TAX AND WEALTH ADVISOR ALERT: KEEPING IT IN THE FAMILY

For those of you who spend time in the estate planning arena, in helping your clients get the right property to the right people at the right time, you inevitably run into "the conflict": The conflict between the mathematical truth that it is better, tax-wise, under virtually all circumstances, to have your clients give away property as soon as possible: and the reality that people are (and should be) reluctant to cede control over their wealth, which they generally worked very hard to build. The problem with this conflict is that we as planners tend to fall too quickly and easily into what business consultants call "the tyranny of the or." We concede that the math and the control are mutually exclusive. But, luckily, that is simply not true.

Let's assume that our clients are a successful couple in their early 50s. Their net worth is $8 million. If they die without any growth in their combined estate, they owe no estate taxes given the $5 million (indexed) exemption. But if they do not both die soon, their assets could increase in value to more than $10 million (indexed), the amount that they could exclude from estate taxation, under current law, working together. In fact, if we assume that their assets will grow at a 6% rate and that the survivor will live into his or her mid-80s, the million should double in value 3 times – to 14 million, then 28 million then 56 million.

Even with modest appreciation, then our clients will have a large estate tax bill. And if the $7 million is in assets that would be hard to sell quickly (such as real estate), or that we do not want to have to sell (such as a family business), the estate tax problem could get to be difficult and expensive to solve.

But right now, we have a great solution. We can have Mom and Dad make a gift right now, in an amount equal to the current gift tax exemption, while keeping enough to live comfortably. In other words, they can give away "the extra" (the property that is more than what they believe they will need to live comfortably); or, stated another way, those investment assets that they will never need to touch, based upon reasonable projections.

The problem is again, at least in my world, not a lot of this kind of planning is getting done. SO the question is, why not? While the answers to that question are probably as varied and as numerous as the people who answer it, the answers tend to boil down to these two themes:

1) We recently experienced, as a country, one of the worst economic stretches in our history. From late 2008 through early 2009, what felt like "enough" became "not enough" almost overnight. Having just experienced that national economic nightmare, people are less willing to part with what seems to be "the extra."

2) Even if our clients had not just survived the Great Recession, andeven if they did have some level of confidence, people in their mid-50s, with at least 30 years of life expectancy in front of them, are reluctant (to say the least) to relinquish control over a portfolio they've worked a lifetime to build.

So are we back to the beginning? Do we have that common planning tug of war: The raw, compelling math that screams, "should clients give it away?" versus pulling against the raw human fears of losing control and becoming a pauper?

The difference is that we have an intelligent solution that guides our clients away from the tyranny of the or. Let's go back to our $8 million example and let's assume Mom and Dad believe that, based upon their lifestyle and growth assumptions, they will conservatively need $2 million to live comfortably. Therefore, using our terminology, $6 million is the extra. So let's take that $6 million and title it in such a way, that under state law, half of that property is owned exclusively by Mom and half is owned exclusively by Dad. Dad, then, using his gift tax exemption, will give his property to a trust. Under that trust, Mom will have the right to control, enjoy, and transfer the property. And then Mom will do the same thing: transfer her property to a trust designed for Dad's benefit.

If we do this, the $6 million is out of Mom and Dad's estate. When they die, presuming that they consume the income and growth on the $2 million they keep, they will owe nothing in estate taxes. The trusts, who own the $6 million, and the appreciation on that property, are designed to avoid estate inclusion; in fact, they can be designed as dynasty trusts to avoid estate inclusion forever.

In discussing this idea with thoughtful and curious clients, inevitably those clients will raise a couple of issues or concerns, such as:

1. What if Dad and Mom get divorced? Generally, upon divorce, the judge will divide the marital assets equally between the spouses. So, if we did nothing, the family court judge would take the $8 million of property that Mom and Dad own and divide it equally, $4 million to each. If we do engage in our plan, the judge will take the $2 million that Mom and Dad own and divide it equally between them ($1 million to each), and each spouse will continue to control the trust created by the other spouse. Assuming no growth in the trust assets, each would have control over an additional $3 million. At the end of the day, each would control $4 million, with only $1 million being subject to estate tax. In other words, even in divorce, both are in a better situation then they would have been in has they not engaged in our plan.
2. What if Mom or Dad dies? If we do no planning, Dad and Mom collectively had control over $8 million. After the gifts, assume Dad dies, Mom would have control over the $2 million outside of the trusts and the $3 million in the trust Dad created for her. As to the trust she creates for Dad, she would have no control over, or access to, the property in that trust. So it appears that, upon Dad's death, Mom has a reduction in the property over which she has control.

On that point, the first thing to remember is that the property in the trusts is "extra," property Mom and Dad really had no intention of tapping into. Stated another way, Mom and Dad believed that $2 million was a sufficient amount for the two of them to live out their lives comfortably. Now, if we do nothing, Mom has more than twice that amount ($5 million) to rely on. She should be just fine. But, if Mom and Dad are concerned, they should remember that the property in the trusts are extra, and therefore, chances are they will not be tapping into that property in a way that will stunt its economic growth. So if the property grows at 6, and Dad lives another twelve years the chances of which are very good), then Mom will once again have control over $8 million; $2 million outside of the trust and $6 million in the trust she controls. And, to hedge against asset underperformance and/or Dad's early demise, Mom can use the property in the trust Dad created for her to purchase a life insurance policy on Dad's life which could literally ensure that she will always have access to $8 million of property.

Finally, in implementing this good idea, it is critical to work with competent legal counsel who has wisdom and experience in trust design and the reciprocal trust doctrine. The trusts created by Mom and Dad can be (in fact, will be) similar. But they cannot be identical and wise counsel will know where the key differences in the trusts need to be.

EMPLOYMENT LAWSCENE ALERT: NLRB'S GENERAL COUNSEL DETERMINES THAT MCDONALD'S IS A JOINT EMPLOYER WITH ITS FRANCHISEES

In a decision that could have far reaching implications for industries that rely on the franchisor/franchisee business model, the NLRB's General Counsel, Richard Griffin, Jr., determined that 43 unfair labor practices charges against McDonald's, USA, LLC may move forward under a "joint employer" theory finding that McDonald's should be held liable along with its independently owned franchisees based upon allegations that the franchisees violated worker's rights in responding to workplace protests. The NLRB General Counsel's decision to move forward against McDonald's not only attempts to extend liability under the National Labor Relations Act to franchisors for acts of its franchisees, but it may also open the door for unions to more easily organize multiple independently owned franchise locations operating under agreement with a single franchisor.

The "joint employer" theory is a legal concept that treats two allegedly separate employers as one. The "joint employer" theory does not depend upon the existence of a single

integrated enterprise, but, rather, assumes in the first instance that companies are "what they appear to be" – independent legal entities that have merely chosen to handle jointly… important aspects of their employer-employee relationship. Typically, a joint employer relationship is found between two companies where the non-employing company actively and significantly exerts control over the same employees on those matters governing the essential terms and conditions of employment such as hiring, firing, discipline, supervisions, and direction.

The NLRB General Counsel's decision to target McDonald's as a joint employer comes in unison with big labor's recent efforts to protest wage and benefits levels for fast food workers. These recent protests over wages and benefits is big labor's attempt to attack the franchisor/franchisee business model by deeming independently owned stores to have the deep pockets of its franchisors – ignoring the economic realities of the franchisor/franchisee business model. For example, the SEIU has staged protests at different fast food establishments across the country demanding wages as high as $15/hour for all fast food workers based upon the fallacy that that such wages are appropriate given the corporate franchisor's finances. Wage demands of this type ignores the economics of operating an independent and locally-owned franchise where wages and benefits are often set based upon local market conditions as well as a franchisee's own profit and loss rather than upon the finances of its franchisor.

The NLRB General Counsel's decision to move forward with complaints that attempts to now treat McDonald's as a joint employer with its franchisees provides ammunition to big labor to further its war over wages and benefits against fast food franchisees by blurring the line between a small independently and locally-operated franchisee and its affiliated large corporate franchisor. In addition, with the NLRB willing to make clear that a corporate franchisor can now be held liable for unfair labor practices as a joint employer with its franchisees, it is only logical that the NLRB's next step will be to permit unions to organize fast food establishments based upon petitioned collective bargaining units that consist of multiple franchisee locations of a single franchisor even though the locations are independently owned and operated by different independent owners.

The NLRB General Counsel's decision to treat McDonald's as a joint employer does not currently have the effect of law. Once the NLRB issues the complaints, these cases will have to proceed through the adjudicative process leading up to a hearing before an administrative law judge before the cases might reach the full National Labor Relations Board for a decision.

Given the political make-up of current NLRB members, political ideologies will definitely pave the way for the NLRB's General Counsel's viewpoint on joint employer liability to prevail against McDonald's before the NLRB despite three decades of legal precedent that would hold otherwise. Needless to say, the battle will not end at the NLRB, as it would be expected that this issue will most likely wind-up before the U.S. Supreme Court who will make the

ultimate decision on this important issue.

At this point, the NLRB will try to achieve settlement with McDonald's before proceeding to hearing with these cases. It would be expected that McDonald's will oppose any attempts to settle these cases and try to move these cases beyond the NLRB and into the courts where strong legal precedent has mostly rejected the joint employer theory for businesses set up under the franchisor/franchisee business model. It is in the federal court system where McDonald's has the best opportunity to defeat the NLRB's new approach against the fast food and other industries that rely on the franchisor/franchisee business model.

We will keep you informed of these cases before the NLRB as they develop.

TAX AND WEALTH ADVISOR ALERT: STATE OF CELEBRATION CONTROLS—ONE OPEN QUESTION FROM WINDSOR IS RESOLVED

The United States Supreme Court issued a landmark decision in Windsor, holding that if a couple is married and resides in a state (or province) that allows same sex marriage, then that couple is married for purposes of federal law (including the Internal Revenue Code). A question left unanswered by the Supreme Court in Windsor was, if a couple got married in a state that allows same sex marriage (the state of celebration), but resides in a state that does not allow same sex marriage (the state of residence), how is the couple treated under the Internal Revenue Code?

Luckily for planners, the IRS jumped into this definitional void. In Revenue Ruling 2013-17, the IRS makes it clear that it will administer the Code looking solely to the state of celebration. So if a same-sex couple marries in Massachusetts (a state that recognizes same-sex marriage), and then moves to Wisconsin (a state that does not recognize same-sex marriage), for federal tax purposes, the couple is married. Of course, for state tax purposes, the couple will not be treated as married, leading to challenges for planners who will need to consider state tax consequences that differ from federal tax consequences in planning for their same-sex married clients.

EMPLOYMENT LAWSCENE ALERT: EEOC ISSUES UPDATED ENFORCEMENT GUIDANCE ON PREGNANCY DISCRIMINATION

On July 14, 2014, the U.S. Equal Employment Opportunities Commission ("EEOC") issued updated enforcement guidance regarding the Pregnancy Discrimination Act ("PDA") and the Americans with Disabilities Act ("ADA") as they apply to pregnant workers. The EEOC's guidance discusses a number of issues related to pregnancy discrimination and other pregnancy related issues and provides insight into the agency's interpretation of those issues and employers' obligations under the PDA and ADA relative to pregnant employees. The EEOC also issued a question and answer sheet about the EEOC's enforcement guidance and pregnancy related issues and a fact sheet for small businesses.

Among a number of other issues, the EEOC's guidance discusses:

•The PDA's coverage as it relates to current pregnancy, past pregnancy, and a woman's potential to become pregnant or intended pregnancy.
•Discrimination based on lactation and breastfeeding and other medical conditions related to pregnancy or child birth.
•When employers may be required to provide light duty for pregnant employees.
•The prohibition against forcing an employee to take leave because she is pregnant and other issues related to parental leave.
•When employers may have to provide reasonable accommodations to employees with pregnancy-related impairments.
•Other legal requirements affecting pregnant workers, such as the Family and Medical Leave Act and Section 4207 of the Patient Protection and Affordable Care Act (requiring employers to provide "reasonable break time" for breastfeeding employees to express breast milk).
•The EEOC's proffered best practices for employers in handling pregnancy-related matters in the workplace.

The EEOC's updated guidance provides a clear indication of the EEOC's position and interpretation relative to the PDA and ADA as they relate to pregnancy discrimination and other pregnancy related issues in the workplace. While this guidance may provide some insight into the agency's position and likely enforcement efforts, employers should remember that it is merely guidance and does not have the force and effect of law.

One of the more controversial elements of the EEOC's new guidance arises from the EEOC's position that employers' failure to treat pregnant employees the same as non-pregnant employees similar in their ability or inability to work is a violation of the PDA. This becomes problematic for employers who have traditionally reserved light duty positions for workers

with restrictions resulting from an on-the-job injury while not providing light duty to employees who have similar temporary restrictions. The EEOC takes the position that the PDA requires employers who offer light duty work to employees who have restrictions resulting from injury on the job to offer that same light duty work to a pregnant employee with the same restrictions.

In light of this new guidance, employers should reevaluate their practices and policies related to pregnancy and pregnancy-related issues, especially with regard to requests for accommodation, and more carefully consider each and every employment action and decision involving pregnancy in the workplace.

TAX AND WEALTH ADVISOR ALERT: IRS PROVIDES RELIEF FOR SURVIVING SPOUSE TO ELECT PORTABILITY

2010, as part of the Job Creation Act, Congress allowed a surviving spouse to utilize a previously deceased spouse's unused estate tax exclusion. This planning technique is known as "portability." In 2012, as part of the American Taxpayer Relief Act, portability became permanent (or as permanent as any federal statute can be). One of the requirements for portability is that the first spouse to die (the "decedent spouse") needs to file a Form 706 estate tax return and elect portability, prior to death; based on the value of the estate, filing an estate tax return would not otherwise be required. In other words, if the first spouse to die did not file a 706 prior to death, portability is lost.

At least that is what planners thought until the IRS issued Revenue Procedure 2014-18. In that Revenue Procedure, the IRS states that:

1. If a decedent died after 2010 and before 2014,
2. That decedent was a citizen or resident of the US upon his or her death,
3. The decedent's estate was not required to file an estate tax return based on the value of the estate (and taxable gifts), and
4. The decedent's estate did not file a timely return electing out of portability then, prior to December 31, 2014, the estate can file a form 706 and that return will be deemed properly filed.

TAX AND WEALTH ADVISOR ALERT: ESTATE PLANNING AFTER WINDSOR

The federal tax code (the "Code") offers several benefits (and a few burdens) to married couples. In 1996, the United States Congress passed a statute known as the Defense of Marriage Act ("DOMA"). Under DOMA, with respect to any federal statute, a married couple meant a husband and wife; a man married to a woman. Because the Code is a collection of federal statutes, same-sex couples legally married under the laws of a state that provided for same-sex marriage received none of the benefits provided to married couples under the Code.

One of these benefits the Code provides is the unlimited marital estate tax deduction: Under the Code, one spouse can leave an unlimited amount of property to the other spouse without the imposition of estate tax. Edith Windsor and Thea Spyer were a lesbian couple married in Ontario, Canada in 2007. In 2009, Spyer died and left her entire estate to Windsor. At the time of Spyer's death, both Windsor and Spyer were residents of New York, a state that, at that time, had legalized same-sex marriage and legally recognized same-sex marriages entered into in other states and countries. So, at the time of Spyer's death, under New York law, Spyer left her entire estate to her spouse. But under DOMA, Spyer did not leave everything to her spouse; Windsor could not qualify under the Code as Spyer's spouse as they were both women. Windsor filed her tax return, paid the estate tax and then sued for a refund, arguing that DOMA was unconstitutional. The District Court and the Second Circuit Court of Appeals agreed with Windsor.

The case was then argued in front of the United States Supreme Court. In a landmark decision, the Supreme Court determined that DOMA violated Windsor's and Spyer's constitutionally protected right to equal protection. In essence, the majority opinion held that historically, the definition of marriage is a matter left to the states. In passing DOMA, Congress violated that tradition of state-defined marriage. That departure was due to Congressional bias, and that bias violated the equal protection clause of the US Constitution.

The majority opinion answered this question: If a same sex couple is married in a state that defines same sex marriage as marriage, how is that couple treated for federal purposes (including the tax code)? The answer is clear: The same as any other married couple. But the decision leaves at least two other critical planning questions unanswered: (1) If a couple gets married in a state that allows same sex marriage, but moves to a state that does not, how are they treated for federal purposes, married (consistent with the laws of the state where the marriage took place, or what sometimes is called the state of "celebration") or unmarried (consistent with the laws of the state of domicile which does not allow same sex marriage?) (2) Can a state disallow same sex marriage if, in fact, that disallowance is a

violation of equal protection? Hopefully, these questions are resolved in the future.

So after Windsor, estate planners should handle planning for a same-sex married couple in exactly the same fashion they handle planning for a heterosexual married couple. The planner should help the couple build a plan that takes care of the people they care about. The plan will accomplish that goal by getting the right property to the right people at the right time. The plan will ensure that the right people are making the right decisions. And the plan will be allowed to take advantage of the tools provided under the Code to married couples including (but not limited to) the unlimited marital deduction, income tax free transfers, and the ability of an inheriting spouse to treat the transferring spouse's IRA as his or her own.

EMPLOYMENT LAWSCENE ALERT: IS YOUR BUSINESS EXPOSED TO LIABILITY FOR YOUR COMPANY'S LEASED EMPLOYEES/TEMPORARY WORKERS?

TAX AND WEALTH ADVISOR ALERT: THE FIRST CLUE TO THE IRS' POSITION AND THE TAX COURT'S THOUGHTS ON MATERIAL PARTICIPATION OF A TRUST FOR THE 3.8% NET INVESTMENT INCOME TAX—ARAGONA TRUST V. COMM'R., 142 T.C. 9 (2014)

Beginning in the 2014 tax year, when a taxpayer's Adjusted Gross Income ("AGI") exceeds a threshold amount, the taxpayer will be subject to a 3.8% tax on his or her net investment income. Net investment income includes income from a business in which the taxpayer does not "materially participate." The section of the Internal Revenue Code (the "Code") dealing with the tax on net investment income (specifically Code section 1411) borrows its critical material participation definition from Section 469 of the Code which deals with the rules on deductibility of losses from passive activities. Under Code section 469, while the rules for

measuring the material participation of a human being are straightforward, when the taxpayer who owns an entity is a non-grantor trust, the guidance is conspicuously absent. In fact, Section 1.469-5T(g) of the Treasury Regulations entitled "Material Participation of Trusts and Estates," has no information; it is simply blank. In the regulations to Section 1411, the IRS admits it provides no guidance on material participation by trusts, but states that it hopes to provide future guidance through Regulations promulgated under Code section 469.

So, in essence, when a business is owned by a non-grantor trust, the taxpayer is left without guidance on whether the business' income is subject to the net investment income tax. However, a recent case does provide insight into the IRS' and Tax Court's position on the matter. In *Frank Aragona Trust v. Comm'r.*, the IRS posits that, under Code section 469, a trust cannot materially participate. If the IRS succeeded in that argument, all income from an active business owned by a non-grantor trust would be subject to the 3.8% tax. The IRS also argued, in the alternative, that if the Tax Court held that a trust can materially participate, it is the services that the trustee provides *as the trustee and not the services the trustee provides as an employee of the business* that can be counted towards the material participation standard.

The Tax Court disagreed with the IRS on both counts. It held that a trust can materially participate, and the services of the trustee, whether as an employee of the business or as trustee count towards meeting the material participation standard. This ruling should provide some comfort for taxpayers who utilize non-grantor trusts for estate planning and asset protection purposes to hold businesses, as the Tax Court gives a framework for meeting the material participation standard. At the same time, it should serve as a cautionary tale that holding business assets in that way might lead to IRS scrutiny and challenge.

ATTORNEY GRANT C. KILLORAN ELECTED TO THE AMERICAN BAR ASSOCIATION HOUSE OF DELEGATES

The law firm of O'Neil, Cannon, Hollman, DeJong and Laing S.C. is pleased to announce that Grant C. Killoran recently was elected by the State Bar of Wisconsin to serve a two-year term as one of its five Delegates to the American Bar Association House of Delegates.

The House of Delegates is the policy-making body of the ABA. Control and administration of the ABA is vested in the House of Delegates. Established in 1936, the House of Delegates

has over 500 members and its actions become the official policy of the ABA, the nation's largest lawyer association.

Mr. Killoran previously served as a Delegate to the ABA House of Delegates from 1997-1999 and 2003-2009.

Mr. Killoran is a shareholder with and the Chair of O'Neil, Cannon, Hollman, DeJong and Laing's Litigation Practice Group. He has diverse trial experience, focusing on complex business and health care disputes.

EMPLOYMENT LAWSCENE ALERT: U.S. SUPREME COURT UNANIMOUSLY REJECTS PRESIDENT'S NLRB APPOINTMENTS

Earlier this year, we alerted employers when the U.S. Supreme Court heard oral arguments in *National Labor Relations Board v. Noel Canning*, a case involving the President's appointment of three members to the National Labor Relations Board ("NLRB") without U.S. Senate approval while the U.S. Senate was on break.

Today, Thursday, June 26, 2014, the U.S. Supreme Court unanimously held that the President exceeded his authority in appointing those three members to the NLRB while the U.S. Senate was on an extended holiday break. Although the Supreme Court ultimately found that the President does indeed have the power under the U.S. Constitution to make "recess appointments" during breaks *between formal sessions* of the Senate and also during breaks in *the midst of a formal session*, the Senate breaks during which the President made his appointments to the NLRB were not considered to be in a formal "recess" within the meaning of the Constitution.

The Supreme Court's decision in *Noel Canning* opens the door for both employers and unions to call into question hundreds of decisions issued by the NLRB in recent years. This could force the NLRB to revisit certain of its decisions and may force the Board to issue new decisions in those matters. We will continue to keep you informed of the latest developments and effects of the Supreme Court's decision in *Noel Canning*.