
THE LAW FIRM OF
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A PROFESSIONAL CORPORATION

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To: Clients and Friends
From: The Attorneys at Bove & Langa
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THE BOVE & LANGA REPORT



FIRM UPDATE

We are very pleased to share with you some honors that our colleagues have attained. Melissa has been elected and is presently serving as the President of the Boston Estate Planning Council, an organization of over 700 lawyers, accountants, insurance professionals, financial advisors, trust officers, and planned giving professionals who specialize in estate planning.

As reported this month in *Boston Magazine*, Kelly was recognized by *Law & Politics* as a “Rising Star” – one of New England’s top attorneys practicing in the area of estate planning who is under the age of 40. Additionally, in the field of estate planning, Alexander has once again been recognized by *Law & Politics* as a New England Super Lawyer and Melissa has joined the New England Super Lawyer ranks for the first time.

Bob will be presenting for the Massachusetts Bar Association in December on Trust Basics for the General Practitioner and has been actively involved in promoting new legislation in the various legal organizations to revise the Massachusetts Homestead statute.

Our staff has also been busy, with legal administrator Adrienne Lynch spearheading a study group of other Boston legal administrators working to develop guidelines for law offices implementing the new state and federal privacy guidelines. Additionally, we are quite proud that paralegal Jaclyn O’Leary will be completing her law degree at Suffolk University School of Law in December. Last but certainly not least, Jennifer Collins received her paralegal certificate from Northeastern University earlier this year.

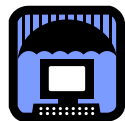


FOREIGN BANK ACCOUNT UPDATE

In our last newsletter, we commented on the IRS crackdown on US persons who held financial accounts in foreign jurisdictions. A sort of “amnesty” program was announced early in the year allowing delinquent US taxpayers to come clean, reporting all such accounts and related income for the past six years, and paying a substantially reduced penalty. This “Voluntary Disclosure Program” (VDP), attracted thousands of US taxpayers, including many we were able to help, but unfortunately, the program ended October 15, 2009.

Unreported foreign accounts and their related unreported income can result in serious penalties, both civil and criminal, for US persons. Even those who failed to meet the deadline of the VDP, however, should still consider their own voluntary reporting, as it is an established policy of the IRS to be somewhat more tolerant and cooperative with taxpayers who come forward on their own, as opposed to taxpayers whose violations have been discovered by the IRS in an audit or blanket investigation designed to uncover such failure to comply with the law. In deciding whether or not to voluntarily file, keep in mind that once you become aware of the responsibility, if you continue to file an income tax return but fail to report the foreign bank account, you would be committing a crime each year.

Accordingly, we encourage people who may have foreign accounts that exceeded \$10,000 in the aggregate for any of the preceding six years to consider reporting those accounts and income. We would be pleased to review each individual situation and advise you of your options and exposure to penalties.



ASSET PROTECTION PLANNING

Each year there are several websites that publish “The Stella Awards”. These are reports of actual court cases awarding plaintiffs huge and unreasonable damage awards similar to the case of Stella Liebeck, who sued McDonald’s for burns she received from hot coffee she bought there. The coffee spilled as Stella was in a car holding the cup between her legs. Stella was awarded more than a million dollars.

To help you, should you end up on the losing end of a case that makes next year’s Stella Awards, the main theme of this Bove & Langa Report is planning to help you protect your assets in the event you, too, serve your coffee too hot. We begin with a set of true/false questions to test your awareness of the issues.



Asset Protection 101: Will You Make The Cut? Your local butcher specializes in “making cuts” but doesn’t he always seem ready to offer advice about any matter under the sun, from how to raise children to how to cut off the claims of creditors? Answer the following true/false questions to test whether your asset protection IQ is a cut above the butcher’s:

- **A Massachusetts principal residence owned by a married couple as “joint tenants” is protected from creditor claims.**

False: For creditor protection, a married couple should own their principal residence as “tenants-by-the-entirety”.

- **The principal residence of a homeowner in Massachusetts is protected from creditors.**

False: A homeowner must record a declaration of homestead in the Registry of Deeds where the principal residence is located in order to protect up to \$500,000 of equity in the principal residence.

- **Umbrella insurance is the type of insurance that is required to cover your residence from storm damage.**

False: If you hit someone with a golf ball while playing golf, if someone slips and falls on your driveway, or if your tree falls on your neighbor’s Lamborghini, umbrella coverage will be there for you! This is relatively inexpensive insurance that provides additional coverage in excess of your auto and homeowner liability protection. We recommend that all of our clients obtain as much as they are able, preferably \$3 million or more of umbrella coverage.

- **The beneficiary of a life insurance policy on your life is protected from your creditors.**

True: In Massachusetts, a lawful beneficiary is entitled to the proceeds against creditors of the insured.

- **You serve on the Board of Directors of the local youth soccer club, and the President absconds with all the club’s money. You don’t need to worry about liability exposure because you are just performing a public service.**

False: You can be subject to liability for actions taken by an officer of a non-profit organization if you serve on the Board. To avoid a “red card”, encourage the organization to obtain Directors & Officers (“D&O”) insurance

and provide a copy of the D&O policy to your own insurance professional for an independent review.

- **You loaned your child your car when she left for college, but since you are no longer the one driving the car, you are not liable for damages in the event the car is involved in an accident.**

False: As long as you still own the car, you are subject to liability. It is advisable to transfer the ownership of the car to your child and have your child obtain insurance.

- **Parents' liability is limited to the payment of rent if they co-sign a lease with their child.**

False: To limit liability to rent payments, and nothing more, parents are advised to just guarantee the payment of rent.

- **All of your retirement assets are protected from your creditors.**

False: In Massachusetts, most retirement plans are protected, but IRA's have limited protection.

- **Annuities are not protected from creditors of the owner.**

True: In Massachusetts, non-retirement annuities are not protected.

How Do You Compare With The Butcher?

- 6 or more correct: You're definitely prime.
- 3 to 5 correct: Not bad, but you need some fattening up.
- 2 or less correct: About right for McDonalds, coffee included.



Can You Trust Your Trust? First, some background. A “trust” is an arrangement created by a person – the “settlor” – where power is given to someone – the “trustee” – to have legal title and control over the trust’s assets (bank and investment accounts, for example) and also names one or more persons – the “beneficiaries” – to enjoy the benefits of the trust property. The trustee manages the trust assets for the benefit of the beneficiaries. Whether the trust arrangement will provide protection against creditors depends upon many factors, including whose property funded the trust, when the transfer happened, who controls the distributions, the identity of the beneficiaries, and where the trust is located. The clear majority rule in the United States is that you cannot create a trust, fund it with your own property, name yourself as beneficiary, and protect the trust property from your creditors. This is called a “self-settled” trust, and simply stated, if you establish such a trust, your creditors can

reach whatever the trustee is empowered to give you, even though there may be other beneficiaries. This is the law in Massachusetts, and under this rule, everything in your typical revocable estate planning trust is reachable by your creditors.

If, on the other hand, you created a Massachusetts irrevocable trust, transferred \$1 million into the trust, and provided that the trustee could only pay you the income, then your creditors could only reach the income interest, and the \$1 million principle would be protected. This assumes the timing of the trust is proper. That is, if you transfer the \$1 million to the trust when you have existing creditors, or creditors who are foreseeable, and the transfer renders you unable to pay them, the “fraudulent transfer” rules would permit those creditors to reverse the transfer and reach the \$1 million.

A minority of states (eleven and growing) permit exactly what Massachusetts prohibits, with Delaware and Alaska having the oldest and most thoughtful laws. There, you can fund an irrevocable trust and name yourself as a beneficiary with promised protection from your creditors (there is very little case law). Again, timing is important, and there are certain “super creditors” that can still reach inside such a “domestic asset protection trust” (DAPT). These super creditors vary in the different asset protection states, but almost all asset protection jurisdictions permit the enforcement of a child support order against a DAPT.

Trusts established in some foreign jurisdictions, called “foreign asset protection trusts” (FAPT), also permit you to be a beneficiary of your own trust. In these jurisdictions, the fraudulent transfer rules are often more favorable to a settlor, and the foreign trustees have greater experience in defending trusts against creditor claims. Whether a Massachusetts trust, a DAPT, or an FAPT meets a particular need depends upon a careful study of the all the facts and a clear understanding of your particular situation and goals.

Fortunately, asset protection is much easier attained when you are simply trying to protect your assets from a child’s creditors and not your own. If a child’s inheritance is left in a “fully discretionary” trust with an independent trustee deciding upon the nature and timing of distributions, under current law, including Massachusetts law, a child’s creditors will be unable to reach those trust assets. This is often an effective way to provide your child with a “prenuptial” without having the child undergo what can often be a painful process with his future spouse. You might protect all or just a portion of the inheritance – every client’s situation is different.

Hopefully you now know enough to ask the right questions of your advisors. And you know that you can’t necessarily trust your trust to give you the protection you desire.



CYA – Cover Your Assets With Business Planning. A question we are often asked is whether a client’s business protects her from liability exposure. The answer is not a simple one, and an example might be helpful to walk through the issues: Let’s assume George and Martha are owners of a very successful nationwide chain of yoga studios called YogaYes. George runs the business and is a 60% owner. Martha put up the capital and is a 40% owner. At

the flagship studio, an employee fails to mop the floor following a rigorous class causing a visiting yogi to fall, hit his head, and suffer brain damage. Hearing the news, a distraught George causes an accident driving home, seriously injuring a pedestrian. Are George and Martha's personal assets protected from the claim of the visiting yogi – the claim that arose “inside” the business (an “inside liability”)? Is YogaYes protected from the claim of the pedestrian – the claim that arose “outside the business” (an “outside liability”)? The answer to these questions will differ depending upon the type of entity used to operate the business.

- *YogaYes Inc. – A Corporation:* A corporation provides inside liability protection, protecting George and Martha's personal assets from the yogi's claim against the business. But, contrary to widespread belief, a corporation does not provide outside liability protection, meaning that the pedestrian in a successful personal injury suit against George could obtain George's 60% shareholder interest and vote to liquidate YogaYes Inc., thereby reaching the business assets.
- *YogaYes – A Partnership:* There are three common types of partnerships, each of which provides a different level of protection: a general partnership (“GP”), a limited partnership (“LP”), and a limited liability partnership (“LLP”).

YogaYes GP: General partners own a general partnership. As general partners, all of George and Martha's business and personal assets are available to satisfy the yogi's claim against YogaYes GP. Holy Svengali! But George's personal creditor – the pedestrian – cannot reach the business assets. All the pedestrian can obtain is a “charging order” against George's partnership interest. We'll move on to the other types of partnership, and circle back to discuss what a “charging order” is later on.

YogaYes LP: Martha hates the idea that her passive investment in the partnership exposes her to such personal liability, so instead they consider a limited partnership where there are both general partners and limited partners. George, as the active business owner, is the general partner. Martha, the passive investor, is the limited partner. So, George's liability to the yogi is the same as above, his personal assets are at risk. Martha, however, now has limited liability. The yogi's reach is limited to her investment in YogaYes LP. Note that George could limit his “inside liability” exposure by holding his general partnership interest as a separate corporation (George, Inc.) and thus only exposing George, Inc. to the unlimited liability exposure. What about the pedestrian? Again, he must look to George's personal assets to satisfy his claim, and can only obtain a charging order against George's partnership interest.

YogaYes LLP: George is now complaining about having two business entities, YogaYes LP as well as George Inc. Not to worry! In the limited liability partnership George and Martha can both be limited partners (there is no general partner) so that the yogi can only reach the assets of the LLP. YogaYes LLP is protected from the pedestrian's claims against George, but the business will still have to deal with the charging order.

- *YogaYes LLC – A Limited Liability Company:* George is the 60% “member” of YogaYes LLC, and Martha is the 40% member. The liability protections practically mirror those of the LLP, but George and Martha may prefer the LLC structure in anticipation that one or the

other might leave the business: an LLC (like a corporation) can exist with a single owner, but a partnership must always have at least two owners.

Let's now turn back to the "charging order". Begin by remembering that the charging order concept only applies to partnerships and LLCs in Massachusetts (and most other states). Briefly, a "charging order" is the outside creditor's right (here, the pedestrian) to receive any distributions YogaYes makes to George. If YogaYes has business reasons not to make distributions of profit to the owners (the company is saving to open a new studio, for example), then the pedestrian has little recourse but to wait until YogaYes decides to make a distribution to George, or to pursue a settlement with George. In addition, the pedestrian with a charging order has absolutely no management or voting rights, meaning that the pedestrian cannot participate in the decision to make distributions, nor can he participate in the decision to continue or to dissolve YogaYes. Obviously there are limits to how far this can be taken. Nevertheless, there are probably a number of legitimate business reasons to withhold distributions or to make only limited distributions to George and Martha. Note, importantly, that if YogaYes never makes a distribution (greed, greed, greed – oink, oink, oink), at some point a Massachusetts court might order a "foreclosure" on the charging order and give the pedestrian the opportunity to acquire George's entire YogaYes interest in a foreclosure sale. Even so, the pedestrian would still be unable to participate in the operation of YogaYes, but would be entitled to George's 60% of ongoing distributions and 60% of liquidation proceeds (even if it exceeded the pedestrian's claim against George!).

As you can see, George and Martha have a lot to think about as they choose a business structure for YogaYes. But whatever is chosen, the asset protection inherent in each of the entities is only available if the entity is properly managed as a business and not as a personal bank account for a business owner, and if no debts of the business are personally guaranteed by an owner of the business. Choosing the entity is only the first step. If George and Martha don't respect the entity, neither will a court.



A Special Strategy for (Happily) Married Couples: A special protective strategy developed by our firm for (happily) married couples is the post-marital property settlement agreement. It is well-settled law that under the marital relationship, each spouse has rights to a share of the marital estate, depending in part on the spouse's respective contribution to the relationship. We believe that it is not necessary to go through a divorce to establish the respective rights of the spouses, but rather, that they can recognize and agree upon those rights themselves. This would be done under a written agreement between the spouses after full disclosure of their respective assets and while each is represented by independent counsel. The terms of the agreement are then reflected in an actual division of the marital assets as called for under the agreement. In some cases, it will be advisable to record the agreement with respect to certain assets (particularly real estate) to put creditors "on notice" of the ownership. If properly carried out, we believe that a post-marital agreement can successfully protect marital assets from a non-debtor spouse's creditors, even, perhaps, in the face of existing claims, on the basis that the transferee spouse had a pre-existing right to her or his share of the marital assets.

IN CLOSING ...

We have to acknowledge that reading some of this material can be – as Melissa puts it – a snooze. Nevertheless, we all work hard to accumulate assets for our own and our family’s benefit, and it is important that we become aware of ways to protect those assets. Unfortunately, we are coming up on a time of the year that has a way of causing a *reduction* in assets, so we may have a little less to protect, but the issues are no less important.



A HOLIDAY MESSAGE

The “hustle and bustle” of the holidays often draws our attention away from some of the more mundane issues of life, including asset protection and its important place within estate planning. In a sense this is fine, because instead we turn our attention to family, friends, and the spirit of giving to others. With that in mind, we thought we would add a little more humor to the mix by offering our own holiday story – that of an estate contest, but not just any estate – the estate of someone who the “cold within him froze his old features, nipped his pointed nose, made his eyes red, his thin lips blue, and he spoke shrewdly in a grating voice.” Can you guess? Bah, humbug, we’re not telling! Just go to our website and click on “Holiday Story” to see for yourself.

With our sincere appreciation, and our warmest and heartfelt wishes to all of you for a happy and healthy holiday season.

The Bove & Langa Report has been specially prepared by the attorneys at Bove & Langa. The material provided herein is for educational and informational purposes only and should not be construed as legal advice. Always consult your attorney – hopefully at Bove & Langa.

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