

LEGAL NEWS

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HOME IS WHERE THE BUSINESS IS

by Philip D. Nykamp

The advantages of operating a business from your home are numerous, but you need to balance these advantages against legal considerations that may not be apparent. Attention to these matters at the outset of starting a home-based business can help you avoid legal pitfalls and can greatly enhance your prospects for success.

Business Organization

Your business may be a glorified version of a former hobby, but, as an ongoing business, the enterprise needs to take a legal form best suited to your circumstances. Factors such as tax issues, the number of employees (if any), and avoiding personal liability will influence the decision on a business's legal structure. The most common choices are sole proprietorship, partnership, corporation, and limited liability company.

"Just what qualifies as a 'business use' under a zoning ordinance is not always clear.."

Zoning and Building Codes

A plan for a home-based business will stall if local land-use regulations prohibit a business from being run on property that is zoned "residential." Just what qualifies as a "business use" under a zoning ordinance is not always clear however, and home-based businesses may be permitted if certain restrictions or conditions are met. In one case, for

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MEDICAID AND NURSING HOME BENEFITS

by David M. Dubin

Medicaid is a governmental program that provides health insurance coverage for low-income children, seniors, and people with disabilities. As the baby boomers age, Medicaid's other role, as a source of nursing home benefits, is getting more attention. Each of the states operates its own Medicaid program, subject to some overriding rules set up by Congress and the federal Centers for Medicare and Medicaid Services. The following is an overview of some of those rules. Be aware that the specific requirements can vary from state to state, and must be checked before making decisions.

Asset Rules

An individual may have no more than \$2,000 in "countable" assets to be eligible for Medicaid nursing home benefits. Assets that are not counted in this calculation include personal possessions, one motor vehicle (valued up to \$4,500 for an unmarried recipient and of any value for the resident's spouse), a princi-

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FINAL RULES ON CAPITAL GAINS

by Stephen B. Latham

The Internal Revenue Service has issued its final rules on the capital gains tax exclusion that is available on the sale of a taxpayer's principal residence. A taxpayer may exclude up to \$250,000 from the sale of a principal residence, and the exclusion doubles to \$500,000 for married taxpayers. However, the taxpayer must have owned and used the property as a principal residence for a total of at least two of the five years before the residence is sold.

The final rules focus on the part of the Internal Revenue Code that allows a taxpayer who fails to meet the above condition to still have an exclusion in a reduced amount. There are three grounds for claiming a reduced exclusion: change in employment, health, and unforeseen circumstances. For each of these grounds, the regulations provide a general definition and one or more "safe harbors"—specific reasons for the sale of the residence. If the safe harbor for a particular ground applies, a sale (or exchange) is deemed to be "by reason of" that ground. If no safe harbor applies, the taxpayer still can claim one of the grounds on the basis of all of the surrounding facts and circumstances.

For example, the safe harbor for claiming a reduced exclusion because of a change in employment applies when the new place of employment is at least 50 miles farther from the residence that was sold than was the former place of employment. As for

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WITHDRAWAL RULES FOR INHERITED IRAs

by Anne Marie Goodale

The IRS has established rules for determining the minimum amount that must be withdrawn each year from an inherited traditional IRA. When an individual inherits an IRA, the rules differ somewhat depending on whether the individual was the decedent's spouse. In any case, there is a substantial incentive for following the rules, because the failure to take minimum withdrawals results in a stiff penalty equal to 50% of the shortage. Since complying with the rules can be a convoluted process and a mistake could be costly, it makes sense to be guided by professional advice.

Surviving Spouses

The starting point is the general requirement that minimum withdrawals must begin at the age of 70 1/2. If an IRA owner dies before April 1 of the year after he or she turned 70 1/2, or at any earlier time, the surviving spouse can handle the IRA in any of three ways. First, the spouse can transfer the account to his or her own name, so that it is treated as if it always belonged to the survivor. If the survivor is substantially younger than 70 1/2, this has the benefit of putting off mandatory withdrawals for years, during which time there will be more tax-deferred growth in the IRA. This choice also has the benefit of using a longer joint life expectancy figure in calculating the minimum withdrawals, meaning less is taken out and taxes are reduced.

Second, the surviving spouse simply can leave the IRA in the deceased spouse's name and begin taking mini-

num withdrawals when the deceased spouse would have been able to do so. The third approach is to invoke the "five-year rule," which allows the surviving spouse to do whatever he or she wants with the account until December 31 of the fifth year after the year in which the other spouse died. By that date, however, the account must be emptied and the resulting taxes must be paid. The five-year approach is not available if the deceased spouse died on or after April 1 of the year after turning 70 1/2.

"... complying with the rules can be a convoluted process and a mistake could be costly ..."

Other Individual Heirs

If the deceased individual named a non-spouse beneficiary for the IRA, the beneficiary must begin taking minimum withdrawals over his or her own life expectancy, starting by December 31 of the year in which the account owner died. Additional withdrawals must be taken by December 31 of each successive year. To calculate the minimum amount to be withdrawn, the beneficiary must divide the account balance for the previous year by his or her life expectancy, as given in tables published by the IRS.

As with surviving spouses, an heir can use the five-year rule to liquidate the inherited account by the end of the fifth year after the original owner died, before which time the heir can withdraw as little or as much as desired. Also, as with surviving spouses, the five-year rule is not available if the IRA owner died on or after April 1 of the year after turning 70 1/2. ■

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example, a court ruled that a city ordinance allowed a professional office to be operated as a secondary use of a residence. As long as the business use of the property remained incidental to the dominant use of the property as a home, even other professionals or support personnel aside from the homeowner could work out of the residence.

When your home doubles as a business office, compliance with local building codes becomes a bigger issue. Features that may not apply to a residence can come into play, such as provisions for parking and handrails or ramps for providing access for persons with disabilities. Your electrical system could need an overhaul in order to comply with the code, especially if the business requires computers or other technologies not necessarily found at home.

Insurance

Because a fledgling business is vulnerable to financial injury from lost or damaged business property or injury to a client, you will also need adequate insurance. Simply continuing your homeowner's insurance without changes may not be sufficient when starting up an in-home business, especially since such policies generally are meant to cover personal property only. The simplest and least expensive solution may be to add a "rider" to an existing policy that covers business assets and liability. Another alternative is a new, separate policy covering anything related to the business.

The importance of having the right insurance is illustrated by a case in which homeowner's insurance did not cover the medical expenses incurred by an employee who was injured on the premises of a home-based business. A married couple lived on the second floor of their home while using the first floor to house their construc-

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Reverse Piercing Of The Corporate Veil

by Christopher D. Kelley

Generally, business entities such as corporations or limited partnerships are legally separate and distinct from the shareholders and members who compose them. When justice requires it, however, courts have ignored the separation of the business and the individual and have allowed a creditor of the business to satisfy the debt from the assets of an individual closely connected to the business. This concept is known as "piercing the corporate veil." A variation on the idea, called reverse piercing of the corporate veil, allows someone to reach the assets of the business entity to satisfy a claim or judgment obtained against a corporate insider. In both instances, a court

disregards the normal protections given to a business structure in order to prevent abuses of that structure.

Neither type of "piercing" is done lightly. There must be such a blurring of the lines between a business and an individual that the separate personalities of the two no longer exist. Moreover, while a court's analysis is highly dependent on the facts of each case, typically the party seeking to disregard the distinction between a business and an individual associated with it must show that the individual controlled or used the business so as to evade a personal obligation, perpetrate a fraud or a crime, commit an injustice, or gain an unfair advantage.

Recently, a state supreme court approved the use of "reverse piercing" to allow two creditors of an individual

to use the assets of a limited partnership controlled by that individual to satisfy his personal debts. The businessman owned or controlled various business entities. The creditors showed that the revenue from the largest of these, a limited partnership, was transferred to a corporation owned by the same individual. Then the funds were used to pay for the businessman's lavish lifestyle, including such items as a second home, country club membership, luxury vehicle, credit card bills, and college tuition for the businessman's son. Under these circumstances, the legal distinction between the partnership and the person controlling it had become a fiction to be ignored in the interests of justice. ■

MEDICAID *cont'd.* from pg. 1

pal residence in the same state where benefits are sought, prepaid funeral plans and a small amount of life insurance, and assets deemed to be inaccessible. To promote the independence of the nursing home resident's healthy spouse, usually referred to as the "community" spouse, that spouse may keep one-half of the couple's countable assets, up to a maximum of \$92,760 in 2004. The least that a state may allow the community spouse to retain in 2004 is \$18,552. The couple's assets are totaled as of a "snapshot date," which is when a spouse enters a long-term facility in which he or she then stays for at least 30 days.

Transfer Penalty

To avoid giving benefits to those who present a false picture of poverty, there is a transfer penalty that is imposed when people transfer assets

without receiving fair value in return. The government divides the amount so transferred by the average monthly cost of a nursing home in the state in question. The person is then ineligible for Medicaid during the resulting number of months. Several provisions limit the impact of the transfer penalty. First, Medicaid officials can consider only transfers made during the last 36-month "look-back period" preceding the application for Medicaid (or 60 months for transfers made to certain trusts). As a result, it is prudent not to apply for benefits in the three years after a large transfer. Second, the transfer of assets to particular categories of individuals, such as spouses and blind or disabled children, will not bring about a penalty. Finally, a penalty can be completely wiped away, or "cured," if the transferred asset is returned, or the penalty may be reduced to the extent that the

asset is partially returned.

Treatment of Income

The starting point for dealing with income under Medicaid is that nursing home residents pay all of it, less certain deductions, to the nursing home. The types of deductions are as follows: a \$50 per month allowance (subject to some variations among the states) for the resident's personal needs; a deduction for any uncovered medical costs, including premiums for medical insurance; for married applicants, an allowance for the spouse at home if he or she needs income support; and a deduction for any dependent children living at home. In New York, income of the community spouse is counted towards the applicable income levels. There may be ways for the community spouse to keep most, if not all, of his or her income. ■

Grandparent's Visitation Rights

by Janice L. Snead

What rights do grandparents have when a family is torn apart by death or divorce? Do grandparents have any rights to stay in contact with their grandchildren?

In New York State, visitation is not automatic but rather subject to the discretion of the Court. In making its determination, the Court will take into consideration the existing relationship between grandparents and grandchild, the basis of the parental objections to visitation, and whether or not visitation is deemed to be in the child's best interest. It is not sufficient that the grandparents allege love and affection for their grandchild. They must establish a sufficient existing relationship with their grandchild, or in cases where that has been frustrated by the parents, a sufficient effort to establish one, so that the court perceives it as one deserving the Court's intervention.

Unfortunately, fighting for visita-

tion rights can be very costly and time consuming. Be prepared to testify about your relationship with your grandchildren, your relationship with the parents, and the last time you saw or spent time with your grandchildren. Also be prepared to discuss your personal history, including any medical troubles or problems with the law.

You will also have to answer to the objections to your visitation rights brought by the parents. The court will take the parents' decision-making processes into account when resolving these disputes. Many courts feel that parents have a fundamental right to autonomy in child rearing. If a parent can prove that a grandparent cannot perform some tasks independently or correctly, the courts may insist that visitation be supervised or may not grant visitation rights at all.

While the circumstances will vary in each case, the courts will always give the children's welfare the highest priority. ■

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tion business. They used an adjoining garage to store personal belongings. When a company employee was searching in the garage for company records, he slipped and injured himself. An exclusion in the homeowner's policy for "business pursuits of any insured" meant that the injury was not covered under the policy.

In conclusion, if you intend to establish a business office in your home, it would be prudent to seek the advice of an attorney before operations commence to review local zoning regulations that may restrict or limit such activity. You should also consult with your counsel regarding the formation of the appropriate entity that, together with adequate insurance coverage, will protect you from any personal liability from business activities. ■

CAPITAL GAINS *cont'd. from pg. 1*

health, the safe harbor that smoothes the way for the reduced exclusion is a physician's recommendation of a change of residence for reasons of health. A sale or exchange of a residence due to unforeseen circumstances refers to the occurrence of an event that the taxpayer could not reasonably have anticipated before purchasing and occupying the residence. Simply wanting to move to a preferred home or moving due to improved financial circumstances does not qualify. The specific events that make up the safe harbor for this ground include, among other things, such circumstances as death, divorce, natural or man-made disasters affecting the house, and even multiple births from a single pregnancy. ■

Twomey Latham Offers Free Real Estate Brochure

How To Buy A Home On The East End, an informative brochure prepared by our Real Estate Department, is available to you at no cost. The brochure offers 64 common questions and answers that provide solutions to buying a home on the east end of Long Island. Below are a few sample questions and answers.

Q *How do I choose a real estate professional to work with?*

A In today's economy, many individuals have no spare time to search through lists of "For Sale By Owner" classifieds. Instead, they solicit a well-established, reputable real estate company and have sales agents do the work for them. A real estate professional will stay in touch with the purchaser and keep the purchaser informed of new listings that meet the buyer's criteria. Choosing such a professional is one of the most important aspects of real estate sales. Realtors and brokers dedicate their time and energy to marketing and selling property, so find an energized professional. Look for a broker who is organized, truthful, and someone you are comfortable with. Scanning the advertisements in the local newspapers or asking a friend who has recently purchased property are good starts.

Q *What if there are zoning violations affecting the property?*

A The first thing you should do is contact your attorney. There are various ways to clear up zoning violations affecting the property. Having the structure that is in violation moved or torn down or by obtaining a variance from the zoning ordinance are three examples.

Call today to get your free copy and if you have a question that does not appear in the brochure, feel free to call our office to get an answer. ■