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LABOR & EMPLOYMENT LAW

EMPLOYER ON THE HOOK FOR TREBLE DAMAGES FOR FAILURE TO PAY EARNED VACATION ON EMPLOYEE'S TERMINATION DATE — AND PAYING WAGES BEFORE EMPLOYEE FILES COMPLAINT IS NO EXCUSE

BY DAVID R. KERRIGAN AND MICHELLE M. DE OLIVEIRA

A recent decision by the state's highest court has reinterpreted the Massachusetts Wage Act's damages calculation for a late wage payment to a discharged employee, holding that an employer that does not pay earned wages in full on an employee's termination date is liable for treble damages, attorney's fees, and costs regardless of whether the employer pays the employee in full before the employee files a complaint. This case has significant consequences for employers moving forward.

The Massachusetts Wage Act requires employers to pay discharged employees the full amount of all wages earned through the termination date, including all unused and accrued vacation time, on the termination date. If wages are not timely paid, an employee may seek three times the unpaid wage amount as damages (i.e., trebled damages). Until this decision, courts interpreted the Wage Act so that if an employer paid the late wages before an employee filed a complaint, the employer would owe three times the lost interest.

In a groundbreaking decision, *Reuter v. City of Methuen*, Massachusetts' Supreme Judicial Court (SJC) rejected this interpretation in finding that the statute entitles employees to three times their late wages, regardless of whether the employer pays the employee before a lawsuit.

In *Reuter*, the City of Methuen discharged an employee for stealing — and she was owed $8,952.15 for accrued vacation at the time of her termination. The City of Methuen did not pay her in full on her termination date but paid her for all accrued vacation time three weeks *after* her termination. Over a year later, the employee's attorney sent Methuen a demand letter seeking three times the late wages in damages. In response, Methuen paid an additional $185.42, representing three times the interest accrued during the three-week delay between her termination and payment of her remaining wages. After the employee brought an action seeking three times the total unpaid wages, the trial court agreed with Methuen, finding that the employee was only entitled to three times the interest lost during the three-week delay in her vacation pay.

On appeal, the SJC reversed the trial court's decision, based on the Wage Act language that "the employee shall be awarded treble damages, as liquidated damages, for any lost wages and other benefits." The court found that "lost wages" include late paid wages, regardless of whether the employer paid the employee in full before a lawsuit was filed. While the court recognized some ambiguity in the statutory language, it found that allowing employees to recover treble damages for late wages is consistent with the statute's purpose of ensuring prompt payment of wages.

This decision reinforces the importance of timely paying employees in full for all wages earned, including upon termination. Employers must be ready to pay an employee who is terminated in full for all wages earned through the termination date, including vacation and commissions, on the termination date — and not a day later.

This requirement may present practical problems if an employee engages in misconduct and immediate action may be required — but if full pay cannot be made on that day, suspension with pay is a better practice until the exact amount of pay can be determined and issued. Even a brief delay in paying the full amount of wages could result in liability for three times the late wage amount. Individuals with specific questions are encouraged to speak with an employment attorney. ■

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This alert is for informational purposes only and may be considered advertising. It does not constitute the rendering of legal, tax or professional advice or services. You should seek specific detailed legal advice prior to taking any definitive actions.

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PROBATE LAW

ASSET PROTECTION: IS IT THE RIGHT RITE OF PASSAGE FOR YOUR CLIENT (AND FOR YOU)?

BY MELISSA LANGA AND KAREN L. WITHERELL

As every estate practitioner knows, trends happen in estate planning just as often as they happen in all other aspects of life. Some days in our practice, we get the sneaking suspicion that all of our clients got together and decided that asset protection trusts (APT) are the new cool thing and everyone has to have one to maintain their social standing within the group. While we know that there were no such behind-the-scenes machinations, it is hard not to wonder if there is some sort of nexus when client after client comes in looking for asset protection.

There are many wonderful resources out there regarding the pros and cons of asset protection and the various planning techniques. Such resources will walk you through the planning analysis to take when deciding whether or not your client is best served setting up a foreign asset protection trust (FAPT) or would be better advised to look at a domestic asset protection trust (DAPT) structure for their needs. What we wish to focus on in this article is the more human side of asset protection planning for one's clients, such as: (i) are you are the right attorney for the job? (ii) based on the client's circumstances, is an APT even appropriate? (iii) is the client actually up for putting such a structure in place and living with the consequences? and (iv) documenting the engagement, trustee selection, and due diligence.

ARE YOU THE RIGHT ATTORNEY FOR THE JOB?

Before considering taking on an asset protection client, you need to take a hard look at your practice expertise. Not everyone can be an expert in all things, and it is important to know and accept this fact. It is common for trusts and estates lawyers to decide to not include every aspect of trusts and estates as part of their practice. For example, our firm does not do probate litigation as part of our practice because we understand that litigation requires a specialized skill set that takes time and practice to develop.

Every time an attorney considers taking on a new area of practice, even one that seems to be a natural offshoot of one's typical practice, a good attorney should always consider if this is a matter that such attorney can take on. You may never have done a DAPT before, let alone a much more complex FAPT structure. You need to decide for yourself whether and to what degree your practice will include asset protection planning using APT structures. The two most important considerations to review are: (i) your competency, and (ii) the prohibitions against the unauthorized practice of law.

ARE YOU COMPETENT TO DO ASSET PROTECTION TRUST PLANNING?

The ethical rules governing the practice of law are clear that you cannot accept a client if you are unable to competently address the issues presented by that engagement. So, how do you begin to develop a trusts and estates practice that includes APTs?

1. **Research and Read:** On your own dime, research and study the law regarding APTs.
2. **Don't Undersell Yourself:** Do not underestimate your asset protection knowledge. There are many standard estate planning tools that include asset protection elements. Further, your client may receive ample protection without an APT by using planning techniques that are already part of your wheelhouse.
3. **Don't Oversell Yourself:** Do not overestimate your asset protection knowledge. You are not an APT specialist if you've never done an APT. Be upfront with your client. If you have done good work in the past, the client may have faith in you. Even so, you cannot proceed unless you independently assess your ability to competently accomplish the task.
4. **Align with An APT Lawyer:** If you feel you cannot competently undertake your first APT alone, you should align yourself with a lawyer who has APT experience. Three common options are to: (i) co-counsel with an experienced APT lawyer; (ii) hire an experienced APT lawyer yourself to bounce ideas off and to review your work; and (iii) turn the client over to an experienced APT lawyer and shadow the lawyer during the engagement to learn the ropes. Whatever route is chosen, the arrangement must be fully disclosed to the client, and you need to make sure your malpractice insurance provider will cover the arrangement should something go amiss.

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Unauthorized Practice of Law: Ethical issues can also arise when the APT will be located in a jurisdiction where you are not licensed to practice. We all can't live in Alaska, right? To protect yourself from a claim of the unauthorized practice of law, best practices include:

1. **Learn Local Ethical Rules:** Familiarize yourself with the ethical rules of the APT jurisdiction. Never simply assume the rules are the same as those for your own jurisdiction.
2. **Disclose the Need for Local Counsel:** In the early planning stages, preferably in the

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first engagement letter (more on that below), inform your client of the need to engage local counsel to review the APT prior to its implementation. It is not uncommon for a client to balk at what they perceive as unnecessary costs to bring in another attorney. This step is not, however, unnecessary duplication of work but rather a critical part of ensuring that the APT put in place is the best possible protection for the client. If the client refuses, be prepared to cut the client loose. We have noticed in our own practice that a client who starts to balk at the initial stages of APT planning likely will try to nickel and dime the entire process, and in the case of an APT, you really do get what you pay for. As the attorney, you do not want to be pushed into shoddy work due to the client's economizing. If the client is not willing to pay the costs necessary to set up a well-drafted APT, the client is not right for APT planning.

3. **Actually Consult with Local Counsel:** Locate and actually consult with counsel in the APT jurisdiction. If you do not know who to consult, most trust companies within the APT jurisdiction can provide you with some introductions. There are always going to be local rules and practices that you will not be able to determine just through your own research. Local counsel will help you avoid pitfalls and help ensure that the product that you provide is in keeping with what is needed in that specific jurisdiction.

OK, YOU HAVE DECIDED THAT YOU ARE PERFECT FOR THE MATTER, BUT HOW ABOUT THE CLIENT? ARE THEY THE RIGHT CLIENT FOR YOU?

It is important to always remember that no one is entitled to your legal expertise. You choose your clients. The old legal practice chestnut that "The most money I ever made was on the client I turned away" applies especially to the realm of asset protection planning. You do not want to make the client's problems your problems. The one thing that we always recommend keeping in mind is that your law license and your legal reputation are far more valuable to you than any one client can ever be. Careful due diligence before deciding to accept the engagement is incredibly important for your own protection and also to ensure that any structure you put in place will provide the sought protection.

WHY HAS THE CLIENT CONTACTED YOU?

The first step in evaluating any client is to determine why they have come to you looking for asset protection planning. If they are looking for protection from a current creditor or they think they are about to be sued, walk away from that engagement! Attempting to craft an effective asset protection plan when the creditor has already knocked on the client's door is like trying to put toothpaste back into the tube. It's messy and you should not do it. The one valuable thing that you can do for a client who already has a creditor is to provide the client with an asset protection audit to review what protections may already be in place for them, such as a primary residence with a previously recorded homestead declaration or a retirement account where they have not yet reached the withdrawal age. Also, once the current issue has been resolved and they are again free of current and pending creditors, they may be a good candidate for such asset protection planning in the future.

The right kind of client for asset protection planning is a client who has no current creditors and no expectation of a creditor looming on the horizon. Often, this client is seeking asset protection because she happens to simply work in a field where lawsuits are common, and the client knows that it is a risk. In our own practice, we regularly work with medical professionals and real estate developers seeking information about asset protection since they know a future lawsuit is simply a fact of life in their profession.

IS THE CLIENT WILLING TO ACTUALLY GIVE UP CONTROL OF THE ASSETS? NO 'WINK, WINK' CLIENTS!

It is not enough for the client to simply be free of any creditor claims; the client must also have the right mindset to participate in asset protection planning for the structure you put in place to work. The web is full of misleading information about APTs, including claims that assets within an APT are fully accessible to a client, that is to say, the client can reach in and take back the assets whenever the client so chooses. A client who believes this claim to be true is not a good candidate for an APT. Why? A client who treats an APT like a personal piggybank will find that a judge will treat the APT the same way. A client cannot think of the APT as a sham arrangement. It is not. The client relinquishes real control to the APT trustee, who is empowered to exercise its discretion — the power to say "yes" to a distribution request includes the power to say "no." And the client needs to be willing to hear "no" now and then.

Our clients are regularly surprised when we review with them that to get the protection that they want really does mean that the client will give up control over the asset. Some clients accept this as just the cost of getting the protection that they are looking for. Other clients, however, will try to have their cake and eat it too with questions such as, "What if I put in a 'friendly' trustee?" or "How about if the trust contained X provision?" Again, these are the clients who are not good candidates for the structure. At best, they will abide by the structure but be resentful about the restrictions and blame you for the situation. At worst, they will constantly try to find ways to work around the structure and ultimately undermine all of the protections of the APT.

A word here about the APT trustee: when interviewing a possible trustee of an APT, be wary of the trustee who is too willing to accommodate whatever your clients want. The "wink, wink" trustee is as bad as, if not worse than, the "wink, wink" client. More on trustee selection below.

WILL THE CLIENT EMBRACE 'NEST EGG' PLANNING?

It is best to be wary of the client whose goal is to place all of her assets within an APT. Think about it. Who would do that? Who would be willing to place herself at the mercy of an APT trustee with complete discretion for any and all access to funds? Hardly anyone, and such a client may well fall into the "wink, wink" category. For a taste of how a judge may view a total transfer of funds, you might read the Anderson case. (*Federal Trade Commission v. Affordable Media LLC*, 179 F.3d 1228 (9th Cir. 1999). While the case contains egregious facts, the case is illustrative of judicial temperament nonetheless.

The better approach is to treat an APT as "nest egg" planning, where the client keeps sufficient assets outside the APT to support the client's lifestyle on a day-to-day basis. Those assets remaining outside of the APT will probably be subject to the claims of creditors unless protected in some other manner, such as holding as tenants by the entirety or held within an ERISA retirement account. Limited assets are transferred to the APT, to be kept in reserve for a future date when they might be needed by the family due to unforeseen circumstances.

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DOES THE CLIENT EVEN HAVE ASSETS THAT CAN BE TRANSFERRED INTO AN APT?

Often, a client may look like a great candidate on paper: no known or reasonably anticipated creditors, willing to cede control to an APT trustee, buys into the concept of nest egg planning. But one vital element remains to be analyzed: do the client's assets align with an APT? Taxable investment accounts, cash equivalents, and cash are best. Even so, if the client has disclosed such individually owned assets on a personal financial statement (PFS) provided to a lender, transfer of those assets into an APT may require an amendment to the PFS.

Some examples of difficult assets include:

1. **Real Estate:** A real estate developer with multiple parcels of immovable real estate and no liquid assets is not an ideal candidate for an APT. It may be possible to "move the immovable" by placing a parcel of real estate within an LLC, with the APT owning the LLC, but the fact remains that a court in the jurisdiction where the real estate is located may find a way to attach the interest or at least restrict sales and such while litigation is ongoing. And even if the client understands this risk, the existence of a mortgage on the real property may render the transfer to the LLC unattractive due to the need to refinance.
2. **Business Interests:** Nothing inherently stops an APT from owning a business. But often there are factors that get in the way. These include:
   a. The APT trustee does not want the liability of owning a business.
   b. Co-owners will not consent to the transfer.
   c. The APT may hinder the raising of capital from lenders and investors.
   d. An FAPT triggers difficult U.S. tax issues.
3. **Retirement Accounts:** Since retirement accounts must remain in the name of the individual plan participant, they are unsuitable for funding an APT.

The classic example of a prime APT candidate who falls short in the transferrable asset category is the surgeon with a beautiful home, the island vacation getaway, a great income and a large retirement account. In such a situation, there are not many available assets to plan with as far as an APT is concerned.

INFORMED DECISION-MAKING

The typical estate plan with its revocable trusts and other documents is itself a complicated structure that many a client struggles to understand, despite flow charts, executive summaries and the like. Add an irrevocable APT with its multitude of bells and whistles, and the chance that the overall structure is understood can be slim to none (and Slim just left the building!). The client always looks to the lawyer for its expertise and knowledge, and you must be able to clearly explain the various options available to the client, including the possible perils of each option. Never oversell the ability of an asset protection plan to thwart a creditor. The right client will be one who can digest complex information and make an informed choice. An APT is not for the weak of heart. Be wary of the client who says, "Whatever you say, pal, I'll do it." It's not your choice; it's their choice.

DOCUMENTING THE ENGAGEMENT AND DUE DILIGENCE

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First Engagement Letter

We have found that breaking the asset protection engagement down into separate parts is best for both the lawyer and the client. The first engagement letter should focus solely on the due diligence required to permit the lawyer to understand if the next step is possible, i.e., the actual design and implementation of an APT.

Before the first engagement letter is sent, you might alert the potential client that the purpose of the first engagement is to protect your firm from engaging in any prohibited activity and to protect the client from paying for a plan that will not work. The first engagement letter establishes the attorney-client relationship, thereby providing the amount and degree of confidentiality and protection such a relationship confers under law while due diligence is undertaken.

In addition to all the bells and whistles you include in your typical engagement letter, the first engagement letter for an asset protection plan should include:

1. **A Limited Scope of Services:** For example: "You have requested our representation to advise you regarding estate planning matters. However, before we can enter into such an engagement, due diligence is required. Accordingly, for the present and until modified by a separate engagement letter, our representation is limited to conducting a due diligence review to determine whether or not we will be able to provide effective estate planning advice. Our due diligence review will focus on confirming your solvency, confirming that no assets owned by you or involved in your estate plan are related to money laundering or other prohibited activities, and confirming that you have assets that may potentially fund a protective trust. If we are satisfied that we may proceed, this first engagement will end with our preparation and your signing of an Affidavit of Solvency."
2. **Other Lawyers:** If you intend to align with another lawyer outside of your firm with greater APT expertise, disclose your plan in the engagement letter and explain the finances of the arrangement.
3. **File Retention Language:** Adjust your file retention language to account for the 10-year statute of limitations in bankruptcy.
4. **An Advisor Authorization Letter:** In addition, it can be helpful to include in the first engagement letter an "authorization letter," which the client signs, granting the client's other advisors permission to disclose information to the lawyer. Typical advisors include bankers, wealth managers, accountants, other lawyers (such as a business lawyer, litigation lawyer, and a referring trusts and estates lawyer), trust officers and insurance advisors. At the very least, obtain the name and contact information of each of these individuals. Have your client send an introductory email introducing you to each advisor.

DUE DILIGENCE CHECKLIST

Now that the first engagement letter is signed, it is time to undertake the due diligence required for you and your firm to determine whether or not to proceed to the next stage of planning. Below is a checklist of actions the lawyer should consider to determine that the client both is acceptable to the lawyer and has the ability to implement an APT. For ease of reference and retrieval, keep all the due diligence information in one file.

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1. Obtain the following information:
   a. The full legal name of the client and any other names that may have been used in the past. (Prior names alone are not a deal breaker — there are many legitimate reasons why there may have been a prior name, such as a marriage, divorce, gender fluidity, or the Americanization of a name following immigration).
   b. A reference letter from a banker and accountant. Also include a reference from the referring attorney if there is one.
   c. A reference letter from a person who has a long relationship with the client (friend, business associate, clergy).
   d. A color copy of the client's passport and a color copy of the client's driver's license — also ask for copies of such documentation for the client's spouse and children (if any) and all proposed beneficiaries of the APT.
   e. A copy of a recent utility or phone bill addressed to the client at the client's current home address.
   f. Copies of the last three years of tax and information returns filed with the IRS.
   g. Copies of any gift tax returns.
   h. A copy of the client's resume or 10-year employment history.
   i. An explanation from the client as to the source of her wealth.
   j. A list (with values) of all the client's liabilities, including outstanding debts (personal and business), personal guarantees, existing judgments and existing lawsuits.
2. Ask the trial lawyer representing the client in an existing lawsuit, if any, to provide the following information:
   a. The name of the case and the court of filing.
   b. A professional assessment of the merits of the case.
   c. The amount of the client's professional liability coverage applicable to this claim.
   d. An assessment, based upon the trial lawyer's experience in such matters, of the likelihood that a settlement or judgment would exceed the policy limits.
   e. Confirmation on whether any of the client's property has been attached, whether an injunction against transfers has been issued, and whether any court order prohibiting transfers or estate planning has been issued.
   f. A copy of the complaint.
3. Make a list of any reasonably foreseeable creditors of the creditor. Ask for a brief review of the facts and copies of any correspondence related to the possible claim.
4. Ask if the client has ever had a professional license suspended or revoked, or has received a professional reprimand.
5. Perform a web-based search of the client (a real rabbit hole — everyone has their favorite websites).
6. Ask if the client has ever been arrested or convicted of a crime or has been investigated by the IRS.
7. Consider conducting a background check. Some practitioners require the client to consent to a background check.

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INSOLVENCY ANALYSIS

Once you have gathered all the financial information, you must determine whether the client is "insolvent" (and therefore no planning should be done in light of the fraudulent transfer laws) or whether the client is "solvent" and, if so, to what degree. Here is a simple balance sheet analysis: First, add together all assets that are reachable by a creditor. Do not consider protected assets, such as, for example, a qualified retirement plan account (IRA accounts not exempt in all states), homestead property, tenants by the entirety property, third-party spendthrift trusts of which the client is a discretionary beneficiary, insurance (in some jurisdictions), annuities (in some jurisdictions) or property with a secured creditor.

Next, add together all known liabilities with all reasonably anticipated liabilities.

Finally, subtract the liabilities from the reachable assets. If the result is a positive number, say, $2 million, then the client has assets that may be transferred to an APT without the transfer being deemed a fraudulent transfer. (Leave your client some wiggle room — valuations sometimes are fluid.) If the result is a negative number, you have an insolvent client who cannot proceed with an APT structure at this time.

AFFIDAVIT OF SOLVENCY

An affidavit of solvency is important evidence that you have done your due diligence and have come to the reasonable conclusion that you will not be assisting in a fraudulent transfer should an APT be formed and funded. In some APT jurisdictions, it is a required element of the formation of the APT, and almost all legitimate APT trustees will require one. Here is a sample affidavit that a squeaky-clean client might sign:

[SAMPLE] AFFIDAVIT

NOW COMES the undersigned, Nervous Ned of Nest Egg Harbor, Massachusetts, who, being duly sworn upon oath, and in contemplation of the transfer of assets to one or more entities of various nature and in various jurisdictions, in connection with a comprehensive estate plan designed to better suit his family and business objectives, herewith represents to T&E Law Firm PC that the following statements are true and correct to the best of his knowledge:

1. No particular transaction has occurred that I expect will develop into a future claim by any personal creditor of mine.
2. There are no pending, threatened, or reasonably anticipated claims, lawsuits, or other proceedings against me personally. I am not involved in any administrative proceedings brought by or on behalf of any international, national, state, or local government or any agency thereof or any other administrative body as of this date that could result in a claim or claims against me.
3. Following any contemplated or proposed transfer of my property to any individual, limited partnership, limited liability company, foundation, trust, or other entity in which I or my intended beneficiaries may have an interest, I will be solvent and able to pay my reasonably anticipated debts as they come due from my income and from the balance of my property after such transfer. I do not have the intent to hinder, delay, or defraud any existing or anticipated creditor.

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4. I am not engaged in or about to become engaged in business activities or any transaction for which the value or extent of my remaining assets will be unreasonable in relation to any personal liability I may have with respect to the business activities or transaction.
5. I do not contemplate filing for relief under any of the provisions of the U.S. Bankruptcy Code or any other bankruptcy law, nor am I involved in any situation that I reasonably anticipate would cause me to file for relief, or give cause for involuntary filing, under any of the provisions of the U.S. Bankruptcy Code or any other bankruptcy law in the foreseeable future.
6. I understand generally the provisions of the Money Laundering Control Act, a copy of which has been made available to me. I have read the attached summary of the Act, and I confirm and represent that none of the assets that I may transfer as contemplated in this affidavit has been derived from any of the activities specified in such Act.
7. I am fully compliant with all of my tax, duty, exchange control, and financial information reporting requirements to every international, national, state, and local government, agency thereof, and other administrative body.
8. I have not been charged with and am not under investigation for corruption, money laundering, fraud, or any other crime in any jurisdiction.
9. The attached personal financial statement is complete and accurate.

I declare under penalty of perjury that the foregoing is true and correct.

Executed this _____ day of ___________, 2021.
Nervous Ned
[ADD NOTARY CERTIFICATE]
Attachment to Affidavit

SUMMARY OF THE U.S. MONEY LAUNDERING CONTROL ACT

The U.S. Money Laundering Control Act (the "Act") makes it criminal for anyone to conduct or attempt to conduct certain financial activities that involve the proceeds of unlawful activities. As the transfer of assets into a limited partnership, trust or other entity may constitute a financial activity within the scope of the Act, it is necessary that you swear under oath that none of the assets intended to be transferred into such entities was derived from any of the criminal activities specified in the Act. The specified unlawful activities under the Act consist primarily of drug trafficking offenses, financial misconduct, environmental crimes and other specified crimes, each of which is described further below.

Drug trafficking offenses include the manufacture, importation, sale or distribution of controlled substances; the commission of acts constituting a continuing criminal enterprise; the illegal procurement of precursor chemicals; and transportation of drug paraphernalia.

Covered financial misconduct includes the concealment of assets from a receiver, custodian, marshal or other officer of the court; from creditors in a bankruptcy proceeding; or from the Federal Deposit Insurance Corporation, the Resolution Trust Corporation, or a similar agency or person. It also includes the making of a fraudulent conveyance in contemplation of a bankruptcy proceeding or with the intent to defeat the bankruptcy law; the giving of false oaths or claims in relation to a bankruptcy proceeding; bribery; the giving of commissions or gifts for the procurement of loans; theft, embezzlement or misapplication of bank funds or funds of other lending, credit or insurance institutions; the making of fraudulent bank or credit institution entities or loan or credit applications; and mail, wire or bank fraud or bank or postal robbery or theft.

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Environmental crimes include violations of the Federal Water Pollution Control Act, the Ocean Dumping Act, the Safe Drinking Water Act, the Resources Conservation and Recovery Act, and similar federal statutes.

Other specified crimes include counterfeiting, espionage, kidnapping or hostage-taking, copyright infringement, entry of goods by means of false statements, smuggling goods into the United States, removing goods from the custody of Customs, illegally exporting arms, and trading with United States enemies.

SECOND ENGAGEMENT LETTER

Congratulations, you have made it past the first planning stage and are ready to begin designing the best plan for your client. A second engagement letter should be signed, and this letter will be very similar to your standard engagement letter with your estate planning clients, except that the financial exploration stage will have already been completed. Additions to your standard letter might include provisions for the client to:

A. **Keep Financial Information Current:** Your client's agreement to update financial and liability information throughout the engagement.

B. **Update the Affidavit of Solvency:** Your client's willingness to sign another affidavit of solvency if asked (these engagements can go on and on, and you might want to be reassured you are working under current facts).

C. **Sign a Local Counsel Agreement:** The client's agreement to retain local counsel in the APT jurisdiction to review documents.

D. **Agree to New File Retention Language:** The expanded file retention language (mentioned earlier).

TRUSTEE SELECTION

It may seem counterintuitive, but once the client decides that an APT is to be a part of her estate plan, the first item of business should be selection of the trustee, not the design of the APT itself.

A. **Selecting the Jurisdiction:** You must first help your client decide where the APT should be located, as that will drive where you will look for a trustee. Unfortunately, the comparison of DAPT and FAPT jurisdictions is beyond the scope of this outline.

B. **Types of Trustees:** As stated above, it is very important that an APT be operated as a true discretionary trust and not as the settlor's piggybank. For this reason, it is often preferable for a trust company experienced in the operation of discretionary trusts to serve in the role of trustee. But it is not necessary.

C. **Trustee Interview:** Ideally, you and your client will interview several trustees before the client selects the initial trustee. If possible, a generic flow chart of the proposed structure might be given to the trustee in advance so the trustee understands what it is being asked to undertake (for example, whether there will be an LLC owned by the APT and the type of assets that will fund the LLC). Here is a

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list of questions to use in the interview (some assume the trustee is a corporate trustee):

1. Does the FAPT corporate trustee comply with IRS reporting requirements? Is the trustee willing to work with the client's U.S. accountant?
2. What are the details regarding the trustee's indemnity insurance? What are the claim limits?
3. Can the trustee provide references, preferably attorneys they have worked with in the APT arena?
4. What is the process for the trustee to accept the trust? Will the trustee accept an affidavit of solvency prepared by the client's lawyer, or does the trustee have its own form? What other forms need to be completed (and get copies of such forms)? What are the trustee's Know Your Customer procedures?
5. Is the trustee willing to serve as a directed trustee and take direction from an investment advisor? Are there any restrictions on what type of assets can be held by the APT?
6. Will the trustee take direction from a trust protector? Is there any internal process undertaken before action is taken based upon the direction?
7. If a beneficiary exercises a power of appointment, what is the internal process to comply with the appointment?
8. How is the trustee fee determined? Is it a fixed fee or a percentage of the assets? What is included in the fee: review and acceptance of the trust? (Or is this a separate fee?) Maintenance of trust records? Trustee meetings and minutes? An annual audit? Is the fee paid annually or more frequently? What is the fee for the registration of an APT (if any — fairly common in FAPT jurisdiction), or is it included in the trustee fee? Does the trustee charge a fee if it is removed as trustee? Is there a termination fee should the APT be moved to another jurisdiction?
9. If the APT must be registered in the jurisdiction, will the trustee take on the responsibility of keeping the registration up to date (with fees paid from the APT)?
10. Is the trustee willing to prepare trust accounts as required by the terms of the trust? Are such accounts included in the trustee fee?
11. Disclose that you will be preparing the trust instrument. Ask if there are any provisions the trustee requires. Ask if the trust instrument will be reviewed by the trustee's local counsel and, if so, ask the trustee to provide the name and contact information of local counsel. Ask if the trustee has a sample APT to share with you. (Some do, some don't. Even if you have your own "master" APT form, you should still ask for a copy and see if there is anything you can use to improve your form!)
12. What is the trustee's experience with APTs? How many? What size?
13. Has the trustee ever had to defend an APT against a creditor?
14. What will be the internal governance structure of the trust? Who is the family's primary contact?
15. How will the trustee ensure continuity of service should someone involved with the APT move or retire?
16. How does the trustee protect against malfeasance?
17. How does a beneficiary ask for a distribution? How will the trustee exercise its discretion to make distributions to a beneficiary? Will the beneficiary have to provide any financial information?
18. How quickly can a beneficiary get a distribution?
19. How does the trustee educate the beneficiaries on the purpose of the trust and what to expect in terms of distributions and involvement in the business of the trust?
20. Is the trustee comfortable with a "letter of wishes"? How has the trustee used a letter of wishes in the past?
21. How does the trustee keep track of where a beneficiary lives?
22. How does the trustee keep the beneficiaries up to date with how the trust is performing?
23. Is there any information the trustee believes the client would find useful?

DISENGAGEMENT

Once the terms of the engagement have been fulfilled, and the APT has been formed and funded, it is recommended that you terminate the engagement in writing. Let the APT operate as any fully discretionary trust would operate. Do not get into the business of managing the beneficiary-trustee relationship. If the client wants a distribution, it is the trustee who should receive the request, not you. Where an FAPT exists, and the client would like your ongoing assistance with the multitude of IRS filing requirements, and you'd like to take this on, then this matter can be the basis of an independent engagement.

CONCLUSION

Whenever contemplating a new engagement in an area that you have not previously worked in, it is important to look beyond the excitement of a new challenge and determine if the engagement is really one you want to be involved in. Expanding one's practice into asset protection planning can be intellectually and financially rewarding but, as with every new venture, it is important that the decision is made thoughtfully and with full information. The truth of the matter is that not every client who wants an APT structure is going to be right for it — she may not have the necessary solvency, or she may not be able to live with the restrictions, or she may simply not have the liability risk that justifies the expense of an APT structure. Sometimes, the client just needs your counsel as to other protective steps that are more appropriate for her situation and that having an APT to keep up with the neighbors is just not the right plan for her. ■

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Note: This article is based on Melissa Langa's presentation and presentation materials for the 55th Annual Heckerling Institute on Estate Planning, "The Three Faces of Asset Protection," May 4, 2021, and a version of the article was published by Wealth Strategies Journal in November 2021.

TAXATION LAW

STATE AND LOCAL TAX (SALT) LIMITATIONS AND WORKAROUNDS

BY WILTON B. HYMAN

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I. INTRODUCTION

One of the more controversial and disruptive tax changes in the Tax Cuts and Jobs Act of 2017 (Pub. L. No. 115-97) was the limitation imposed on state and local tax deductions for individual taxpayers.[1] This change was controversial because it disproportionately harmed states and localities with high-income residents, particularly those states and localities that imposed higher income and property taxes, which fund government services, and are typically led by Democrats.[2] The change was disruptive because of the efforts made by states to provide workarounds so that their residents could avoid, or minimize, the impact of the limit on their previously unlimited state and local tax deduction.

This article will discuss § 164(a), and the changes made to it under the Tax Cuts and Jobs Act. It will then discuss the ways in which states have attempted to provide workarounds for their residents, to avoid the state and local tax limit. Finally, this article will discuss Massachusetts' recently enacted legislation, providing a tax workaround for owners of interests in pass-through entities.

II. STATE AND LOCAL TAXES

IRC § 164(a) allows taxpayers to deduct: (1) state, local and foreign real property taxes; (2) state and local personal property taxes;[3] and (3) state, local and foreign income, war profits, and excess profits taxes, for the taxable year in which they are paid or accrued, whether or not connected to a trade or business.[4] State and local taxes are taxes "imposed by a State, a possession of the United States, or a political subdivision of any of the foregoing, or by the District of Columbia."[5]

§ 164(b)(5) allows taxpayers to elect to deduct general sales taxes, in lieu of state and local income taxes.[6] State, local and foreign taxes not listed in those previous categories are also deductible, if paid or accrued in carrying on a trade or business or a profit-seeking activity under § 212.[7]

With the exception of state, local and foreign property taxes, paid in connection with a trade or business or profit-seeking activity,[8] deductions for state and local taxes (hereinafter "SALT") are itemized deductions[9] for individual taxpayers who elect to itemize rather than take their standard deduction.

The Tax Cuts and Jobs Act of 2017 (hereinafter "TCJA") added § 164(b)(6), which applies to individuals and disallows a deduction for foreign real property taxes, and limits the aggregate deduction for state and local real property and personal property taxes, and state and local income tax (or general sales tax, if elected), to a maximum of $10,000 per taxable year ($5,000 for a married taxpayer filing a separate return), for the 2018 to 2025 taxable years.[10]

The $10,000 limitation does not apply to an individual taxpayer's state, local and foreign real and personal property taxes, or to state and local sales tax, if paid or accrued in carrying on a trade or business or in connection with a profit-seeking activity under § 212.[11]

The TCJA nearly doubled the standard deduction for tax years 2018 through 2025,[12] and suspended the personal exemption for that same period of time.[13] The increased standard deduction was projected to reduce the number of taxpayers who itemized their deductions from approximately 46.5 million taxpayers in 2017 to just over 18 million taxpayers in 2018.[14] While the increased standard deduction simplifies the tax-filing process for taxpayers, the Tax Policy Center estimated that the percentage of taxpayers who would receive a tax benefit, or reduction in their tax liability, due to the SALT deduction fell from 25% in 2017, before the TCJA took effect, to 10% in 2018, as a result of the TCJA changes.[15]

III. THE CHARITABLE DEDUCTION WORKAROUND

Before the enactment of the TCJA, many states allowed taxpayers to make donations to "state governments or to state-government sponsored programs," entitling those taxpayers to a state tax credit, which reduced their state tax liability.[16] The taxpayer also received a charitable deduction for federal tax purposes, pursuant to § 170(a), for the full amount of the donation.[17] Those donations supported "natural resource preservation, private school tuition scholarships, college financial aid, shelters for victims of domestic violence," and other state programs.[18]

Due to concerns that individuals would use these tax credit programs to circumvent the § 164(b)(6) $10,000 limitation on state and local tax deductions through the use of § 170(a) charitable deductions, Internal Revenue Notice 2018-54 announced the Treasury Department and the IRS's intention to propose regulations to address the federal tax treatment of these programs.[19] On Aug. 27, 2018, Treasury issued proposed regulations providing that taxpayers who made a charitable donation and were entitled to a state or local tax credit as a result must reduce their charitable deduction under § 170(a) by the state or local tax credit, since it "constitutes a return benefit, or quid pro quo."[20]

The Treasury Department acknowledged the disadvantage imposed on taxpayers making a donation and receiving a state tax credit that reduced their federal charitable deduction, versus a taxpayer who paid their state tax liability in full and could deduct those payments pursuant to § 164(a).[21] To address this issue, the Department of Treasury and the IRS announced a safe harbor rule,[22] which allows individuals who itemize and make a charitable donation that entitles them to a state tax credit to treat the portion of the donation that is disallowed as a deduction under § 170(a) as a payment of state or local taxes for purposes of § 164(a), entitling them to the SALT deduction, subject to the $10,000 limit.[23] Treatment of the disallowed donation as payment of state and local tax under § 164(a) applies to the taxable year the donation was made, to the extent the state tax credit reduced the taxpayer's state tax liability, either in the year of payment or for the preceding year. If the state tax credit is not fully utilized to offset state tax liabilities for the taxable year in which the donation was made, or tax liabilities for the preceding year,[24] then excess credits carried forward to future tax years that reduce state tax liabilities may be treated as a payment of state or local taxes.[25] Finally, the safe harbor requires that the charitable contribution be

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cash or a cash equivalent.[26]

IV. THE PAYROLL TAX DEDUCTION WORKAROUND

Another means of circumventing the $10,000 deduction limit on state and local taxes is for states to increase payroll taxes paid by employers, and offset that tax increase either by reducing the revenues collected through state income taxes, or by providing an offsetting tax credit to employees.[27] Employers subject to the tax increase would deduct their payroll taxes as an ordinary and necessary trade or business expense under § 162(a),[28] and their employees' reduced after-tax income would be offset by the reduction in their income tax liability.[29]

This proposal raises concerns, including: (1) the reduction in employees' take-home pay, and how it would address preexisting fixed contract or compensation arrangements between employers and their employees; (2) the ability of the state to increase payroll taxes sufficiently to balance out reduced income tax receipts; and (3) the rise in payroll taxes increasing tax regressivity by imposing a disproportionate tax burden on lower-paid workers.[30]

V. INTERNAL REVENUE NOTICE 2020-75

Internal Revenue Notice 2020-75 announced the Department of Treasury and the Internal Revenue Service's intention to issue proposed regulations clarifying that partnerships and S corporations can deduct state and local income taxes in calculating their non-separately stated income or loss,[31] for the taxable year in which those taxes were paid, and thereby avoid the $10,000 limitation applicable to individual taxpayers under § 164(b)(6).[32] The entity-level tax also reduces the partner's distributive share and the S corporation shareholder's pro rata share of pass-thru income.[33] The proposed regulations apply to entity-level state or local tax payments made on or after Nov. 9, 2020, and also to tax payments made after Dec. 17, 2017, and before Nov. 9, 2020, if made pursuant to a law enacted prior to Nov. 9, 2020.[34]

IRC § 702(a)(8) requires that partners include their distributive share of partnership non-separately stated income or loss in calculating their taxable income. IRC § 1366(a)(1)(B) requires that S corporation shareholders include their pro rata share of S corporation non-separately stated income or loss in calculating their taxable income. Non-separately stated income or loss includes all income, gains, losses or deductions of the partnership or S corporation other than items that "if separately taken into account by any [partner or] shareholder could affect the [partner's or] shareholder's tax liability for that taxable year differently than if [they] did not take the item into account separately."[35] Non-separately stated items include ordinary income, gains, losses and deductions.[36]

The tax treatment announced in Notice 2020-75 is supported by Rev. Rul. 58-25, which involved a city ordinance that imposed an earned income tax on the net profits of unincorporated businesses and on city residents' shares of net profits from unincorporated trades or businesses.[37] Rev. Rul. 58-25 relied upon Regulation § 1.62-1(d), which distinguished between taxes "directly attributable to a trade or business or to property from which rents or royalties are derived," such as property taxes, which are deductible in computing adjusted gross income, as compared to taxes that are remotely connected to the trade or business, such as "State taxes on net income," which are treated as itemized deductions.[38]

Rev. Rul. 58-25 provides the basis for using the entity-level state or local tax payment in calculating the entity's non-separately stated income or loss, which is reflected in the partner's or S corporation shareholder's distributive or pro rata share of non-separately stated income or loss.[39]

VI. MASSACHUSETTS' PASS-THROUGH ENTITY WORKAROUND

On Sept. 30, 2021, Chapter 63D, titled "Taxation of Pass-Through Entities," took effect in Massachusetts. Chapter 63D applies to taxable years beginning on or after Jan. 1, 2021, and allows an "eligible pass-through entity," which includes S corporations, partnerships and LLCs that are treated as an S corporation or partnership for federal tax purposes, to elect to pay an excise of 5% on the pass-through entity's income that is allocable to and included in the taxable income of the partner, S corporation shareholder or LLC member.[40] The partner, S corporation shareholder or LLC member, referred to as a "qualified member," is allowed a refundable credit for the tax imposed under Chapter 63D, reducing their state personal income tax liability.[41] The credit is equal to the qualified member's proportionate share of the tax due and paid by the pass-through entity under Chapter 63D, multiplied by 0.9.[42] The credit is allowable for the qualified member's taxable year in which the taxable year of the pass-through entity ends.[43]

Chapter 63D does not apply to any taxable year in which the $10,000 limitation on state or local taxes under IRC sec. 164(b)(6) is not applicable, due to its expiration, or otherwise.[44]

The Chapter 63D excise is in addition to any other taxes applicable to the pass-through entity under Massachusetts law, and is due and payable on the entity's original filed tax return, at the same time as the partnership information return or a corporate excise return.[45]

Collection of the tax is subject to the administrative provisions of M.G.L. ch. 62C.[46]

The election by the pass-through entity to pay the excise under Chapter 63D is made on an annual basis, and is irrevocable for the year in which the election is made.[47] All partners, S Corporation shareholders and LLC members are bound by the election for the taxable year in which it is in effect.[48]

The commissioner of the Department of Revenue is required to issue regulations to provide guidance on complying with Chapter 63D, and that may also address: (i) the allowance of the credit to qualified members with income from eligible pass-through entities that also have income from eligible pass-through entities; (ii) Chapter 63D's applicability to estates and trusts; and (iii) required estimated payments of the Chapter 63D excise by eligible pass-through entities and their qualified members, consistent with Chapter 62B.[49]

VII. CONCLUSION

The SALT deduction limit under § 164(b)(6) added complexity to the tax code, and to state-level legislation, as the states attempt to provide workarounds to their residents. Keep in mind that § 164(b)(6) expires at the end of 2025, which raises questions as to what changes we should anticipate in the future. In addition, despite state attempts to provide workarounds for their residents, the relief provided by the workarounds is not applicable to all taxpayers who are impacted by the $10,000 deduction limit. ■

1. Other changes affecting individuals during the 2018-2025 tax years include: limiting the mortgage interest deduction on principal residences to $750,000 of acquisition indebtedness (instead of $1,000,000) incurred after Dec. 15, 2017; disallowing miscellaneous itemized deductions, such as unreimbursed employee trade or business expenses, tax preparation expenses and investment-related expenses; and limiting personal casualty losses,

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except in federally declared disasters. https://www.taxpolicycenter.org/briefing-book/how-did-tcja-change-standard-deduction-and-itemized-deductions.

2. Richard Rubin, "Democrats and Affluent Suburbs Join to Fight Tax-Break Cap," Wall Street Journal, June 25, 2019, at https://www.wsj.com/articles/democrats-and-affluent-suburbs-join-to-fight-tax-break-cap-11561503637?mod=Searchresults_pos1&page=1.
3. Personal property taxes are annual exactions imposed on personal property, based on its value. IRC § 164(b)(1). § 164(a)(3) allows a deduction for "state and local, and foreign, income, war profits and excess profits taxes."
4. H. Report No. 115-466 (1st Sess., 2017) 259. § 164(a)(4) also allows a deduction for generation-skipping taxes (GST) "imposed on income distributions."
5. § 164(b)(2).
6. General sales taxes are taxes imposed at a single rate, at retail, on a broad range of items, such as food, clothing and motor vehicles. IRC § 164(b)(5)(B).
7. IRC § 164(a).
8. IRC § 62(a)(1), (2), (4).
9. IRC § 63(b), (d), (e).
10. § 11042, Pub. L. No. 115-97; § 164(b)(6)(B) also includes state and local war profits and excess profits taxes, for purposes of the $10,000 limitation.
11. § 164(b)(6); "In the case of State and local income taxes, the deduction is an itemized deduction notwithstanding that the tax may be imposed on profits from a trade or business." H. Report No. 115-466 (1st Sess., 2017) 259.
12. IRC § 63(c)(7); H.R. 1, "Tax Cuts and Jobs Act," § 11021.
13. IRC § 151(d)(5); H.R 1, "Tax Cuts and Jobs Act," § 11041.
14. https://www.jct.gov/CMSPages/GetFile.aspx?guid=5ce9eb00-6770-497c-b637-05caf612a358, at 6.
15. https://www.taxpolicycenter.org/briefing-book/how-did-tcja-change-standard-deduction-and-itemized-deductions.
16. Kamin, Gamage, Glogower, Kysar, et al, "The Games They Will Play: Tax Games, Roadblocks, and Glitches Under the 2017 Tax Legislation," 103 Minn. L. Rev. 1439, 1477-1481 (2019); Charitable tax credits available in Massachusetts include donations of certified land to a public or private conservation agency, M.G.L. ch. 62, § 6(p) and M.G.L. ch. 63, § 38AA; and low-income housing tax credits, M.G.L. ch. 62, § 6I 1(a), (b)(4), (c)(1) and (c)(3). Bankman, et al, "Caveat IRS: Problems with Abandoning the Full Deduction Rule," 88 State Tax Notes 547, 573.
17. I.R. Notice 2018-54. "Under current law, a donor is not required to reduce the amount of a federal charitable contribution deduction by the value of state tax benefits generated by the gift," Bankman, et al, "State Responses to Federal Tax Reform: Charitable Tax Credits," 83 State Tax Notes 641-643.
18. Bankman, et al, "State Responses to Federal Tax Reform: Charitable Tax Credits," 83 State Tax Notes 641, 642.
19. 2018-24 I.R.B. 750.
20. 83 FR 43563; IRC reg. § 1.170A-(h)(3)(i). I.R Notice 2019-12, p. 3.
21. I.R. Notice 2019-12, p. 5.
22. I.R. Notice 2019-12, p. 6.
23. *Id.;* IRC reg. § 1.164-3(j)(1), (3).
24. IRC reg. § 1.164-3(j)(1).
25. IRC reg. § 1.164-3(j)(2).
26. IRC reg. § 1.164-3(j)(4).
27. Kamin, Gamage, Glogower, Kysar, et al, "The Games They Will Play: Tax Games, Roadblocks, and Glitches Under the 2017 Tax Legislation," 103 Minn. L. Rev. 1439, 1481 (2019); New York State recently enacted an optional payroll tax workaround for employers, "The Employer Compensation Expense Program," N.Y. Tax Law §§ 850-857.
28. Kamin, Gamage, Glogower, Kysar, et al, "The Games They Will Play: Tax Games, Roadblocks, and Glitches Under the 2017 Tax Legislation," 103 Minn. L. Rev. 1439, 1481 (2019).
29. *Id.* at 1482.
30. *Id.*
31. IRC § 702(a)(1)-(7), which applies to partners, and § 1366(a)(1)(A) both require partners and S corporation shareholders to report their distributive share of partnership tax items or S corporation tax items, respectively. Those sections require that certain partnership or S corporation tax items be separately stated, so they cannot be aggregated with other entity-level tax items before they pass through to the partners or S corporation shareholders, due to those items affecting partners and shareholders differently, based on their own individual tax circumstances. Examples of separately stated items include short-term capital gains or losses, long-term capital gains or losses, and charitable deductions, each of which may have a different tax impact to a partner or S corporation shareholder, depending upon whether they have offsetting capital gains or losses, or sufficient adjusted gross income, that would allow them to avoid tax on the gains, or to deduct the loss or charitable deduction.
32. I.R. Notice 2020-75, §§ 1, 3.02(3)-(4).
33. H.R. Rep. No. 115-466, at 260 n. 172 (2017).
34. I.R. Notice 2020-75, § 4.
35. IRC reg. § 1.1366-1(a)(2).
36. IRC § 64 defines "ordinary income" as including gain from the sale or exchange of property that is not a capital asset or sec. 1231 property, and IRC § 65 defines "ordinary loss" as including losses from a sale or exchange of property that is not a capital asset.
37. Rev. Rul. 58-25, 1958-1, C.B. 95.
38. *See* IRC Regulation § 1.62-1T(d).
39. I.R. Notice 2020-75, §§ 2.01(5), 3.02(3).
40. M.G.L. ch. 63D, §§ 1, 2. The technical term for the pass-through entity's income that is subject to the excise is "Qualified income taxable in Massachusetts," which is defined as "the income of an eligible pass-through entity determined under chapter 62 allocable to a qualified member and included in the qualified member's Massachusetts taxable income under said chapter 62." M.G.L., ch. 63D, § 1.
41. M.G.L. ch. 63D, §§ 1, 2. A "qualified member" includes a natural person, or a trust or estate subject to tax under § 10 of Chapter 62, and includes state residents, nonresidents or part-year residents. M.G.L. ch. 63D, § 1; Jason Zorfas, "Massachusetts enacts an elective tax on pass-through entities, Sept. 30, 2021, at https://taxnews.ey.com/news/2021-1775-massachusetts-enacts-an-elective-tax-on-pass-through-entities, Note 4.
42. M.G.L. ch. 63D, § 2.
43. *Id.*
44. M.G.L. ch. 63D, § 3.
45. M.G.L. ch. 63D, § 4.
46. M.G.L. ch. 63D, § 5.
47. M.G.L. ch. 63D, § 6.
48. *Id.*
49. M.G.L. ch. 63D, § 7.

VAS HOLDINGS V. COMMISSIONER OF REVENUE: TAXING OUT-OF-STATE ENTITIES ON THE SALE OF A MASSACHUSETTS BUSINESS

BY EVELYN A. HARALAMPU

WHAT WAS AT STAKE

At issue in a recent, significant tax decision of the Supreme Judicial Court (SJC) was whether the Massachusetts commissioner of revenue could tax an out-of-state shareholder on the gains it derived from the sale of a Massachusetts business. The out-of-state entity, VAS Holdings & Investments, LLC ("VAS Holdings"), had no business activity in Massachusetts other than its investment in Cloud5 LLC ("Cloud5"). Rather, VAS Holdings was structured as a tax pass-through, the main business of which was investment.

The Appellate Tax Board (ATB) sought to impose a Massachusetts capital gains tax on VAS Holdings based on a theory of "investee apportionment," which establishes a tax nexus to the commonwealth by the investment of an out-of-state shareholder in a Massachusetts business. The SJC rejected that theory and held that although "investee apportionment" is constitutional, the ATB had no statutory basis for asserting it to tax the capital gains of VAS Holdings.

DIFFERING TAX THEORIES

The ATB acknowledged that VAS Holdings had no integrated business with Cloud5 and asserted an alternate theory for finding tax nexus. Instead, the ATB found nexus for taxation based on the out-of-state shareholder's realization of the economic benefits and protections derived from Massachusetts when it sold its share in the Massachusetts business.

VAS Holdings countered that the only principle Massachusetts could use to tax it was the "unitary business principle." Under that principle, an out-of-state entity may be taxed by Massachusetts if it is functionally integrated with a Massachusetts entity, sharing central management and economies of scale with it. Absent a "unitary business" with a Massachusetts entity, an out-of-state entity cannot be taxed because no state statute supports the apportionment of Massachusetts tax to an out-of-state entity based only on its in-state connections.

THE SJC DECISION

The SJC noted that "investee apportionment" passes muster under the due process and commerce clauses of the U.S. Constitution because it establishes an appropriate nexus between an out-of-state investor and a sale of a business within the state. However, the SJC rejected the ATB assertion that it had the power to tax VAS Holdings under "investee apportionment" in the absence of any Massachusetts statute supporting it. Rather, the SJC took the position that the ATB had overstepped its authority by asserting a theory that the Legislature had never adopted. Massachusetts, under M.G.L c. 62 s. 32B, taxes out-of-state businesses only on a unitary business principle.

Citing Massachusetts case law in support, the SJC stated that no method of determining tax liability is valid unless authorized by statute and executed in accordance with its terms. The Legislature, and not the taxing authorities of Massachusetts, establishes tax policy and the mechanics of taxation.

TAX POLICY AND THE LEGISLATURE

The Massachusetts Legislature has made the policy decision that unless an out-of-state business is so tied to an in-state business as to establish a unitary function, management, and economies of scale, capital gains from the sale of the in-state business cannot be taxed by Massachusetts to the out-of-state business. Such a policy can favor Massachusetts startups and other businesses by allowing them to attract out-of-state business investors that are free of Massachusetts capital gains taxes once the Massachusetts business is sold. Massachusetts, in turn, reaps the economic benefits of such enriched, in-state businesses without necessarily eroding its tax base, as profitable, ongoing businesses and higher employment rates contribute to income tax collections within the commonwealth. ■

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YOUNG LAWYERS DIVISION

A LANDMARK VICTORY FOR MASSACHUSETTS CONSUMERS: THE SUPREME JUDICIAL COURT PROVIDES RECOVERY FOR LOSS IN VEHICLE VALUE TO CAR ACCIDENT VICTIMS

BY ROBERT J. HARTIGAN

On Oct. 19, 2021, the Massachusetts Supreme Judicial Court (SJC) released its decision in the case of *Jarrett McGilloway & another vs. Safety Insurance Company et al.* The ruling is a victory for consumers whose motor vehicles were damaged and repaired following a collision where another party was at fault.

When a vehicle is damaged in a motor vehicle collision, it suffers a loss in value (and resale value), even after that vehicle is fully repaired. This concept of loss in value is known as diminished value, or inherent diminished value (IDV). Although IDV damage has been a well-known term in the automobile industry for years, impacting hundreds of thousands of car owners, it was not a recognized or recoverable damage here in Massachusetts — at least not until the recent victory at the SJC by attorney Kevin J. McCullough, a founding partner at the law firms of Mazow/McCullough PC and Forrest, Mazow, McCullough, Yasi & Yasi.

The fight in *McGilloway* focused on, among other issues, whether or not IDV damages are recognized here in Massachusetts, and whether or not those IDV damages were covered under Part 4 of the 2008 edition of the Standard Massachusetts Automobile Insurance Policy.

After working its way through the Suffolk Superior Court, the case was heard at oral argument at the SJC on May 5, 2021. In a resounding, unanimous (all seven justices agreed) decision, the SJC held that IDV is a recognized damage and covered under Part 4 of the 2008 edition of the Standard Massachusetts Automobile Policy.

One of the defendants, Commerce Insurance, argued that by allowing consumers to pursue IDV damages, the court would "cause a seismic shift in the insurance marketplace" and "economically destabilize the insurance marketplace". *McGilloway.* The SJC rejected that argument. Commerce also maintained that IDV damages would be almost impossible to calculate:

> At oral argument, counsel for Commerce also argued that IDV damages are "very difficult, if not impossible" to calculate with regard to vehicles. However, as the motion judge noted, Safety "admits that IDV may be suffered in some cases" and "concedes" that IDV may be quantifiable." Moreover, as discussed *supra*, numerous other States recognize and permit recovery of IDV damages. Accordingly, we are not persuaded by Commerce's arguments here.
> *McGilloway*

As stated in the SJC's decision, for years, other states have recognized IDV damages in the context of automobile property damage. *See, e.g., American Serv. Ctr. Assocs. v. Helton,* 867 A.2d 235, 243 (D.C. 2005) (claim for property damage to motor vehicle caused by collision with another vehicle; "when a plaintiff can prove that the value of an injured chattel after repair is less than the chattel's worth before the injury, recovery may be had for both the reasonable cost of repair and the residual diminution in value after repair, provided that the award does not exceed the gross diminution in value"); *State Farm Mut. Auto. Ins. Co. v. Mabry*, 274 Ga. 498, 508-509 (2001) (insurer required to pay claimant IDV damages under insurance policy where vehicle suffered IDV following repair); *Papenheim v. Lovell,* 530 N.W.2d 668, 672 (Iowa 1995).

Although the legal issue was recently addressed by the SJC in the *McGilloway* case, for years, Massachusetts consumers have been disappointed when finding out the value or resale value of their vehicle(s) following a collision and repair of the applicable damages. In fact, an entire industry has developed from the concept that damaged and repaired vehicles suffer a loss in value, including CARFAX and other similar companies tracking the history of a motor vehicle. In the past, most consumers were unaware of this damage and loss in value until after it was too late to try to recover the damage. Further, for the consumers who were actually mindful of the concept and knew that their respective vehicles had decreased in value post-collision and repair, the motor vehicles insurance companies in Massachusetts were refusing to pay those claims and/or for IDV damages.

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The SJC decision is consistent with the long-standing legal principle that an injured party is entitled to be made whole. The "made whole doctrine" recognizes that a tort victim has a fundamental right to be made whole, and fully compensated for all damages.

So how does a car accident victim pursue a claim for IDV damages? First, the victim should obtain a copy of any police reports, vehicle damage appraisals, and photographs showing the damage that was caused. Additionally, they will need to show the vehicle's loss of value. IDV damages are readily determinable through a utilization of an appraisal report and the National Automobile Dealers Association (NADA) guidebook. One method of calculating IDV damages is by subtracting the NADA rough trade-in value from the NADA clean retail value. After the individual gathers all of that information, they can then send a demand to the third-party insurer for settlement of the IDV claim.

McGilloway is an extremely significant decision here in Massachusetts because the law now allows car accident victims a chance, and the ability, to recover the loss in market value of their vehicle following a collision and repair, which is a tremendous win for Massachusetts consumers. ■

THE VALUE OF AN ASSOCIATE FOR TRIAL

BY NICOLE J. COCOZZA

We all know as litigation attorneys that trials are time-consuming and expensive and require substantial preparation. In the months leading up to trial, an associate can add significant value to the trial team. The associate should have a more in-depth understanding of the law and facts to help prove claims and defenses and evaluate damages at trial, as associates most of the time have done the case's day-to-day tasks, such as drafting written discovery responses, reviewing documents and performing legal research. I have been fortunate in my career to have been a part of several firms that included me as a trial team member. Most recently, I was part of a trial team in my first federal court case, where I took on multiple roles. Below are what I believe are the six most important benefits of having an associate for trial.

1. **Be the Trial Team Coordinator:** Partners are busy during the final stages of the case, and your role should be to guide the partner to trial. Your role should include making a task list of assignments that need to be done before trial. The list needs to include deadlines, motions to be filed, witness outlines, documents to be marked as exhibits, demonstrative aids, and practical items such as supplies needed. You should assign a team member to each task and review the list regularly to make sure nothing is forgotten. You should volunteer to take on any and every task no matter how big or small.
2. **Be a Know-It-All:** Read everything — depositions, pleadings, exhibits, key cases and significant court rulings. You need to have a strong grasp of the facts that support your case and the facts that impact your case. Remember that the complaint and answer establish the burden of proof at trial. You need to be the expert in the allegations, the evidence and the law.
3. **Become an Expert on Documents:** There is a good chance that you have already been involved with the initial stages of discovery, including document responses. Review the documents that have been produced in discovery by making a detailed chart of relevant documents to be used as trial exhibits. You should highlight the following in the chart: (1) the content of the document, (2) who produced the document, (3) where and when the document was used during the litigation, (4) authors of the content, (5) admissibility of the document to prove or defend the case, and (6) the reasons for non-admissibility of documents that the opposing side intends to introduce. You should ensure that all documents are easily identifiable with bates numbering, which will make it easier searching for documents. At this stage, you should master the rules of evidence before trial. An associate who is also familiar with all the documents may be asked to take a last-minute trial deposition or defend an expert deposition. You can also add value if you can easily locate key documents for cross-examination of a witness at trial and on redirect examination of your own witness.
4. **Become an Expert on Legal Issues:** You need to think through every stage of the trial — you will want to familiarize yourself with the most recent case law pertaining to the claims and defenses at trial. You should start by reviewing the jury instructions to become familiar with the claims and defenses. You then should start making a list of any legal issues for trial that can be developed into motions in limine — which you should take the initiative to write. If you have mastered the law and are well prepared, you will often be given the opportunity to argue legal issues that may arise at the final trial conference or during trial.
5. **Take the Contrarian View:** Your role should also involve challenging assumptions and taking the contrarian view. You should present alternate perspectives for the trial team to consider that will encourage them to explore solutions that they had not previously considered. Presenting alternatives well in advance can become most helpful while preparing for cross-examination of a witness.
6. **Understand Courtroom Technology:** Visit the courtroom well in advance to identify practical or technical issues. There will be courtrooms that have the latest technology while others do not. Make sure you know how to use the technology available and address any other practical issues in advance of trial. Reach out to the courtroom clerk to set up a time to assess the courtroom technology. You may need to schedule more than one visit to access and walk through the courtroom technology that you will be using for trial. You should also have the lead trial attorney visit the courtroom to show them how the technology works and how an exhibit will look depending on the technology used, such as a projector or television — the fewer surprises, the better.

Associates are a vital part of any trial team. More firms should be giving associates the opportunity to get involved with trial. As an associate, you should feel confident knowing you have put in the effort preparing the case for trial. Indeed, the last few weeks are consumed by motions in limine, witness preparation, trial briefs, cross-examination role-play, and rehearsal and refinement of opening and closing arguments. The reason you should be second chair for this trial is that you know the facts and law as well or better than anyone on the trial team. Associates need to make an appeal to their partners as to why they should have a seat at counsel's table on trial day. ■

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VIRTUAL LITIGATION: A MEANS FOR INCREASING DIVERSITY, ACCESS TO JUSTICE AND ATTORNEY WELL-BEING

BY PETER CHANDLER

Stating the obvious: Attorneys, particularly younger attorneys, prefer virtual legal practice for routine matters. The legal profession, for far too long, has been slow and recalcitrant to adopt beneficial technology. I am young enough to remember being taught the (then) "benefits" of Word Perfect — a once-upon-a-time competitor with Microsoft Word, except not compatible, like Word, with every other computer in the country. In fact, at least in New York, despite Microsoft Word being a ubiquitous, built-in computer program, Word Perfect was *the* legal document application for quite some time.

For whatever reason, the legal industry generally lags behind other industries by what often seems like decades. A perfect example of this is e-filing. Back in 1986 (i.e., 36 years ago), even the IRS, not exactly known for efficiency, was test piloting the e-filing of tax returns. Yet, e-filing of legal documents remains a sporadic occurrence throughout the country, despite its obvious benefits. In every other industry, slow adoption of relevant, time-saving and cost-effective technology results in extinction.

Much is said about the systemic issues facing the legal industry, yet almost nothing is said about how utilizing technology in litigation can assist in diversifying our legal industry, increasing access to justice and boosting attorney well-being. At the outset, the use of technology makes legal practice more cost-efficient, which opens justice up to a broader pool of people. As technology advances, the cost of litigation generally trends downward, and the lifespan of the average case shortens. The end result is quicker and more affordable justice, a broader consumer base and an increased awareness of our profession.

Use of technology also greatly eases the burden of participation. Any attorney faced with mobility issues has myriad challenges in today's practice. Just think about the oldest courtroom you have been in — not exactly a user-friendly place. Not long ago, I remember being in a Brooklyn courtroom, watching an attorney in a wheelchair forced to shout, from the hallway, because he physically could not get inside the courtroom for a simple compliance conference. This is appalling and beneath the dignity of the legal profession. There is a simple solution: videoconferencing.

Nor is this something that impacts just attorneys with disabilities. Many plaintiffs have experienced significant, mobility-impairing injuries. Yet, these same individuals will get dragged into in-person depositions. There, in a foreign location, they sit in an uncomfortable chair, reliving a life-altering trauma, as they field question, after question, after question for hours on end. All so the defense attorney can "get a feel for who they are as a person." This has become an untenable justification. If the pandemic has taught us anything, it has been how to "get a feel" for someone virtually. Again, a solution squawks at our profession: videoconferencing.

In line with driving costs down and easing the burden of participation, the use of technology keeps at the forefront the customer experience. After all, attorneys, at bottom, represent and primarily deal with actual people. The general populace does not lawyer for a living. As such, all litigation that they must personally attend to is a disruption to, and not a part of, their daily lives. It takes them away from their work, their families and friends, or their medical treatment.

Thus, when anyone gets noticed or subpoenaed for an in-person deposition, this imposes unwanted planning upon them: work must be taken off, children must be accounted for, transportation must be obtained, and on and on. All of these disruptions, it goes without saying, also cost money (e.g., lost income, child care, travel, etc.). And, frequently, the individuals who end up being forced to attend in-person events *need* that money for other things. This is even worse if the individual does not live near the relevant attorney-picked location, which is often the case. Somehow this has been allowed to be the norm, despite the legal industry's apparent drive for diversity, inclusion and increased participation. A glaringly obvious solution can ease this burden: videoconferencing.

Our failure to maximize the use of pertinent technology, particularly for routine matters, also results in a great disservice to attorney well-being. Videoconferencing frees up attorneys, who would otherwise be forced

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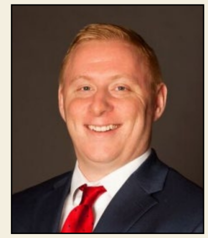

to travel or sit silently in a courtroom waiting to be called, to do more essential and valuable legal work. Non-party witness depositions and routine court appearances should be done via videoconferencing. The idea that attorneys are regularly required to waste several waking hours — the monetary burden of which either gets shifted to the client in the form of increased legal fees or eaten as a loss by the practitioner — attending required, momentary and often inconsequential events is a market inefficiency that would not be tolerated in any other private industry.

And that is why institutional clients have, increasingly, begun to slash attorney travel time. This results in dead time for attorneys, rendering their work unprofitable and essentially free. Attorneys (at least the ones billing by the hour) must then expend even more time at the office — away from their family and friends and other pursuits — to make up for an easily avoidable non-billable event, just to meet their annual billing quota. This is a perfect example of a headache that drives individuals away from or out of the legal profession, which results in less overall diversity, diminished access to justice, and discontent within the profession.

If the legal industry wants to have a frank discussion about diversifying its ranks, giving all individuals equal access to the legal system and improving attorney well-being, it needs to take a cold hard look at the systemic issues that make participation painful for practitioners, its consumer base and the public writ large. As Massachusetts continues to open up, I hope, possibly naively, that more virtual work will be adopted by practicing attorneys for the sake of our profession's future and the justice seekers we represent. ■

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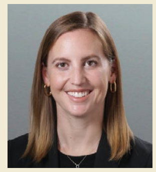

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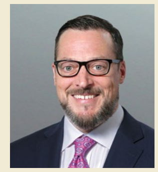

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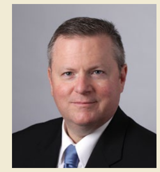

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