

Legal Advisory

IDEAS AND STRATEGIES FOR YOU AND YOUR BUSINESS / FIRST QUARTER 2008

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Where Do Debtors Stand Now?

“If you don't _____, I'll sue you!” Have you ever uttered this sort of statement (fill in the blank for the appropriate action)? You probably have, although there is considerably more to initiating a lawsuit than making a thinly veiled threat.

To determine if you have a valid cause of action, it is helpful to break down the lawsuit into basic legal elements. For instance, if you are dissatisfied with the installation of a deck or patio, a lawsuit against the contractor may be based on the following four elements:

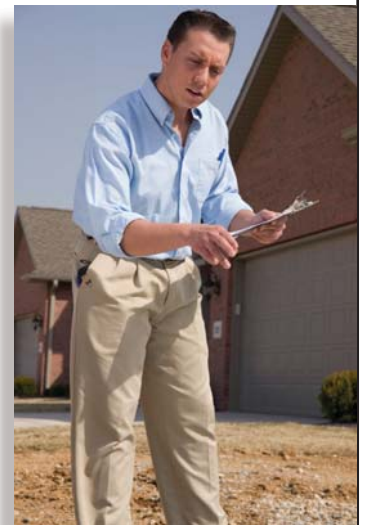
1. Formation of contract: This shows that there is a legally binding contract to perform the work. Naturally, it is advisable to obtain contracts in writing. Otherwise, you will have to prove the existence of an enforceable oral contract.

2. Performance: You must demonstrate that you have held up your end of the bargain. For example, if you were required to make a series of payments while the work was being performed, canceled checks can serve as proof of payment.

3. Breach: A breach occurs when the other party fails to meet the terms and conditions of the contract. This is usually the crux of the matter. In our example, you would have to prove that the contractor failed to provide satisfactory workmanship in a timely fashion (or failed to provide any services at all).

4. Damages: This is the amount of the economic loss suffered as a result of the contract breach. Assuming that the work will be assigned to another contractor, this should be a relatively simple matter for this type of breach.

Even if your case looks solid, you might pursue several alternatives to a trial. For starters, you may be able to work out a compromise with the contractor that both sides can live with. Alternatively, you might hire a third-party mediator to resolve any differences you cannot iron out. Finally, you may be able to submit the case to binding arbitration (depending on the conditions set forth in the contract).



(see *Go to Court* on next page)

COPING WITH ESTATE-TAX CHANGES

The old axiom is that the only two things certain in life are death and taxes. But now there is a great deal of uncertainty concerning the imposition of the federal estate-tax laws.

Background: Under the monumental Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA), several sweeping changes in the federal tax law will culminate with the outright repeal of the estate tax after 2009. However, unless Congress enacts subsequent legislation in this area, the federal estate tax will be revived in 2011 under pre-EGTRRA levels.

To further complicate this matter, various proposals to revise or permanently repeal the federal estate-tax law have been debated in Congress.

At this time, the most practical approach is to play it safe. Assume that the current law will remain in place and estate tax—in some form or another—will continue to exist for the foreseeable future.

Keeping that in mind, the following is a brief summary of the main changes under EGTRRA.

- ◆ The estate-tax exemption, available through the unified estate- and gift-tax credit, is gradually increasing. For decedents dying in 2008, it can shelter up to \$2 million from estate tax. This credit shelter will top out at \$3.5 million for 2009 before the estate tax is completely repealed in 2010. Meanwhile, the top estate-tax rate drops to 45% for 2008 and 2009.

- ◆ Unlike the estate-tax exemption, the gift-tax exemption stays locked at \$1 million for 2008 and thereafter. Furthermore, the gift tax remains in effect after 2009. As with the estate-tax rates, the top gift-tax rate will be 45% for 2008 and 2009. After 2009, the gift-tax rate will be equal to the top individual income tax rate, which is currently set at 35%.

- ◆ In 2010, heirs will no longer benefit from a “step-up” in basis to the value of assets received at death. Instead, they must carry over the decedent’s basis. However, there are two key exceptions to this rule: (1) the basis for qualified assets can be increased by a step-up of \$1.3 million and (2) the basis for assets transferred to a spouse can be increased by an additional step-up of \$3 million.

- ◆ The generation-skipping tax (GST), which applies to certain transfers to grandchildren, is scheduled for the same repeal and revival as the estate tax. Lifetime transfers are eligible for a generous \$2 million exemption in 2008, rising to \$3.5 million in 2009. The top GST rate is reduced to coincide with the reduction in the estate-tax rates.

In light of these changes and their impending “sunset,” certain estate-planning techniques such as charitable remainder unitrusts (CRUTs) and Qualified Terminable Interest Property (QTIP) trusts may be considered. You may want to incorporate a CRUT or QTIP trust into your overall estate plan.

Your situation should be evaluated based on your personal circumstances. Consult with an estate-planning adviser. 📌

SHOULD YOU GO TO COURT?

(continued from front page)

What can you do if the opposing party does not pay up? You may identify property—such as real estate or investments—that is owned by your opponent. Then local law enforcement officials may be instructed to attach the property or, in certain situations, garnish that person’s wages.

Other complications may arise. Naturally, you should rely on your attorney to provide assistance in this area. 📌



When You Are on Thin Legal Ice

Let's say you attend a hockey game at the local arena. As you settle back in your seat, you are struck by a puck shot into the stands. So it is you—not one of the players—who is carted off on a stretcher.

Once you get back on your feet, you want to know whether you can sue someone—the team or the player who shot the puck—for the injuries you have suffered.

Caution: This type of lawsuit is not likely to succeed. It all has to do with a legal principle known as "assumption of risk." Briefly stated, the principle means that you knowingly took the risk that you could be injured in this manner when you acquired your tickets to the game. By your assumption of risk, the team, owners and players are relieved of liability for your injury.

Of course, applicable state and local laws may be the controlling factors in any particular case.



AFTER THE FIRING: LEGAL RIGHTS SURVIVE

It's not enough to know when it is legally acceptable to fire an employee. Business managers must also be aware of the rules concerning employees after employment has been terminated. Similarly, employees should know that leaving a job does not necessarily mean leaving their legal rights behind. Here are some of the main considerations relating to a termination of employment.

Health coverage: This is often a critical issue for employees who lose their jobs. Under the oft-cited Consolidated Omnibus Budget Reconciliation Act (known as COBRA), a company with 20 or more employees must provide terminated full-time employees with the right to continue group medical coverage. The employee is generally required to pay the full cost of the coverage (plus a 2% administrative fee that may be added).

An employer must also meet certain notification rights under COBRA. For instance, an election notice must be sent to an employee when his or her employment is terminated for any reason and medical coverage is about to be discontinued.

Vacation pay: As a general rule, employees accrue vacation days during the year and draw from that "bank" when they actually take vacation. When an employee leaves, the value of vacation time that has accrued, but has not yet been used, must be paid. The


accrual method is determined by the employer, but it is legally binding.

Sick pay: If your company accrues sick leave as well as vacation pay, an employee will be entitled to be compensated for unused sick days upon termination.

Severance pay: Severance pay is legally obligated to be paid only in the case of layoffs. The right to receive severance pay depends on company policy in addition to any prevailing employment or union contracts.

401(k) plan rollovers: Following termination of employment, an employee is no longer permitted to contribute to the employer's 401(k) plan. However, an employee can roll the funds over tax-free to another qualified retirement plan or a traditional IRA (within certain restrictions). Alternatively, the employee may choose to take a lump-sum distribution or leave the funds in the account (if the plan permits this).

Job search assistance: Again, in the case of an involuntary termination, many companies provide professional assistance in finding new employment. This is a function of policies included under the company employment manual or union contract.

Practical approach: If you are an employer, take precautions to meet all the legal requirements in this area. If you are an employee, make sure you understand your rights upon termination. 



NEW LANDSCAPE FOR BANKRUPTCY CASES

Now that the dust has settled over the highly publicized bankruptcy law enacted in 2005—the Bankruptcy Abuse Prevention and Consumer Protection Act—where do debtors stand? It depends on their situation.

The new rules prohibit certain debtors from filing under Chapter 7 debt elimination. Instead, they must repay at least part of their debt under a Chapter 13 repayment plan. Also, all debtors are required to participate in credit counseling before they file for bankruptcy.

Here are the key changes in the bankruptcy law.

Chapter 7 eligibility: Previously, any debtor could choose Chapter 7 over Chapter 13. Under the new rules, you must measure your current monthly income against the median income for a household

of your size in your state. If your income does not exceed this median threshold, you are able to file under Chapter 7. On the other hand, if you exceed the limit, you must meet a “means test” to qualify for a Chapter 7 filing.

Credit counseling: Before you can file for bankruptcy under

either Chapter 7 or Chapter 13, you must submit to credit counseling with a U.S. government-approved agency. Counseling is required even if it is apparent that a repayment plan will not meet your needs. **Caveat:** This does not necessarily mean you have to agree to any specific arrangement. However, if a repayment plan is proposed, it must be filed with the bankruptcy court.

At the close of the bankruptcy case, another counseling session will be scheduled to address personal financial management. You must submit proof to the court that you attended the session before your debts can be discharged.

Chapter 13 requirements: In the past, Chapter 13 filers had to devote all of their “disposable income” (i.e., the amount left after paying actual living expenses) to the repayment plan. Under the latest rules, you still must forfeit disposable income, but the calculation is generally less favorable if your income is higher than the median for your state.

Miscellaneous changes: The bankruptcy law includes numerous other changes, including the methodology for valuing property and the length of time a filer must live in a state to use that state’s exemption laws.

To analyze how the new bankruptcy rules apply in a particular situation, consult with legal counsel. 📧

B R I E F S

◆◆**Employment Contracts**—A recent case points out the need for forfeiture clauses in contracts. **Facts:** A chief operating officer (COO) signed a multiyear contract with his company. Then, three female employees accused him of sexual harassment. After an investigation, the company fired the COO and refused to pay him for the remaining years. **Result:** The Third Circuit Court sided with the COO because the contract did not include any exceptions.

◆◆**Taking on the IRS**—An individual in a new case convinced the Tax Court that certain income the IRS claimed should have been taxable actually constituted loans and gifts from family members. But the Court also determined that it was reasonable for the IRS to maintain its position under the circumstances. Thus, the taxpayer could not recover his court costs and attorney fees—even though he prevailed on the main issue.

◆◆**Better Late than Never**—Is punctuality always essential? It depends. In a new case, a paraplegic who used a wheelchair was sometimes late due to disability related reasons. Otherwise, he was an exemplary employee. After a new tardiness policy was adopted, the company fired him. **Result:** The Eleventh Circuit Court said that reasonable accommodations should be determined on a case-by-case basis.

◆◆**Look-back Period**—A common estate planning technique is to try to reduce an elderly person’s assets to qualify for Medicaid assistance. But gifts made by that person still count as assets he or she owns under the “look-back rule.” Previously, the look-back period for most transfers was 36 months. Under the Deficit Reduction Act of 2005, the look-back period has been increased to 60 months. 📧