditor cannot seize the assets of either LLC. If there is a lawsuit against Henry for an unexpected reason, the business and the real estate—secure in the LLCs—are insulated from the claim. Although the membership interests held by the trust are subject to a charging order, this remedy is generally not effective and is unlikely to be pursued by a plaintiff.

A variety of estate planning features are easily integrated into this plan. The Privacy Trust has provisions that allow Henry's wife to continue the management of the family assets if something happens to Henry. Guardians and successor trustees are named to act on behalf of the children if both parents should die. Probate is avoided, estate taxes are minimized, and the proper structure is in place to provide for the survivors.

### *Bank and Brokerage Accounts*

If Henry had liquid savings in a bank or brokerage account, we would add a third LLC as the owner of the account. The ownership of the LLC would be placed in the trust. As we discussed, when our goal is privacy and asset protection we attach an asset protection vehicle—such as an LLC to the plan.

All financial accounts require the name and identifying information for the authorized signatory. Although the account is in the name of the LLC, we will need to provide a signatory. If Henry uses his name and Social Security number, the account will be disclosed in a search. The proper strategy is to have the trust company act as signatory. Henry can manage the investments and even make trades in the brokerage account. The trust company issues checks according to Henry's instructions.

With the Privacy Trust–Plan #2, the account is both private and protected. The account is in the LLC and Henry is not connected to it in the public filings or on the signature card. His ownership of the account won't be discovered through any available search techniques. If a lawsuit or a claim develops against Henry for any reason, the funds are legally insulated against liens or collection actions in the LLC.

## Summary

Information about your financial life is a valuable commodity. With limited exceptions, public and private entities that have information about you use it to market products or sell it to others who do the marketing. County and state governments sell real estate ownership data, driving records, and court filings to list vendors and information brokers. Financial firms use sophisticated software to analyze your saving and spending patterns and target investment products you are likely to buy.

As a result, information about your real estate ownership is directly available for public view and financial accounts are immediately accessible by hundreds or hundreds of thousands of company employees and hired sales forces. From there, it is only a small step into the hands of a lawyer, business competitor, or a determined ex-spouse—armed and eager to use this information for personal advantage.

Since we cannot control the flow of personal information from the bank or brokerage firm, our approach is to restrict access in the first instance. If your name or identification number is on the record, you have provided valuable information about yourself that is subject to widespread dissemination. Instead, we recommend that you limit access to your ownership records and details by using a Privacy Trust to hold property and financial accounts.

A Privacy Trust can be created solely for the legitimate purpose of concealing the ownership of assets from public view in order to avoid privacy intrusions. This is often an important part of a sound plan for both business and personal reasons. The Privacy Trust–Plan #1 is designed to directly own your home and savings accounts, and to provide a convenient and cost effective strategy to accomplish privacy goals.

The Privacy Trust–Plan #2 is designed to add particular asset protection features to the overall plan. Property may be owned by an asset protection vehicle such as a corporation, Family Limited Partnership, or Limited Liability Company to shield Dangerous Assets from each other and from Safe Assets. The ownership of the entity is then held by the Privacy Trust. In chapters 9, 10, and 11, we will familiarize you with popular offshore strategies for privacy and asset protection. We'll debunk some of the myths and examine the real advantages and disadvantages presented by these techniques.

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