

To: Clients and Friends  
From: The Attorneys at the Law Firm of Bove & Langa, P.C.  
Re: Important Recent Developments and Planning Opportunities: March 2006

## **FIRM UP-DATE**

Alexander was invited to speak on the subject of Trust Protectors at an International Estate Planning Conference in New York sponsored by the New York State Bar and the Society of Trust & Estate Practitioners (STEP) in March. Melissa has been appointed to the Animal Rescue League of Boston's Planned Giving Committee. The oldest Animal Rescue League in the United States, having its start in 1899 as an organization concerned with the welfare of work horses, the League is a world recognized innovator of rescue techniques as well as operating as an adoption shelter, and was instrumental in coordinating the pet rescue efforts following the devastation of Katrina. In March, Bob will join Alexander at Massachusetts Continuing Legal Education to lecture on the effect of the new Bankruptcy Abuse Prevention and Consumer Protection Act on homestead protection and other asset protection matters. Finally, we announce that Lynn has decided to leave the bustle of our downtown practice to open her own law firm in the suburbs. We will miss Lynn's quick legal mind and sharp wit and wish her the very best in the future.

## **NEW DEVELOPMENTS**

**A Refund For Massachusetts Capital Gain Taxes Paid In 2002?** Taxpayers who had a capital gain transaction after April 30, 2002, may be entitled to a refund. In order to claim the refund, the Department of Revenue (the "DOR") has set up a special abatement process with strict requirements. The DOR is strongly encouraging taxpayers to use the online application which is available at the DOR's website, [www.mass.gov/dor](http://www.mass.gov/dor). If taxpayers choose to file a paper application, they need to use Form CA-6. The filing deadline for the abatement for most taxpayers is June 30, 2006, so time is of the essence.

In reviewing whether you are entitled to a refund, it is important to note several key issues. The DOR is not able to automatically determine the potential refund since the taxpayer did not previously have to provide the relevant holding period information for the affected capital gains. Also, the law provides that the refunds will be paid without interest in four annual installments, however, the DOR may refund payments that total \$1,000 or less in a single lump sum. Remember the state refund will be treated as income for federal income tax purposes.

**Medicaid Update:** Congress and the President have recently imposed substantial limitations on the ability to qualify for Medicaid as part of the recent Budget Act known as the Deficit Reduction Act. Among some of the key provisions, the new law imposes longer penalty periods for transfers made to qualify for Medicaid, and the start date of the penalty period has been deferred in some cases to the later of the date the applicant enters the nursing home or applies for benefits. There are also new limitations imposed on the use of an annuity as part of a Medicaid plan. Going forward, the institutionalized annuitant must name the State as the primary beneficiary in the event the

annuitant dies. There are many other changes that will impact the ability to qualify for Medicaid that will be spelled out by new regulations to be issued by the government.

**2006 By The Numbers:** As many of you know, our federal gift and estate tax laws are currently in a state of flux with no certainty in sight. So here are some of the 2006 numbers to keep you in the loophole, oops, loop. For federal gift and estate tax purposes you can gift \$1 million over your lifetime, but you can pass \$2 million (less any amount you have gifted) at your death. So if you want to make a really large gift, we recommend that you...well, let's talk. The generation-skipping transfer tax exclusion, which is the amount you can pass to grandchildren and lower generations without a penalty tax, is also \$2 million for 2006. The Massachusetts estate tax exclusion is only \$1 million, so everything in excess of that passing on death will be taxed by Massachusetts.

The federal annual gift tax exclusion has gone up this year to \$12,000 per donee, and remember that these annual gifts do not use up any of your \$1 million lifetime gifting exclusion. As a reminder, payment of tuition and medical expenses (including health insurance premiums) if paid directly to the institution or provider, are also tax free gifts that do not use any of your \$1 million lifetime gifting exclusion. We have no gift tax in Massachusetts.

**Kinder, Gentler, SSI Rules:** Supplemental Security Income (SSI) is a federal program that supplements the income of aged, blind, or disabled persons who meet certain income and asset guidelines. In general, SSI provides cash to meet the basic needs of shelter, food, and clothing. Where a family wishes to insure that a disabled child will qualify for SSI benefits, an estate plan can be crafted to shelter the disabled child's inheritance by placement of the disabled child's share of the family wealth into a fully discretionary trust. Thereafter, the trustee must be mindful of federal rules that will reduce the SSI benefit if the disabled child receives certain income or in-kind support from the exempt trust. New rules effective in 2005 now permit the trustee to provide clothing for the disabled child, either by cash distribution or by purchasing the clothing and giving it to the disabled child, without reducing the SSI benefit. The disabled child may now also own one car of any value (to be used by the child or by a member of the child's household) and is no longer limited to a \$2,000 ceiling on the value of household goods.

**The Massachusetts Principal And Income Act:** After years of debate, on January 2, 2006, the Massachusetts legislature passed the Massachusetts Principal and Income Act. In short, the Act is intended to provide guidance as to what constitutes principal and what constitutes income of a trust, and also to give trustees the power to make adjustments between principal and income when making distributions to beneficiaries. For example, say your father sets up a trust for your benefit during your lifetime, which pays all of the income to you but upon your death distributes all the remaining trust property to your brother. Your father funds this trust with stock. Clearly, you are entitled to receive all of the dividends. However, are you entitled to receive the proceeds of gain (as "income") if the trustee sells the stock for a profit or is it "principal" to be held for your brother? What if the stock was paying dividends equal to roughly 2% of the value of the shares? Could the trustee make an adjustment between income and principal to provide you with income equal to at least a 4% or 5% of the value of the trust property? These are the types of questions the Act covers,

so if you are an income beneficiary or remainderman of a trust, you should be aware that Massachusetts may now offer you a better deal than you are used to getting.

**Medicare Prescription Drug Coverage Has Begun:** For those who joined a prescription drug plan prior to December 31, 2005, the new Medicare prescription drug coverage began on January 1, 2006. This new insurance is available for everyone with Medicare, regardless of income and resources. If you are eligible but have not yet chosen a plan, you must do so prior to May 15, 2006, to activate coverage for 2006. After May 15<sup>th</sup>, the next enrollment period begins November 15, 2006, and you may pay a penalty for failing to join a plan during your earlier period of eligibility. If you join prior to May 15<sup>th</sup>, your coverage will begin the month after you join. Those eligible should have received a handbook from Medicare entitled “Medicare & You 2006”, which provides a comparison of the drug plans available in each state. This information is also accessible on the Medicare website, [www.medicare.gov](http://www.medicare.gov), or you can call 1-800-MEDICARE (1-800-633-4227). The main factors in choosing a plan are cost and coverage.

**No Risk Life Insurance – Too Good To Be True?** One of the more recent pitches proposed by some financial advisors is the no-lose no-risk two year premium financing plan for life insurance. Briefly, a person would purchase a large insurance policy under a plan where a lender would finance 100% of the first two years’ premiums on a non-recourse basis. (“Non-recourse” means the purchaser would not be personally liable on the loan). At the end of the two year period, the person (the insured) would have the option of: (1) walking away from the plan with no obligation (the lender would acquire the policy), or (2) taking over the policy by accepting liability on the loan and paying future premiums, or (3) selling the policy to a third party. This last option would typically arise where the insured was of an advanced age and had a material downturn in health status after the policy was issued. Thus, from a purely financial standpoint, the insured had something to gain and nothing to lose.

It was the “nothing to lose” that gave the New York Office of General Counsel some concerns in reviewing this somewhat aggressive plan, together with the fact that the insured probably would not have purchased the policy in the first place absent the favorable financing arrangement. While it must be noted that this is only one state’s opinion on the matter, the General Counsel, representing the New York Insurance Department, struck down the plan as being “an arrangement intended to facilitate the procurement of policies solely for resale.” And we agree that the motivation to purchase the policy in this case is not for the insurance per se, but rather for the “economics” of the deal.

## PLANNING OPPORTUNITIES

**Asset Protection Can Begin At Home:** Asset protection can take many forms. A good plan will consider all the possible options, from the simplest to most complex, and it will apply those that, in the opinion of the advisor, will provide the appropriate protection for the particular client and family. Certainly not everyone needs an offshore trust or a Delaware limited liability company. Sometimes a simple declaration of homestead will do. In many cases, the best asset protection is adequate insurance coverage. In this regard, many people overlook the protection offered by an

“umbrella” policy, easily available through their homeowners and automobile insurance. For a reasonable annual premium, such policies offer coverage from \$1 million to \$5 million for non-business personal liabilities which may occur (we generally recommend \$3 million of coverage). This type of coverage could protect you against loss of your home and life savings in the event of a catastrophe. To obtain coverage call your homeowner’s or automobile insurance agent.

### **Thinking About A Florida Domicile? What You Need To Know About The**

**Intangibles Tax:** The intangible personal property tax is a tax imposed on a Florida resident (individual or entity) who owns, manages, or controls certain intangible personal property (including stocks, bonds, mutual funds, loans, notes, ownership interest in an LLC, and sometimes accounts receivable) including a trust beneficiary who has a certain type of beneficial interest in a trust. The tax is imposed on the intangible personal property owned by the Florida resident as of January 1<sup>st</sup>, and is based upon the value of that property as of December 31<sup>st</sup> of the previous year. The first \$250,000 of assets subject to the tax are exempt (\$500,000 for a married couple), and thereafter the tax is imposed at the rate of 50¢ per every \$1,000 (in 2006). Thus, for example, the intangible personal property tax for an unmarried individual on \$5 million would be about \$2,375 (after the \$250,000 exemption). The tax is paid annually by June 30<sup>th</sup> and there are discounts if you pay before June 30<sup>th</sup>.

There are numerous exemptions to the Florida intangibles tax, including cash, certain money market accounts, U.S. and Florida bonds, and property owned by certain trusts, even if the trustee is a Florida resident. To avoid the imposition of the tax, you simply hold your assets in an exempt manner. How? Well, assuming you wish to continue to invest in equities (and who doesn’t!), you can avoid the tax by giving ownership and control to what is called in the trade an irrevocable fully discretionary “FLINT trust” (for Florida Intangibles Trust) for a period of time ranging from sometime before January 1<sup>st</sup> to sometime within the succeeding year. We recommend a FLINT trust last at least 4 months before the assets revert back to the taxpayer since the Florida Department of Revenue has approved of a 4 month FLINT Trust in an opinion to a taxpayer.

**Retirement Benefits:** For those of you who selected the beneficiaries for your retirement accounts so long ago that you could have listed Elvis as a beneficiary, it’s probably time to call your benefits administrator or plan custodian. Even if it wasn’t quite that long ago, you should check to make sure that your beneficiary designations are coordinated with your estate plan. Because of the overlap of income and estate tax considerations, planning for retirement benefits is often difficult, especially where the best course for a family is to name a trust as the account’s beneficiary. Taking the time to make sure that you have designated the correct beneficiaries for your retirement plan – and that the beneficiaries are designated correctly – can allow for greater tax-deferral, lower income taxes, and greater security for the loved ones you leave behind.

## ESTATE PLAN MAINTENANCE

**When You Wish Upon A Trust:** It is a fact that most trusts designed to continue after the death of the creator and his or her spouse, typically for children and grandchildren, direct the trustee only in a very general way as to making distributions. For instance, we commonly give the trustee the discretion to distribute for the “health, education, maintenance, and support” of the beneficiaries. While this covers most situations, it is not very specific in advising the trustee exactly how you might distribute trust funds in every case if you were living. And since it is your trust, your family and your money, shouldn't the trustee have a better idea of just how you might decide? Recently, more and more clients who establish trusts are following our recommendations to prepare statements to their future trustee advising them what the clients had in mind when they envision the administration of the client's trust. Such statements are called “letters of wishes” and are designed to give the trustee some insight into what you, the creator of the trust, had in mind in distributing the trust funds. While the usual letter of wishes is not actually binding on the trustee (that is, the trustee could decide not to respect it), it does give the trustee considerable and valuable guidance as to your wishes in administering the trust. Think about preparing a letter of wishes for your trustee.

**Gift Tax Returns:** Don't forget that in addition to your income tax returns, federal gift tax returns are also due in April. Gift tax returns are due if you made any gifts in 2005 of cash or property in excess of \$11,000 to any one donee, or if you made gifts of property that you valued at less than \$11,000 per donee with the help of a valuation discount. Regardless of whether an out-of-pocket gift tax is owed, the return should be filed. This is particularly important if there are any issues open to challenge by the IRS, such as the value of gifted interests in real estate or a business, because the filing of a complete gift tax return will start the running of the three year statute of limitations for the IRS to challenge your gift. Without a return, there is no limit to the IRS' time to challenge your gift values, which can result in unexpected adverse tax consequences. Don't wait for the tax crunch in April, get things in motion now to be sure to meet the filing deadline.

**Keep Your Records:** For those of you with corporations, partnerships, and limited liability companies, it is important to remember that even if your partners are also at the family dinner table, you are still running a business. Keeping business records up to date is quite simple and quite necessary. Massachusetts corporations and limited liability companies must file an Annual Report with the Secretary of the Commonwealth, and it is a good idea to check the entity's history on the Secretary's website to ensure all of your Annual Reports have been filed since to date. [You may also have to file in another state depending on where the entity is organized, holds property, or does business.] Every business should also be having at least one annual meeting, if not more frequent meetings throughout the year to discuss what has happened over the past year and what the goals are for the coming year. Minutes of this meeting should be prepared and added to the record book as evidence that it occurred and who participated. All votes with regard to major decisions, including the acquisition or sale of property, changes in the business goals, the appointment or continuation of elected positions (president, treasurer, directors, etc.), and the like should be voted on and documented in the record book as well. It is a good idea to add notes of any major discussions or transactions throughout the year even if there was no formal meeting. In addition to

having a record of what was discussed and decided in the event of confusion or a dispute, these business records could serve as evidence that you are operating a valid business and not just seeking liability protection or other entity benefits for your family hobby.

## SUMMARY

We hope you have found this newsletter informative. If you wish to discuss adding a letter of wishes to your plan, the filing of a gift tax return, the maintenance of your business records, a FLINT trust, or any other idea mentioned above, please do not hesitate to contact any of us.



### Corporate Filing Tips



In this age of technology, it is quite easy to access your corporate filing records right online. You can also file many forms online making it easier than ever to keep up with your records. Go to [www.sec.state.ma.us/cor](http://www.sec.state.ma.us/cor).

### Savings Bond Tip

To transfer U.S. savings bonds to your trust, go to [www.publicdebt.treas](http://www.publicdebt.treas) and follow the links to Form PD F 1851 (Request to Reissue United States Saving Bonds to A Personal Trust). The form is self-explanatory, but anyone at our firm can assist you if you encounter a problem.