



2015

CRITICAL LEGAL DEVELOPMENTS

VisTaTech Center, Livonia, Michigan

November 2, 2015

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**Discussion of the Supreme Court Decision in
Obergefell v. Hodges (6/26/15)**

Monica D. Moons

DISCUSSION OF THE SUPREME COURT DECISION IN

OBERGEFELL v. HODGES (6/26/15)

I. SUMMARY OF THE SUPREME COURT DECISION

- A. On June 26, 2015, the U.S. Supreme Court decided Obergefell v. Hodges, 2015 US Lexis 4250 (June 26, 2015), in a 5-4 decision holding that same-sex couples nationwide have a constitutional right to marry.
- B. Obergefell negates Michigan's 2004 law limiting marriage to heterosexual couples, as well as same-sex marriage restrictions in other states. The decision also means that all 50 states must recognize same-sex marriages, even in cases where that state's residents previously entered into a same-sex marriage in another state where the marriage was then legal.

II. IMMEDIATE EFFECTS

A. Statutes.

Many Michigan laws must now be updated in light of the Obergefell decision. This process will likely take years. For example, the language in many laws must be changed from "husband" and "wife" to "spouse." The Michigan Law Revision Commission has been tasked with making those changes.

B. Family Law.

1. Parent-Child Relationship.

- a. Even though the Obergefell decision gives same-sex couples the right to marry, it left many unresolved issues in family law. One of the biggest issues Obergefell does not resolve is the parent-child relationship in cases with same-sex married parents.
- b. It is important to stress to clients that getting married is not enough when it comes to parents and children - they must take affirmative steps to make sure both parents have legal rights. Michigan laws and cases referencing parenting and custody reference opposite-sex couples or "husband" and "wife"; the law has not been tested with same-sex married couples. Each set of facts must be carefully analyzed. There is no guaranty that any specific method a practitioner may use to establish a parent-child relationship will work.
- c. Same-sex married couples need to take affirmative steps to establish their parental rights. Some methods of establishing parental rights have previously been available only to heterosexual couples (married and unmarried) and they are still untested in cases of same-sex married couples.

- d. Same-sex couples need to establish parental rights for both spouses. Though untested, a few potential approaches for establishing parentage for same-sex married couples are as follows:
- (1) Second parent (step parent) adoption. In this approach, one parent is the sole custodial parent and the other spouse files for second parent adoption to legally establish a parent-child relationship. See §21.51 (Step Parent Adoptions) of “Paternity, Adoption, and Surrogacy,” Chapter 21 of Michigan Family Law. Michigan Family Law (7th Edition, Edited by Hon. Marilyn J. Kelly, Judith A. Curtis, and Richard A. Roane).
 - (2) Affidavit of parentage. This form has been used by unmarried opposite-sex parents to voluntarily and legally establish paternity. Theoretically, a same-sex spouse could also file an affidavit of parentage to establish a legal parent-child relationship. MCL 722.1004. See Acknowledgment of Parentage Act (1996 PA 305) and Affidavit of Parentage (Form DCH-0682) and Instructions.
 - (3) Order of filiation. Same-sex married couples may also request an order of filiation. Historically, orders of filiation have been used for opposite-sex couples to establish paternity and to identify the non-custodial parent who pays child support. See §§21.21–21.25 (Order of Filiation) “Paternity, Adoption, and Surrogacy,” chapter 21 of Michigan Family Law.
- e. Same-sex married parents with children born after Obergefell may have an easier time establishing the parental rights of both spouses. Under Lord Mansfield’s rule, there is a rebuttable presumption that a child born during a marriage is a child of that marriage. Serafin v Serafin, 401 Mich 629, 258 NW2d 461 (1977). However, this rule has not yet been tested since the Obergefell decision with same-sex couples. Therefore, practitioners should be cautious and counsel same-sex married parents with children born after Obergefell to establish parent-child relationships through another method, as well, such as those noted above.

2. Divorce.

- a. Same-sex marriage also means that same-sex couples can divorce. However, while Obergefell made it possible for same-sex couples to marry and to have their out-of-state marriages recognized, it does not resolve the issue of when the marriage occurred for purposes of divorce. For example, if a Michigan same-sex couple married in Massachusetts, before it was legal in Michigan and now they want a divorce, what is the date of the marriage? Is it the date they married in Massachusetts? The date

it was recognized in Michigan? What if the couple was in a committed relationship for 10 or 20 years before the Massachusetts marriage?

- b. While the date of marriage issue has not yet been resolved, when a same-sex couple was together long before the date they married, consider whether invasion of property is appropriate. See "Property Division," chapter 15 of Michigan Family Law.

3. Custody and Parenting Time.

After Obergefell, judges will uniformly apply the 12 best interest factors in custody cases involving same-sex married parents. See "Child Custody and Parenting Time," chapter 12 of Michigan Family Law.

III. OPEN QUESTIONS

- A. The Obergefell decision is new enough and controversial enough that same-sex married couples are well advised to take steps to ensure that their marital status will be recognized under federal and Michigan law.
- B. Same-sex married couples remain nontraditional families, and they (and their lawyers) should retain official evidence of their marital status in case that relationship is ever challenged.
- C. Although most of Michigan's probate and trust laws are gender neutral and refer to "spouses," there are Michigan laws that refer to "husband and wife." These gender specific state laws may prove "trippers" until they are revised or construed. Legislation already has been drafted to, for example, call for the issuance of marriage licenses to two "individuals."
- D. Certain legal issues, like second parent adoption, remain so sensitive that same-sex couples with children should secure expert and experienced legal help to protect their families.
- E. Those interpreting and applying Michigan law, whether county clerks, probate registers, or judges, will be grappling with the transformation wrought by Obergefell. For example, will local assessors balk or demand extra proof of marital status when reviewing property transfer affidavits? What will title companies require? Particularly during this period, same-sex couples should express their intentions for one another in arrangements that are as clear, private, and enforceable as possible.

IV. PROBATE AND ESTATE PLANNING IMPLICATIONS

- A. Obergefell Simplifies Estate Planning for Married Same-Sex Couples.
 1. With a few reservations and possible exceptions, married same-sex couples will now enjoy in Michigan the same rights and benefits available to opposite-sex couples under Michigan law. The burdens of marital

status also apply. In other words, tax and estate planning for married couples—same-sex or opposite-sex—should be the same.

2. Since the Supreme Court's decision in United States v Windsor, No 12-307, 2013 US Lexis 4921 (June 26, 2013) in 2013, most federal laws applicable to opposite-sex couples have been applicable to same-sex couples. In a state where same-sex marriage was recognized (like New York, where the Windsor case arose), state laws governing marital status also applied to same-sex and opposite-sex couples in the same manner. After Windsor, federal laws like Social Security and veteran's benefits that look to the state of domicile of a married couple to determine eligibility, applied equally to same-sex and opposite-sex married couples in states where same-sex marriage was recognized, but not necessarily in states (like Michigan) that did not recognize same-sex marriage.
3. Prior to Obergefell, the relationship of a Michigan same-sex married couple could not be recognized for any purpose due to state constitutional and statutory bans. Obergefell makes a dramatic difference in a state like Michigan because civil marriages now can be performed and recognized here, and valid same-sex marriages entered into elsewhere can be recognized for purposes of Michigan law. With recognition of marital status comes predictability and enforceability of legal arrangements based upon marital status. As one commentator I read put it, the "gay exception" is over.
4. Obergefell has practical significance, affecting every day matters like income tax compliance, real estate transfers, and marital agreements. For example, prior to Obergefell:
 - a. A same-sex married couple residing in Michigan was required to file federal income tax returns as a married couple (either jointly or married filing separately), but they were required to file Michigan income tax returns as unmarried individuals. Now they can file jointly both at the federal and state levels.
 - b. One member of a same-sex married couple could not transfer a home to or in trust for his or her spouse without uncapping for property taxes because the exemption for transfers to spouses did not apply to a couple whose marriage was not recognized in Michigan for any purpose. Now, such an interspousal transfer should not lead to uncapping.
 - c. A Michigan same-sex couple could enter into a valid marriage in Canada or California, but they couldn't enter into a prenuptial or postnuptial agreement or even divorce in Michigan.

B. Estate Planners May Now Rely on Michigan Law.

Now that the legal rules for married couples, both same-sex and opposite-sex, are the same, planning for same-sex couples is much simpler. Estate planners

no longer have to create separate “Domestic Partner” documents for same-sex married couples. For example:

1. The couple may now refer to one another in their documents as spouses, without further explanation or fear of referring to their relationship as a couple. Prior to Obergefell, a same-sex married couple needed to be cautious about identifying one another as “spouse” for fear that a court might not enforce a gift based upon a relationship that could not be recognized in Michigan for any purpose.
2. Prenuptial Agreements should now be options for same-sex couples, with the marriage itself furnishing consideration. Before Obergefell, a same-sex married couple needed to contrive other consideration for any enforceable domestic partnership agreement.
3. Because divorce should now be available to a same-sex married couple living in Michigan, statutes that terminate marital rights upon dissolution of a marriage will apply to same-sex couples. Before Obergefell, the inability of a same-sex couple to divorce left the couple whose relationship dissolved in legal limbo.

C. Powers of Attorney and Patient Advocate Designations.

1. A spouse has statutory priority to be appointed as guardian or conservator for an incapacitated spouse. Before Obergefell, however, the relationship of same-sex spouses was not recognized under Michigan law, though it should be now.
2. Advice to same-sex and opposite-sex couples remains the same: put your intentions in writing by signing a Patient Advocate Designation and Durable Power of Attorney for finances.

D. Probate After Obergefell.

1. Intestacy and statutory rights are available, but estate planning is preferable. After Obergefell, a same-sex spouse now has statutory priority as the spouse of an intestate decedent to be appointed as personal representative. Same-sex spouses also are entitled to intestate succession, spousal allowance, elective share, and statutory protection afforded to an omitted spouse.
2. Same-sex couples should still pay careful attention to estate planning, because the statutory default provisions will not necessarily carry out a married couple’s intentions for one another.
3. There should no longer be controversies about wrongful death or insurable interest matters. There no longer should be any question as to whether a surviving same-sex spouse is entitled to participate in a wrongful death proceeding or whether the surviving spouse has an insurable interest in a spouse's life.

E. Gift and Estate Taxes.

After Obergefell, the unlimited federal estate and gift tax marital deductions are available, so tax deferral and minimization are available to same-sex couples regardless of the size of their estates. For couples exposed to estate tax, the planner no longer needs to counsel “marital deduction substitutes,” like using charitable deductions via Charitable Remainder Trusts (“CRTs”), Charitable Lead Trusts (“CLTs”) or valuation discounts. The marital deduction can take any available form, including outright transfers, beneficiary designations, and properly structured trusts. Portability also is available for estate tax purposes, subject to the same rules for all married couples.

F. Social Security and Veterans Benefits.

Social Security survivor benefits and veteran's benefits recognize marriages based upon the state of domicile. Now that same-sex marriage is recognized in all 50 states, Attorney General Lynch announced that it is the federal government's intention that these benefits apply to all married couples. See "Attorney General Lynch Announces Federal Marriage Benefits Available to Same-Sex Couples Nationwide," Department of Justice, Office of Public Affairs (July 9, 2015).

G. Domestic Partner Benefits.

Many companies prior to the U.S. Supreme Court ruling offered benefits to same-sex couples as domestic partners. However, with the Court ruling eliminating the barriers same-sex couples faced in getting married, employees should expect that domestic partnership benefits may be eliminated for unmarried same-sex couples.

H. Income Tax Implications.

1. The Michigan Department of Treasury has indicated that, based on Obergefell, same-sex married couples who were married in previous tax years can file amended tax returns reflecting the marital status for those that were married and that they have four years to do so. See Michigan Department of Treasury Notice, “Michigan Income Tax Filing Status for Married Same-Sex Couples” (July 1, 2015).
2. However, because Michigan has a flat tax rate, not every Michigan same-sex married couple would benefit from filing an amended Michigan return. Those that may benefit from filing an amended return are those couples:
 - a. Where only one spouse has income.
 - b. Where the homestead property taxes would differ.
 - c. Who are now eligible for the earned income credit.
 - d. Where one or both are retired, if the older spouse was born between 1946 and December 31, 1952, and they have

retirement income or passive income that takes the place of retirement income.

3. Following Obergefell, same-sex married couples will have all of the federal income tax advantages (joint filing, IRA rollover at death, etc.) as well as the disadvantages of heterosexual married couples. Many of the “anti-abuse” provisions are based on relationships arising out of lineage or marriage. Some techniques that worked when same-sex marriage was not recognized for tax purposes will not work now; for example, losses between related parties are not recognized.

**Recent Developments in
Typical Estate Planning Circumstances**

Mark G. Landau

RECENT DEVELOPMENTS IN TYPICAL ESTATE PLANNING CIRCUMSTANCES

I. ADJUSTED 2016 FIGURES FOR ESTATE, GIFT AND GST TAX ITEMS

A. Unified estate and gift tax exclusion amount.

For gifts made and estates of decedents dying in 2016, the exclusion amount will be \$5,450,000 (up from \$5,430,000 for gifts made and estates of decedents dying in 2015).

B. Generation-skipping transfer (GST) tax exemption.

The exemption from GST tax will be \$5,450,000 for transfers in 2016 (up from \$5,430,000 for transfers in 2015).

C. Gift tax annual exclusion.

For gifts made in 2016, the gift tax annual exclusion will be \$14,000 (same as for gifts made in 2015).

D. Special use valuation reduction limit for farm or closely-held business interests.

For estates of decedents dying in 2016, the limit on the decrease in value that can result from the use of special valuation will be \$1,110,000 (up from \$1,100,000 for 2015).

E. Determining 2% portion for interest on deferred estate tax.

In determining the part of the estate tax that is deferred on a farm or closely-held business that is subjected to interest at a rate of 2% a year, for decedents dying in 2016, the tentative tax will be computed on \$1,480,000 (up from \$1,470,000 for 2015) plus the applicable exclusion amount.

F. Increased annual exclusion for gifts to non-citizen spouses.

For gifts made in 2016, the annual exclusion for gifts to non-citizen spouses will be \$148,000 (up from \$147,000 for 2015).

II. PORTABILITY OR NO? THE DEATH OF THE CREDIT SHELTER TRUST?

A. Portability of Deceased Spousal Unused Exclusion ("DSUE").

1. Under IRC 2010(c), for decedents dying after December 31, 2010, their estate can elect to transfer any unused exclusion amount to the surviving spouse. The amount received by the surviving spouse is called the deceased spousal unused exclusion, or DSUE, amount.

2. If the executor of the decedent's estate elects transfer, or portability, of the DSUE amount, the surviving spouse can apply the DSUE amount received from the estate of his or her last deceased spouse (defined later) against any tax liability arising from subsequent lifetime gifts and transfers at death.

- B. Last deceased spouse limitation.
 - 1. The last deceased spouse is the most recently deceased person who was married to the surviving spouse at the time of that person's death.
 - 2. Remarriage does not affect the designation of the last deceased spouse and does not prevent the surviving spouse from applying the DSUE amount to taxable transfers.
- C. Making the election.
 - 1. A timely-filed and complete Form 706 is required to elect portability of the DSUE amount to a surviving spouse. The filing requirement applies to all estates of decedents choosing to elect portability of the DSUE amount, regardless of the size of the estate. A timely-filed return is one that is filed on or before the due date of the return, including extensions.
 - 2. A portability election is irrevocable.
- D. Special rule where value of certain property is not required to be reported on Form 706.
 - 1. Regulations provide that the executors of estates which are not otherwise required to file Form 706 under section 6018(a) do not have to report the value of certain property qualifying for the marital or charitable deduction.
 - 2. For such property, the executor may estimate the value in good faith. The amount to be reported on Form 706 will correspond to a range of dollar values (rounded upward to the nearest \$250,000) and will be included in the value of the gross estate.
- E. Final Regulations were effective June 12, 2015.
 - 1. Final Regulation 20.2010-2 adopts the 2012 proposed Regulations with clarifications.
 - 2. Requirement of a "complete and properly prepared" return.
 - a. For marital and charitable deduction assets for estates under the exemption amount, the IRS allows a description of assets within \$250,000 and information qualifying assets for the marital or charitable deduction.
 - b. Simplified reporting is not applicable if value of bequest is needed to determine the value passing to another recipient or eligibility under other Code Sections (example - special use valuation, generation skipping, less than the entire interest is includible, disclaimer, or a partial Qualified Terminable Interest Property ("QTIP") election).
 - c. The Final Regulations clarify availability of extensions for estates below the threshold amount. PLR 201537012 (9/11/2015). The IRS allowed the extension of time beyond 9 months to elect

portability under Section 301.9100-3 (regulatory relief) where the taxpayer relied on a qualified tax professional.

- d. Effect of election where DSUE amount is uncertain. If the estate tax return is timely filed and later adjustments are necessary (e.g. claim against estate that will increase DSUE), an adjustment to the DSUE will be allowed.

F. Portability Advantages.

1. Simplicity.

- a. As mentioned above, an advantage of relying on portability is simplicity, at least in the eyes of many married couples. They may perceive that, rather than being bequeathed to a credit-shelter trust equal to the otherwise unused estate tax exemption of the first decedent, portability permits the first decedent's assets to be left outright to the surviving spouse.
- b. Assets can also be transferred to a QTIP trust that qualifies for the marital deduction for better control.

2. Basis step-up.

A second advantage of portability is that the assets acquired from the first decedent generally will receive a new (or second) automatic change in basis under IRC 1014 when the surviving spouse dies.

3. IRD tax-efficiency.

A third advantage arises where the estate of the first decedent includes sufficiently large amounts of Income in Respect of a Decedent ("IRD") property that the first decedent's unused estate tax exemption would have to be funded with IRD property. If a credit-shelter trust is funded with rights to IRD, income taxes on the IRD will erode the wealth that ultimately was intended to pass to the couple's descendants at the death of the surviving spouse, in effect wasting the exemption on assets used to pay income taxes. The DSUE amount, by contrast, is fixed as of the first decedent's death, so long as the surviving spouse does not fail to use up the DSUE amount prior to remarrying and surviving a second spouse.

4. Market declines.

A fourth advantage of portability is that the DSUE amount is not reduced if the assets inherited from the first decedent decline in value.

5. Lower state exemption amount.

A fifth advantage of portability arises where the first decedent's estate could be subject to a state estate tax and the state exemption amount differs from (usually is smaller than) the federal estate tax exemption.

6. Avoidance of funding formulas.

Portability also permits a couple to avoid using "optimum" or "reduce-to-zero" funding formulas.

G. Portability disadvantages.

1. GST exemption.

One disadvantage is that the unused GST exemption of the first decedent is not portable and will be lost (wasted) to the extent not otherwise used by him or her. By contrast, if property equal to the unused GST exemption of the first decedent passes to a credit shelter trust, the GST exemption can be allocated to the credit shelter trust.

2. Creditors' claims.

a. A second disadvantage is that assets passing outright to the surviving spouse will be subject to the claims of creditors of the survivor, including any subsequent spouse if the surviving spouse remarries.

b. However, a QTIP trust can protect the assets from the creditors of the surviving spouse.

3. Loss of control.

a. A third disadvantage of portability is that, if assets are left outright to the surviving spouse, he or she will not be protected from "unwise" financial decisions, such as transferring assets to another spouse.

b. A QTIP trust is a possible solution.

4. Lack of indexing.

A fourth disadvantage is that, unlike one's own estate and gift tax exemption, the DSUE amount ported over to the survivor is not indexed for inflation. Property passing from the first decedent may grow by the time the survivor dies. If the growth occurs within a credit-shelter trust that uses up all of the first decedent's estate tax exemption, more property will be protected from estate tax than if the first decedent's estate tax exemption is instead ported to the surviving spouse.

5. Remarriage forfeiture.

A fifth disadvantage is that if the surviving spouse remarries and survives a second spouse, the DSUE amount of the first spouse, if not previously used to make gifts, is forfeited.

6. More audit risk.

A sixth disadvantage is additional audit risk. The statute of limitations on the first death (3 years) runs until the statute of limitations on second

death (example - 20 years later) to determine the unused exclusion amount.

H. Planning.

1. Estates that will never exceed the "\$5,000,000 exemption."
 - a. For these estates, clients typically decide not to file Form 706 to make the portability election. The cost to prepare the return would not be worthwhile.
 - b. Of course, the value of the estate can unexpectedly increase and/or the exemption can decrease.
2. Estates that may exceed the "\$5,000,000 exemption."
 - a. Discuss with the client the benefit in filing the portability election (potential savings of estate tax on amounts over the exemption) vs. the cost of preparing the return.
 - b. Many clients view this as an extra insurance policy.
 - c. Consider the age and health of the surviving spouse as well as the nature of the assets.
3. Estates over the "\$5,000,000 exemption". File the election.

I. Tips on Filing the Election.

1. Obtain full supporting information to support basis - required for IRS reporting. A higher value passing to the surviving spouse will result in less capital gain tax on a subsequent sale although it will increase the size of the surviving spouse's estate.
2. Take a deduction for claims against the estate and funeral expenses. This will lower the amount passing to the credit shelter trust, thereby increasing the amount of the DSUE available for the surviving spouse.

III. CONTINUING VIABILITY OF DISCOUNTING TECHNIQUES

A. Proposed regulations.

Regulations are not yet issued under IRC 2704(b) to limit/eliminate discounts of family owned equity interests in family companies.

1. New regulations were last proposed in President Obama's 2013 Greenbook Proposal. The Greenbooks for Fiscal 2014, 2015 and 2016 omitted the proposal.
2. The Greenbook proposal would have eliminated certain categories of restrictions that reduce fair market value for family controlled companies.

- B. IRC 2704(b)(4).
1. Treasury is authorized to issue regulations that will disregard certain restrictions if the effect would be to reduce value below fair market value.
 2. This may apply to active and passive companies.
 3. The benefit of no family attribution would still apply.
- C. Planning - Act Now.
1. For clients with estates over the exemption amount (\$5,430,000-2015), a common technique would be for the owner to transfer a minority interest of an entity to his/her children.
 2. For example, if a client transferred a 20% interest in a \$1,000,000 LLC to each of his 3 children (client retains 40%), a 20% interest for gift tax purposes will be less than the \$200,000 pro rata value.
 3. With a 30% discount (\$60,000), the value for gift tax purposes would be \$140,000 vs. \$200,000.
 - a. \$60,000 (per child) would escape estate tax, as well as the appreciation from the gift tax value to the date of death value.
 - b. To avoid the transferred assets being subject to the creditors of the children, consider an irrevocable trust for the benefit of the children to hold the transferred assets vs. the child owning the assets outright.
 - c. The client must also be clearly advised that he would retain (in this example) only 40% of the income and 40% of any sale proceeds.
 - d. Also note that at the client's death, a further discount could be taken on the 40% retained interest.
 - e. The client can still manage the entity by retaining a majority of the voting interest, or being the manager of an LLC or using voting and nonvoting interests.
 4. A gift tax return must be filed (Form 709) to adequately disclose the discount to start the 3 year statute of limitations. IRS Field Attorney Advice 20152201F: Documentation on gift tax return did not rise to the level of disclosure required to trigger statute of limitations.

IV. PLANNING IMPLICATIONS

- A. Increasing consideration of joint trusts, time or restricted distributions, creditor protection, and income tax planning.
- B. With the increase in the exclusion amount (\$5,430,000 - 2015), a married couple each with their own trust has an opportunity to consider one single joint trust. Many factors are important to consider whether this option fits a client's situation. The chart on the next page helps identify these factors.

Examples

- Estates below \$5,000,000
- Estates between \$5,000,000 - \$10,000,000
- Estates above \$10,000,000
- 1st marriage / 2nd marriage
- Adult children
- House / IRAs / Investments

<u>Factors:</u>	<u>1 Single Joint Trust</u>	vs.	<u>2 Separate Trusts</u>
Ease of Administration	Yes		No (accounting, tax return, residuary beneficiaries)
Control	Surviving Spouse		Decedent Spouse (Independent (Co)Trustee(s))
Distribution for Husband and Wife	Same Beneficiaries		Different
Estate Tax	100% in survivor's estate (Portability election-\$10,860,000)		Residuary Trust - Survivor's Estate - estate tax free. Including increase in value
Creditor Protection for Client	No		Yes-transfer assets to less risky spouse
Basis Step Up	50%		100% • 1 year rule
Creditor Protection for Children • IRA Beneficiary	In Trust		In Trust
Avoid Probate	Yes		Yes
Discounting	N/A		IRS Regulation to be issued (Family passive assets)
GST - Avoid Estate Tax (Children)	Forfeit GST exemption (Not portable)		Use GST exemption

DISTRIBUTIONS TO ADULT CHILDREN

September, 2015

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Most Protection	<u>Trust Structure</u>	<u>Trustee</u>
10	Discretionary Trust	Independent <ul style="list-style-type: none"> • Bank/Institution • Individual
9	Suspend distributions with specified events - divorce, creditors, drugs	
8		
7	Support Trust - The standard is critical <ul style="list-style-type: none"> • <u>"Exception Creditors"</u> <ul style="list-style-type: none"> • Child/spousal support • US or state claim • Creditors who provide services • <u>Exception</u> – Distributions in excess of support 	
6		Related party - family
5	Principal distributions at intervals (ages 25/30/35) or events	
4		Beneficiary as Trustee
3	Right to withdraw	
2		
1	Outright	
Least Protection		

DRAFTING PROVISIONS

1. Spendthrift Clause
2. Holdback provision if creditors seek funds
3. Trustee removal provisions
 - Beneficiary right to remove (with cause?) and select a co-trustee/successor trustee - independent
4. Incontestability clause

PREFERRED FUNDING

1. Investment account – Trust owner
2. IRA – designate subtrust as beneficiary vs children directly
 - Conduit IRA - life expectancy of each beneficiary
3. Insurance – Trust as beneficiary
4. Real Estate
 - Tenancy by the entireties (Husband and Wife)
 - Trust

**Current Concerns in Medicaid and
Special Needs Planning**

Kathryn Gilson Sussman

CURRENT CONCERNS IN MEDICAID AND SPECIAL NEEDS PLANNING

ESTATE RECOVERY

- A. Estate Recovery applies to Medicaid beneficiaries who are 55 years of age or older and have received long term care services on or after September 30, 2007. MCL 400.112g - 400.112k.
- B. Currently, Estate Recovery only applies to probate assets. To avoid Estate Recovery, avoid probate of any assets (MCL 400.112g).
 - 1. Allowable assets of Medicaid recipient are generally homestead (\$552,000 maximum value), personal property, vehicle, irrevocable funeral contract and burial space items and other assets which total \$2,000 or less.
 - 2. If homestead is owned by a Living Trust, it is a countable asset.
 - 3. Ladybird Deed for homestead is a solution because it allows homestead to be non-countable and avoids probate.
- C. Estate Recovery amount is limited to total Medicaid benefits paid by the State. Medicaid contracted amount is lower than private pay amount.
- D. When Michigan Department of Health and Human Services (MDHHS) learns of the Medicaid recipient's death, a notice and questionnaire is sent to the estate representative.
- E. Estate Recovery claim of State is subject to creditor claim rules of EPIC (Estate and Protected Individual Code):
 - 1. Priority of claims against Estate (MCL 700.3805).
 - a. Costs and expenses of administration.
 - b. Reasonable funeral and burial expenses.
 - c. Homestead Allowance (MCL 700.2402). Surviving spouse, or if none, minor or dependent children are entitled to homestead allowance of \$22,000 for 2015.
 - d. Family allowance (MCL 700.2403). A reasonable family allowance (\$27,000 maximum for 2015 without a court order) for up to 1 year is payable to surviving spouse and minor children whom decedent was obligated to support.
 - e. Exempt property (MCL 700.2404) - household furniture, automobiles, furnishings, appliances and personal effects of \$15,000 for 2015 (or other assets if there is not \$15,000 worth of exempt property) to surviving spouse, or if none, to decedent's children jointly.

- f. Debts and taxes with priority under federal law, including medical assistance payment subject to recovery under 42 USC 1396p.
- g. Reasonable and necessary medical and hospital expenses of the decedent's last illness.
- h. Debts and taxes with priority under other laws of Michigan.
- i. All other claims.

Secured Creditor's Claim (i.e. mortgage, equity loan, care loan) has priority over all unsecured debt to the extent of the amount secured and has priority over allowances.

2. Creditor Notice.

- a. Limitation on claim of creditor (MCL 700.3803). Claim against a decedent's estate, including a claim of the State, is barred against the estate, personal representative, decedent's heirs and devisees, and other non-probate transferees unless claim is presented within one of the following time limits:
 - (1) Within 4 months after notice to creditors is published.
 - (2) For a known creditor, within 1 month after actual notice is sent or within 4 months after notice to creditors is published, whichever is later.
 - (3) If no notice is given, within 3 years after decedent's death.
- b. Personal Representative can settle creditor claims, so they can negotiate with the State (MCL 700.3813).
- c. If Personal Representative distributes estate assets to beneficiaries, beneficiary must return the item distributed (or its value) (MCL 700.3911).

F. Small Estate Proceedings which do not require Creditors Notice:

- 1. Homes for the aged, nursing homes, morgues and police departments may turn over cash of up to \$500 and clothing to a beneficiary or heir (MCL 700.3981).
- 2. Court ordered small estate, in which Probate Court, upon filing of appropriate form, enters order directing estate (including either or both personal or real property) with a net value of less than \$22,000 plus the amount of funeral expenses for 2015 be turned over to whomever paid for the funeral (if not the estate), or to the spouse, or if no spouse to the heirs. However, if proceeds are turned over to heirs, other than a spouse, heirs must turn funds over to creditors who claim them within 63 days of order. However, there is no requirement that anyone notify creditors (MCL 700.3982).

3. Non-judicial small estate process applies to personal property (not real estate) if net estate has a value of less than \$22,000 for 2015. Sworn statement is presented to bank, broker or other holder of personal property if 28 days has passed since decedent's death. Recipient may be obligated to turn funds over to creditor who claims them, but there is no requirement for anyone to notify creditors (MCL 700.3983).
4. Summary Closing of Estate can be used by Personal Representative, if value of estate is less than costs of administration, funeral and burial expenses and allowances. Under this procedure, the Personal Representative collects the proceeds and files a closing statement. No advance notice to creditors is required, although the Personal Representative must file the closing statement with any unsatisfied creditors, who then have 28 days to object (MCL 700.3988).

G. Protections for Homestead.

1. Estate Recovery will be deferred as to homestead in probate estate of Medicaid recipient during period one or more of the following are residing in homestead:
 - a. Surviving spouse.
 - b. Surviving child who is under 21, blind or disabled.
 - c. Sibling who lived in homestead for at least 1 year before Medicaid recipient entered the nursing home.
 - d. Caretaker relative who lived in homestead for at least 2 years before the Medicaid recipient entered the nursing home and who can prove that during that time, but for the care he or she provided, the Medicaid recipient would have needed nursing care. "Caretaker relative" means any relation by blood, marriage or adoption within fifth degree of kinship to the Medicaid recipient.
2. Hardship Waivers.
 - a. Hardship waiver available for homes of modest value (MCL 400.112g(3)(e)(i)). The Statute provides an amount (equal to ½ the value of the average home in the county) is excluded from being reached by the State. However, the current position of the State is that hardship exception only applies to a homestead with a total value less than 50% of the value of an average home in county the where homestead is located.
 - b. Income-Producing Asset (MCL 400.112g(3)(e)(ii)). Portion of estate that is primary income-producing asset of survivors, including, but not limited to, a family farm or business.
 - c. Means test prerequisite for heir:
 - (1) Household income is less than 200% of poverty level (\$23,540 for 2015), and
 - (2) Household resources (with no exemptions) do not exceed \$10,000.

MICHIGAN DEPARTMENT OF COMMUNITY HEALTH
MICHIGAN ESTATE RECOVERY QUESTIONNAIRE

Instructions: (Print or typewritten)

- Complete each section and sign at the end of this form.
- Provide a copy of the deceased Medicaid member's death certificate and any other documentation requested on this form. *(No exceptions; a copy must accompany this questionnaire.)*
- Mail completed form and all requested documentation in the enclosed (postage paid) envelope provided to:

Michigan Department of Community Health
 Third Party Liability
 P.O. Box 30435
 Lansing, Michigan 48909

If you have any questions about how to complete this form, you may call the TPL Division toll-free at 1-844-TPL-MDCH.

Person Completing this Form	
(Check one)	Name: _____
<input type="checkbox"/> Personal Representative	Address: _____
<input type="checkbox"/> Attorney for Estate	_____
<input type="checkbox"/> Other (Specify) _____	Telephone: _____
Court Information	
Has a petition for probate of the estate been filed? <input type="checkbox"/> Yes <input type="checkbox"/> No If YES, provide a copy of the inventory.	
If YES, provide: Probate Case Number: _____ Date Filed: _____	
County Probate Court: _____	
If No, do you anticipate a petition for probate being filed? <input type="checkbox"/> Yes <input type="checkbox"/> No	
Have there been any third party lawsuits filed on behalf of the estate? <input type="checkbox"/> Yes <input type="checkbox"/> No	
If YES, provide: Case Number: _____ Date Filed: _____	
County Court: _____	
If NO, do you anticipate any third party lawsuits being filed? <input type="checkbox"/> Yes <input type="checkbox"/> No	
Deceased Medicaid Member Information	
Last Name: _____	Date of Birth: _____
First Name: _____	Date of Death: _____
Middle Name: _____	Social Security Number: _____
Marital Status: (at time of death) <input type="checkbox"/> Married <input type="checkbox"/> Divorced <input type="checkbox"/> Widowed <input type="checkbox"/> Never Married	
<i>Check appropriate status</i>	
If checked married, provide a copy of the marriage license.	
Is the deceased Medicaid member's spouse still living? <input type="checkbox"/> Yes <input type="checkbox"/> No	
Spouse Last Name: _____	Date of Birth: _____
Spouse First Name: _____	Date of Death: _____
Spouse Middle Name: _____	Social Security Number: _____

AUTHORITY: MCL 400.112g
COMPLETION: Completion is voluntary, but is required for an Estate Recovery exemption.

The Department of Community Health is an equal opportunity employer, services and programs provider.

Statutory Exemption Information

A. Is the deceased Medicaid member survived by a child under the age of 21 OR a child of any age who has been deemed blind or permanently disabled by the Social Security Administration? Yes No

If Yes, provide a copy of the child's birth certificate and recent Social Security Administration determination of disability, and:

Child's Name: _____

Child's Date of Birth: _____ Child's Social Security Number: _____

B. Is there a caretaker relative residing in the home that has been residing in the home for at least 2 years prior to the deceased Medicaid member's admission to a facility? Yes No

Caretaker's Name: _____

If YES, provide copies of driver's license and bank statements to show residence for the 2 year period, AND a statement from a physician stating that the care provided allowed the deceased Medicaid member to reside at home rather than in an institution.

C. Was there a sibling residing in the home for 1 year prior to the deceased Medicaid member's admission to a nursing facility with an equity interest in the home? Yes No

Sibling's Name: _____

If YES, provide copies of driver's license and bank statements to show residence for the 1 year period, AND a statement of equity interest in the home.

Asset Information

D. Did the deceased Medicaid member own a home or other real property at the time of death? Yes No

If YES, complete Homestead and/or Other Real Property and provide a copy of the deed showing ownership.

Homestead

Address:	Approximate Market Value: \$
----------	---------------------------------

Type of ownership (i.e., tenants in common, life estate, joint tenants, fee simple, etc.)

Other Real Property

Address:	Approximate Market Value: \$
----------	---------------------------------

Type of ownership (i.e., tenants in common, life estate, joint tenants, fee simple, etc.)

E. Did the deceased Medicaid member have any bank accounts at the time of death? Yes No

If YES, provide a copy of the bank statement and complete the information below:

Bank Name:

Is this a joint account? <input type="checkbox"/> Yes <input type="checkbox"/> No	Account Number:	Account Balance:
---	-----------------	------------------

F. Did the deceased Medicaid member own other personal property (i.e., vehicles, jewelry, other personal items of value)? Yes No

List any other personal property :

I certify that the information contained in this form is true and complete to the best of my knowledge. I understand that the Michigan Department of Community Health is relying on this information when determining the value of Medicaid's claim and/or granting an exemption from Estate Recovery.

Signature of person completing this form

Date

**Preparing the Closely Held Business for
Transfer to the Next Owner**

Christopher M. Williams

PREPARING THE CLOSELY HELD BUSINESS FOR TRANSFER TO THE NEXT OWNER

I. CLOSELY HELD BUSINESS

A. What is a closely held business?

1. For our purposes, a closely held business is a private company owned by a relatively small group of people.
2. Features:
 - a. Oftentimes, family owned.
 - b. Ownership transfers are restricted.
 - c. Management issues can be settled by written agreement.
 - d. Minority shareholders have key rights.
 - e. Flexible entity choices for tax purposes.
 - (1) Limited liability company.
 - (2) "S" corporation.
 - (3) "C" corporation.
 - (4) Partnership.
 - f. Not necessarily small.

B. Most businesses in the United States are closely held businesses and therefore they represent a significant segment of the U.S. economy.

II. BUSINESS SUCCESSION PLAN

A. What is a business succession plan?

A business succession plan is a well-thought out strategy for transferring ownership, management, and control of a business, which is implemented by business practices and legal documents that support the plan.

B. What are the benefits of a business succession plan?

1. Provides business continuity, keeping the business alive.
2. Preserves financial benefit for the owner and his or her family.
3. Provides opportunities for the next generation.

4. Helps to attract and retain employees committed to the business.
5. Ensures a smooth transition.
6. Clarifies authority and decision making.
7. Maximizes business value.
8. Increases attractiveness to successors by being non-principal dependent.
9. Minimizes taxes upon the transfer of the business.

C. Why don't all closely held business owners have a business succession plan?

1. Too busy.
2. Overwhelming. Not sure where to start.
3. Family dynamics.
4. Fear of facing mortality.
5. Identity is too invested in the business. They can't imagine ever retiring.
6. They believe that they already have a business succession plan.
 - a. Will.
 - b. Verbal agreement.

III. DEVELOPING THE BUSINESS SUCCESSION PLAN: WHAT DO YOU WANT TO DO?

How is a business succession plan created?

1. A business succession plan needs to be developed in consultation with professional advisors.
 - a. Advisors will ensure that all issues are addressed and provide options.
 - b. Key advisors include:
 - (1) Attorneys.
 - (2) Accountants.
 - (3) Financial advisors.
 - (4) Insurance agents.
 - (5) Valuation experts.

- (6) Business brokers.
 - (7) Bankers.
2. Planning involves fact gathering and evaluation.
- a. Owner must conduct a self-evaluation.
 - (1) Evaluate goals.
 - i. When to retire?
 - ii. When to give up control?
 - iii. Role during transition?
 - iv. Who to transfer the business to?
 - (2) Evaluate future financial needs.
 - i. Future income needs.
 - ii. Retirement.
 - iii. Assets and liabilities.
 - (3) Evaluate estate plan.
 - i. Is there an estate plan in place?
 - ii. Does it need to be updated?
 - iii. Do fiduciaries have business experience and authority?
 - b. Owner must evaluate the business.
 - (1) Who are the key leaders, employees, and advisors?
 - (2) Future strategic plan for the business.
 - (3) Future industry trends.
 - (4) Entity choice for operating business and affiliated enterprises.
 - (5) Corporate formalities.
 - (6) Problem assets, products, employees, customers, and contracts.

- (7) Evaluate financials.
- c. Owner must evaluate prospective successors.
- (1) Family members.
 - i. Do they want anything to do with the business?
 - ii. Do they have the capability to run the business?
 - iii. If more than one, do they get along?
 - iv. How will extended family relationships be impacted?
 - (2) Current partners and shareholders.
 - i. Are they interested in staying in the business?
 - ii. Do they have financial resources to purchase business?
 - iii. Are resources sufficient for the business to redeem?
 - iv. Is there an agreed to mechanism regarding price?
 - (3) Employees.
 - i. Capability and training to run business?
 - ii. Financial resources to purchase business?
 - (4) Competitors.
 - i. Interested in purchasing the business?
 - ii. How will they handle current employees?
 - iii. Are the business cultures complementary?
 - (5) Unrelated third party.
 - i. How are they found?
 - ii. How will they handle current employees?
 - iii. Are the business cultures complementary?

3. Contingency planning must be addressed.
 - a. Death.
 - b. Disability.
 - c. Retirement.
 - d. Divorce.
 - e. Termination of employment.
 - f. Bankruptcy.

IV. IMPLEMENTING THE BUSINESS SUCCESSION PLAN: HOW TO DO IT

- A. Business practices to implement the plan.
 1. Developing a vision for the business to identify future leaders.
 2. Focusing on sustainable profits.
 3. Delegating responsibilities.
 4. Valuing the business.
 5. Identifying potential successors.
 6. Identifying and developing talent.
 7. Developing a timetable for transitioning the business.
 8. Conducting internal due diligence review and making adjustments.
 9. Creating job descriptions and defining roles.
 10. Addressing compensation, profit-sharing, and incentive programs.
 11. Following corporate formalities.
 12. Operating through governance structure (e.g. Board of Directors).
- B. Options for transfer.
 1. Family Members.
 - a. Sale.
 - (1) Equity or asset sale.
 - (2) Option to purchase.

- (3) Right of first refusal.
 - (4) If purchase price is paid in installments, cash flow from equity can be used to make payments.
 - b. Lifetime gifts.
 - (1) Lifetime transfers to reduce the taxable estate.
 - (2) Create voting and non-voting ownership interests.
 - i. Permits owner to retain control.
 - ii. Discounts for transfer of non-voting interests.
 - c. Stock Bonus Program for employed family members.
 - d. Other estate planning options.
 - (1) Grantor Retained Annuity Trust ("GRAT").
 - (2) Intentionally Defective Grantor Trust ("IDGT").
- 2. Surviving shareholders and partners.
 - a. Cross-Purchase upon triggering events.
 - (1) Mandatory or optional.
 - (2) Right of first refusal.
 - b. Redemption by the company upon triggering events.
 - (1) Mandatory or optional.
 - (2) Right of first refusal.
- 3. Employees.
 - Sale.
 - (1) Equity or asset sale.
 - (2) Option to purchase.
 - (3) Right of first refusal.

4. Competitors and Unrelated Third Parties.
 - a. Equity or asset sale.
 - b. Merger.
- C. Options to provide continuing income to owner post-transfer.
1. Sale on an installment basis.
 - a. Promissory Note.
 - b. Self-cancelling installment note ("SCIN"). Repayment extinguishes upon death of business owner provided certain criteria are met.
 2. Employment Agreement.
 - a. May also be a means for providing continuing benefits.
 - b. May cover non-competition.
 3. Consulting Agreement.
 4. Deferred Compensation Plan.
 5. Income from Passive Business Assets (e.g. real estate or equipment).
 6. Structure sale as a private annuity.
- D. Life Insurance.
1. Create cash flow in the event the principal dies.
 2. Source of funds to buy-out the business owner.
- E. Tax Matters.
1. Due to the illiquidity of a private business, taxes present a serious obstacle to transferring the business to the next generation and may lead to a forced sale or liquidation of the business.
 2. Do a complete tax analysis of transfer options.
 - a. Transfer taxes.
 - (1) Federal Estate Tax.
 - (2) Federal Gift Tax.
 - (3) Generation-skipping transfer tax.

- b. Basis of equity transferred.
 - c. Capital gains tax.
 - d. Income tax.
 - e. Available deductions.
 - 3. Take full advantage of estate planning techniques to reduce the tax burden.
 - a. Business owner and spouse should structure property holdings and estate plans to take advantage of applicable credit amount and shelter from taxation the balance of the assets through marital deduction.
 - b. Structure the business entity to take advantage of valuation discounts (e.g. liquidating and voting control discount).
 - c. Make lifetime gifts to reduce estate taxes.
 - d. Used leveraged estate planning techniques to increase the amount of tax-free transfers (e.g. GRATs, SCINs, IDGTs, etc.).
 - e. The estate plan of the business owner should be structured to enable the personal representative to take advantage of post-mortem tax elections.
- F. Legal documents to implement the plan.
- 1. Buy-Sell Agreement.
 - 2. Employment Agreement.
 - 3. Amendments or restatements of organizational documents.
 - a. Articles of Incorporation or Organization.
 - b. By-laws or operating agreements.
 - 4. Purchase agreement.
 - 5. Redemption agreement.
 - 6. Option agreement.
 - 7. Estate Plans.
 - a. Trust.

- b. Will.
- c. Power of Attorney.

V. TIMING: WHEN SHOULD THE PLAN BE CREATED?

- A. A business succession plan should be created as early as possible.
 - 1. More planning options are available.
 - 2. Protects against unplanned transfer events (e.g. death, disability, etc.).
- B. A business succession plan should be regularly reviewed and updated.

**Guidance for Dealing with Employees
in the Closely Held Business**

**David A. Lawrence
Sarah Heisler Gidley**

GUIDANCE FOR DEALING WITH EMPLOYEES IN THE CLOSELY HELD BUSINESS

I. FEDERAL LAWS AND REGULATIONS YOU SHOULD KNOW

- A. Title VII of the Civil Rights Act of 1964.
 - 1. The Civil Rights Act prohibits employers from discriminating against employees on the basis of sex, race, color, national origin and religion.
 - 2. Generally applies to employers with 15 or more employees.

- B. Americans with Disabilities Act of 1990 ("ADA").
 - 1. The ADA prohibits discrimination against individuals with disabilities who have the qualifications to perform the essential functions of the job.
 - 2. Applies to all stages of employment and requires the employer to make reasonable accommodations for employees with disabilities.
 - 3. Generally applies to employers with 15 or more employees.

- C. Equal Pay Act ("EPA").
 - 1. The EPA prohibits sex-based wage discrimination between men and women in the same establishment who perform jobs that require substantially equal skill, effort and responsibility under similar working conditions.
 - 2. Pay differential is permitted when they are based on seniority, merit, quantity or quality of production, or a factor other than sex.
 - 3. Virtually all employers are covered.

- D. Age Discrimination in Employment Act ("ADEA").
 - 1. The ADEA prohibits employment discrimination against anyone 40 years of age or older, but does not protect certain types of employees, such as high level managers and public safety personnel.
 - 2. Generally applies to employers with 20 or more employees.

- E. Older Worker Benefit Protection Act ("OWBPA").
 - 1. The OWBPA is an amendment to the ADEA.
 - 2. It is illegal for an employer to:
 - a. Use an employee's age as the basis for discrimination in benefits.

- b. Target older workers for restructuring and layoff programs.
 - c. Require older workers to waive their rights under the ADEA without observing certain safeguards.
- F. Employment Retirement Security Act ("ERISA").
 - 1. ERISA sets minimum standards for most voluntarily established pension and health plans in private industry to provide protection for individuals in these plans.
 - 2. ERISA does not require any employer to establish a retirement plan.
- G. Immigration Reform and Control Act of 1986 ("IRCA").
 - 1. The IRCA prohibits discrimination on the basis of citizenship or immigration status.
 - 2. Employers may only hire persons who may legally work in the U.S. (i.e. citizens and nationals of the U.S. and aliens authorized to work in the U.S.).
 - 3. Employers must verify the identity and employment eligibility of anyone to be hired, which includes completing the Employment Eligibility Verification Form (I-9).
 - 4. Employers must keep each I-9 on file for at least three years, or one year after employment ends, whichever is longer.
- H. Personal Responsibility and Work Opportunity Act of 1996.
 - 1. This act requires employers to report the name, address and social security number of every new employee within 20 days of hire to a designated state agency. See www.mi-newhire.com.
 - 2. States will match new hire information against child support records to locate parents, establish a support order, or enforce an existing order.
 - 3. States will also report new hire information to a national directory to detect and prevent public benefit payments to employed persons.
- I. Family Medical Leave Act ("FMLA").
 - 1. FMLA requires covered employers to provide up to 12 weeks of unpaid, job-protected leave to eligible employees for the following reasons:
 - a. Incapacity due to pregnancy, prenatal medical care or child birth.

- b. To care for the employee's child after birth or placement for adoption or foster care.
 - c. To care for the employee's spouse, son, daughter or parent, who has a serious health condition.
 - d. For a serious health condition that makes the employee unable to perform the employee's job.
 - 2. FMLA applies to private companies with 50 or more employees.
 - 3. Employees are eligible for leave if they have worked for their employer for at least 12 months, at least 1,250 hours over the past 12 months, and work at a location where the company employs 50 or more employees within 75 miles.
- J. Health Insurance Portability and Accountability Act ("HIPAA").
- 1. The HIPAA "privacy rule" protects from unauthorized disclosure any personally-identifiable health information (protected health information or "PHI") that pertains to a consumer of health care services.
 - 2. The privacy rule applies only to "covered entities" which are health plans, health care clearinghouses and health care providers. To the extent that an employer operates in one of those capacities, it is a "covered entity." Most employers will not be a covered entity. However, if an employer has any kind of health clinic operations available to employees, or provides a self-insured health plan, or acts as an intermediary between its employees and health care providers, it may handle PHI that is protected by the privacy rule.
 - 3. PHI includes:
 - a. Health care claims or health care encounter information.
 - b. Health care payment and remittance advice.
 - c. Coordination of health care benefits.
 - d. Health care claim status.
 - e. Enrollment or disenrollment in a health plan.
 - f. Eligibility for a health plan.
 - g. Health plan premium payments.
 - h. Referral certifications and authorization.

- i. First report of injury.
 - j. Health claims attachments.
 - 4. Covered entities must adopt written privacy procedures, designate a privacy officer, provide required written notices to employees, and comply with certain other requirements.
- K. Fair Labor Standards Act ("FLSA").
 - 1. The FLSA establishes minimum wage, overtime pay, recordkeeping and youth employment standards for most public and private employers.
 - 2. The FLSA does not require: vacation, holiday, severance or sick pay; meal or rest periods, holidays off; overtime pay for weekend or holiday work; pay raises or fringe benefits.
 - 3. The FLSA applies to employers whose annual sales are more than \$500,000 or who are engaged in interstate commerce. However, "interstate commerce" is interpreted very broadly, so that nearly all workplaces are covered.
 - 4. The current federal minimum wage is \$7.25 per hour. If an employee is subject to both state and federal minimum wage laws, the employee is entitled to the higher minimum wage. Michigan's minimum wage is higher.
 - 5. Nonexempt employees must receive overtime pay for hours actually worked over 40 per workweek at a rate of not less than 1½ times the regular rate of pay. A workweek is any fixed and regularly recurring period of 168 hours - seven consecutive 24-hour periods.
 - 6. Employees are either "exempt" or "nonexempt" depending on their salary and the type of work they do.
 - a. Exempt: Some types of jobs are considered exempt by definition, such as farm workers, seasonal workers, and airline employees. Otherwise, an employee is exempt if the employee:
 - (1) Is paid at least \$23,600 per year (or \$455 per week), is paid on a salary basis, and performs exempt job duties.
 - (2) Performs exempt job duties, which include:
 - i. Executive - supervises other employees, primary duty is management.
 - ii. Professional - requires specialized or advanced education and training, does not include skilled

trades, but does include creative professionals and "computer professionals" (such as programmer, software engineer or similarly skilled worker).

iii. Administrative - support business, such as human resources, payroll and accounting.

iv. Outside Sales Employees - primary duty must be to make sales or obtain orders or contracts (the minimum salary requirement does not apply).

b. Non-exempt: All other employees are non-exempt and are entitled to overtime pay.

7. Violations and Penalties.

a. Common FLSA violations include:

(1) Misclassifying employees as exempt.

(2) Using unpaid "interns".

(3) Paying incorrectly for travel time.

(4) Not accurately tracking hours actually worked.

(5) Providing comp time in lieu of overtime.

(6) Misclassifying independent contractors.

b. The FLSA may be enforced through civil lawsuits by the federal government, criminal prosecutions by the Department of Labor, or private lawsuits by employees.

c. Violations of the FLSA may result in penalties including back pay, interest, attorneys' fees, court costs and liquidated damages. Employers may be assessed civil money penalties of up to \$1,100 for each willful or repeated violation of the minimum wage or overtime pay provisions of the law. The FLSA also allows for claims against individual corporate officer and supervisors for "willful" breaches of the law. Individuals may face fines of up to \$10,000 per violation and jail time for a second conviction.

L. Fair Credit Reporting Act ("FCRA").

1. The FCRA regulates the use of credit checks for employment purposes.

2. Before an employer gets a consumer report, it must:

- a. Tell the applicant or employee that it might use information in the consumer report for decisions related to employment. This notice must be in writing and in a stand-alone format (not on the employment application).
 - b. Get permission from the applicant or employee.
 - c. Certify compliance to the company from which it obtains the consumer report.
3. Before an employer takes adverse action based on information in a consumer report, it must give the applicant or employee:
- a. A notice that includes a copy of the consumer report the employer relied upon.
 - b. A copy of "A Summary of Your Rights Under the Fair Credit Reporting Act" issued by the federal Consumer Financial Protection Board.
 - c. After an employer takes adverse action based on information in a consumer report, it must give the applicant or employee notice of that fact, which includes: (i) the name, address and phone number of the consumer reporting company that supplied the report; (ii) a statement that the company supplying the report did not make the decision to take unfavorable action; and (iii) a notice of the person's right to dispute the accuracy or completeness of any information the consumer reporting company furnished.

M. Classification of Independent Contractors vs. Employees.

1. It is crucial that employers correctly classify a worker's status as an independent contractor or employee. Incorrect classification may lead to audits, fines and penalties.
2. Employers do not have to pay Social Security or Medicare taxes or federal unemployment insurance, or withhold federal income taxes, for independent contractors. The IRS will consider a worker an employee, not an independent contractor, if the employer has the right to direct and control the way he works, including the details of when, where and how the job is accomplished. The IRS uses a 20-factor test to evaluate the relationship:
 - a. Level of instruction.
 - b. Amount of training.
 - c. Degree of business integration.
 - d. Extent of personal service.

- e. Control of assistants.
- f. Continuity of relationship.
- g. Flexibility of schedule.
- h. Demands for full-time work.
- i. Need for on-site services.
- j. Sequence of work.
- k. Requirements for reports.
- l. Method of payment.
- m. Payment of business or travel expenses.
- n. Provision of tools and materials.
- o. Investment in facilities.
- p. Realization of profit or loss.
- q. Work for multiple companies.
- r. Availability to public.
- s. Control over discharge.
- t. Right of termination.

3. Whether a worker is an employee or independent contractor for purposes of FLSA, FMLA and civil rights statutes (Title VII, Elliott-Larsen, ADEA, ADA) is often determined by applying an "economic reality test." In addition to considering the degree of control the employer exercises, it takes into account the degree to which the worker is economically dependent on the business, including the following factors:

- a. The degree to which the employer controls or directs the manner in which work is performed.
- b. Whether the worker's opportunity for profit or loss depends on his or her managerial skills.
- c. Whether the worker's duties are performed for the employer on an ongoing or permanent basis.

- d. Whether the service performed by the worker is an integral part of the employer's business.
- e. The extent of the worker's investment in equipment or materials needed to perform the job.
- f. The degree to which the worker is engaged primarily for the benefit of the employer.

II. STATE LAWS AND REGULATIONS THAT YOU SHOULD BE AWARE OF

A. Elliot-Larsen Civil Rights Act ("ELCRA").

- 1. ELCRA is Michigan's version of the federal Civil Rights Act, but broader. It prohibits discrimination on the basis of race, color, religion, national origin, age, sex (including pregnancy), height, weight, or marital status.
- 2. ELCRA covers all employers unlike federal laws, which cover only employers with 15 or more employees.

B. Persons with Disabilities Civil Rights Act ("PDCRA").

- 1. PDCRA prohibits discrimination against an individual with a disability who is otherwise qualified to perform the essential functions of the job.
- 2. Applies to all stages of employment and requires the employer to make reasonable accommodations for employees with disabilities.

C. Michigan Occupational and Health Safety Act ("MIOSHA").

- 1. Under MIOSHA, employers must protect their employees by providing a safe workplace that is free of recognized hazards that may cause death or serious physical harm.
- 2. Employers must comply with MIOSHA standards and regulations and post notice and use other means to tell employees about their rights and obligations under MIOSHA.
- 3. Employees may not be fired for filing a complaint about unsafe working conditions.

D. Workforce Opportunity Wage Act.

- 1. The act was enacted on May 27, 2014 and repealed Michigan's prior minimum wage law.

2. Michigan's current minimum wage is \$8.15 per hour, and will increase through 2018 as follows:
 - a. January 1, 2016, \$8.50.
 - b. January 1, 2017, \$8.90.
 - c. January 1, 2018, \$9.25.
3. The act covers any employer with 2 or more employees, and therefore is broader than the FLSA. Employees are entitled to the higher Michigan minimum wage.
4. Overtime pay requirements mirror the FLSA.

E. Youth Employment Standards Act.

1. Covers every organization that employs minors (anyone under the age of 18 unless they have graduated from high school or have passed the GED).
2. The act restricts the type of work minors may perform, the hours during which they may work and the number of hours they may work each week.

F. Whistleblowers' Protection Act ("WPA").

WPA prohibits an employer from disciplining, discharging, or otherwise discriminating against an employee regarding wages, terms, conditions, location or privileges of employment because the employee reports or is about to report a suspected violation of the law.

G. Bullard-Plawecki Employee Right to Know Act ("ERKA").

1. Employees have the right to review and copy their "personnel records" upon written request. Personnel records which are not provided upon the employee's request cannot be used against the employee later in litigation.
2. A "personnel record" is defined as "a record kept by the employer that identifies the employee, to the extent that the record is used or has been used, or may affect or be sued relative to that employee's qualifications for employment, promotion, transfer, additional compensation, or disciplinary action." This may be broader than what employers typically maintain in a personnel "file."
3. Employers may not disclose disciplinary information to a third party without providing the employee with written notice.

4. Employers must review personnel records and delete disciplinary records more than four years old.

III. CURRENT ISSUES

A. Effect of Obergefell v. Hodges, 2015 US Lexis 4250 (June 26, 2015).

1. Employee Benefits

- a. The Supreme Court's decision in Obergefell requires employers to address benefits, tax and other employment issues for employees in same-sex marriages who work or reside in a state, like Michigan, that did not previously recognize employees' same-sex spouses.
- b. Employers with fully insured health and welfare plans will now be required to offer the same coverage to same-sex spouses that is offered to opposite-sex spouses. Employers with self-insured plans may not be required to provide coverage to same-sex spouses (because they are exempt from state insurance laws), but may face claims of discrimination or other lawsuits if they fail to do so.
- c. Employers should review their payroll procedures regarding taxes to ensure proper federal and state taxation to same-sex spouses for all benefits offered.
- d. 401(k) and other qualified retirement plans should not be impacted. In 2013 the Supreme Court ruled that federal law recognized same-sex marriage in United States v. Windsor, 570 US 12-307 (2013). That holding, and subsequent guidance from the IRS requiring recognition of same-sex marriage for all federal tax purposes, means that 401(k) and other qualified retirement plans should already be in compliance.
- e. Employers that offer domestic partner benefits should reevaluate the need for continuing these benefits.

2. Discrimination.

- a. Neither Title VII of the Civil Rights Act or the Elliott Larsen Civil Rights Act explicitly prohibits discrimination based on sexual orientation or gender identity/expression. Obergefell is not an employment case and does not expand the protected classes under these civil rights laws.
- b. In the past, courts have ruled that Title VII does not cover discrimination based on sexual orientation. However, in a decision issued July 17, 2015, the U.S. Equal Employment Opportunity Commission ("EEOC") said that employers who

discriminate against LGBT workers are violating Title VII. The EEOC concluded that "sexual orientation discrimination is sex discrimination because it necessarily entails treating an employee less favorably because of the employee's sex." David Baldwin v. Dept. of Transportation, EEOC Appeal No. 0120133080. The EEOC's decision is not binding on courts, and the long-term impact remains to be seen.

B. Medical marijuana laws.

1. The Michigan Medical Marijuana Act (MAMMA) permits marijuana use and distribution under specific, limited circumstances.
2. MAMMA states that "nothing in this act shall be construed to require an employer to accommodate the ingestion of marijuana in any workplace or any employee working while under the influence of marijuana."
3. Courts have upheld an employer's right to enforce zero tolerance drug policies, notwithstanding legal medical marijuana use under the MAMMA. See, e.g., Cassias v. Wal-Mart Stores Inc., 695 F.3d 428 (6th Cir. 2012) (employee, a cancer patient with a prescription for medical marijuana, was terminated for failing drug test).

**Recent Developments Concerning
Real Estate Ownership in Michigan**

Dawn T. Yeaton

RECENT DEVELOPMENTS CONCERNING REAL ESTATE OWNERSHIP IN MICHIGAN

I. MICHIGAN REAL PROPERTY OWNERSHIP RIGHTS FOR MARRIED COUPLES FOLLOWING THE SUPREME COURT DECISION IN OBERGEFELL V. HODGES

- A. Michigan statutes expressly provide certain real property rights to married couples who are husband and wife. The legislature is seeking to determine if and/or how those rights will be applied in the same-sex marriage context. Two areas in real property that are unsettled are dower rights and tenancies by the entirety.
- B. Tenancy by the Entireties: Under current Michigan law, when a husband and wife take title to real property, they do so as tenants by the entirety ("TBE").
1. Protections and benefits of TBE.
 - a. One spouse cannot take any action affecting title to the property without the consent of the other.
 - b. Both spouses have rights to any income generated (MCL 557.71).
 - c. Upon the death of one spouse, title automatically vests in the surviving spouse (as with joint tenancy with right of survivorship).
 - d. The marital estate is protected from creditors unless such claims are against both the husband and wife (MCL 600.6023a).
 - e. There are no transfer taxes incurred, nor is the taxable value uncapped, if real property held in the name of one spouse is transferred to both spouses, creating a tenancy by the entirety (MCL 207.505(i), MCL 207.526(i), and MCL 211.27a(7)(b)).
 2. Purpose of TBE
 - a. Michigan appellate courts have stated that the purpose of the protections and benefits of TBE is to protect the marital estate. Tkachik v Mandeville, 282 Mich App 364, 764 NW2d 318 (2009).
 - b. These protections and benefits are afforded both spouses, equally. There is no differentiation based on gender.
 3. Anticipated legislative resolution.
 - a. Extending TBE to same-sex spouses would not create a conflict with its stated purpose of protecting the marital estate.

- b. The Michigan Bar Association is working on proposed language for TBE, and all related statutes, that would eliminate the use of husband and wife as the definition of a married couple.
 - c. As of today, no bill has been introduced.
4. Practical concerns if a same-sex married couple wishes to acquire property prior to a legislative or judicial determination that TBE will apply to all married couples.
- a. Care should be taken when describing the couple's status as the grantee on the deed and the nature of the estate being conveyed.
 - b. If it is unclear that the grantees are married or if tenancy by the entireties is not deemed valid for same-sex married couples, the couple could hold title as tenants in common. However, tenancy in common affords none of the protections and benefits of TBE.
 - c. We recommend the following language, as an example:

John Smith, husband, and Bill Jones, husband, as a married couple and as tenants by the entireties, unless such tenancy by the entireties is deemed invalid under the laws of Michigan, then as joint tenants with full right of survivorship.

The alternative language vesting title as joint tenants with right of survivorship is to ensure that if tenancy by the entireties is not extended to same-sex married couples, then the couple will at least take title with the added security of the right of survivorship.

- C. Dower Rights: In Michigan, a widow has the statutory right to elect to take a one-third life estate interest in the real property owned by the husband during their marriage upon the husband's death (MCL 558.1). Michigan is the only state that still has dower rights.
- 1. Protections and benefits of Dower.
 - a. If a widow is unhappy with what she received under her deceased husband's will, she has the option of claiming her dower interest.
 - b. Dower rights in real property owned during the marriage are not terminated if the husband sells or finances the property without the wife's consent.

2. Purpose of Dower.
 - a. Dower is a statutory right given to a widow who is married to a husband. It is gender specific.
 - b. Michigan has upheld dower against Equal Protection Clause claims brought by husbands who believe Michigan's dower to be discriminatory. See, e.g., Eifler v Swartz (In re Estate of Miltenberger), 275 Mich App 47, 737 NW2d 513 (2007), stating that dower serves the important governmental purpose of protecting needy spouses and remedying past economic discrimination against widows by pointing to the current gap in average wages earned by men and women.
3. Anticipated legislative resolution.
 - a. Abolishing dower has been suggested for many years.
 - b. There are currently draft statutory revisions being circulated which would abolish dower in Michigan.
 - c. There has been no bill introduced at this time.
4. Practical concerns if a same-sex married couple wishes to sell or finance real property title in the name of only one spouse.
 - a. The title-holding spouse should be described as a married person.
 - b. The non-titled spouse should be defined as a spouse and sign the deed or mortgage to acknowledge the conveyance or security interest as to any interest (including homestead rights) he or she may have in the property.
 - c. This would ensure that, should dower rights be held to apply to all married couples, the dower interest will not cancel out or take priority over the ownership or security interest.

It is not certain how long it will take the Michigan Legislature to resolve the uncertainty of the application of tenancy by the entirety and dower rights to same-sex married couples. In the interim, a same-sex spouse who wishes to purchase, sell, or mortgage real property should seek legal counsel.

II. P.A. 310 OF 2014, MICHIGAN'S NEW "UNCAPPING" WITH FAMILY MEMBER TRANSFERS STATUTE

- A. Under Michigan law, a transfer of ownership causes the taxable value of the transferred property to be uncapped, or adjusted, in the calendar year following the year of transfer of ownership (MCL 211.27a).
- B. The Michigan statute addressing uncapping of the taxable value lists specific types of conveyances that are deemed "transfers of ownership" leading to an adjustment in the taxable value, and also provides that certain conveyances are excluded from the definition of "transfers of ownership" and would not cause the taxable value to be uncapped (MCL 211.27a(6) and (7)).
- C. The statute was recently amended to exclude from the definition of "transfer of ownership" conveyances to a grantor's spouse, or grantor's or grantor's spouse's mother, father, brother, sister, son, daughter, adopted son, adopted daughter, grandson, or granddaughter ("Family Member") for transfers of residential real property occurring on or after December 31, 2014 (MCL 211.27a(7)(t)). Proof of the relationship may be required upon request from the local assessor or the Department of Treasury.
- D. To qualify for this exclusion, the real property being conveyed must:
 - 1. Be classified as residential real property for property tax assessment purposes under MCL 211.34c. It does not have to be homestead property.
 - 2. Not be used for any commercial purpose following the conveyance.
- E. In addition to the general exclusion from the definition of transfer of ownership for conveyances of residential property to a Family Member, the legislature lists the following exceptions to the specific conveyances that are deemed transfers of ownership leading to uncapping effective as of December 31, 2014:
 - 1. Transfer of residential property to a trust where a Family Member is the sole present beneficiary (MCL 211.27a(6)(c)).
 - 2. Transfer distributing residential property from a trust where the distributee is a Family Member (MCL 211.27a(6)(d)).
 - 3. Change in the sole present beneficiaries of a trust where the substituted or added beneficiary is a Family Member (MCL 211.27a(6)(e)).
 - 4. Transfer distributing residential property to a Family Member by will or intestate succession (MCL 211.27a(6)(f)).

F. Despite the legislature's apparent goal of minimizing the monetary impact of keeping a home in the family, not all intra-family transfers are exempt from uncapping. The following intra-family transfers would cause the taxable value to uncap:

1. Life Estates. Transfer of ownership to a Family Member where the grantor retains a life estate is specifically stated to be a transfer of ownership at the time that the life estate terminates (MCL 211.27a(7)(c)). According to the State Tax Commission, the uncapping upon termination occurs even if the transfer is to a Family Member. This includes transfers by Lady Bird Deeds where the grantor retains a life estate and a power of appointment to change the beneficiary during his or her lifetime. The specific provision regarding uncapping for life estates "trumps" the general exclusion of transfers to Family Members from the definition of transfers of ownership.
2. Distribution from a Trust or Will to a Trust. Distributions from a trust or a will are included in the definition of transfer of ownership if the distributions are made to a trust, even if the beneficiary or beneficiaries of the trust are Family Members. Uncapping of the taxable value of the residential property can be avoided by a two-step conveyance: (1st) to a Family Member; and (2nd) from the Family Member into a trust. Both transfers would not cause the taxable value to be adjusted, but this process would require confidence in, and cooperation of, the Family Member.
3. Conveyance into a Limited Liability Company ("LLC"). One estate planning technique that has been used is to place property into an LLC whose membership is made up entirely of Family Members ("Family LLC"). Under the current uncapping statute, a conveyance of real property into a Family LLC or out of a Family LLC will cause the taxable value to be adjusted, without regard to whether it is residential real property being transferred for the benefit of the Family Member.

A bill has recently been introduced in the Michigan House of Representatives (House Bill 4645, 9-15-15) which, if enacted, would exempt a conveyance of residential real property if the transferor or transferee is an LLC with at least one member being a Family Member. There does not appear to be any legislative movement regarding intra-family life estate transfers or transfers into a trust for the benefit of a Family Member at this time.

**Overview of Michigan Real Estate
Ownership Options and Techniques**

Gregg A. Nathanson

OVERVIEW OF MICHIGAN REAL ESTATE OWNERSHIP OPTIONS AND TECHNIQUES

I. THE CASE STUDY: FACTUAL ASSUMPTIONS

- A. The property to be transferred ("Property") is the home currently owned by the parents ("Parents"). The parents want to transfer the home to their Son and Daughter ("Children").
- B. The Parents own the Property as tenants by the entireties.
- C. The Property is currently the Parents' principal residence for purposes of qualifying for the lower principal residence exemption ("PRE") real property tax rate.
- D. The Property has a relatively low taxable value ("TV") for purposes of determining real property taxes.
- E. The Parents purchased the Property forty years ago for \$10,000.
- F. The current fair market value of the Property is \$1,000,000.
- G. All parties want the Children to own the Property when the Parents die.
- H. The Parents want to remain in the Property for at least another three to five years.

II. OPTIONS FOR STRUCTURING THE TRANSFER

- A. Transfer to the Parents' Revocable Living Trust ("Trust").
 - 1. Overview.
 - a. Parents transfer Property to their Trust.
 - b. Parents are the settlors, initial trustees, and sole present beneficiaries of the Trust.
 - c. Children are the successor trustees and contingent beneficiaries under the Trust.
 - 2. Advantages.
 - a. Parents retain control of the Property during their lifetime and can change their mind and sell or mortgage the Property without Children's consent.
 - b. As long as they are living on the Property, the Parents would keep their principal residence exemption.
 - c. There is no reassessment (uncapping) of the taxable value either at the time of the transfer into the Trust or at the time of the

transfer out of the Trust to the Children upon the second Parent's death.

- d. Children receive a stepped-up tax basis to fair market value upon the Parents' death so, if the Children sell the Property shortly after receipt, there would be no taxable capital gain.
- e. There would be no real estate transfer taxes into or out of the Trust.
- f. The Property would not have to go through probate.

3. Disadvantages.

The Property is not excluded from the Parents' estate for estate tax purposes.

B. Joint Tenants with Full Right of Survivorship.

1. Overview.

- a. Parents transfer the Property to themselves and their Children, as joint tenants with full right of survivorship (JTWFS).
- b. Assuming the Children outlive the Parents, when the second Parent dies, the Children will hold title to the property jointly.

2. Advantages.

- a. As long as they are living on the Property, the Parents would keep their principal residence exemption.
- b. There is no reassessment (uncapping) of the taxable value either at the time of creation of JTWFS or upon either Parent's death.
- c. Children receive a stepped-up tax basis to fair market value upon the Parents' death.
- d. There would be no real estate transfer taxes.
- e. The Property would not have to go through probate.

3. Disadvantages.

- a. The Parents would not have sole control over the Property during their lifetime.
- b. The Property automatically goes to the Children on the second Parent's death and this cannot be changed without the Children's consent.

- c. The Property is not excluded from the Parents' estate for estate tax purposes.
- C. Transfer into a Family Limited Liability Company ("LLC").
 - 1. Overview.
 - a. Parents transfer the Property into an LLC in which both the Parents and the Children hold membership interests.
 - b. The Parents may be the Managers, or there may be two classes of membership interest - voting and non-voting - with Parents owning all voting interests.
 - c. The Parents' estate plan would provide for the transfer of their membership interests to their Children upon their death.
 - 2. Advantages.
 - a. The Parents could maintain control over the Property during their lifetime if they are designated such power by owning a class of voting membership interests or as managing members or managers under the LLC operating agreement.
 - b. The Property would not have to go through probate.
 - 3. Disadvantages.
 - a. The transfer into the LLC would probably uncap the Property's taxable value. Taxable Value might not uncap if Parents initially transfer the Property to Parents and Children, then Parents and Children transfer the Property into the LLC and own LLC in same percentages as they owned Property pre-transfer, and the LLC has a business purpose (the latter of which is unlikely).
 - b. When the Parents die, the taxable value could uncap again if (and at such time as) more than 50% of the membership interests in the LLC are transferred.
 - c. Note: Michigan House Bill 4645, if enacted, would exempt a transfer of residential property from uncapping taxable value when the transferor or transferee is a limited liability company, the other party to the transfer is "closely related" to at least one member of the LLC, and the property is not used for commercial purposes following the transfer. The Bill defines "closely related" as spouses and the member's or the member's spouse's mother, father, brother, sister, son, daughter, adopted son, adopted daughter, grandson or granddaughter.
 - d. Property owned by an LLC cannot qualify for a principal residence exemption.

- e. The transfer of the Property into the LLC might be subject to real estate transfer taxes unless the consideration is less than \$100.

D. Life Estate.

1. Overview.

- a. Parents transfer the Property to the Children but retain the right to live there until the time of their death.
- b. The Children's remainder interest is fully vested at the time of initial transfer.

2. Advantages

- a. The Property would not have to go through probate.
- b. The Parents could maintain their principal residence exemption.
- c. The Property's taxable value would not uncap upon initial transfer.
- d. The Property will get a stepped-up tax basis to fair market value on the date of death of the Parents.

3. Disadvantages.

- a. The taxable value will uncap at the time of the Parents' death (according to the State Tax Commission).
- b. The transfer of the Property will be subject to real estate transfer taxes upon the termination of the life estate unless the consideration is less than \$100.00.
- c. The Parents could maintain control over the Property to some extent but cannot undo the transfer to the Children.
- d. The Property is not excluded from the Parents' estate for estate tax purposes.

E. Life Estate with Power of Sale (aka Lady Bird Deed).

1. Overview.

- a. Parents transfer the Property to the Children but retain the right to live there until the time of their death.
- b. Parents retain the right to change their mind, and sell, mortgage, or alter who gets the Property upon their death.

2. Advantages.

- a. The parents retain control over the Property during their lifetime.

- b. The Property would not have to go through probate.
- c. The Parents could maintain their principal residence exemption.
- d. The Property will get a stepped-up tax basis to fair market value on the date of death of the Parents.

3. Disadvantages.

- a. The taxable value will uncap at the time of the Parents' death (according to State Tax Commission).
- b. The transfer of the Property will be subject to State transfer taxes upon the termination of the life estate unless the consideration is less than \$100.00.
- c. The Property is not excluded from the Parent's estate for estate tax purposes.

F. Life Lease.

1. Overview.

Parents transfer the Property to the Children, but have a written lease agreement giving them the right to occupy the Property for the term of their lives.

2. Advantages.

- a. The Property would not have to go through probate.
- b. The Property is excluded from the Parents' estate for estate tax purposes.
- c. The Parents could maintain their principal residence exemption.
- d. The Property's taxable value will not uncap at the time of the initial transfer to the Children or upon the death of the Parents.

3. Disadvantages.

- a. The Parents could maintain control over the Property to some extent but cannot undo the transfer to the Children.
- b. The Parents retain only the rights of tenants and must trust in the Children's ability to properly manage the asset.
- c. The transfer of the Property will be subject to State transfer taxes.

G. Transfer to a Qualified Personal Residence Trust ("QPRT").

1. Overview.

- a. Parents create the QPRT with the Children as beneficiaries.
- b. Parents retain the right to all of the income earned by the Trust, if any, and use the Property for the term rent-free ("retained income interests").
- c. If the Parents are still alive at the end of the QPRT term, title transfers out of the Parents' estate and the Children (or Trusts for the children) are the owners.
- d. If Parents outlive the QPRT term, they must execute a formal arm's length lease and pay fair market value rent to the Trust if they wish to remain on the Property.
- e. Parents are prohibited from purchasing the Property even after the term expires.
- f. If Parents die during the term, the value of the Property is included in the surviving Parent's estate, the Property reverts back to his or her estate where it can be used to pay debts, and the Parent has the ability to change the beneficiaries during his or her life ("retained reversion interest").

2. Advantages.

- a. During the QPRT term, if the Parents are living on the Property, the Parents would keep their principal residence exemption. On the conclusion of the term, when the Property transfers out of their estate, they would no longer have an ownership interest entitling them to the principal residence exemption.
- b. There is no reassessment (uncapping) of the taxable value at the time of the transfer into the QPRT. Gift tax is paid on a discounted valuation that takes into account the value of the retained income and retained reversion interests, which may be under the lifetime gift tax exemption.
- c. If Parents survive for the entire QPRT term, the Property is no longer included in their estate(s) and has been transferred at a discounted valuation. Further, if Parents enter into a lease with the new owners, any rent payments they pay moves funds out of their taxable estates with no estate tax consequences, possibly decreasing estate taxes.
- d. There would be no real estate transfer tax with the transfer of the Property into the QPRT.
- e. Since the Property is passing as a gift, the basis in the Property is the Grantor's basis (carry-over basis). If the Children inherit the Property and then sell it, they will pay capital gains tax on the difference between the sale price and Parents' basis. However, if

Parents die during the QPRT term, the Property is included in their Taxable Estate(s) and will get a stepped-up tax basis to fair market value on the date of death of the Parents.

3. Disadvantages.
 - a. Children have to pay income tax on the rent amounts received, (but that tax may be less than the estate tax they would pay if that same amount were inherited).
 - b. If the Parents die prior to expiration of the QPRT term, the entire value of the Property will be included in their estate for estate tax purposes.
 - c. The opportunity of a stepped-up tax basis is lost if the Parents survive the term of the QPRT and ownership passes to Children during a Parent's life. The Children take Parents' basis - carryover basis - because the transfer was a gift during the Parent's life.

Guidance for Preparing Gift Tax Returns (Form 709)

Kathryn Gilson Sussman

GUIDANCE FOR PREPARING GIFT TAX RETURNS (FORM 709)

I. AUTOMATIC ALLOCATION OF GST EXEMPTION

- A. The potential problem arises when there were transfers after December 31, 2000 to an Irrevocable Trust.
- B. Under IRC 2632(c), automatic allocation of Generation-Skipping Transfer Tax ("GST") Exemption applies to transfers (made after December 31, 2000) to an Irrevocable Trust ("GST Trust") that is not a direct skip but may be subject to GST tax in the future (Indirect Skip).
 - 1. GST Trust means a trust which could have a future generation skipping transfer with several exceptions, such as where the trust provides more than 25% of the principal could be distributed or withdrawn by a non-skip person before age 46 (including multiple dates before the non-skip person attains age 46), or where the trust would be included in the gross estate of a non-skip person.
 - 2. Example of GST Trust is an Irrevocable Life Insurance Trust ("ILIT") that provides for life use for children, then to grandchildren at death of child.
 - 3. Automatic allocation GST exemption occurs even if the Donor does not allocate GST on a gift tax or file a gift tax return.
- C. To avoid automatic allocation of GST exemption, Donor must opt out on a timely filed gift tax return.
- D. At the Donor's death, in order to properly assess how to allocate the Donor's remaining GST exemption, the preparer of the federal estate tax return will need to review all gift tax returns which were filed and receive complete information as to the amount and dates of all transfers to all Irrevocable Trusts.

II. ANNUAL EXCLUSION GIFTS TO IRREVOCABLE TRUSTS DO NOT NECESSARILY QUALIFY FOR ANNUAL EXCLUSION FOR GST PURPOSES

- A. Prior to March 31, 1988, a gift to an Irrevocable Trust which qualified for the annual gift tax exclusion was also exempt from GST tax.
- B. After March 31, 1988, under IRC 2642(c), a gift which qualifies for the annual gift tax exclusion is nontaxable for GST purposes only if made: (1) outright to a skip person (two or more generations below that of the transferor), or (2) to a trust with only one beneficiary who is a skip person where the assets of the Trust at the beneficiary's death will be includible in the beneficiary's gross estate.

III. CRUMMEY NOTICES

- A. In order for a transfer to the Irrevocable Trust to qualify for the annual gift tax exclusion, the trust must grant some or all of the trust beneficiaries a right of

withdrawal for a short duration (typically 30 days) over gifts made to the trust ("Crummey Power").

- B. The IRS may request copies of Crummey Notices as part of the audit of a Gift Tax Return or Federal Estate Tax Return.

IV. NEW BASIS CONSISTENCY REPORTING REQUIREMENTS

- A. Under IRC 6035, the executor of any estate required to file an estate tax return filed after July 31, 2015 (which includes a 706 filed for portability) must furnish to both the IRS and the person acquiring property included in the decedent's gross estate "a statement identifying the value of each interest in such property as reported on such return and such other information with respect to such interest as the Secretary (of Treasury) may prescribe."
- B. This statement must be furnished by the executor at such time as the IRS prescribes, but no later than the earlier of (1) 30 days after the 706 is required to be filed, (including extensions) or (2) 30 days after the 706 is filed.
- C. Recently, in Notice 2015-57, the IRS postponed the date the statement must be furnished to the IRS and beneficiary acquiring the estate property until February 29, 2016.
- D. In general, the beneficiary must use the value reported on the 706 for reporting gain or loss (or depreciation) on the beneficiary's income tax return. If the property received by the beneficiary does not increase the estate tax liability (i.e. qualifies for a marital deduction or a charitable deduction or where the gross estate is under the exclusion amount), this requirement does not apply to the beneficiary.
- E. Penalties.
 - 1. Executor: There is a \$250 penalty imposed for each failure to file this statement with the IRS (capped at \$3,000,000 per calendar year). If such failure is due to intentional disregard, the penalty is the greater of \$500 or 10% of the total amount of the items which were required to be reported to the IRS.
 - 2. Beneficiary: If the beneficiary's income tax return uses a basis in excess of the amount provided in the executor's statement to such beneficiary, there is a 20% penalty applied to the resulting tax underpayment.

V. ESTATE TAX CLOSING LETTER

- A. For federal estate tax returns (Form 706) filed after June 1, 2015, an estate tax Closing Letter will only be issued if requested.
- B. The IRS requests that the request not be made until 4 months after the Form 706 is filed.

C. To request a Closing Letter, which will be issued to the executor at the address of record, call (866) 699-4083 and provide the following information:

1. Name of Decedent;
2. Decedent's Social Security Number; and
3. Date of Death.

**Top Things Clients Must Know Regarding the
Affordable Care Act**

Lawrence F. Schiller

**TOP THINGS CLIENTS MUST KNOW REGARDING
THE AFFORDABLE CARE ACT**

I. **DETERMINATION OF APPLICABLE LARGE EMPLOYER ("ALE")**

- A. The shared responsibility obligation (also known as the employer mandate) requires an offer of group health coverage to a certain percentage of full-time employees and applies to employers with a total number of employees of 50 or more (100 or more in 2015).
- B. Employee count is based upon the average number of employees per month in the prior year.
- C. The term "Employer" includes all members of the same controlled group or affiliated service group.
- D. Number of employees includes full-time equivalents ("FTEs").
- E. All common law employees are considered when determining ALE status, no matter how many hours are worked.
 - 1. Full-time employees, including seasonal workers, during the month (full-time is an employee averaging at least 30 hours of service per week, or 130 hours in a month).
 - 2. Part-time employees (i.e., not full-time), including seasonal workers – add all hours of service during the month (not exceeding 120 per employee), and divide by 120 to determine FTEs for the month (rounded to hundredths, or 0.xx).
 - 3. Add the number of full-time employees and FTEs for each month during the year, and divide the total by 12 to determine the monthly average (rounded down to the next lowest whole number).
 - 4. For these purposes, "hours of service" are the same as for tax-qualified plans.
 - a. Including hours for which the employee is paid or entitled to payment for performing services.
 - b. Including hours for which the employee is paid or entitled to payment for not performing services (e.g., vacation, holidays, illness and jury duty).
 - c. Excluding hours as a volunteer.
 - d. Including on-call hours (use a reasonable determination, but it is not reasonable to exclude paid hours, hours spent at employer's premises, or hours where employee's activities are subject to

substantial restrictions preventing effective use of time for the employee's own purposes).

- F. Certain workers are excluded from the count, including:
 - 1. Independent contractors.
 - 2. Leased employees (as defined for pension purposes).
 - 3. Sole proprietors.
 - 4. Partners in a partnership.
 - 5. Two percent S corporation shareholders.
- G. Seasonal worker exception prevents employer from being ALE during the current year, if:
 - 1. Employer actually exceeds 50 employees for no more than 120 days (4 months) in the prior year.
 - 2. Employees who were in excess of 50 during that period were seasonal employees.

II. HEALTH REIMBURSEMENT AND SIMILAR ARRANGEMENTS

- A. What are we talking about here?
 - 1. Health reimbursement arrangements ("HRAs") include arrangements funded solely by an employer which reimburse an employee for medical care expenses incurred by the employee (or spouse, dependents, and children who have not attained age 27) up to a maximum dollar amount for a coverage period, and would therefore include so-called medical expense reimbursement plans ("MERPs") where reimbursements are excluded from the employee's income.
 - 2. Employer payment plans are arrangements where an employer reimburses an employee for substantiated individual health insurance premiums, or makes premium payments directly to the insurance company for individual health insurance policies, and the employer payments are excluded from the employee's income.
 - 3. Health flexible spending accounts ("health FSAs"), which are part of an employer sponsored Section 125 cafeteria plan, are arrangements where an employee reduces compensation on a pre-tax basis (and the employer may add additional employer funds not included in the employee's income) and is able to use the funds for medical expenses.
- B. HRAs, employer payment plans and health FSAs are all considered group health plans and therefore must meet market reforms applicable to group health plans

(such as the annual dollar limit prohibition and the preventative services requirement) or they are subject to a non-compliance excise tax of \$100 per day per individual covered by the plan (with respect to which limited transition relief has been granted for part or all of 2015).

1. An HRA cannot meet market reforms standing on its own, but can meet market reforms if it is integrated with a non-HRA group health plan under the following circumstances:
 - a. The employer offers a group health plan (other than the HRA) to the employee that does not consist solely of excepted benefits (e.g., accident-only coverage, disability income, certain limited-scope dental and vision benefits, and certain long-term care benefits).
 - b. The employee receiving the HRA is actually enrolled in a group health plan (other than the HRA) that does not consist solely of excepted benefits, regardless of whether the employer sponsors the plan (non-HRA group coverage).
 - c. The HRA is available only to employees who are enrolled in non-HRA group coverage, regardless of whether the employer sponsors the non-HRA group coverage (for example, the HRA may be offered only to employees who do not enroll in the employer's group health plan but are enrolled in other non-HRA group coverage, such as a plan maintained by the employer of the employee's spouse).
 - d. The HRA is limited to reimbursement of one or more of the following: co-payments, co-insurance, deductibles, and premiums under the non-HRA group coverage, as well as medical care (as defined under IRC 213(d)) that does not constitute essential health benefits.
 - e. Under the terms of the HRA, an employee (or former employee) is permitted to permanently opt out of and waive future reimbursements from the HRA at least annually and, upon termination of employment, either the remaining amounts in the HRA are forfeited or the employee is permitted to permanently opt out of and waive future reimbursements from the HRA.
2. Employer payment plans (employer reimbursement for or payment of individual health care premiums) cannot be integrated with another health care plan, and therefore will not meet market reforms, even though amounts expended will not be included in the employee's income.
3. Health FSAs will be treated as providing only excepted benefits, and therefore will not be subject to market reforms, under the following circumstances:

- a. If the employer also makes available group health plan coverage that is not limited to excepted benefits.
- b. If the health FSA is structured so that the maximum benefit payable to any participant cannot exceed two times the participant's salary reduction election for the health FSA for the year (or, if greater, cannot exceed \$500 plus the amount of the participant's salary reduction election).

III. THE SMALL BUSINESS HEALTH OPTIONS PROGRAM ("SHOP") MARKETPLACE

- A. The SHOP Marketplace is intended to assist small employers in obtaining lower-cost health coverage for their employees (even though they are not required to provide such coverage).
- B. The SHOP Marketplace is open to employers with 50 or fewer employees (increasing to 100 in 2016).
- C. The number of employees is determined in a different manner than for purposes of status as an ALE.
- D. To be eligible, the employer must offer coverage to all full-time employees.

IV. NON-DISCRIMINATION REQUIREMENTS

- A. Non-discrimination requirements still have not been issued, even in proposed format (except with respect to wellness programs).
- B. The requirements were to have been applicable in 2011.
- C. The requirements will prohibit discrimination in insured health plans in favor of highly-compensated employees, and will be similar to rules regarding non-discrimination in self-insured plans.

V. GUIDANCE ON AFFORDABLE CARE ACT IMPLEMENTATION

The Department of Labor / EBSA website has extensive implementation FAQs (<http://www.dol.gov/ebsa/healthreform/regulations/acaimplementationfags.html>) as well as topically-organized final and proposed regulations and other official guidance (<http://www.dol.gov/ebsa/healthreform/>).

VI. NEW RETURNS

- A. IRS Forms 1094-C and 1095-C.
 - 1. ALEs must file Form 1095-C (Employer-Provided Health Insurance Offer and Coverage) and Form 1094-C (Transmittal of Employer-Provided Health Insurance Offer and Coverage Information Returns) with the IRS annually, no later than February 28 (March 31 if filed electronically) of the year immediately following the calendar year to which the return relates.

2. ALEs are required to furnish a statement to each full-time employee that includes the same information provided to the IRS, by January 31 of the calendar year following the calendar year for which the information relates.
3. An ALE member can provide the required statement to the employer's full-time employees by furnishing a copy of the Form 1095-C filed with the IRS. Alternatively, these returns and employee statements may be provided by using substitute forms. A substitute form must include all of the information required to be reported on Forms 1094-C and 1095-C, and must comply with applicable revenue procedures or other published guidance relating to substitute returns.
4. Transition relief provides that employers do not have to file information returns with the IRS and furnish statements to their full-time employees until 2016 for the 2015 year. Thus, under this transition relief, the first statements to employees must be furnished by January 31, 2016, and the first information returns to the IRS must be filed by February 28, 2016 (March 31, 2016, if filed electronically).

B. IRS Form 720.

1. A patient-centered outcomes research fee is imposed on issuers of specified health insurance policies and plan sponsors of applicable self-insured health plans for policy and plan years ending on or after October 1, 2012.
2. The fee is currently \$2.08 per covered individual.

Helping Clients Follow Needed Business Formalities

Gary Schwarcz

HELPING CLIENTS FOLLOW NEEDED BUSINESS FORMALITIES

I. PURPOSE OF FORMALITIES

- A. When a corporation is established and maintained properly, a corporation is treated under the law as an independent entity, with many of the rights afforded individuals. (Note that many of the comments provided below also apply to partnerships and limited liability companies.)
 - 1. As a separate and distinct entity from its shareholders, only a corporation's assets can be seized to pay judgments or satisfy other debts owed by the Corporation if corporate formalities are followed.
 - 2. The advantages also include the possibility of perpetual business existence and the potential for special tax treatment under the Internal Revenue Code.
 - 3. Incorporating a business is only the first step in protecting your client's assets from creditors.
- B. Failure to comply with corporate formalities could result in unintended consequences such as shareholders having personal liability, or adverse income tax consequences.
 - 1. Failure of the corporation to hold meetings, adopt resolutions, maintain minutes, comingling corporate assets with personal assets, or failing to sign documents in the appropriate corporate form, could void the benefits and protections associated with a corporate entity.
 - 2. Small family run businesses often disregard corporate formalities as being unnecessary administrative work.
 - 3. Even in the closely held family corporation, the shareholders and members of the board of directors should hold regular meetings.
- C. Corporate formalities are the basic rules and formalities of governing the operation of a corporation.
 - 1. A corporation should keep records of its corporate activities, generally through corporate minutes.
 - 2. In addition to keeping corporate minutes, shareholders and members of the board should have regular meetings, maintain books, issue stock, and adopt corporate bylaws.

II. CORPORATE MINUTES

- A. Reasons for documenting a corporation's actions include:
 - 1. Following corporate formalities creates defenses against law suits attempting to establish personal liability of directors or officers for exercising business judgments and specific authorizations.

2. Following corporate formalities can establish authority for corporate actions for the benefit of outside parties.
 3. Documentation of transactions between shareholders and a corporation helps protect the shareholders from liability to third parties by maintaining the limited liability shield.
 4. Documentation can protect the owners from claims of minority oppression or breaches of fiduciary obligations by explaining the business reasons for corporate decisions.
 5. Documentation protects managers, directors and officers from liability to the shareholders by demonstrating how their duties have been discharged.
 6. Documentation protects directors and officers from liability to third parties by demonstrating how the business judgment rules have been satisfied.
 7. Documentation can communicate actions and the rationale to employees and other personnel who are not shareholders.
 8. Landlords and banks often demand documentation of corporate approval as a condition into entering into certain business transactions.
 9. Documentation provides a useful record that avoids misunderstandings.
 10. Documentation can provide evidence of certain elements of desired tax treatments, such as providing the reasoning behind "reasonable compensation" to support its deduction.
 11. Documentation can provide evidence that certain transactions involving a conflict of interest have been properly discussed and approved.
 12. Documentation can provide important evidence bearing on employment relations, such as reasons for employee discipline or discharge.
- B. Documentation of corporate minutes will:
1. Substantiate limited liability for corporate debt obligations.
 2. Document and substantiate income and loss positions in the event of an Internal Revenue Service audit.
 3. Document authorization of contracts and obligations executed by the Corporation.
- C. Where possible, minutes should include the following:
1. Election of the directors and officers.
 2. Statement of corporate policies and procedures.

3. Declaration of dividends or distributions.
 4. Authorization of contracts.
 5. Compensation of officers and key employees.
 6. Changes in tax status.
 7. Adoption, changes in, and contributions to employee benefit plans.
 8. Capital transactions.
 9. Loan and guarantee transactions.
 10. Authorization of employee contracts.
 11. Acquisition of property.
 12. Designation of banks.
 13. Engagement of lawyers, accountants and other professionals.
 14. Approval of mergers.
 15. Issuance of shares.
 16. Authorization to sign checks, deposit funds and make withdrawals.
 17. Approval of financial statements and audit reports.
- D. Will the failure to keep corporate minutes in and of itself result in piercing the corporate veil? Typically the answer is no, but it is one of the factors that the Internal Revenue Service or a court would consider when deciding whether to pierce the corporate veil.

III. OTHER CORPORATE FORMALITIES

- A. To insure that a corporation's status as a distinct entity remains viable, the corporation must act like a separate and distinct entity and the shareholders must treat it as such. Otherwise, a court or the Internal Revenue Service may find the corporation is merely an alter ego of the individual owners. The following corporate formalities should always be followed:
1. The corporation's financial and corporate records should be documented.
 2. The corporation and shareholders must treat themselves as separate entities and thus the corporation must have its own bank account, which should not be used for personal expenditures.
 3. The corporation must be fully capitalized. Even a single shareholder corporation must be appropriately capitalized.

4. The corporation should pay dividends, if appropriate.
 5. Failure to properly document a loan made by a shareholder to the corporation could result in the Internal Revenue Service or a court re-characterizing the loan as a capital contribution. If the corporation borrows money from a shareholder, have the corporation sign a promissory note with a stated due date and interest rate.
 6. Corporations should maintain insurance coverage with adequate limits for their type of business. For most corporations, this will mean carrying:
 - a. General liability insurance.
 - b. Auto insurance.
 - c. Workers compensation insurance.
 - d. Product liability insurance.
 7. The corporation should submit all State of Michigan required annual filings.
 8. Every signature on behalf of the corporation should include the corporation's name, the officer's signature and words showing that the officer is signing on behalf of the corporation.
 9. Document any transactions between the corporation and any of the shareholders.
 10. If the corporation is going to own equipment previously owned by a shareholder, make a list and sign a bill of sale that transfers the title to the corporation.
 11. If the corporation leases a building from a shareholder, there should be an executed lease.
 12. If the corporation has more than one shareholder, the shareholders should have a written agreement restricting share transfers and addressing buyouts on a shareholder's death and for other triggering events.
- B. When owners of a closely held corporation make a loan to a corporation or borrow from the corporation, the transaction must be properly documented.
1. If the loan is not properly documented, it may be deemed to be a constructive dividend.
 2. If a shareholder makes a loan to the corporation which is not properly documented, the loan may be deemed to be a capital contribution.

IV. PIERCING THE CORPORATE VEIL

- A. Once corporate formalities are not strictly observed, whoever is suing the corporation can "pierce the corporate veil" and, if successful, the protection available to shareholders for corporate liabilities will no longer exist.
1. Creditors will try to attach individual liability for debts to shareholders.
 2. Courts can impose liability on individuals for actions of the corporation if the corporation is not run as a distinct entity from its shareholders.
 3. If corporate formalities are not followed, then the Internal Revenue Service on audit may deny corporate specific tax deductions.
 4. Courts often look at the following factors in determining whether it is appropriate to pierce the corporate veil:
 - a. Whether the corporation failed to follow corporate formalities, such as having by-laws and minutes of shareholder and board of director meetings.
 - b. The absence of corporate records.
 - c. Whether the shareholders are syphoning money from the corporation for personal use.
 - d. Whether there are officers and directors with no corporate function.
 - e. Comingling of funds and other assets between major shareholders and the corporation.
 - (1) This means that corporate income should be deposited into corporate bank accounts, not in the shareholders' bank accounts.
 - (2) Similarly, personal income should be deposited and personal expenses must be paid from personal accounts.
 - f. Inadequate capitalization.
 - g. No corporate assets.
 - h. Whether the corporation has entered into contracts with no intent to make good on the obligations.
 - i. Failure to issue stock.
 - j. Failure to observe corporate formalities.
 - k. Non-payment of dividends.

- I. Insolvency.
 - m. Non-functioning of officers or directors.
 - n. Diversion of assets from the corporation by a shareholder.
 - o. Failure to maintain arms-length relationships among related entities.
 - p. Whether in fact the corporation is a mere façade for the operation of the majority owner.
- B. To minimize the risk of the Internal Revenue Service piercing the corporate veil, minutes should be kept documenting board of directors' and shareholders' decisions.
 - 1. The corporate minutes are the first line of defense against the Internal Revenue Service should an audit take place.
 - 2. If a corporation is audited by the Internal Revenue Service, the Internal Revenue Service agent will demand the original minute book as part of the audit.
 - 3. Keeping regular corporate minutes may:
 - a. Prevent the Internal Revenue Service from claiming the shareholders or executives are receiving unreasonable compensation.
 - b. Protect against Internal Revenue Service claims of excess accumulating earnings.
 - 4. The corporation and its shareholders may suffer adverse tax consequences if the corporation's income and expenses are re-characterized by the Internal Revenue Service as personal income and expenses, including:
 - a. Loss of deductions.
 - b. Imposition of interest.
 - c. Penalties.
- C. Many shareholders of closely held corporations intermingle their own assets into their corporations.
 - 1. The line between what is owned by the corporation or what is personally owned often becomes blurred.
 - 2. If a shareholder borrows equipment from the corporation, the use of the equipment should be properly documented and recorded in the corporate minutes.

V. MICHIGAN BUSINESS CORPORATIONS ACT

- A. According to the Michigan Business Corporations Act, a corporation must keep:
 - 1. Books and records of account.
 - 2. Minutes of the proceedings of its shareholders, board, and executive committee, if any.
- B. The Michigan Business Corporations Act requires the shareholders to hold an annual meeting.
- C. The Michigan Business Corporations Act does not require any specific meetings of directors.
- D. The good standing of the corporation will be suspended if the Michigan annual report is not filed for a two-year period.