

Harvell and Collins, P.A. Quarterly Report

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It is our pleasure to send you the March Edition of our **NEWSLETTER** for the year 2007.

This **NEWSLETTER** will concentrate on various legal concepts and we would suggest that you keep it with your important files to refer to from time to time.

For those of you who have not received our **NEWSLETTER** in the past and are new clients, our **NEWSLETTER** attempts to keep you informed of any new developments in local, state, and federal law that might affect your personal life or your business. The **NEWSLETTER** will advise you on these developments and, when appropriate, make suggestions that will help you deal effectively with these changes. Also, the **NEWSLETTER** will serve as a way to communicate with you. As always, if you would like to have us address a particular matter, please feel free to call or write, and we will address that issue in a future **NEWSLETTER**.

We always try to expand the scope of our services and sharpen our skills in the areas of practice that we provide. We would like to take this opportunity to remind you of the services provided by this law firm.

“The Right Advice at the Right Time”
Visit us at www.harvellandcollins.com

If you have not done so already, we encourage you to visit our website. The website serves as yet another way to render superior service to our clients. There is a wealth of information disclosed on the web site, including important links to useful government agencies that will assist our clients in obtaining valuable information.

“About the Firm” presents the history and purpose of the law firm. “Staff Profile” introduces our lawyers and legal assistants. Contact information is provided for all employees. The website provides an extensive list of services offered by Harvell and Collins, P.A.

Please visit us at www.harvellandcollins.com. We look forward to comments from our clients regarding our website.

“Let’s Talk Legal”

Radio Station: WTKF - 107.3 FM

As many of you know, Harvell and Collins, P.A., presents a talk radio program each and every Tuesday at 7:30 a.m. The purpose of the live radio program is to present to the listening audience legal information and allow the listeners to call in and ask questions. We have thus far discussed the following topics:

- Estate Planning
- Elder Law and Medicaid Planning
- Litigation in all Courts
- Estate Administration
- Real Estate Transactions
- Corporate and Business Transactions
- Family Law and Domestic Relations

If you have suggestions for a topic to be discussed, or if you have a question, give us a call. Or, call in during the show at 1-800-818-2255. Please join us on Tuesday mornings, bright and early on the talk station at WTKF - 107.3 FM.

We are now archiving our weekly radio program on the website so that our clients may listen once again to the program by visiting our website at www.harvellandcollins.com.

Changes in Medicaid Rules

As most of our clients know, the Medicaid program provides many planning techniques for those who know and understand the applicable law. Unfortunately, the Medicaid laws are also very complex and somewhat serve as a “moving target” for elder law practitioners. Sound and up-to-date advice is essential when dealing with Medicaid eligibility laws.

You may have heard that the Medicaid laws will soon be changing. It is true that in 2006 Congress passed the Deficit Reduction Act (DRA), affecting the Federal Medicaid eligibility rules once implemented by the states.

The State of North Carolina is currently considering specifically how it will implement the changes into the current Medicaid eligibility rules in this state. We anticipate that the new rules will take effect in North Carolina on April 1, 2007.

The planning techniques most often utilized by Harvell and Collins, P.A., will not be affected by the new Medicaid eligibility rules. Here at the firm, we take much care in providing planning techniques that will not be negatively impacted by changes in the law. Our clients should take comfort in the fact that their asset protection plans provided by this law firm will remain in tact even upon implementation of the new DRA rules.

The proposed primary changes to the Medicaid Eligibility Rules in North Carolina are as follows:

- The “look back” period will be extended from three years to five years.
- The sanction period for gifts will begin to run upon application for Medicaid instead of upon the date of the gift.
- The “homeplace” with an equity value of \$500,000.00 or more will be a countable asset even if the “intent to return home” is signed.

Harvell and Collins, P.A., will continue to provide the most advanced and cutting-edge asset protection plans available under existing law, and we will continue to strive to notify our clients of any changes to the Medicaid laws through future Newsletters and our weekly radio program. If you have any specific questions about the DRA changes, please feel free to contact us at our office.

Family Limited Partnerships and Family Limited Liability Companies **Estate Planning Vehicles for the Masses**

For years, family limited partnerships (FLPs) have been popular vehicles for commercial and residential developers, landlords, and ordinary real estate owners. More recently, the use of family limited liability companies (FLLCs) has grown in popularity among this class of individuals. FLPs and FLLCs offer a range of advantages to real estate owners.

Typically, real estate owners create FLPs and FLLCs for liability protection. By carefully structuring and managing these business entities, owners can limit potential liability that may arise from lawsuits involving their real estate holdings. By limiting their liability to the value of their investments, owners are able to shelter their personal assets and other investments. This is especially important for individuals who own multiple real estate holdings that are developed and managed independently of one another. In such situations, if one development project has problems, all the rest do not suffer.

Aside from their ability to limit liability, both FLPs and FLLCs are uniquely suited to provide real estate owners with estate, gift, and income tax benefits that allow persons to pass wealth to future generations at a reduced rate. Real estate owners create such FLPs and FLLCs with the purpose of preserving and maintaining unified and consistent management of the properties that may be contributed to the entity. These entities also allow families to keep assets consolidated in a single location and provide a vehicle to foster the development of investment asset understanding and expertise within a family.

FLPs and FLLCs are also beneficial as investment entities; they facilitate the making of gifts because no transfers of cash or securities have to be made each time a gift is desired. Gifts can be made by simply executing an assignment of units, similar to a stock power used to make a gift of stock. Because each completed gift will be a gift of non-management units, the value of each conveyed unit will be a fraction of the percentage interest of the market value of the underlying entity assets that the gift conveys. This “discount” is created because the units given carry with them no management powers and no unilateral ability to sell or cash-in the unit for full underlying asset value. Accordingly, this creates a valuation discount and provides gifting leverage in that it allows more underlying value to be given away than will be recognized for federal gift tax purposes.

To better illustrate the gifting aspect of the FLP and FLLC, consider the following example:

If one conveys \$1 million into an FLP or FLLC and takes back 10 voting (management) units and 990 non-voting (non-management) units, each unit would have a percentage value of approximately \$1,000 (\$1 million divided by 1,000 shares). Based on the annual gift tax exclusion of \$12,000, an individual could arguably give away 12 non-voting units without generating any adverse gift tax. However, under the terms of the management agreement governing the business entity, the non-voting units generally have no control over issuing dividends or the management of the company. Similarly, a gift of non-voting units is not attractive to an outside third party because the company is run by one family and the third party would own no controlling share in the company. Thus, the interest is less marketable. When these facts are coupled with restrictions on the transferability of interests to non-family members, then non-voting units are not very desirable to outside parties. It is, therefore, appropriate to discount the value of each share to account for the lack of control and marketability. These discounts may range anywhere from 10% to 40% or more. Thus, these discounts allow you to pass on more than 12 units without exceeding the annual exclusion amount.

Individuals who are considering FLPs or FLLCs must be aware that the IRS does not like these entities to the extent they are used to achieve gift valuation discounts. Efforts have been undertaken by the Treasury Department to achieve a legislative repeal of these companies as an estate planning tool. Recent cases have suggested one must approach FLPs and FLLCs with great care in terms of drafting the restrictions and language contained therein. Notwithstanding the IRS scrutiny, FLPs and FLLCs continue to be viable estate planning techniques as long as the family is willing to live with the possibility of an IRS challenge and adjustments may be necessary with respect to any gift or estate taxes paid. Depending upon the circumstances, potential estate planning benefits to be derived from the FLP and FLLC typically outweigh the disadvantages; when there is significant estate tax liability facing an estate, the risks are worth taking. When combined with the liability protection available, FLPs and FLLCs are a must for real estate owners to consider.

The Durable Power of Attorney

A Durable Power of Attorney is a legal document whereby you appoint, prior to any mental or physical incapacity, a person or institution to handle your personal and business affairs should you become mentally or physically unable. The document is durable in that its legal validity continues notwithstanding your mental or physical incapacity.

Although it is difficult to make any statement regarding estate planning which applies to all persons, it is probably safe to state that everyone should have a Durable Power of Attorney. If a sudden accident or illness were to happen, who would have the legal authority to continue to handle your personal and business affairs?

In the alternative, and in the absence of a power of attorney, a special court proceeding must be instituted to have a guardian appointed, and you must be declared legally incompetent. This court proceeding can be time consuming and expensive. It is a cumbersome proceeding in that at least two attorneys are necessary, one to represent the petitioner for guardianship and one to represent the alleged incompetent person.

In addition to the Durable Power of Attorney, there exists the Health Care Power of Attorney, whereby one designates an agent for the limited purpose of making final health care decisions.

Like all estate planning documents, the power of attorney should be tailored to your special needs and requests. It is not the only consideration or single cure to planning for the possibility of mental or physical incapacity, but it is certainly an important first step.

Estate Taxation

Under the tax law enacted in 2001, whatever you own is subject to the federal estate tax upon your death, until 2010. For the year 2010, estates will be entirely free from federal taxation. However, the law that includes this provision expires at the end of 2010. Thus, unless Congress acts in the interim, the estate tax rules will then revert to those prevailing in 2002. For 2007, the tax rate on estates is 45%.

That said, not all estates will be taxed while the estate tax is in effect. First, a spouse can leave any amount of property to their surviving spouse free of federal estate tax if that spouse is a U.S. citizen. Second, the estate tax applies only to estates valued at more than \$2 million in 2007, and this threshold will increase incrementally until it reaches \$3.5 million in 2009. The federal government allows you this tax credit for gifts made during your life or for your estate upon your death. Third, gifts to charities are not taxed.

Most states also have an estate or inheritance tax, but more and more have moved to a so-called "sponge" tax, which ultimately does not cost your estate. In such cases, the states take advantage of a provision in the federal estate tax permitting a deduction for taxes paid to the state up to certain limits. The states simply take the full amount of what you are allowed to deduct off the federal taxes. However, under the 2001 tax law, the allowable state deduction was phased out and disappeared in 2005. This means that many states are changing their estate tax laws to compensate for the difference. These changes may call for a restructuring of your estate plan and you should check with your attorney.

<i>Tax Year</i>	<i>Tax Rate</i>	<i>Exemption Equivalent</i>
2001	37-55%	\$675,000
2002	41-50%	\$1,000,000
2003	41-49%	\$1,000,000
2004	45-48%	\$1,500,000
2005	45-47%	\$1,500,000
2006	46%	\$2,000,000
2007	45%	\$2,000,000
2008	45%	\$2,000,000
2009	45%	\$3,500,000
2010	N/A	N/A

Making Gifts: The \$12,000 Rule

One simple way you can reduce estate taxes is to give some or all of your estate to your children (or anyone else) during their lives in the form of gifts. Certain rules do apply, however. There is no actual limit on how much you may give during your lifetime; but if you give any individual more than \$12,000 in any calendar year, you must file a gift tax return reporting the gift to the IRS. Also, the amount above \$12,000 will be counted against a \$1 million lifetime tax exclusion for gifts. Each dollar of gift above \$1 million reduces the amount that can be transferred tax-free in your estate.

The \$12,000 figure is an exclusion from the gift tax reporting requirement. You may give \$12,000 to each of your children, their spouses, and your grandchildren (or to anyone else you choose) each calendar year without reporting these gifts to the IRS. In addition, if you are married, your spouse can duplicate these gifts. For example, a married couple with four children can give away up to \$96,000 in 2007 with no gift tax implications. In addition, the gifts will not count as taxable income to your children (although the earnings on the gifts if they are invested will be taxed).

What Can Estate Planning Do for You?

The first step in planning your estate is identifying your major objectives. Here are some typical objectives and preliminary suggestions on how to meet these objectives:

- Clearly provide for your immediate family.
- Provide for other relatives such as parents and grandchildren who need help and guidance.
- Transfer your property to your beneficiaries quickly.
- Plan for the unforeseen such as an incapacity.
- Minimize expenses such as probate fees, bonds and attorney fees.
- Choose executors and/or trustees for your estate.
- Greatly ease the strain on your family.
- Help a favorite charity.
- Reduce the taxes on your estate.
- Make sure your business runs smoothly after your death.

Postscript

This writing is intended to generally familiarize you with various legal issues. The scope of this document is necessarily limited, and consultation with your attorney or tax advisor should always precede taking any action.