THE LAW FIRM OF

BOVE & LANGA

A PROFESSIONAL CORPORATION

TEN TREMONT STREET, SUITE 600

BOSTON, MASSACHUSETTS 02108

Telephone: 617.720.6040 Facsimile: 617.720.1919

WWW.BOVELANGA.COM

To: Clients and Friends

From: The Attorneys at the Law Firm of Bove & Langa, P.C.

Re: Important Recent Developments: March 2005

FIRM UPDATE

We are pleased to note that members of our firm continue to share their knowledge and expertise with other professionals and members of the public through seminars and articles. For instance, our colleague, Bob Ryan, is presenting a lecture in May to professionals on Massachusetts estate tax and Mass Health (Medicaid) regulations; Lynn Buskey is doing pro bono legal work supervising local law students in providing legal services to indigent clients in the Boston area through Shelter Legal Services Foundation, Inc.; Melissa is presenting at an American Bar Association seminar in Washington, D.C. on the subject of establishing an asset protection trust; and Alexander will be presenting at the annual meeting of the Top of the Table in Hawaii in September (the Top of the Table group is an elite subdivision of the Million Dollar Round Table at which Alexander spoke last year). Those of you who belong to professional or other groups that you feel would benefit from a presentation within our areas of expertise should feel free to contact us to discuss the possibility of having a member of our firm make a presentation to your group.

NEW DEVELOPMENTS

Don't Want to Wait 20 Years To Collect On Your Massachusetts Lottery Winning Ticket? Effective July 2004, the state of Massachusetts now allows a lottery winner to convert annual payments into a current lump sum payment by assigning the right to the future payments. This applies to all games offered by the Lottery. Unfortunately, in order to receive the lump sum, the winner must file a Petition in Superior Court to request that the Court assign their right to the winnings to a person or entity named as the assignee in a Court Order. Currently, only the Norfolk Superior Court is processing these requests since the Lottery Headquarters are located in Norfolk County. There are specific entities authorized by the state to purchase the stream of annual payments, and at least some will allow a winner to assign less than the full number of remaining payments. In order to take advantage of this option, you must first win the lottery, and then you must actually receive the first payment from the state.

Massachusetts income tax treatment of certain estates and trusts. Massachusetts beneficiaries of estates and trusts have been accustomed to having Massachusetts income tax on estate and trust income paid by the estate or trust, even when the beneficiary receives distributions. This is very different from the federal taxation of estate and trust income, which flows through to beneficiaries to the extent they receive distributions. With certain exceptions, Massachusetts has now brought its taxation of estate and trust income into line with federal law. What does this mean for you? Life has gotten harder for Massachusetts beneficiaries, who must now include estate or trust income in calculating their Massachusetts estimated tax payments, as they do with their federal estimated tax payments. But life has gotten easier for executors and trustees of estates and trusts, who are no longer required to make Massachusetts estimated tax payments if they distribute income to Massachusetts beneficiaries.

What Is The "Value" Of Donating A Used Motor Vehicle or Boat To Charity? The value of a charitable deduction placed on the donation of a used motor vehicle or boat to charity has commonly been based on the "fair market value" of the item, generally determined by the use of a trade journal, such as the Kelley Blue Book. However, effective January 1, 2005, the determination of the value of the donation is subject to new, stricter requirements. For example, if the value of the motor vehicle or boat is considered to be greater than $500, the donation must be reported on IRS Form 8283, and the condition of the vehicle must be taken into consideration in determining fair market value. If the charitable organization sells the motor vehicle or boat, then the deduction will be limited to the gross proceeds from the sale, which must be reported by the charitable organization to the IRS. Only vehicles that a charity retains for use in charitable purposes will qualify for a charitable deduction based on its fair market value. The Internal Revenue Service is expected to issue more guidance on this issue during the year.

Massachusetts income tax treatment of installment sales. For federal income tax purposes, the capital gain on installment sales is automatically deferred to the year in which payment is received. Many clients are surprised when they learn that Massachusetts has historically treated installment sales differently, requiring the taxpayer to make a separate election to defer the gain and post a bond if the deferred tax exceeded $1,500. Massachusetts has now relaxed these requirements and brought its tax treatment of such sales more into line with federal law. A separate election and bond is no longer required if the gain is less than $1 million. Clients should remember, however, that Massachusetts still requires a separate election and posting of a bond if the gain equals or exceeds this $1 million threshold or if the taxpayer elects out of the federal installment sale treatment. In addition, those with installment sale gain of less than $1 million cannot elect out of installment sale treatment for Massachusetts purposes unless they elect out for federal purposes as well.

New Rules For Nonqualified Deferred Compensation. There are new rules that apply to most nonqualified deferred compensation plans for amounts deferred after December 31, 2004. The new law potentially applies to any arrangement which postpones payment of compensation to another year, including severance agreements, defined benefit nonqualified plans, Supplemental Executive Retirement Plans (SERPs), and arrangements with non-employees, such as directors and consultants. Under the new rule, codified in Section 409A of the Internal Revenue Code, restrictions are imposed on funding, distributions, and elections to participate in the plan. Unless specific conditions are met, all nonqualified deferred compensation will be

taxed once an employee is *vested* as opposed to the prior law which generally did not impose a tax until the funds were distributed to the employee. In addition, violations of Section 409A will result in a 20% penalty in addition to the immediate taxation of deferred compensation. The Internal Revenue Service is expected to issue guidance during 2005, since it is anticipated that most deferred compensation plans subject to Section 409A will require amendment by the end of 2005. Obviously, these rules are quite complex, so if you expect to receive nonqualified deferred compensation, you should discuss these new rules with your tax advisor.

PLANNING OPPORTUNITIES

Tired of the 9-5 Routine? Business Owners Can Semi-Retire and Take Advantage of New Low Tax on Qualified Dividend Income. Congress gave individual (non-corporate) shareholders a gift for tax years 2003 – 2008 when it decided to tax "qualified dividend income" at the capital gain rate of 15% rather than at the higher ordinary income tax rate. An unintended benefit of the law is the flexibility it has given business owners – Mom and Dad – who want to move the company to the next generation while still remaining active on a part-time basis. Prior to the new law, the trick was to structure the succession plan so that the redemption of the older generation's stock was treated as a "sale or exchange" to avoid dividend treatment. But this required Mom and Dad to redeem all of their ownership interest and cease participation in the company, even as an employee, in order to avoid their "cash out" being taxed as a dividend at the ordinary income tax rates. With the new lower dividend rate, Mom and Dad can remain involved in the company they created while enjoying the financial benefits of cashing out. Many factors must be analyzed to determine which redemption method is best for a particular family. If you are contemplating a transition, we would be happy to meet with you and your accountant to begin the planning process.

Proud to Live in America? If Not, There's a Tax to Pay! Our tax code has long contained rules governing the tax treatment of U.S. citizens who renounce their citizenship and move abroad. These rules also cover certain green card holders who turned in the card. In a nutshell, if the taxpayer's intention was to avoid U.S. tax, then the IRS imposes a ten year income tax regime upon the expatriate. The subjective test of intent has now been replaced with an objective test that simply asks "Are you wealthy?" If yes, then the ten year income tax regime applies. If not, then you may go your merry tax-free way, even if your sole intention was to avoid tax. So, are you "wealthy?" You are if your net worth is at least $2 million *or* if your "net income tax" (as defined in Sec. 38(c)(1) of the Internal Revenue Code) averaged over a five year period is greater than $124,000. And once you leave, watch out for return visits. An expatriate who is physically present within the U.S. for more than 30 days in a tax year will be treated that year as a U.S. resident for federal tax purposes. Thus, the expatriate who summers on Nantucket will subject her gifts made that year to the gift tax (regardless of the situs of the gift), and may be subjecting her worldwide assets to the estate tax. As with any tax law there are exceptions, and the new law also has important notice requirements. So it will be wise to consult with a tax advisor before any action is taken. In other words, look before you leave.

The Meaning Of Life (Estates). A life estate results when a person transfers property (typically a home) to one or more others (typically children) who are called the "remaindermen" and reserves the right to continue to live in the property for life. On the death of the life tenant, but not before that, the remaindermen then own the property outright. Use of the "simple" life estate is a popular method of asset protection, including

protecting the home in the event the parent enters a nursing home and qualifies for Medicaid. There are, however, a number of tricky issues to this seemingly simple plan, such as income tax issues and practical issues relating to the sale of the home during the life of the life tenant. If you have such a plan or are thinking of it, you should get all the details before taking your life estate into your own hands.

Split Purchase Of A Residence. For families with large estates, one of the few remaining loopholes in the estate tax laws is the split purchase of a residence. Under this plan, a member of the older generation (typically a parent) and one or more members of a younger generation (typically children) would jointly purchase a residence in specially designated shares, which is what gives rise to the benefit. That is, the parent would purchase a life estate in the residence and the child would purchase the remainder. For tax planning, the transaction must be done through a special trust. Since the life estate ends on the parent's death, and since the parent never owned any more than a life estate in the property, there is no value to include in the parent's estate. An example will illustrate: Gloria, age 68, and her daughter, Glenda, jointly purchase for $ 1 million a summer home that is to be used by Gloria for her life. Thus, Gloria purchases a life estate, which at her age is valued at $461,010, and Glenda buys the remainder for the balance of $538,990 (with her own funds – this is important). Whether Gloria dies a month later or ten years later, none of the home's value will be taxed in her estate, and Glenda will own the property estate tax free.

Using 529 Plans to Purchase College Residence. Have you ever wondered whether you can use money in a 529 Plan to invest in a residence for your child while he or she is away at college? You can, but with certain restrictions. Spending from a 529 Plan for this purpose is limited to the amount set annually by the school as the cost of off-campus housing. To work with this limitation, you could purchase the residence and enter into a rental agreement with your student. Your student could then withdraw money from the Plan and pay you rent up to the allowable amount. This will, of course, generate rental income; but there are many ordinary rental expenses, such as maintenance expenses, real estate taxes, condominium fees, mortgage interest, depreciation, and even reasonable travel expenses to monitor the property, that can offset this income. If you sell the residence when your child graduates, there will, hopefully, be a gain on the sale. This will result in taxable income, but it will generally be taxed at the preferred long term capital gain rates and it is, after all, gain!

Tying the Knot? With the frequency of divorce, prenuptial agreements (also called antenuptial agreements) are becoming more common. A prenuptial agreement should be considered in many circumstances, such as if the parties have disparate wealth, if one or both anticipates a sizable inheritance, or in a second (or third or fourth...) marriage when there are children from the previous marriage(s). As they grow in popularity, prenuptial agreements are being more frequently tested in our courts. Some are successful, while others fail to provide the expected protection. There are many things that can impact the dependability of a prenuptial agreement, for example, signing under duress too soon before the wedding (don't even bother bringing a pen to the altar!), both parties not having competent legal representation, or one party's failure to adequately disclose assets. Recently, an important case was decided in the Massachusetts courts wherein the waiver of alimony by the poorer spouse was void under the circumstances of that case, and alimony was awarded despite the couple's prenuptial agreement. Note that the court did not hold that a waiver of alimony would always be void, but it must be reasonable under the circumstances at the time the agreement is entered into,

taking into consideration such factors as the age, education, and other resources (or lack thereof) of the spouse waiving alimony rights. The lesson here is that it is important to understand just what types of provisions will and will not be enforceable in a divorce, otherwise you'll have difficulty *un*tying your knot.

Can You Avoid the New Massachusetts Estate Tax? Massachusetts had once been considered an unattractive place to spend your golden years due to a harsh estate tax, and back then, many elders relocated to more favorable estate tax jurisdictions, such as Florida. Subsequently, Massachusetts adopted an estate tax law similar to Florida's and lured its old taxpayers back home. Well, they've gone and done it again! The new Massachusetts estate tax laws are now (again) harsher than some other states, including Florida, and it just may be time to migrate south once again. Although changing your residency to Florida is a viable estate tax planning technique in light of the new tax laws, like any planning, it must be done properly to be effective. Not only must residency be established under a facts and circumstances test (and the taxing authorities will put you to the test!), but it is also important to understand that any "Massachusetts property" will still be taxed by Massachusetts regardless of the decedent's residence absent additional planning with regard to structuring such assets. So it is important to consult with your estate planning attorney to properly structure your assets, particularly if they are of a sort that you can't take with you (like that vacation home on the Cape), to ensure your Massachusetts estate tax is eliminated, or at least reduced to the extent possible.

PRACTICAL TIPS

Tips for Buying, Selling, and Holding Real Estate. If you have ever purchased or sold real estate you have probably experienced the stress that most people suffer from such a significant transaction. There are ways to reduce this stress and move forward with the confidence that you have taken the proper steps to protect yourself and minimize the potential problems that buyers and sellers alike often encounter. The first piece advice, of course, is to engage an attorney *at the start of the process*. More often than not, clients engage an attorney after the listing, or after the offer is accepted, or even after the purchase and sale agreement has been signed. By that time, the problems have already begun – whether they know it yet or not. Let your attorney know that you are beginning the process and have them review *any and all agreements* that you are asked to sign, including the broker's agreement and especially the offer and the purchase and sale agreement. These documents are not simply boilerplate red tape; they are legally binding contracts that can come back to haunt you if not carefully reviewed. Just think, if its not important, why would you be asked to sign it?

Already purchased? If you have recently purchased real estate, have you checked with your estate planner to ensure it is titled to properly fit into your estate plan? The way real estate is held can have consequences to your estate plan with regard to your efforts to avoid probate administration, to protect against creditors, and even to reduce your estate taxes. No single plan fits every person or every couple, so it is important to make your attorney aware of your goals and to keep the attorney informed when new assets are acquired so that title may be reviewed for its overall fit into the plan. If you are considering the purchase of new property, you can avoid additional estate planning steps by working with your estate planning attorney *prior to the purchase* to take title in a manner that best fits into your estate plan.

Did You Gift Or Loan Your Child Money To Purchase A Home? Often we meet with clients who indicate they made a "gift" to a child in order to assist in the purchase of a home or other investment, but then it is revealed that the parent expects that the gift be repaid. In deciding whether to make a gift or loan to a child, it is imperative that the expectations be understood and agreed to by all parties and be properly disclosed to third parties (e.g., a commercial lender). If it is agreed that a loan is actually being made, then proper documentation should be put in place with the terms clearly spelled out so that there is no misunderstanding at a later date. And if it is agreed that a gift is being made, a gift tax return may need to be filed.

We hope you enjoyed our newsletter, and if you wish to discuss any of these matters or have any suggestions of what you would like to see in future newsletters, please call or email any one of us.

$ Tax Tips $

Taxpayers who itemize deductions are entitled to deduct contributions made by cash, check, or credit card to tax-exempt U.S. charities for the tsunami relief efforts on their *2004* income tax return if the contribution was made by January 31, 2005.

You can also deduct unreimbursed commuting expenses, including FAST LANE tolls and MBTA passes. Be sure to check the limitations on this deduction.

Don't forget that you have until April 15th to make your retirement plan contributions for the 2004 tax year. Be careful to watch the contribution and deduction limitations.

This update is provided for educational and informational purposes only
and is not intended and should not be construed as legal advice.

This update is provided for educational and informational purposes only and is not intended and should not be construed as legal advice