ISSUE 63

Protecting Your Nest Egg

"Why do I need to create multiple entities to protect my assets?" Steve Pierce, owner of Pierce Floral Shops, asked. "I already have all of my business interests in a Limited Liability Company. Doesn't that protect me and my business?"

The answer provided by his lawyer was about what you would expect. "Yes. And no."

Putting all of your assets in a limited liability entity such as an LLC or a Corporation can provide personal liability protection to the owner of that business with an important exception. If the owner is responsible for the event leading to the liability (as is often the case in smaller businesses) the fact that the company is a limited liability entity doesn't protect the owner from personal liability.

Further, there is little asset protection for the owner if a creditor is successful in its action against the company. Since the bulk of most business owners' wealth is in the assets of their companies, a successful creditor attack against the company will wipe out the majority of most owners' wealth by wiping out the value of the ownership interest in the business.

One solution (perhaps the easiest) is to have several smaller nest eggs; in other words, create several or multiple entities. If one entity is attacked successfully by creditors, its assets will disappear. But, if properly planned, the bulk of the overall assets, contained in the other entities, will survive intact.

Steve owned several retail locations, each with their own exposure to operational liabilities such as employee-based law suits or customer based law suits (imagine for a moment a scenario where numerous customers of one location contract food poisoning).

By creating a separate legal entity for each location, the liabilities of that location will more likely be confined to the assets of the particular location and entity. Had Steve owned a business with just one location, his ownership interests would be better protected if he separated the real estate (or perhaps the equipment used in the business) from the operations.

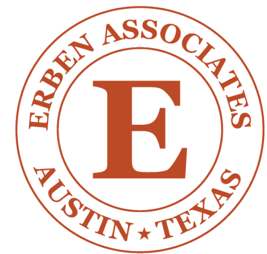
One common suggestion is to transfer the real estate used by the business into an LLC (owned solely by Steve and his family) and the operations in a separate

entity (such as an S Corporation or LLC). Once again, valuable assets, such as the real estate, will tend to be protected from the liabilities of the business operation, and even, to the extent the LLC is owned by others, from Steve's personal creditors. personal creditors.

When we proposed this multiple entity strategy, Steve responded as most owners, do. "All well and good," he answered, "but how much will this cost me?" In order to put to rest the visions of escalating legal and accounting fees swirling about in his mind, we answered, "Not much." Why? The creation of new entities is a one-time legal fee (of several hundred to a few thousand dollars). The accounting fees, both in the year of creation, and on an on-going basis, would be relatively inconsequential as long as the new entities being created are "flow-through" tax entities such as an S Corporation or LLC. There would, of course, be annual legal fees for any required state filings.

As always, you must consult with your own legal and tax advisors for a definitive answer before proceeding. Our experience, however, tells us that the potential benefits of creating multiple entities are far greater than the additional professional fees.

The next issue of The Exit Planning Review™ will discuss the significant income tax, estate and gift tax savings made possible by using a multiple entity business structure.



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