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Responsibility for Oil Spills

New York has a "strict liability" statute under which the party who is legally considered to be the "discharger" of fuel oil is financially responsible for the cost of the clean up regardless of fault or negligence.

When an oil spill occurs, there is an obligation to report the same to the New York Department of Environmental Conservation which will investigate the matter and determine the extent of the problem - specifically whether or not the oil has penetrated into the soil and/or into the water supply and, if so, to what level.

If the responsible property owner engages affirmatively a clean-up company and directly pays for that clean-up, there is no further involvement by the State other than to confirm that the clean up has been done properly and completely. However, it is often the case that the landowner does not clean up the property. In such a case, New York State DEC will employ and pay for the contractor to appropriately clean up the land and then sue the property owner for reimbursement. The State's highest court in State v. Speonk Fuels, 3 NY3d 720, recently ruled that the discharger is not entitled to a hearing as to whether or not the State's incurred costs were reasonable. That holding has been upheld as not violating any constitutional right of the discharger. In a further case, State v. Neill, decided in April, the Appellate Court in Albany held that after the landowner cleaned up the oil discharge on his property and the State requested that he engage in a further testing of soil on land adjacent to the property and the landowner declined, the State could do so and recover its investigative and monitoring costs, even though ultimately no discharge of petroleum products was found off of the site. The court held that the reimbursement by the discharger of oil, even for a negative testing process, was covered by the strict liability provisions of the statute. The lesson here is that when dealing with the State DEC, immediately cooperate and try to retain contractors on one's own to keep the price down. because the State has no motivation to do so, as it will successfully recover whatever cost the contractor charges the State.

Finally, in a decision by the State's highest court, Southroad Associates v. IBM, when the dispute is between the landlord and a tenant, unless the lease provides that the tenant is required to return the land to its pre-lease condition at the end of the term of the lease, the use of the phrase "premises" will not impose upon the tenant the requirement to do anything other than comply with the governmental cleanup orders. In this case, IBM had met the government standards, but the landlord asserted that the soil, bedrock and ground water met pre-contamination conditions. The court rejected the landlord's claim against IBM because the natural meaning of the word "premises" referred only to buildings.

A landlord should use more precision in a lease if he or she wants to hold a tenant responsible for ground conditions at the end of the term of the tenancy. ■

NEWS OF THE FIRM

*We are pleased to welcome **Chirag Kabrawala** as an Associate of our firm. He is a graduate of the University of Miami and Nova Southeastern University Law School. He previously worked as an attorney in the nationwide accounting firm of Deloitte and Touche, specializing in international tax. He also has a strong background in business law. His fiancée is a surgical resident at Albany Medical Center. He is providing strong support for the business and tax departments of our practice.* ■

***Andrea Sibincich** has been promoted from receptionist/collection paralegal to full time real estate paralegal. Karen Nosal, who had previously been our part-time file clerk, is now our full-time front desk receptionist and collection paralegal.* ■

***Jed Wolkenbreit** became a grandfather in June for the second time, when his daughter Randi gave birth to Ryan Samuel Singer.* ■

***Robert Ganz** was re-elected in July as President of the Guilderland Public Library.* ■

Family Limited Partnerships and Family Limited Liability Entities as an Estate Planning Tool

A series of recent cases has both revitalized the usage of family limited partnerships ("FLP") and family limited liability companies ("FLLC") and underscored the need to conform to the letter of the law when utilizing such vehicles for wealth transfer planning techniques.

Estate planners frequently utilize FLPs and FLLCs to assist in family wealth transfers. Among the many advantages offered by these entities are the following: a method for reducing the size of your taxable estate while at the same time allowing you to retain full control and management of your estate; a way to effectively compound your available gift and estate tax credits and exemptions; and a way to spread income among children who are in lower tax brackets.

(1) Retain Control Over Assets

Assets can be transferred to a limited partnership without losing control of those assets, to the extent desired. In the context of a limited partnership, a general partner has responsibility for management of the partnership and limited partners or non-voting members who have limited liability generally have no management responsibilities. The general partner retains control even if he retains only a minority interest. Even as little as a one percent general partnership interest gives the general partners 100 percent control.

One advantage of an FLLC over a FLP is that an FLLC provides limited liability to all of its members, not just the limited partners. Another advantage an FLLC has over a FLP is that all of the voting members can participate in the management of the FLLC without losing their limited liability status. Whereas, in a FLP, only the general partners can participate in the management of the business.

(2) Gifts of FLP and FLLC Interests

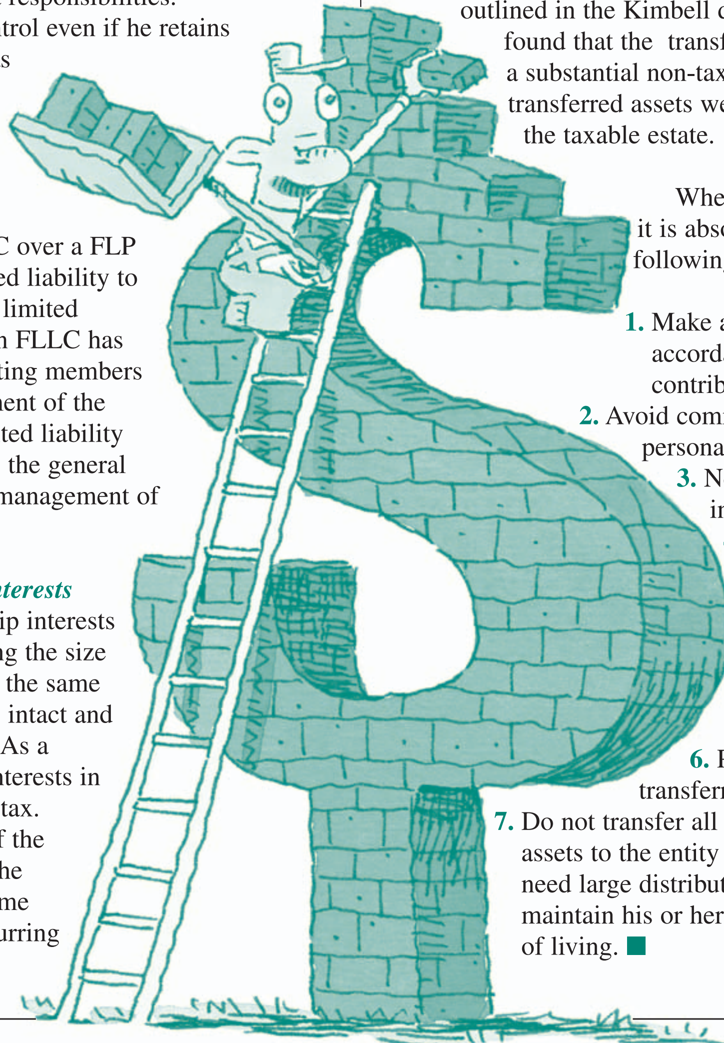
Lifetime gifts of partnership interests are an excellent way of reducing the size of your taxable estate, while at the same time keeping certain properties intact and under your continued control. As a general rule, lifetime gifts of interests in property are subject to the gift tax. However, through utilization of the annual gifting exclusions and the unified credit, substantial lifetime gifts may be made without incurring this tax.

The tax savings achieved through lifetime gifting can be further compounded through the use of valuation discounts. There are two types of valuation discounts available. The first, the minority discount, is applicable where a gift of a minority interest in a closely-held business is made. The minority discount is based upon the fact that the lack of control in a closely-held business reduces the value of the minority interests. The other valuation discount is the discount for lack of marketability. Because partnership interests are not listed on a securities exchange, there is no ready market for the partnership interest. Marketability discounts of up to forty or fifty percent are often found acceptable by the courts (although the IRS may challenge them).

(3) Recent Caselaw

A recent case has revitalized the usage of FLPs as a wealth transfer technique. In Kimbell v. United States, the Court held that objective factors should determine whether a family entity is legitimate and should be respected for estate tax valuation purposes. Until the United States Supreme Court finally resolves the issue of valuation with regard to family limited liability entities, there can be no absolutes in how the IRS will respond to such entities when a valuation discount is claimed for federal estate tax purposes.

In a recent decision, Estate of Strangi v. Commissioner, the United States Court of Appeals reinforced the principles outlined in the Kimbell decision. In Strangi, the Court found that the transfer of assets to an FLP lacked a substantial non-tax purpose and, accordingly, the transferred assets were properly included within the taxable estate.



When creating an FLP or FLLC, it is absolutely vital to do the following:

1. Make all distributions of income in accordance with capital contributions.
2. Avoid commingling entity assets with personal assets.
3. Never put a personal residence in a family business entity.
4. Comply with all terms and formalities of the operative agreement governing the entity.
5. Place active operating assets in the entity.
6. Properly title all assets transferred to the entity.
7. Do not transfer all of the older generation's assets to the entity such that the person would need large distributions from the entity to maintain his or her standard of living. ■

Employment Discrimination is Expensive

While courts are often employer oriented in preliminary aspects of employee related discrimination cases (often dismissing portions of claims or granting summary judgment if the Plaintiffs cannot put forth an adequate case), if the cases go to juries, the results are most often in favor of the employee claiming discrimination.

The jury awards can be very substantial. According to a study by Jury Verdict Research, Inc., the following are the size of different types of verdicts in the Northeastern portion of the United States.

Liability	Award Median	Probability Range	Total Range	Award Mean
Age Discrimination	$375,790	$156,094-$948,750	$419-$7,000,000	$816,080
Disability Discrimination	420,300	170,000-674,850	4,567-1,707,000	484,646
Race Discrimination	94,403	48,000-462,500	8,000-3,200,000	412,660
Sex Discrimination	210,000	58,626-637,500	1-12,670,000	868,743
Discrimination Northeast Region, Overall	260,000	74,972-575,000	1-12,670,000	678,043

The different types of discrimination claims which are successfully brought are heavily weighted in four areas: Sex (36%); Age (22%); Race (18%); and Disability (15%). Other types of discrimination are rarely brought: Religion (2%); Pregnancy (3%); and National Origin (4%).

The lesson should be clear. Each employer should take all necessary measures to create a workplace which is free from discriminatory actions so that it does not find itself in front of a jury wondering about what the size of the verdict in favor of the discriminated employee will be. ■

What We're Up To

Rob Ganz completed a four year piece of litigation with an eve of trial settlement involving a minority shareholder's claim of fraudulent concealment in the acquisition of his shares by the majority shareholder. ■

Dave Siegfeld is involved in a Binghamton real estate transaction involving 21 separate properties on behalf of a downstate investor. ■

Rick Friedman is handling numerous tax assessment challenges and other real estate leasing and rehabilitation transactions in the downtown core areas of Albany and Cohoes. ■

Jed Wolkenbreit continues to grow our New York City practice in the areas of corporate representation, real estate and physician representation. ■

Chirag Kabrawala is providing tax and business planning support to our firm's clients and recently handled an asset sale for one of our client's manufacturing businesses. ■

LLC, C Corp, S Corp– How Do I Decide?

Anyone starting a new business will be faced with the decision about what form of business enterprise he or she should use.

Our answer is to initiate an analysis of various personal, business and tax factors to hopefully come to the one "right" conclusion. We have prepared a more detailed analysis which you may request from our office, but here is a short summary of some of those factors.

1. Formation Requirements. A Sole Proprietorship is simply one person doing business. There are no formal requirements except that New York requires the filing of a certificate of doing business. It does not create a separate entity and gives no name protection.

A general partnership usually has no formal registration requirements. It may be established informally without a written agreement (although better form certainly is to have a formal written agreement). A limited partnership, as a creature of a State statute, must observe certain formalities. In addition, the partnership must follow the organizational requirements imposed by that State. Similarly, a limited liability company must file its articles of organization with the State, and must comply with State requirements that are a condition of its limited liability status.

Of the major forms of business, C and S corporations have the most burdensome requirements regarding formalities of existence. These requirements reflect the fact that a corporation is a separate legal entity from its owners. A corporation must file a certificate of incorporation with the Secretary of the State in the jurisdiction of organization. It must also adopt bylaws, elect a board of directors, hold organizational meetings, and keep minutes thereof.

Partnerships and LLCs are both relatively simple to administer. Corporate governance provisions may be more complicated. On the other hand, partnerships and LLCs are usually more complicated from a tax point of view.

If the new company is to have investors, they often want some say in the management of their investments.

In some cases, investors may be more comfortable with a corporation, simply because State law covering corporate governance is better known and understood than the governance of LLCs. Investors may prefer predictability to other advantages an LLC may offer.

2. Tax Aspects of Formation When a C or an S corporation is formed, the owners generally contribute property or services to the entity in exchange for stock. If property is contributed, the owners do not recognize gain on receipt of the stock, provided they are in control of the company.

The tax consequences of forming a partnership or a limited liability company taxed as a partnership are similar to those governing corporate formation. A contribution to the entity in exchange for an ownership interest is generally not a taxable event. However, the partnership nonrecognition rules are more liberal than the corporate rules.

A partner (or LLC member) who contributes services in exchange for a partnership interest generally recognizes gain equal to the value of the interest received. However, if the partner receives only a right to future partnership profits as opposed to a capital interest, then no gain is recognized.

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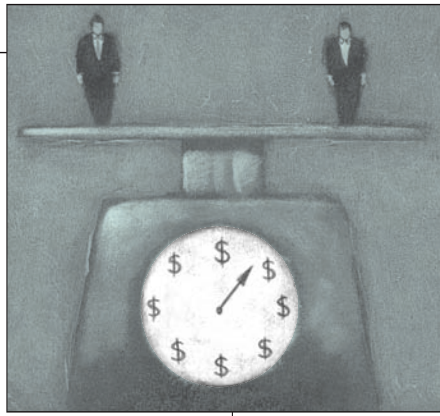

3. Limited Liability of Owners In general, the owners of a C or an S corporation are not personally liable for the entity's obligations. However, an owner who guarantees a debt or commits a tort while acting on behalf of the entity may lose this protection. This protection may also be lost if the corporate veil is "pierced." This can occur if the entity either is poorly capitalized or fails to maintain a separate identity from its owners. A limited liability company also provides its owners with limited liability.

Unlike a corporation or limited liability company, a sole proprietorship or a general partnership does not afford its owner's limited personal liability. The owners are personally liable for partnership debts and for the acts of fellow owners performed in furtherance of partnership business. General partners in a limited partnership have the same type of personal liability as do their counterparts in a general partnership. However, the liability of limited partners who do not manage the business is limited to the extent of their respective investment in the enterprise.

4. Taxation as Separate Entity versus Pass-Through Entity One of the biggest factors affecting the choice of entity decision is whether the entity should be taxed as a separate entity or whether its items of income, credit, loss, and deduction should pass through and be reported by the owners on their personal tax returns. C corporations are taxed as separate entities. One disadvantage to a C corporation is that its earnings can be taxed twice.

S corporations, partnerships, and limited liability companies taxed as partnerships provide pass-through treatment. In general, there is no entity-level tax, so the earnings are only taxed once—at the owners' marginal rates. Unlike S corporations, partnerships permit special allocations of tax attributes provided such allocations have substantial economic effect.

5. Owner Compensation An owner of a C corporation can be compensated through salary, fringe benefits, pension and profit sharing plans, and dividends. Nonliquidating distributions to shareholders are dividends to the extent of corporate earnings and profits. The excess is treated as a return of capital. Salaries, to the extent they are reasonable in amount, are effectively taxed only once (as income to the owner) because they are deductible by the entity. Most types of fringe benefits and pension and profit sharing plans receive tax-favored treatment in that they can be funded with pre-tax dollars and often do not generate current income to the recipient.

Because S corporations, partnerships, and limited liability companies taxed as partnerships are pass-through entities, each owner is allocated a share of the entity's income and other tax attributes based on the owner's ownership interest. These items are then reported on the owner's individual return.

6. Fringe Benefits A C corporation has the greatest ability to provide fringe benefits on a tax-favored basis. Such benefits can include life insurance (with limits), health insurance, certain death benefits, and meals and lodging in limited circumstances. In addition, contributions by the corporation to a qualified pension plan may also be deductible when made but not currently taxable. The corporation can also set up a cafeteria plan to let employees pick and choose fringe benefits. This flexibility is much greater than that afforded partnerships and S corporations.

In general, a partnership or a limited liability company may deduct the cost of providing the benefit, but the owners must include the value of such benefit in income. This same rule applies to any shareholder in an S corporation who owns at least 2% of the corporation's stock.

7. Flexibility Partnerships and LLCs are far more flexible than corporations in current allocation of profit and loss. This flexibility can be a plus in situations where, for example, a cash investor can currently use losses and is willing to bear the burden of a rapidly diminishing capital account. An S corporation, on the other hand, has almost no flexibility in allocating losses to its shareholders.

8. Raising Capital Capital can be raised from venture capitalists by both partnerships, LLCs, and corporations. Investors may want to receive a priority interest in the entity's assets, in the case of liquidation. For a corporation, this usually means the investors are issued preferred stock, or convertible preferred stock, while the founders and employees receive common stock. The existence of two levels of stock immediately rules out the use of an S corporation.
A partnership or LLC can build provisions into its articles of organization giving certain partners or members preference in liquidation.

One advantage of the partnership or LLC is where equity is issued for services. A service provider can ordinarily receive a profits-only interest tax-free. A person receiving stock for services, on the other hand, is taxable, unless the stock is not vested.

Another issue to consider is the difficulty and expense associated with bringing in new investors. If a partnership or LLC is used, then each time a new investor comes on board the partnership or LLC agreement must be modified. This makes issuance of small amounts of equity relatively costly. New investors might be from outside, or they might be employees who are compensated with equity. A corporation (either C or S) is a much more viable choice if a number of sales of equity are envisioned.

9. Dispositions In considering an entity choice, it is necessary to consider the entire life cycle of the business. If an entity will eventually be merged into another entity, then the corporate form is necessary to make the merger tax-free. A partnership or LLC that elects treatment as a corporation can also be acquired tax-free. However, there is less flexibility than if a natural corporation is used. If the entity is disposed of at a loss, then a corporation that issues §1244 stock gives investors an ordinary loss versus a capital loss. ■

DISCLAIMER Actual resolution of legal issues depends upon many factors, including variations of facts and the application of such facts to state and federal statutory and common law. This Newsletter is not intended to provide legal advice on specific subjects, but rather to provide insight into legal developments and issues. The reader should always consult with legal counsel before taking action on matters covered by this Newsletter.