The Golden Rules of Asset Protection

Asset protection means protecting your accumulated wealth from losses and is essential to enjoying the success you create over the long-term.

Regrettably, many business owners don't put sufficient emphasis on asset protection. But this is a mistake because:

- The more successful you've been, the more you have to lose
- The more successful you are, the higher the chances a 'gold digger' will take a crack at you, whether their claim is legitimate or not
- The older you get, the less time you have available to rebuild your wealth following a significant or catastrophic loss.

Unfortunately, disasters occur all too often, and it's usually too late to fix your affairs once the 'horse has bolted'. It's far better to shut the gate before the horse bolts!

Fortunately, with a little planning and sound advice, you can significantly improve your level of asset protection, thereby reducing the impact of both foreseeable and unforeseeable events.

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The purpose of asset protection

The purpose of asset protection is to reduce the impact of events when things go wrong (whether those events are within or outside your control). Asset protection is your last line of defence when:

- You've failed to identify or manage a material risk
- There is no suitable alternative but to accept material residual risk.

How to protect your assets

Legal structure

At the heart of any good asset protection lies your business' legal structure and ownership arrangement.

To a large extent, your business's legal structure determines many key aspects of your asset protection, after tax wealth creation outcomes, capital raising capability (both debt and equity) and your succession and exit planning. All these factors are essential and must be taken into account when selecting the most appropriate legal structure.

Ultimately, your legal structure needs to:

- Provide appropriate control and ownership
- Meet the operational and strategic needs of your business
- Deal with the nuances associated with your particular industry and regulatory requirements
- Accommodate your personal circumstances, goals and objectives.
- Provide the flexibility needed for future growth (expansion of your structure, changes in your family and personal circumstances and so forth)
- Protect the wealth you create from the many risks associated with business and life.

Together, these requirements can make your choice of structure challenging because individual circumstances and industry factors vary from one business owner to the next.

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The two golden rules of asset protection

From an asset protection perspective, your legal structure should effectively reduce your exposure by following fundamental structuring rules.

The two overarching golden rules of asset protection are **to isolate the ownership of current and future**:

- **Business and personal assets from business risk**

- **Business and personal assets from personal risk.**

These two golden rules translate into several structuring tactics.

Structuring tactics for asset protection

By preventing your assets from being exposed to risk, you can effectively protect them when unforeseen and unmanaged risks arise. You can achieve this by:

- **Not trading as an individual or as an individual in partnership with someone else.** Lack of legal separation between business and personal asset ownership exposes every asset to all business risks.

- **Using separate legal entities (companies and/or trusts) to operate business activities.** This means you can isolate all your business operating risks from your personal assets. Likewise, you'll isolate your business assets from any personal risks that might arise.

- **Using different legal entities to separate ownership of material business assets from business trading activities.** By owning assets in a separate legal entity that doesn't conduct an active business, you significantly reduce exposure of those assets from risk. Some intangible assets, such as reputation and goodwill, may still reside in the trading entity. However, these are generally less exposed to legal attack and should be managed by adopting best business practice.

- **Operating different businesses in different legal entities** minimises contagion risk (the chance of something going wrong in one business impacting another business).

- **Limiting the number of directors to a practical minimum.** Where your structure uses companies, don't unnecessarily expose the assets of individuals to potential liabilities by making them a director of a corporate entity if they don't run the company or otherwise need to be a director.

While the corporate veil exists to protect directors, it's not impenetrable and shouldn't be relied upon unnecessarily.

- **Using corporate instead of individual trustees** where your structure utilises trusts and selecting an appropriate appointor or guardian for the trust.

- **Holding personal assets in your partner's name if they aren't exposed to risk.** If your life partner has no business risk exposure, you should generally hold all material personal assets in their name. By isolating ownership of personal assets from the potential liabilities associated with running a business or being a director of a trading company, you add a further layer of protection. For example, where possible, one partner should be the director of any trading companies. At the same time, the other should hold material assets, such as the family home and be a director of any non-trading asset-holding entities.

- **Holding certain personal assets and investments in separate legal entities.** Where you don't have a life partner or your life partner is exposed to business risk, accumulate suitable personal assets and your investments in a separate legal entity established solely for that purpose. You'll limit the value of personal assets you have in your name and, therefore, their exposure to business and personal risk.

- **Accumulating wealth and owning appropriate assets in superannuation.** For many business owners, superannuation provides a high level of asset protection (usually even in bankruptcy). Likewise, self-managed superannuation funds can be a suitable entity to hold certain business assets (to separate business assets from business and personal risk).

Defending yourself

You can't predict or control all risks. From time to time, events occur that force us to rely on defensive asset protection to limit their impact. This means structuring your business and personal affairs to effectively separate assets from risk or limit the amount of equity exposed by appropriately assigning liabilities.

When done correctly, asset protection is a great last line of defence in the face of catastrophe and can go a long way to protecting the wealth you create.

If you'd like to make sure your wealth is protected so that you can enjoy it in the future, call Fortitude Business Consulting on 1300 551 040.