

CLARIFYING THE TAX TREATMENT OF GIFTS TO GRANTOR TRUSTS IN 2010 - NOTICE 2010-19

Back in 2001, Congress passed the Economic Growth and Tax Relief Reconciliation Act (EGTRRA). While many provisions of EGTRRA have been acutely focused on by planners since that time, one provision has received little attention until recently. Under Section 511(e) of EGTRRA, Section 2511(c) of the Internal Revenue Code was added and provides that for transfers between December 31, 2009 and January 1, 2011, except as provided in the regulations, a transfer in trust shall be treated as a transfer of property by gift unless the trust is a grantor trust.

As 2010 approached, planners began to wring their hands over what this provision means: (1) does it make incomplete gifts to non-grantor trusts complete; (2) does it make completed gifts to grantor trusts incomplete or (3) both? In Notice 2010-19, the IRS confirmed that it is the former, but not the latter. So planners can breathe easier knowing that completed gifts to grantor trusts are still an effective planning technique in 2010.

NOT ALL CONDOMINIUMS ARE CREATED EQUAL

Many people fail to see the benefit of consulting with an attorney before making a residential condominium purchase. The real estate attorneys in our firm have been called upon to suggest revisions to declarations and plats for residential condominium projects which were established incorrectly under Chapter 703 of the Wisconsin Statutes. This failure to meet the strict requirements of the law raises serious questions concerning whether a project is, indeed, a condominium under the legal definition.

The expenses that can be incurred by unit owners to correct an ineffective declaration or plat under the Condominium Act can be significant. The problems we have seen in the past could be identified in an initial document review. Armed with that information, a prospective buyer might decide not to purchase a unit in a condominium with such problems.

As many Baby Boomers downsize from their homes to condominiums, they should consider having an experienced real estate lawyer review the condominium documents to make sure there are no problems of this sort hidden in the disclosure materials they receive before they buy.

THINK YOU KNOW HOW FAR YOU HAVE TO GO FOR YOUR EMPLOYEES? THINK AGAIN.

Two recent decisions have surprised both employers and legal analysts evaluating what measures employers must take under the law.

In one case, the Seventh Circuit Court of Appeals concluded, in *Ekstrand v. School District of Somerset*, that a teacher suffering from “seasonal affected disorder” has a “disability” under the American with Disabilities Act and that a school district had to accommodate that disability by moving the teacher to a room with natural light. The appellate court reversed the lower court’s dismissal of the teacher’s failure-to-accommodate claim, concluding that, after the teacher had informed the district that natural light was the “key” to improvement in her seasonal affective disorder, the school district was obligated to provide her with a room allowing natural light unless it would impose an undue hardship on the district to do so.

Elsewhere, the Indiana Court of Appeals recently determined, in *PS2, LLC v. Childers*, that an obese worker who suffered a back injury on the job was entitled to workers’ compensation not only for the cost of the back surgery to remedy the injury, but also for the \$20,000 to \$25,000 cost of lap-band surgery to reduce the employee’s weight in order to promote the success of the back surgery. Despite the fact that the employee was obese (340 pounds) before the accident, the court upheld the state workers’ compensation boards’ decision to require the weight-loss surgery because the obesity was a “pre-existing medical/health condition” that “combine[d] with the accident at work to create a single injury” for which the employee was “entitled to treatment.”

These cases are just two recent examples of continuing developments providing that, what may seem to be reasonable limits of how far employers must go to cover costs or provide reasonable accommodations to their employees related to their jobs, may not actually encompass the expansive obligations of employers under the law.

HEALTH CARE REFORM PASSES; BUSINESSES NEED TO START PLANNING FOR IMPLEMENTATION

The Patient Protection and Affordable Care Act has been signed into law, and with certain modifications to be added through the House Reconciliation Act, health care reform is certain to have a substantial impact on American businesses in the years to come. Among other things, the reform includes over \$400 billion in revenue raisers and new taxes on employers and individuals as well as a laundry list of new reporting requirements. More forms and red tape are in the cards for all of us. Here is a list of a few such changes:

- Starting in 2014, individuals not otherwise eligible for health insurance under a government program shall be required either to maintain minimum essential coverage or to pay an annual penalty;
- Grants for premium assistance tax credits and other benefits to guarantee that certain low income individuals do not have to spend more than a specific percentage of their income on medical insurance premiums;
- Businesses that employ 50 or more workers will have to either provide “minimum essential coverage” to the workers or pay an annual penalty of up to \$2,000 per uninsured employee (the first 30 workers are not included in the penalty calculation);
- Businesses may also face the imposition of penalties for waiting periods in excess of 90 days for employee insurance coverage;
- Businesses of less than 25 employees and average annual wages of less than \$40,000 may be eligible for a sliding-scale small employer tax credit of between 35-50 percent to help offset the cost of employer-provided coverage;
- Restrictions on cafeteria plans are relaxed to encourage small employers to offer tax-free benefits to employees, including those related to health insurance coverage;
- Starting in 2013, higher-income taxpayers will face an increase in their Medicare payroll tax of 0.9 percent upon earned income in excess of \$200,000 for single individuals and \$250,000 for families, and 3.8 percent upon unearned income from interest, dividends, rents and certain passive activities in excess of \$200,000 for single individuals and \$250,000 for joint filers;
- Also starting in 2013, new spending restrictions, contribution limits and nonqualified distribution penalties are imposed upon Qualified Health Savings Accounts (HSAs); the threshold for the medical expense deduction is increased from 7.5 percent to 10 percent of adjusted gross income for individuals under 65 years of age; and the deduction for employers who maintain prescription drug coverage is eliminated for employees who are eligible for Medicare Part D; and
- Starting in 2018, group insurers face a 40% surtax on high-end employer-sponsored health plans in which annual premium payments exceed an inflation adjusted \$10,200 for individual coverage and \$27,500 for family coverage.

The implementation of these taxes and reporting requirements are to be made between now and 2018, depending on the particular item. Each business should begin considering the reform’s impact on its own operations to soften the impending blow. Planning opportunities are sure to arise as the reform moves from Washington to Main Street.

A PARENT'S OBLIGATION TO PROVIDE HEALTH INSURANCE FOR MINOR CHILDREN IN FAMILY LAW MATTERS

Wisconsin law already required courts in family law matters to assign responsibility for providing health insurance for minor children. Recent changes to the Wisconsin Administrative Code clarify this obligation. These changes are contained in section DCF 150.05 of the Code.

In addition to ordering child support for a child, courts are required to specifically assign responsibility for and direct the manner of payment for the child's health expenses under section 767.513, Wis. Stats. Courts are also required to order responsibility for the payment of medical expenses that are not covered by insurance after considering each parent's ability to pay these medical expenses. The requirement under section 767.513 existed prior to the changes to the Code and, as a practical matter, courts already assign responsibility for the payment of uninsured expenses.

Courts may order either or both parents to enroll a child in a private health insurance plan that is accessible to the child and available at a reasonable cost. BadgerCare Plus is not considered a private health insurance plan. Courts may order the non-insuring parent to contribute to the cost to enroll the children in a private health insurance plan in an amount that does not exceed 5% of the non-insuring parent's monthly income available for child support. However, if a person other than a parent has enrolled a child in an accessible private health insurance plan that covers hospitalization and other medical costs without large out-of-pocket deductibles or copayments, courts may determine whether to order a parent to enroll the child in a private health insurance plan. Further, courts may not order a parent whose income is below 150% of the federal poverty level to enroll a child in a private health insurance plan or contribute to the cost of a private health insurance plan unless there is no cost to the parent.

A private health insurance plan is accessible to the child if the plan's service providers are located within a reasonable distance from the child's home, which generally means service providers located within 30 minutes or 30 miles of the child's residence, with a greater distance allowed in some rural areas. A private health insurance plan is available at a reasonable cost if the cost to enroll the child or children does not exceed 5% of the insuring parent's monthly income available for child support and would cover hospitalization and other medical costs without large out-of-pocket deductibles or copayments. The cost to enroll the child or children in a private health insurance plan is the cost to add the child or children to existing coverage or the difference between the cost of self-only coverage and the cost to that parent after adding the child or children.

The responsibility for a contribution to the cost of private health insurance may be in the form of an upward or downward adjustment to a payer's child support obligation. The court would order an upward adjustment to a payer's child support order if the child support recipient is the insuring parent and the payer is contributing to the cost. The court would order a downward adjustment to the payer's child support obligation if the payer is the insuring parent, the child support recipient is contributing to the cost, and the child support recipient's contribution is less than the payer's child support amount.

If there is no private health insurance plan available that is accessible to the child and available at a reasonable cost, courts may order enrollment in a private health insurance plan as a child support deviation, responsibility for a contribution to the cost of the other parent's premium for the BadgerCare Plus unless the parent's income is below 150% of the federal poverty level, which may also be an upward or downward adjustment to a payer's child support obligation, and enrollment in a private health insurance plan if a plan that is accessible to the child and available at a reasonable cost becomes available to the parent in the future.

Should you have any questions about family law matters, contact Gregory Mager.

NEW FCC RULING AFFECTS APPLICATION PROCESS FOR THE CONSTRUCTION OF WIRELESS COMMUNICATION FACILITIES

In an effort to "promote the deployment of broadband and other wireless services by reducing delays in the construction and improvement of wireless networks," the Federal Communications Commission recently issued a ruling that affects the way in which state and local governments review applications to construct wireless communication facilities, such as cell phone towers and other similar structures.

Significantly, under the new ruling, a state or local government may not deny an application for a wireless communication facility solely because one or more cell phone carriers already serve a given geographic market. Moreover, state and local governments now have a specified time period to process an application, depending on the type of structure proposed. Failure by the government to comply with these strict time periods constitutes a "failure to act" and entitles the wireless applicant to commence a lawsuit, which will be heard and decided on an expedited basis. However, this lawsuit must be filed within 30 days of the government's failure to act.

Prior to the ruling, state and local governments had to process an application “within a reasonable period of time.” Not surprisingly, this inexact period of time led to numerous lengthy delays in the application process, frustrating many wireless service providers throughout the country.

With the new ruling in place, it is important for wireless service providers and state and local governments to understand their rights and obligations in the wireless application process.

CARRYOVER BASIS AND THE 2010 ESTATE TAX SYSTEM

The current state and uncertainty of the estate tax system has been a widely discussed, blogged and dissected topic since it became clear, late last year, that 2010 would be a “year without an estate tax.” There has been as much chatter, discussion and rumor mongering about what the estate tax system will look like in 2011; whether we will go back in time to the 2001 system, or forward to a new “2009 looking land” with a \$3.5 million estate tax exemption and a 35% rate.

What has been little discussed, and has the potential to have a broader impact, is the modified carryover basis rule in place in 2010. Under the pre-2010 system, upon death, most assets received a stepped-up basis to their fair market value, often dramatically reducing or eliminating the post-death income tax consequences to beneficiaries. But in 2010, the beneficiaries will not get the benefit of a step-up, but will instead have the decedent’s basis in those assets carryover to them.

There is some relief available. For transfers at death to non-spouses, \$1.3 million of unrealized gain (or step-up) can be allocated to beneficiaries. Transfers to spouses or special Marital Trusts can have up to \$3 million of step-up allocated to them. The personal representative has the discretion to determine which assets to allocate step-up to, and because there are planning opportunities and strategies, that allocation should be made with the advice and counsel of a team of experts, including the attorney, CPA and valuation expert.

The best thing about our current transfer tax system is it has created the impetus for planners to do what they should have always done: build plans flexible enough to deal with changing circumstances. Now is a great time for clients to insure their plans are sufficiently flexible; flexible enough to work under the law as written now, and flexible enough to deal with whatever Congress throws at them in the future. So buckle up, it’s going to be a bumpy

ride.

LEGISLATION MOVING FORWARD TO MAKE ROTH CONVERSIONS VIABLE IN WISCONSIN

The Wisconsin State Senate unanimously approved a bill to allow residents of all income levels to convert a Traditional IRA into a Roth IRA without penalty. The Legislature's Joint Finance Committee also approved the measure and the State Assembly will vote on the bill soon. This legislation has been strongly encouraged by financial and tax advisors because it makes Wisconsin tax law consistent with the federal law.

If this legislation becomes law, Wisconsin residents of all income levels can take advantage of converting a Traditional IRA into a Roth IRA. Prior to 2010, individuals with adjusted gross income in excess of \$100,000 could not do such a conversion. Effective 2010, the federal legislation changed, but Wisconsin was stuck under the prior rules. The advantage that a Roth IRA has over a Traditional IRA is that the funds may be withdrawn income tax free and there are no required minimum distributions for an account owner. However, any taxpayer who does convert a Traditional IRA to a Roth IRA must pay income tax on the amount converted. There are many potential planning techniques that may help to minimize this tax.

BUSINESS BANKRUPTCY OPTIONS

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The three most common avenues available to corporate entities seeking relief from creditors are Chapters 7 and 11 of the U.S. Bankruptcy Code, and Chapter 128 of the Wisconsin State Statutes.

In a Chapter 7 proceeding, which can be filed voluntarily by an insolvent entity, or involuntarily by an insolvent company's creditors, a trustee is immediately appointed by the court to liquidate the company's assets, on a piecemeal basis. It is not possible for a company in a Chapter 7 proceeding to remain open, or reorganize. As soon as a bankruptcy is filed, all creditors are enjoined and restrained from trying to collect their debts.

In a Chapter 11 proceeding, a company is typically able to remain in control of its affairs, and

maintain day-to-day operations in the ordinary course, under supervision of the bankruptcy court, and its creditors. A company may reorganize its debts in a Chapter 11, subject to court approval, and the opportunity for creditors to scrutinize and object to the company's proposed plan for reorganization. A sale of the company, as a going concern, is also possible.

A Chapter 128 proceeding, also known as receivership, or an assignment for the benefit of creditors, is also available to Wisconsin-based companies. It is similar to a Chapter 11 proceeding, however, it takes place in the circuit court for the county in which the company has its place of business, rather than in federal court. A court-appointed receiver, usually selected by the company or the company's lender, may operate the business in the ordinary course while the receiver markets the company's assets for sale, as a going concern.

A receivership can also be started voluntarily, or involuntarily by a company's creditors. Although the filing of a receivership also restrains and enjoins creditors, generally, secured creditors (typically banks) who withhold their consent cannot be bound by a receiver's actions.

Creditors are paid, according to statutory priority, from the proceeds generated by the sale of the company's assets, to the extent such proceeds are enough to pay secured creditors, in full. Or, in the event of a reorganization, creditors are paid, again according to priority, from the company's ongoing revenue.

MANAGING DATA IN A LITIGIOUS WORLD

Almost 99% of today's information created by businesses is generated and stored electronically. The ability to easily and conveniently store large amounts of data has created a hidden liability that did not exist in the age of when companies maintained its information primarily in paper format. This hidden liability is twofold. First, companies create more information than they know what to do with. Second, companies sometimes delete or destroy data and information that they actually do need.

For the unwary, these hidden liabilities may become exposed when your company is faced with a lawsuit.

In today's litigation, the age of electronic data has generated a paradigm shift away from traditional paper documents to digital information. This shift has changed the discovery process in litigation by changing what attorneys are looking for; how they are looking; and where they are looking for relevant information. Companies can expect in today's litigation that the way it stores and preserves electronic information will be a central topic during the

discovery process that will involve not only your record custodians, but also your information technology department. How well a company manages and preserves its electronic information may be an outcome determinative factor for it in litigation.

Today, companies that find themselves involved in a lawsuit oftentimes are faced with attacks through the discovery process as to how they typically store and delete electronic information. The purpose of this inquiry is to set the expectation as to what electronic information, such as e-mails, the company should or should not reasonable have at its disposable for discovery purposes. Companies that do not have a well-drafted and followed record retention plan that addresses electronic information and which incorporates a comprehensive litigation hold policy may find itself at a significant disadvantage in trying to defend what might otherwise be a winnable case. That is why it is more important than ever for all companies, both large and small, to effectively manage their electronic information. This means that companies must be litigation ready by taking affirmative actions that effectively manages and retains electronic information. It is simply too late to start thinking about the manner and method of retention and destruction of electronic data after you have been served with a lawsuit.

The best tools to avoid these hidden liabilities is a record retention policy that addresses electronic information as well as a litigation hold policy that is designed to preserve electronic data once litigation is reasonably anticipated. A record retention policy should be designed so that your company does not destroy information that it is obligated to maintain and at the same time the policy should be designed to destroy or delete information that the company no longer needs and/or is no longer mandated to maintain. Most companies have some sort of document retention policy. These retention policies were originally implemented to manage the volume and space occupied by paper documents. Companies have been less diligent, however, in applying their retention policies to the electronic information that they store on their servers and individual computer hard drives. This lack of diligence in managing electronic data has created a treasure trove for plaintiffs' lawyers looking for the proverbial "smoking gun," such as that e-mail that explains exactly what motivated the company's decision to terminate that troublesome employee.

A litigation hold policy has long been an important concept in litigation. In simple terms, it means that once you are sued, you have to stop destroying documents. It is an easy concept to understand when applied to paper documents, but it becomes a much more complicated task when dealing with electronic information. Electronic evidence can easily disappear, be altered or destroyed if not properly preserved. For example, some companies' computer systems provide for automatic deletion of e-mails and documents, so stopping that process takes an affirmative effort on behalf of management. When implementing a legal hold, a company needs to address the hold requirement from a team effort. Business units, IT, records management and custodial personnel, and either in-house or outside counsel need to be involved and work together in the process of implementing the hold.

How your company routinely stores or destroys electronic data has become an increasingly important subject during a lawsuit. As more lawyers become sophisticated in this topic, companies can expect, as routine, that their electronic records management policies and practices will be warily scrutinized. Consequently, it will be too late to start thinking about electronic data, the method and manner of retention as well as the deletion of such data after you have been served with a lawsuit. The failure to have a properly drafted record retention policy as well as a litigation hold policy may result in serious and adverse consequences for your company and may compromise your company's ability to defend itself in a lawsuit. For example, failure to have these policies in place can result in court-imposed sanctions, adverse jury instructions and significant monetary awards. Thinking ahead and addressing the hidden liabilities created by your electronic information can save your company time and money, and, more importantly, potentially prevent your company from having to incur an unnecessary judgment as the result of electronic information being inadvertently deleted.

Register for Managing Data in a Litigious World Webinar on July 22