MJM LAW, LLC

FALL 2011 NEWSLETTER

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Dear Valued Clients:

Here is a summary of recent cases and developments I found either especially helpful or especially interesting. I hope you agree. Please call, send me an email message, or write me the old-fashioned way with any questions or concerns you have. Mike.

COLLABORATIVE LAW

Collaborative law is different from traditional law in that it (collaborative law) is based upon and relies upon the disputing parties choosing to avoid litigation and committing to that end. It was begun in Minnesota in the late 1980s by a family law attorney who wanted a better way to resolve divorce and child custody cases while minimizing emotional damage to the parties and their families. [1] It is now practiced nationally by thousands of attorneys for many different types of disputes.

In addition to the collaborative law attorneys of the parties, other professionals are typically used

1 I was one of the original members of the fledgling organization but my law practice then was primarily litigation of one type or another and not well-suited to collaborative law. I recently became active in the organization again and advocate its use in all areas of law.

as needed, e.g., a facilitator (usually a trained counselor), an appraiser, and an accountant, with an emphasis being upon the parties agreeing upon those allied professionals in order to keep costs down. The parties then engage in discussions and negotiations designed to determine and honor their respective interests and, yes, feelings..

Although that may sound too "touchy-feely" to some, in practice it is not just a significantly less expensive method of resolving conflict but is rated by clients as being much more satisfying than the historical model of "I lose if you win" confrontation because their interests have not only been *understood* but have also been *incorporated* into the case resolution.

SBA LOANS CAN HELP FINANCE SMALL BUSINESSES

It is no secret that businesses generally, and small businesses in particular, have been through rough times with no strong end in sight. Still, for small business owners there is some good help to be had if you know where to look. One prominent example is the Small Business Administration (SBA) and its Guaranteed Loan Programs.

Contrary to a common misconception, the SBA does not make direct loans to small businesses. Instead, the SBA establishes guidelines for loans, which are then made by its "partners," meaning lenders, community development organizations, and micro-lending institutions. To eliminate some of the risk to its lending partners, the SBA guarantees that these loans will be repaid. In short, a business applicant is actually applying for a commercial loan, *guaranteed by the SBA*, and which is structured according to SBA requirements.

Be aware, though, that SBA-guaranteed loans may not be made to a small business if the borrower has access to other financing on reasonable terms. Because SBA loan guaranty requirements and practices can be changed by the government, it is important for potential applicants to obtain current and accurate information. Here is a short primer on some loans offered by the SBA:

The 7(a) Loan Program

This program, the most basic and most used of the SBA loan programs, is for borrowers who want to start, acquire, or expand a small business. The loan is obtained from a participating lender institution, and it provides long-term, fixed-rate financing for major assets, e.g., land and buildings. The loan proceeds can also be used to acquire equipment, supplies, and materials, or for either long-term or short-term capital needs. Loan terms range from up to 10 years for working capital to up to 25 years for fixed assets. There are a few prohibited purposes for which a 7(a) loan cannot be used, such as for the financing of nonprofits, real estate investments, and monopolistic enterprises.

The CDC/504 Loan Program

The CDC/504 Loan Program is a long-term financing tool designed to encourage economic development within a community. It accomplishes this goal by providing small businesses with long-term, fixed-rate financing to acquire major fixed assets for expansion or modernization.

A Certified Development Company (CDC) is a private, nonprofit corporation that is created to contribute to economic development within its community. CDCs work with the SBA and private sector lenders to provide financing to small businesses.

Typically, a project of this kind includes: (1) A loan secured from a private sector lender, with a senior lien covering up to 50% of the project cost; (2) a loan secured from a CDC (backed by a 100% SBA-guaranteed debenture), with a junior lien covering up to 40% of the project cost; and (3) a contribution from the borrower of at least 10% of the project cost (equity). This arrangement means that 100% of the project cost is covered by contributions of senior and junior lenders, and the borrower itself.

Proceeds from 504 loans must be used for fixed-asset projects, such as the purchase of land, including existing buildings; the purchase of improvements, including grading, street improvements, utilities, parking lots, and landscaping; the construction of new facilities or the modernizing, renovating, or converting of existing facilities; and the purchase of long-term capital assets like machinery and equipment. The CDC/504 Loan Program cannot be used for working capital or inventory, consolidating or repaying debt, or refinancing.

The Microloan Program

The Microloan Program gives small, short-term loans to small business concerns and to certain types of not-for-profit child-care centers. The SBA makes funds available to specially designated intermediary lenders. These are nonprofit community-based organizations with experience in lending as well as in management and technical assistance. These intermediaries make the loans to eligible borrowers. The maximum loan amount is $50,000.00, but the average microloan is just under $15,000.00.

Microloans may be used for working capital, the purchase of inventory or supplies, the purchase of furniture or fixtures, or the purchase of machinery or equipment. Microloan proceeds cannot be used, however, to pay existing debts or to purchase real estate.

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If you are considering applying for an SBA loan, the agency recommends four steps to "get the ball rolling" in its loan programs. First, estimate your business startup costs or the funds that you need to grow the business. Second, contact a local bank or lender to review the available loan programs for small businesses. Third, prepare a draft loan proposal (which will certainly include preparation of a well-reasoned business plan). Finally, discuss all of the above points with someone having solid knowledge of SBA loans, such as a representative of the SBA itself.

CHALK ONE UP FOR THE LITTLE GUY

Nate Thoma is not an attorney. He is and was a soft-spoken, small investor in stocks. Among his investments was Washington Mutual, the big bank that was seized by the federal government in 2008 and ended up in bankruptcy. Just as with so many other Washington Mutual investors, Nate's stake in the bank was wiped out by its failure. But unlike the other investors Nate wasn't willing to accept the *status quo* of a liquidation of the bank just to stand in line to receive pennies on the dollar. So, on behalf of himself and others like him he challenged the bankruptcy filing itself. His big moment came when he was allowed to present his findings and argument to the federal bankruptcy judge.

Nate had spent countless hours investigating Washington Mutual's history and improper conduct of its officers leading up to its bankruptcy filing. At great length and with 33 pages of supporting documents he described this history to the judge. The result? An investigation into the trading actions of some of the very largest "hedge funds" in our country and in the denial of Washington Mutual's proposed bankruptcy plan.

What had Nate learned and presented to the bankruptcy judge? That these large hedge funds were buying up the bank's "trust preferred securities" and its bonds. Because the "trust preferred securities" are paid first in a bankruptcy filing and because ownership of the bank's bonds allowed the hedge funds a dominant voice in the bankruptcy process, small investors like Nate and the others he represented would receive very little--if anything--in the bankruptcy and the hedge funds would receive everything.

Nate's dedication and tenacity resulted in a very favorable settlement between small investors like him and the hedge funds and paved the way for the bank's ultimate successful exit from bankruptcy.

ESTATE PLANNING WITH ILITS

For some people, life insurance may not seem an effective estate planning tool. For example, a life insurance policy remaining in the estate of the insured is subject to federal estate taxes. That outcome can be avoided, though, through use of an Irrevocable Life Insurance Trust (ILIT).

Here is how an ILIT works: At the core of the trust is the life insurance policy itself. The "grantor" of the trust arranges funding of the trust from his or her assets, e.g., annual gifts to the trust to pay the premiums on the policy and to cover administrative costs.

Because the legal owner of the life insurance policy is the trust and not the grantor, the life insurance policy is not considered to be part the grantor's estate. (However, the insured cannot receive any personal financial benefit from the ILIT.) Another plus arising from ownership of the policy by the trust is that the funds are protected from any claims which may be made against the beneficiaries by their creditors.

As with any trust, an ILIT must have a designated trustee to manage and administer it. Typically, the trustee is a bank or a trust company but need not be, and the grantor himself/herself may serve as trustee. The trustee establishes a bank account into which the gifts will be deposited for use in paying the premiums. The trustee is also responsible for a variety of administrative duties, including giving notifications to the beneficiaries under the policy as well as filing the ILIT's tax return, and—if the trustee is not the grantor—upon the death of the grantor, overseeing distribution of the policy's proceeds according to the grantor's wishes as expressed in the trust. This distribution can be all at once or spread out over time, as prescribed by the grantor.

One of the most appealing features of an ILIT is that it can be closely tailored to fit the wishes of the grantor regarding the conditions and circumstances for paying out the proceeds of the ILIT. For example, if the grantor is in a second marriage, part of the ILIT proceeds could go to any children from the first marriage and a part to children of a second marriage.

It is also possible for the grantor to condition receipt of proceeds to a beneficiary upon the beneficiary performing certain prescribed acts or achieving certain prescribed goals. On the more negative side, misconduct by a beneficiary could be used as an effective disqualification.

Bear in mind that an ILIT must comply with certain government rules and regulations if it is to achieve the desired results. Thus, aside from the potential complexities of the instrument itself, the assistance of a professional is a must in navigating the government's requirements for an effective ILIT.

DON'T LOSE YOUR CHARITABLE DEDUCTION

To claim a federal income tax deduction for a charitable donation valued at $250.00 or more, you must obtain from the recipient of the donation a "contemporaneous written acknowledgment" letter or equivalent. Failure to obtain such a letter can result in disallowance of the deduction by the IRS.

The acknowledgment letter, which may be in the form of a "thank you" letter or a formal receipt, must include the following information:

- the name and address of the recipient of the donation;
- the amount of a cash gift or, if not in cash, a description of the donation sufficient to identify the nature of the gift; and, if applicable,
- a statement that no goods or services were provided by the recipient in return for the donation, or a description and good-faith estimate of the value of any goods and services that were provided by the recipient in return for the donation.

As some donor taxpayers have discovered to their consternation, the timing of the receipt of the letter can be as important as its contents: You must obtain the acknowledgment letter by the date of the filing of the tax return for the year in which the charitable contribution was made. If you do not and you are audited, the declared deduction will be disallowed. (Even though the Internal (or as Samuel Clemens said, the *Infernal*) Revenue Service Code expressly states that the donor is not required to obtain an acknowledgment letter if the charitable organization itself files a valid return with required information, you cannot rely upon that provision in an audit because there are yet no “regulations” implementing that provision.)

FINANCIALLY SPEAKING, KEEP IT SIMPLE

In theory, we are all in favor of saving time, labor, and space, not to mention avoiding the stress and anxiety that can come from leading complicated and disorganized lives. In the realm of personal finance, these are excellent reasons to make our lives simpler and more organized. Unfortunately, for most of us, saying and doing are two very different things. Below are some simple, individual steps that may help move the "simplify and organize" process along. A few minutes taking these, or similar steps now, might save hours and many dollars later on.

Direct Deposit

You may be one of those people who likes to have the check in hand for pay, pension, or Social Security benefits so that you can personally deposit it. Still, arranging for a direct deposit into a bank account is safer, easier, and more convenient, and actually allows access to your money more quickly.

Recurring Bills

If your merchant or vendor (such as a utility or insurance company) allows the practice, you can pay recurring bills by automatic withdrawal from your checking account or with a charge to a credit card. In the case of the former, don't forget to record the transaction in your check register. In the same vein are online banking services that allow you to pay bills online instead of by "snail mail."

Online Banking

Aside from bill paying, consider doing virtually all of your banking online, making it effectively paperless. You can go online to handle such tasks as reviewing deposits and withdrawals, tracking balances in your accounts, transferring funds between accounts, and receiving statements. (Of course, if your or your bank's internet service or computer "crashes" you will not be able to review accounts either at the institution or from your home or office. Alas, that is a result of our computer-dependent lives.)

Some FDIC-insured online banks *offering interest* on their checking accounts are Avidia Bank eChecking, Heritage Bank NA eCentive, and Bank of Internet USA Rewards Checking.

Automatic Savings

It is a simple truth that if you establish a system in which something occurs automatically rather than only when you remember it, the "something" is going to occur with greater consistency. So it is with saving for the future. If you can, try to establish with your employer or bank a predetermined amount of money that will automatically be deposited into an account or an investment vehicle on a regular schedule. A bonus for this approach as an investment strategy is that, over the long run, it may provide better returns than jumping in and out of investment markets.

Consolidation

You might want to streamline your finances by consolidating accounts and credit cards. By doing so, you should be able to more easily monitor all of the accounts and cards, lighten your paperwork load, avoid some fees, and perhaps even obtain better deals. If you are combining deposits at one banking institution, though, be careful not to exceed FDIC deposit insurance limits ($250,000.00 for each ownership category in a single institution).

Estate Planning

Even if you have been diligent and already have a Will, review it periodically to make sure it still conforms to your wishes, especially if there have been any intervening major events that might prompt a change. The same goes for other important financial documents, e.g., the beneficiaries and disposition directions for your life insurance policies and retirement accounts.

Document Protection and Location

All of the suggested steps and precautions described above may not matter if your important documents cannot be found if you suddenly die or become unable to communicate for any reason. Therefore, resolve to keep those important documents in a secure place with a comprehensible filing system *and make sure to let your family members know where that secure place is.*

As a reasonable additional precaution, try to have *duplicates* of all of your important documents in a secure location *different from* the location of the original documents. This could be done, for example, by having important information (insurance policy numbers, financial institutions account numbers, etc.) and scanned copies of important documents on a secure website that you could access from any location.

EMPLOYEES WIN BENEFIT PROTECTIONS

A major health services company with thousands of employees overhauled its pension plan a few years ago. The company explained to employees that the then-existing benefits would be converted into a virtual “lump sum”, which would constitute the opening account balance for the new plan. That opening balance would then grow by a percentage of the employee’s pay each year. It all sounded safe and reasonable to the employees.

What was not explained to the employees and what eventually led a class of employees to sue their employer under the federal Employee Retirement Income Security Act (ERISA), was that the beginning balance for many employees with long tenures at the company would be as little as 50% to 70% of the amounts built up under the old pension plan. Using that calculation method, the pension balances for such employees would take years simply to reach the levels of the old plan.

The now illegal practice of that health services employer is known as “wear-away.” The employer’s creation of “underwater” beginning balances effectively tells employees (if the employees ever become aware of it) that prior pensions were overpaid and that before they can receive compensation under a new pension plan they must work off a debt, or “wear it away.” (In essence, this is the modern day equivalent to the “company store” of the first half of the 20th century, in which employees had no place to purchase necessities or to live except in company-provided facilities, which required more money than the employees were paid.)

The health services company employees’ case ultimately reached the U.S. Supreme Court, where the employees achieved a resounding and precedent-setting victory when a majority of the Justices agreed with them that if the company had deliberately provided misleading and incomplete information to its employees in violation of ERISA, a monetary award was appropriate.

SHORT TAKES

New Tax Break for Married Couples

A 2010 tax law providing "portability" of a deceased spouse's unused $5 Million gifting allowance to the surviving spouse became effective January 1 of this year. An often-overlooked provision of the law requires filing of an estate tax return within nine months (with a six-month extension allowed) of the death of the deceased spouse, *whether or not estate tax is owed.* If that filing date is missed, so is the "portability" opportunity. If you believe this law may affect you now or before December 31, 2012, seek professional advice immediately.

Cell Phones as a Fringe Benefit

Under an IRS "guidance" interpreting 2010 legislation (the Small Business Jobs Act of 2010) you will not be considered to be receiving a taxable fringe benefit if your employer provides you a cell phone for "non-compensatory business reasons" *even if you use it for both personal and business purposes.* However, there are some requirements for compliance, which (by IRS example) include: 1. Being able to be contacted at all times for work-related emergencies; 2. Being able to speak with clients at times when you are away from your office; and 3. Being willing to speak to clients in other time zones at times outside your "normal" work day. (Recordkeeping of business use will not be required for this tax-free treatment.)

Rock and Roll Authors May Receive Unexpected Royalties

In recent legal decisions in both Europe and the United States authors of songs may soon begin receiving royalties and compensation for their songs that were previously unavailable. In Europe, the EU Council voted to extend the copyright on sound recordings from 50 to 70 years (especially good news for the Beatles, Rolling Stones, and The Who) and in the United States authors of songs are now just beginning to exercise a little-known right under our own Copyright Act to "terminate" a copyright grant given to others if notice of the termination is provided to the existing copyright owner 35 years after first publishing of a song so long as notice is given to the current holder *in advance* of the termination date.. If the proper format is followed in the termination notice, the original author again has ownership. (The most well-known writer/performing artist to file a termination notice to date is Victor Willis, lead singer of the Village People, who filed his paperwork in August.)

This newsletter is not intended to provide legal advice on specific subjects but rather to provide news and analysis of legal issues and developments. You should always consult with legal counsel before taking action on any matter described in this newsletter.