

To: Clients and Friends
From: The Attorneys at the Law Firm of Bove & Langa, P.C.
Re: Important Recent Developments: September 2004

Firm Update

We are pleased to send you our latest firm newsletter with updates on areas of interest in the law, taxes, our firm, and the Red Sox. As of this writing, the Red Sox are once again giving us hope for an exciting post season. News within the firm includes the enthusiastic welcoming of Attorney Marshal S. Grant to our staff. Marshal has several years experience in estate planning and recently earned his Master of Laws – Taxation degree from Boston University Law School's Graduate Tax Program. We are also pleased to announce the addition of Jaclyn O'Leary to our staff of legal assistants. Jaclyn recently graduated magna cum laude from Boston College. Melissa will once again be teaching estate planning to BU's graduate tax students this fall. Alexander continues on the lecture circuit having recently delivered lectures to LIMRA, a prestigious group of attorneys representing major insurance companies, and to the International Financial Services Group on Nevis at its 20th anniversary conference. Lynn recently joined Alexander on a panel to discuss protecting the home from creditors, and Bob will be speaking in November at the Real Estate Bar Association's upcoming annual meeting on estate and Medicaid planning with real estate.

NEW DEVELOPMENTS

Homestead Protection Increased to \$500,000: The Massachusetts legislature recently voted to increase the homestead protection from \$300,000 to \$500,000 as of October 26, 2004, which means that if you are facing a creditor (in most cases) you can protect up to \$500,000 of the equity in your home to ensure you and your family have a roof over your heads despite creditor problems. It is very important to understand that homestead protection is not automatic in Massachusetts, so you have to actively *declare* homestead protection by filing a simple form at the registry of deeds for the county in which your home is located and paying the recording fee of \$35. You can obtain the homestead declaration form online, from the registry, or by contacting us for assistance. If you have already filed a homestead declaration for your property, there is no need to file again, and the increase will automatically apply as of the effective date, however, any pre-existing liens on your property will not be subject to the increased protection. If you have refinanced since filing your homestead declaration, please visit our website for more information regarding the "ins and outs" of homestead protection.

MassHealth (Medicaid) Up-Date: The Massachusetts state legislature recently repealed many of the changes it made during 2003 to the Medicaid benefit program, which is known in Massachusetts as MassHealth. The laws and regulations that were repealed dealt primarily with the controversial expansion of the state's ability to recover the cost of nursing home care from any assets in which a nursing home resident held any interest at their death. Pursuant to the repeal, probate assets are once again the only assets that are subject to estate recovery. Therefore, clients can once again undertake Medicaid planning which takes advantage of such planning techniques as life estates and irrevocable income-only trusts. Although it is expected that the legislature will revisit the issue of expanded estate recovery, it is expected that next time they will "grandfather" planning that is in place if and when the law is enacted. Therefore, if you or a family member is considering Medicaid planning, we recommend that you make an appointment to review your situation as soon as possible.

Good News From the IRS: To reduce the size of a taxable estate, many of our clients have established irrevocable trusts for the benefit of family members wherein the client continues to pay the tax on the income generated by the trust. The tax advantage of this arrangement is that by keeping the income tax responsibility, the client permits the trust to grow without depletion for the payment of income tax. This type of trust is called a "grantor trust", and for many years the IRS has informally indicated that the payment of the income tax by the client is an additional gift to the trust – even though the Internal Revenue Code clearly places the tax responsibility on the client! Well, the IRS has given up on this position. In Revenue Ruling 2004-64, issued July 6, 2004, the IRS has finally acknowledged that, because the grantor (creator) of a grantor trust has the legal obligation to pay the tax, doing so is not a gift.

Check Out the New Tax-Free Way to Pay For Check-Ups: January 1, 2004 brought into being new Health Saving Accounts ("HSAs") as part of the federal Medicare Prescription Drug, Improvement, and Modernization Act of 2003. What are they? HSAs are available to anyone who has a health insurance plan with a high deductible amount. That is, a plan where you have to pay at least \$1,000 out-of-pocket until the plan benefits kick in (\$2,000 for family coverage). Generally speaking, you may annually contribute to your HSA a total amount equal to the deductible. Individuals between the ages of 55 and 65 may make larger "catch up" contributions. Contributions by your employer are not included in your income, and yet they are deductible by your employer. Your own contributions are tax-deductible as well. Like an IRA, contributions may be invested in the marketplace, earnings are not taxed while within the HSA, and amounts distributed are not taxed if used for qualified medical expenses, including prescription drugs, over the counter drugs, and long term care (or premiums for long term care insurance). Finally, HSAs are portable, which means that if it is set up through an employer, you can take the HSA with you when you change jobs. You may even name a beneficiary who receives the HSA at your death. (It's not that portable!) Obviously, not everyone will qualify for an HSA, but for those who do, the benefit is clear. For example, a 25 year old who socks away \$1,000 a year into an HSA will have roughly \$155,000 at age 65 to spend on qualified expenses (assuming a 6% return).

Massachusetts Estate Taxes: At the risk of sounding like a broken record, we wish to remind our married clients once again that if you have not come in to have your estate plan reviewed in light of the 2003 changes to the Massachusetts estate tax law, you should do so as soon as possible. As noted in our December, 2000, "Massachusetts Estate Tax Advisory" (available on our website or

upon request), Massachusetts has decoupled its estate tax law from the federal law and now imposes an estate tax on estate assets in excess of \$850,000 for decedents dying in 2004. Comparing the Massachusetts exemption to the federal exemption of \$1,500,000 for decedents dying in 2004 results in a difference of \$650,000. Under a plan commonly used for married persons prior to the Massachusetts change, this difference of \$650,000 would now be taxed by Massachusetts on the first death, resulting in over \$64,000 in estate taxes that could otherwise be deferred and possibly eliminated! Although the Massachusetts exemption is increasing to \$950,000 in 2005, and \$1,000,000 in 2006 and thereafter, the federal exemption is increasing at a much faster rate, causing the differential - and the Massachusetts estate tax on the first death - to grow!

Limited Liability Companies: As many of our clients know, we often recommend the use of a limited liability company ("LLC") to hold business assets, particularly real estate or other assets that have an inherent risk of liability for personal injury and large lawsuits. An LLC is very similar to the more familiar entity known as the limited partnership. A limited partnership is a business entity wherein limited partners do not have personal liability for business debts, but instead only risk what they invest in the business. The problem is that every limited partnership must have at least one general partner, and that general partner *does* have unlimited personal liability for debts of the partnership. To cope with this risk, a second entity (a corporation) is often formed to serve as the general partner, which is obviously a costly and complex arrangement, particularly for small business and real estate owners. But each member of an LLC enjoys the limited liability of limited partners in a limited partnership, and there is no equivalent to a general partner who must take on the risk. The LLC enjoys all the same tax and other benefits of a partnership, with the added protection of full limited liability. So what if you are already operating as a partnership or limited partnership? No problem. Converting to an LLC is a tax-free event if done properly. Although it involves some paperwork, tax filings, and of course, legal fees, the process is relatively painless, particularly in light of the tremendous protection an LLC offers to the former general partner.

Low Interest Rates: As everyone knows, interest rates have been at historic lows. But it looks like Alan Greenspan and the Federal Reserve are in the process of changing this. And just as homeowners may want to "lock in" today's low mortgage rates, clients with taxable estates and property with the potential for growth may want to act before these historically low rates disappear. Low interest rates provide extra leverage for certain wealth transfer techniques, such as an installment sale to a family member or a gift with a retained interest. Clients interested in transferring property during their lifetimes, either outright or in trust, should make an appointment to review the planning opportunities available in today's interest rate environment.

Retirement Account Withdrawals: Often when we have the opportunity to assist a family with the administration of an estate after the death of a loved one, we discover that the decedent had substantial retirement assets that were not efficiently managed from a tax standpoint. Although tax law establishes certain minimum amounts that must be withdrawn from a person's retirement accounts, it is important to realize that it is often tax-wise to withdraw greater amounts. The reason is that at death retirement assets are subject to both income and estate taxes, whereas most other investments are only subject to estate tax. The optimum amount to withdraw from retirement accounts depends on many factors, and therefore, it is important to consult with a financial or tax advisor regarding your retirement accounts to determine whether you should be withdrawing funds from these accounts rather than your other investment accounts.

Easing the Cost of Estate Administration: The time will inevitably come when you are not there to help your heirs administer your estate. But you can act now to make that administration easier and less costly. We have advised clients to place assets in trust to avoid probate and maximize estate tax savings. Acting now also cuts down on what needs to be done after your death. For example, those with stocks and bonds registered in their individual names can help their heirs tremendously by holding these assets in brokerage accounts titled in the name of a trust designed for this purpose. Those who prefer not to use brokerage accounts can still assist their heirs by registering stocks and bonds in the name of their trusts rather than their individual names. It is also very helpful to have a list of all your assets and the location of important documents, such as deeds and insurance policies, which can be kept with us or with a family member. Although it may be time consuming, putting your assets in order now is much easier for you and much less costly than it will be for your heirs.

With our best regards,

Alexander A. Bove, Jr.

Melissa Langa

Lynn A. Buskey

Robert H. Ryan

Marshal S. Grant

For the Kids



Kids around on a rainy day? It's never too early for them to start acquiring a healthy respect for money, and a good place to start is the U.S. Treasury's website for kids at www.ustreas.gov/kids.

And don't forget to visit our website at www.bovelaw.com!

Tax Tip



Remember, legal fees for tax planning are deductible on individual income tax returns for 2004 if paid on or before December 31, 2004.