THE

ESTATE PLANNER

January/February 2018

BUY-SELL AGREEMENTS: HANDLE WITH CARE

Estate planning when time is short

International estate planning

If you're a non-U.S. citizen, the rules are different

Estate Planning Red Flag

You're transferring a vehicle to your revocable trust

MacLean & Ema P.A.
Attorneys and Counselors at Law

2600 NE 14th St Causeway
Pompano Beach, FL 33062

954-785-1900 phone
954-942-1006 fax

www.maclean-ema.com

Buy-sell agreements: Handle with care

If you own an interest in a family-owned or other closely held business, a buy-sell agreement should be a key component of your estate plan. These agreements specify whether — and under what circumstances — owners' interests may be transferred, ensuring that the business stays in the family and meeting other important estate and succession planning goals.

Buy-sell agreements should be planned and drafted carefully to ensure that they meet your expectations and don't trigger unwanted tax consequences or intrafamily conflicts.

Consider the benefits

A well-crafted buy-sell agreement provides many benefits, including:

- Keeping ownership of the business within the family or another select group (for example, people actively involved in the enterprise),
- Preventing an owner's former spouse from acquiring a business interest in the event of a divorce,
- Providing owners and their heirs with liquidity to pay estate taxes and other expenses in the event of death or disability,
- Establishing the value of the business for gift and estate tax purposes (if certain requirements are met), and
- Minimizing disputes over ownership succession issues.

Typically, buy-sell agreements achieve these objectives by requiring or permitting the company or the remaining owners to purchase the interest of an owner who dies, becomes disabled or leaves the business. They may also provide the company or the remaining owners with a right of first refusal in the event an owner wishes to sell his or her interest.

Beware the tax implications

Generally, buy-sell agreements are structured either as "redemption" agreements or "cross-purchase" agreements. The former permit or require the *company* to purchase a departing owner's shares, while the latter confer that right or obligation on the remaining owners.

From a tax perspective, cross-purchase agreements are generally preferable. The remaining owners receive the equivalent of a "stepped-up basis" in the purchased shares, in that their basis for those shares will be determined by the price paid, which is the current fair market value. Having the higher basis will reduce their capital gains if they sell their interests down the road. Also, if the remaining owners fund the purchase with life insurance, the insurance proceeds are generally tax-free.

Redemption agreements, on the other hand, may trigger a variety of unwanted tax consequences,

Buy-sell or shareholders' agreement: What's the difference?

The terms "buy-sell agreement" and "shareholders' agreement" are often used interchangeably. But in fact, a shareholders' agreement refers to a broader category of which a buy-sell agreement is a subset.

A buy-sell agreement deals specifically with the disposition of shares of a shareholder who dies, becomes disabled, or wishes to sell his or her ownership interest. Shareholders' agreements typically include buy-sell provisions, but may also include noncompetition, nonsolicitation and confidentiality restrictions; voting procedures; dispute resolution mechanisms; and other provisions related to corporate governance or shareholder relations.

including corporate alternative minimum tax, accumulated earnings tax or treatment of the purchase price as a taxable dividend.

The disadvantage of a cross-purchase agreement is that the owners, rather than the company, are responsible for funding the purchase of a departing owner's interest. And if they use life insurance as a funding source, each owner will need to maintain insurance policies on the life of each of the other shareholders, a potentially cumbersome and expensive arrangement.

Set a fair price

A buy-sell agreement's valuation provision is critical to avoiding unpleasant surprises or conflicts. Generally, the fairest and most effective method of setting the purchase price is to conduct periodic independent business valuations and to base the price on fair market value.

Many agreements set the price using a formula tied to earnings, cash flow, book value or some other objective measure. Although formulas offer simplicity and lower costs, they can't account for subjective characteristics or other factors that drive business value. As a result, they often underestimate or overestimate business value, which can lead to disputes when the buy-sell agreement is invoked.

Define your terms

When putting together a buy-sell agreement, it's important to define your terms carefully and to consider the potential implications of the agreement's language. A recent California Court of Appeal case — *Saccani v. Saccani* — illustrates how the language of a buy-sell agreement can lead to intrafamily conflict years or even decades later.

In that case, Albert Saccani had died, leaving his three sons — Donald, Roland and Gary — as equal shareholders of the family business. In 1991, the sons entered into a shareholders' agreement that, among other things, gave the company a right of first refusal in the event a shareholder wished to sell or otherwise dispose of his shares in a manner other than a "permitted transfer," as defined by the agreement. Permitted transfers included transfers by the shareholders 1) to one another, 2) to their respective descendants, and 3) to estate planning trusts for their respective descendants.

Donald, who had no children, transferred his shares to a revocable trust that gave Gary an option to purchase the shares after Donald's death. Donald died in 2007, and in 2012 Gary exercised the option, acquiring a two-thirds interest in the company. In 2013, Roland died, leaving his one-third interest to his two sons. Roland's sons sued, claiming that the option granted to Gary wasn't a permitted transfer and, therefore, violated the shareholders' agreement. Rather, they argued, the company should have been afforded its right of first refusal, which, if exercised, would have given them a 50% interest in the company.

The court disagreed, finding that the option was a permitted transfer. The court noted that the term "transfer" was broadly defined as "gift, sell, pledge, encumber, hypothecate, assign or otherwise dispose of," which encompassed the option Donald had granted to Gary.

Choose your words carefully

Before signing a buy-sell agreement, test it to see how it'll perform under various scenarios and choose your words carefully to ensure that it fulfills your objectives. In *Saccani*, for example, if Albert had intended for the business to be owned equally by his sons' families, he could have included specific language designed to achieve that result. ∎

Estate planning when time is short

No one wants to contemplate their own mortality or that of a loved one. It's one of the reasons people tend to procrastinate when it comes to estate planning. And for people whose life expectancies are short — because they're terminally ill or advanced in age — planning can be even more difficult. But while money matters may be the last thing you want to think about when time is limited, a little planning can offer you and your family financial peace of mind.

Action steps to take

Here are some (but by no means all) of the steps you should take if you or a loved one has a short life expectancy:

Gather documents. Review all estate planning documents, including your:

- Will,
- Revocable or "living" trust,
- Other trusts,
- General power of attorney, and
- Advance medical directive, such as a "living will" or health care power of attorney.

Make sure these documents are up to date and continue to meet your estate planning objectives. Modify them as appropriate.

> ***Catalog all your assets and liabilities, estimate their value, and determine how assets are titled to ensure that they'll pass to their intended recipients.***

Take inventory. Catalog all your assets and liabilities, estimate their value, and determine how assets are titled to ensure that they'll pass to their intended recipients. For example, do you own assets jointly with your ex-spouse? If so, title will pass to your ex-spouse on your death. There may be steps you can take to separate your interest in the property and dispose of it as you see fit.

If you have a safe deposit box, make sure someone is authorized to open it. If you have a personal safe, be sure that someone you trust knows its location and combination.

Review beneficiary designations. Take another look at beneficiary designations in your IRAs, pension plans, 401(k) plans and other retirement accounts, insurance policies, annuities, deferred compensation plans and other assets. Make sure a beneficiary is named and that the designation continues to meet your wishes. For example, you may find that your ex-spouse is still named as beneficiary of your life insurance policy.

Review digital assets. Ensure that your family or representatives will have access to digital assets, such as email accounts, online bank and brokerage accounts, online photo galleries, digital music and book collections, social media accounts, websites, domain names, and cloud-based documents. You can do this by creating a list of usernames and passwords or by making arrangements with the custodians of these assets to provide access to your authorized representatives.

Consider tax-planning strategies. There are many strategies you can employ to reduce the tax burden on you and your family. For example, suppose your children or other heirs are in a higher tax bracket than you. Counterintuitively, it may make sense to increase your income. Depending on your income you may be able to take a traditional IRA distribution without increasing your tax liability. This strategy may be particularly advantageous if you have significant deductions for medical or other expenses that would otherwise go unused.

For example, suppose that, based on your projection, you know that your itemized deductions will exceed your income and that you'll have negative taxable income for the year. For illustrative purposes, let's say that the projection shows that your deductions and exemptions will exceed your income by $10,000. In that case, your tax liability would be zero. Further suppose that, if you took an extra $10,000 from your IRA, your tax liability would still be zero. Now, instead of the funds sitting in your IRA they're sitting in a non-IRA account.

When your family inherits that $10,000, they're better off from a tax perspective. Why? Because instead of receiving those funds in the IRA, where they'd be subject to income tax upon distribution, they could instead receive the assets income-tax free. If your children are in, say, the 35% income tax bracket, then for each $10,000 received via the IRA, they'd be liable for income tax of $3,500. By moving the money out of your IRA (and paying no tax to do so), then, as a family, you'll have $3,500 more than you otherwise would.

Gaining peace of mind

These are just a few of the many steps you can take to shore up your estate plan when time is short. Although facing your own mortality can be difficult, great peace of mind can come from ensuring that your estate plan fulfills your wishes and minimizes the tax burden on your family.

International estate planning

If you're a non-U.S. citizen, the rules are different

Traditional estate planning strategies generally are based on the assumption that all family members involved are U.S. citizens. However, if you or your spouse is a noncitizen, special rules apply that require additional planning. Let's take a look at how the rules change when one or more noncitizens are involved.

Defining "residency" and "domicile"

If you're a U.S. resident, but not a citizen, you're treated similarly to a U.S. citizen by the Internal Revenue Code. You're subject to federal gift and estate taxes on your worldwide assets, but you also enjoy the benefits of the $5.6 million estate tax exemption and the $15,000 annual gift tax exclusion. And you can double the annual exclusion to $30,000 through gift-splitting with your spouse, so long as your spouse is a U.S. citizen or resident. (Tax reform efforts could significantly increase the estate tax exemption.) Special rules apply to the marital deduction, however, as will be discussed.

Residency is a complicated subject. IRS regulations define a U.S. resident for federal estate tax purposes as someone who had his or her *domicile* in the United States at the time of death. One acquires a domicile in a place by living there, even briefly, with a present intention of making that place a permanent home.

Whether you have your domicile in the United States depends on an analysis of several factors, including the relative time you spend in the United States and abroad, the locations and relative values of your residences and business interests, visa status, community ties, and the location of family members.

What if you're a "nonresident alien"?

If you're a nonresident alien — that is, if you're neither a U.S. citizen nor a U.S. resident — there's good news and bad news in regard to estate tax law. The good news is that you're subject to U.S. gift and estate taxes only on property that's "situated" in the United States. Also, you can take advantage of the $15,000 annual exclusion (although you can't split gifts with your spouse).

The bad news is that your estate tax exemption drops from $5.6 million to a miniscule $60,000, so substantial U.S. property holdings can result in a big estate tax bill. Taxable property includes U.S. real estate as well as tangible personal property — such as cars, boats and artwork — located in the United States.

Determining the location of intangible property — such as stocks, bonds, partnership interests or other equity or debt interests — is more complicated. For example, if a nonresident alien makes a gift of stock in a U.S. corporation, the gift is exempt from U.S. gift tax. But a bequest of that same stock at death is subject to estate tax. On the other hand, a gift of cash on deposit in a U.S. bank is subject to gift tax, while a bequest of the same cash would be exempt from estate tax.

Options for making tax-free transfers

The unlimited marital deduction isn't available for gifts or bequests to noncitizens. However, there are certain options for making tax-free transfers to a noncitizen spouse. For example, you can use the transferor's $5.6 million exemption (provided the transferor is a U.S. citizen or resident). You can also make annual exclusion gifts. (Currently, the limit for gifts to a noncitizen spouse is $152,000.) And last, you can bequeath assets to a qualified domestic trust, which contains provisions designed to ensure that the assets are ultimately taxed as part of the recipient's estate.

Consider your rights

Understanding federal estate tax laws can be complicated — even more so if you, your spouse or both are noncitizens. Discuss your options with your estate tax advisor.

ESTATE PLANNING RED FLAG

You're transferring a vehicle to your revocable trust

If you're like many people, you use a revocable trust — often referred to as a "living trust" — to manage your assets during life and avoid probate at death. And you may know that the trust isn't effective unless you "fund" it — that is, transfer ownership of your assets to the trust and designate it as beneficiary of retirement accounts or insurance policies.

What about automobiles and other vehicles? Should you transfer them to your revocable trust? If you still owe money on an auto loan, the lender may not allow you to transfer the title to the trust. But even after your loan is paid off, there are risks to consider before you make such a transfer.

As owner of the vehicle, the trust will be responsible in the event the vehicle is involved in an accident, exposing other trust assets to liability claims that aren't covered by insurance. So you need to name the trust as an insured party on your liability insurance policy.

On the other hand, because you're personally liable either way, owning a vehicle through your revocable trust may not be a big concern during your life.

After your death, when the trust becomes irrevocable, an accident involving a trust-owned vehicle can place the other trust assets at risk. Keeping a vehicle out of the trust eliminates this risk. The downside, of course, is that the vehicle may be subject to probate, although some states offer streamlined procedures for transferring certain vehicles to heirs.

MACLEAN & EMA P.A.
Attorneys and Counselors at Law

HURRICANES & THE VULNERABLE: WHAT HAVE WE LEARNED?

Arlene Lakin, Esq.

Hurricane Harvey caused devastation in Texas. We all saw video of seniors in a nursing home sitting in filthy water midway up their wheelchairs.

Hurricane Irma caused devastation in Florida and throughout the southeastern USA. We all saw video and news articles about 14 seniors who died in a Hollywood nursing home when they died from heat prostration due to no electric power, therefore, no air-conditioning. While these individuals were literally roasting to death, there was Memorial Hospital next door and no action was taken in a timely, appropriate fashion to rescue these people.

"On September 16, 2017, following the tragic deaths of eight people at the Rehabilitation Center at Hollywood Hills in Broward County, Governor Rick Scott is directing Florida Agency for Health Care Administration (AHCA) Secretary Justin Senior and Florida Department of Elder Affairs Secretary Jeffrey Bragg to issue emergency rules to keep Floridians safe in health care facilities during emergencies. Pursuant to the emergency action, within the next 60 days, all assisted living facilities (ALFs) and nursing homes must obtain ample resources, including a generator and the appropriate amount of fuel, to sustain operations and maintain comfortable temperatures for at least 96-hours following a power outage. This is based on standards already in place at all hospitals in Florida.

The emergency action also requires:

State Fire Marshal Jimmy Patronis to conduct inspections of these generators within 15 days of installation at the facilities;

Local emergency management officials to either approve or deny the emergency management plans already required to be submitted to them by law from residential healthcare facilities to ensure it sufficiently protects life;

Each local emergency management agency must post all approved facility emergency management plans to their website within ten days of the plan's approval; and

Facilities must submit proof of compliance with the emergency rules to AHCA and Elder Affairs within 48-hours of each plan's approval."

These hurricanes have brought to our attention the potential abuse of seniors in facilities. Action is being taken. That is a good thing. However, there is daily abuse of seniors in their own homes - you do not have to be an elder law attorney to be wary of a suspicious situation with a family member, a neighbor, or an acquaintance. If you suspect abuse or self-neglect, how can you look away? Contact family. If family is the problem, then dial Adult Protective Services at 1-800-962-2873. And this does not just apply to seniors (persons 65 or older); this applies to vulnerable persons of any age.