

# covering your assets



PRIMARY CARE

## Protecting Your Assets Under the New Bankruptcy Act

By Robert J. Mintz, Esq.



Strategies for protecting homes and savings from lawsuit risks have been affected by sweeping changes in The Bankruptcy Abuse Prevention and Consumer Protection Act of 2005. For physicians concerned with the issue of minimizing legal exposure, some of the changes are positive and others are clearly unfavorable to certain types of plans. In this article, we'll look at one of the key points in the new law that may affect your current or future asset protection planning.

### Protecting Your Home

The biggest impact concerns the amount of equity in your home that can be protected from a judgment. The amount of equity in a principal residence that can be shielded from a lawsuit judgment (called the homestead amount) varies from state to state. For example, Maryland has no protected amount. New York allows for just \$10,000 while Nevada exempts up to \$200,000 and Massachusetts allows \$300,000 to be protected. Several states—including Florida, Texas, Kansas, Iowa, and Oklahoma—allow for an unlimited exemption.

This unlimited homestead has long been a sore point with the banking industry and many trial attorneys who are often frustrated in their attempts to collect on their judgments. An individual, suspecting that he or she might be facing financial problems or a large damage award, was able to move to Florida or another unlimited homestead state and plow all of his or her savings into a residence. As long as legal residency was properly established, the equity was then protected without any restriction on the amount. For example, suppose Dr. A—

who lives in West Virginia, owns a house worth \$300,000, and has \$700,000 in savings and other property—is named in a lawsuit with big potential damages. The West Virginia homestead protects only \$25,000 of home equity, meaning Dr. A is at risk for most of what he owns. Instead of risking everything on an uncertain outcome to the case, he moves his family to Florida and buys a home for \$1,000,000. The intent is to use the Florida homestead exemption to free him from the threat of the existing lawsuit.

These unlimited homesteads were always viewed as an effective and popular worst-case scenario. Moving the family and practice to another state may be inconvenient, but if it's the only choice, it is better than handing over everything to the plaintiff's attorney. During the past 10 years, this so-called "Florida Option" has been the choice of many prominent CEOs as well as others attempting to avoid financial ruin.

The new law, which applies to bankruptcy filings, curbs this perceived abuse by limiting the exemption to \$125,000 for amounts invested in a home within the prior 40 months. Even if the state homestead amount is more than that (including states that allow unlimited homestead exemptions), money invested within the critical 40-month period can only be shielded to a maximum of \$125,000. Someone who develops business problems or fears a lawsuit with substantial damages won't be able to escape the judgment by sinking large amounts of cash into a homestead-protected house. Anything above \$125,000 will remain available for the creditor. Only those with enough foresight or luck to invest in a residence

more than 40 months before a judgment will be able to take advantage of the full exemption.

Even if you are already a long-term resident of an unlimited homestead state, if you buy a new, more expensive house, the additional investment beyond the \$125,000 is not protected. For example, suppose Dr. X, who has lived in Florida for 20 years, sells her home next year for \$1 million and buys a new home for \$2 million but goes on to lose a lawsuit in 2008. Her new investment of \$1 million, since it was made within the 40 months prior to the judgment, would only be protected to the limit of \$125,000. Similarly, using savings to pay down a mortgage to obtain homestead protection for the funds won't help if it's done within the 40-month window.

### In Closing

The new bankruptcy law creates some changes in the asset protection landscape by making the homestead exemption more complex and subject to delicate timing issues. Asset protection planning should always consider the impact of bankruptcy law when determining the techniques that will be effective in the widest variety of circumstances. As always, you should consult with your attorney or other advisors to make sure that your planning is appropriate and up to date with the latest cases and legislation.

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