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The Seller's Concession

By Jeanine Garritano Wadeson, J.D.
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The proliferation of real estate programs on television networks such as HGTV has led to a relatively new phenomenon in New York real estate practice: when negotiating contracts with their realtor or attorney, home buyers will often ask:

"How much will the seller contribute toward our closing costs?"

In reality, sellers **rarely** contribute money towards a buyer's closing costs. Rather, the typical arrangement involves a **"seller's concession"**, a method of determining a higher contract price for the purchase and sale of real property that allows buyers to increase their mortgage loan amount to cover the expense of their closing costs.

(continued on page 2)

(continued from page 1)

In a standard transaction, for example, when a buyer offers to pay $250,000 for a parcel of real property, the bottom line net price a seller receives is exactly that: $250,000.

When a transaction is structured with the use of the seller's concession, the "contract sales price" will be increased by as much as 6%. The contract will then provide for a seller's concession equal to that 6% figure, resulting in the same "net to seller" price of $250,000.

So in our example above, the contract would be signed at a purchase price of $265,958, with a seller's concession of $15,958 and a net amount to the seller of $250,000.

Seller's concessions can have significant benefits for home buyers. They are a useful tool for the purchaser who perhaps does not have enough cash reserves to pay closing costs out-of-pocket at closing. Or, for the purchaser of a "handyman special," using a seller's concession to have the mortgage loan proceeds cover closing costs allows the purchaser to retain precious funds in his or her bank account to fund renovations. **The potential detriments of a seller's concession to a buyer, however, can be significant and far-reaching.** Assuming a standard mortgage rate of 3.5% and a 35-year term, amortizing the $15,958 of closing costs over the life of the loan ends up costing the buyer significantly more money in the long-run.

In addition, assuming a 100% financing transaction, the buyer walks out of the closing owing $265,958 on a property that he really is only buying for $250,000. The bursting of the real estate bubble in the past decade should act as a cautionary tale to a buyer who is perhaps entering into a transaction that is too far beyond their financial comfort level. **When you have no upfront equity invested in a property and are making payments on a mortgage loan that is more than the fair market value of the property, the motivation to stick it out for the duration of the mortgage may wane.**

From the seller's perspective, there are also significant factors to consider before entering into a transaction with a seller's concession. **The primary burden that shifts to the seller is that of the all-important lender appraisal.** When a contract is structured with a seller's concession, the buyer's mortgage loan is based on the inflated contract price. For a mortgage lender to issue a higher mortgage loan based on the higher price, the property must appraise at the higher price. This provision, in essence, shifts the burden of the concession to the seller; the buyer is gaining the benefit of more financial flexibility but with the added risk that the property won't sufficiently appraise.

Going back to our example, the house that the seller is selling for $250,000 must be deemed to be worth $265,958 by the buyer's mortgage bank. If the property appraises sufficiently, then the transaction proceeds and everyone is happy. But what if the appraiser says the house only has a fair market value of $255,000 - who absorbs the difference? This is where a carefully negotiated contract is key. **The seller can ask for a provision in the contract that requires a buyer to proceed at a contract price that conforms to the appraisal value, with the seller's concession to be adjusted accordingly.** In either scenario, the contract would still provide for the same net to seller of $250,000.

Depending on the buyer's circumstances, this "sliding scale" language may or may not be possible. If the buyer absolutely must have the full seller's concession to afford the closing costs, then a low appraisal can be a fatal blow to a transaction, or can result in the seller being forced to renegotiate a lower "net to seller" amount. In any case, since most lending institutions will not order an appraisal until a fully executed contract is submitted, it can be four to six weeks into a matter before the appraisal results are in. That is precious lost time to a seller.

Another relatively minor issue for a seller to consider is the statutory **New York State Transfer Tax** paid by the seller at closing. The Transfer Tax is based on the contract sale price, so when a seller's concession is in play, the seller is essentially paying tax on sales proceeds they are not receiving. In our example, the seller would pay $1,064.00 in transfer tax on a $265,958 sale price vs, $1,000 on the $250,000 transaction. However, **this consideration is easily resolved with a contract provision that requires the buyer to compensate sellers for the additional transfer tax.**

A seller's concession can be a valuable tool when used responsibly in the appropriate transactions. Only you—with the advice of an experienced lawyer—can decide what is best for your situation.

Glossary

Seller's concession: a method of determining a higher contract price for the purchase and sale of real property that allows buyers to increase their mortgage loan amount to cover the expense of their closing costs

Corporations: The Basics

By Megan R. Conroy, J.D.
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One of the oldest and most widely utilized business entities is the **corporation.** Treated much like an individual under the law, corporations have legal rights and responsibilities separate and distinct from the shareholders, directors, and officers that own and operate the business. **As a general rule, these individuals cannot be held personally liable to the corporation's creditors for debts it may owe.** To take advantage of this limited liability, a business must be legally incorporated and maintained pursuant to the applicable statutes and regulations.

The Key Players

Shareholders, directors, and officers each play an integral role in the maintenance and daily operation of the business. **Shareholders invest in the corporation by purchasing shares of corporate stock.** Each share purchased gives the shareholder an ownership interest in the corporation. The **Directors are elected by the Shareholders to serve on a board and oversee the corporation's affairs.** They collaborate to set major goals and to make major decisions regarding the entity. In some instances, such as in smaller or closely held corporations, directors remain active in the management of the corporation. In large or public corporations, on the other hand, the directors will often delegate the regular managerial duties to the officers. **The officers usually include a president, one or more vice presidents, a secretary, and a treasurer appointed by the board of directors to take care of the day-to-day operations of the business.**

How to Get Started

To incorporate a business, **the Articles of Incorporation, also known in some states as the Certificate of Incorporation, must be filed by one or more "Incorporators" for approval with the Department of State.** The filing fee varies by state, but in New York it costs $125 plus the applicable tax on the shares as required by Section 180 of the Tax Law. The corporation is considered to exist as of the date the Certificate of Incorporation is filed. Once the filing has been approved, the Incorporators can begin issuing shares of stock, holding meetings, electing directors and officers, and adopting by-laws.

C-Corporation vs. S-Corporation

Private corporations can be taxed in one of two ways: under subchapter C (hereafter "**C-corporation**"), or under subchapter S (hereafter "**S-corporation**") of the Internal Revenue Code. All corporations are initially formed as C-corporations, but the shareholders may elect to be taxed as an S-corporation thereafter. C-corporations allow for an unlimited number of shareholders and very few limitations on the transfer and sale of stock. **The major disadvantage of remaining a C-corporation, however, is that it is subject to "double taxation".** That is, the income that the entity is taxed on will be taxed again as ordinary income or capital gains if and when it is distributed to the shareholders in the form of dividends, with the type of taxation depending upon the nature of the dividend. **S-corporations, on the other hand, are subject to "pass-through taxation"**, similar to a limited liability company (see the BSR&B: Legal Notes Vol. 7-No. 5, Sept. 2015 article "Is an LLC Right For Me?" for a brief overview of LLCs). Pass-through taxation allows income, losses, and gains to be reported on the shareholders' individual tax returns and is thus only taxed once.

Because of the pass-through taxation structure, corporations that can meet the qualifications imposed by the IRS will often elect to be taxed under subchapter S. In addition to meeting the IRS' requirements, an election form must also be filed with the IRS. **Some of those requirements are very restrictive, making an S-corporation unsuitable or even impossible for certain businesses.**

Why Choose a Corporation?

Just like limited liability companies and limited partnerships, **corporations offer limited personal liability to the shareholders, directors, and officers of the company for corporate debts.** This benefit is usually the driving force behind incorporating a business, but there are other benefits to choosing this type of entity as well. Corporations, more so than other entities, may take advantage of the fringe benefits available under the Internal Revenue Code.

Another notable advantage of incorporating is the freely transferable nature of corporate stock. The ability to transfer ownership interests with ease not only facilitates estate and business succession planning, but also aids in efforts to raise corporate capital through the sale of stock to investors. It is important to note, however, that this transferability is subject to any restrictions in the corporate documents, such as a buy-sell agreement.

Furthermore, corporations have the ability to exist in perpetuity. The death of a shareholder, director, or officer does not terminate the business. For instance, ownership interests can pass to the heirs of the decedent, or they can be sold to either raise capital or to bring in new investors who may offer greater expertise or a sought after skill.

However, persons thinking of incorporating should be prepared to make an affirmative effort to keep up with the record-keeping and maintenance requirements mandated by statute. **Failure to adhere to these requirements may result in the loss of the personal protection from corporate liability that this entity inherently affords.** Additionally, shareholders, directors, and officers have certain fiduciary duties to the entity that, if breached, can subject them to personal liability for their actions (see the BSR&B: Legal Notes Vol. 5-No. 1, Feb. 2013 article "How to Avoid 'Piercing Corporate Veil' Law Suits" for more information). Nonetheless, for businesses that require the flexible transferability of corporate interests, and for owners who would like to take advantage of the other perks listed above, the benefits of this structure likely outweigh the burdens of the government imposed regulations and fiduciary duties.

What Are Guardianships, And Why Do You Want To Avoid Them?

By Austin F. DuBois, J.D.
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Protecting assets from depletion due to the high cost of long-term care requires detailed knowledge of the law and experience handling those types of cases. However, as long as you have an attorney with that skill set, it is relatively "easy" on the client.

When a client has moderate to advanced dementia and cannot manage his or her own affairs, a well-drafted power of attorney (note that many are not well-drafted) permits the named agent to handle the tasks needed to preserve the principal's assets, which keeps it "easy". Unfortunately, because so many people wait until the last minute to plan, or they have inadequate planning and their power of attorney does not allow the agent to engage in Medicaid planning strategies, the family may need to petition the court to obtain a Guardianship. **Once a family member is appointed as Guardian and granted a Commission to Act, that person can manage their loved one's affairs and help protect their assets.** But the journey there is not a pleasant one.

(continued on page 4)

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The Guardianship process is never a desired option—it is almost always done out of necessity. Sometimes, family members disagree about who should be Guardian. Often, more than one family member will "lawyer up" and litigate. I won't discuss contested Guardianships here, because it is self-evident why family members fighting with each other is bad. In this article, I will explain the general process for a calm, agreeable, uncontested Guardianship proceeding, which nonetheless remains bureaucratic, tedious, time consuming, and expensive.

In an uncontested Guardianship, there are usually four different attorneys involved. The first attorney is the person that the family hires to prepare and file a petition with the court, requesting that the agreed-upon family member be appointed as Guardian. That petition, along with an Order to Show Cause, is signed by the applicable judge and served upon all family members that have an interest in the proceeding (typically, the spouse and children). The court schedules a date and time for everyone to appear before the judge, who also appoints both a Court-Appointed Attorney for the **"Alleged Incapacitated Person" (AIP),** as well as a **Court Evaluator, an attorney that acts as the representative of the court.** So far, our count is three lawyers—all of whom get paid from the AIP's money.

Both the Court-Appointed Attorney and the Court Evaluator meet with and interview the AIP to the extent the AIP is able to have a meaningful conversation. Because the petition asks to take away the AIP's authority to manage his or her own affairs, it's only right that we ensure the person is indeed unable to do so. The Court Evaluator also interviews or takes statements from all interested family members, to ensure there is no good reason for disagreement, and to ensure that the proposed Guardian is fit to serve.

Even assuming everyone, lawyers included, agrees with the substantive points raised in the Petition, at least the lawyers (and oftentimes the AIP) must appear in court to have the judge officially grant the Petition and appoint the Guardian. But the "fun" isn't over yet!

Once the judge signs the order appointing the guardian, the order must be filed with the County Clerk's Office, who will then issue the actual "golden ticket"—**the Commission to Act.** At that point, after months of waiting and thousands of dollars in legal fees, **the Guardian is finally able to help protect the family member's assets.**

"Austin", you might interject, "Didn't you mention that there would be four lawyers? You only mentioned three so far!"

You would be right. **Now the compliance requirements begin.** First, the Guardian must take a Guardianship training course offered by the state. The judge's final order also appoints a **Court Examiner—an attorney to whom the Guardian must submit an initial report of the finances,** and then must continue to submit annual reports showing what exactly has been done with the finances. An extremely tedious task, for which the Guardian likely will hire an accountant or attorney to assist.

The good news? **It is incredibly easy for you to help your family avoid a Guardianship.**

Make sure that your estate plan includes a well-drafted **Power of Attorney** and **Health Care Proxy, which will allow the person(s) that you appoint to make all necessary decisions and take all necessary actions.**

How do you know if a Power of Attorney is thorough? There are some specifics to look out for. For example, be sure it includes **full gifting authority** (not simply the "annual exclusion" or "annual gift tax exemption" amount). But the real answer is to ensure you create your estate plan with an attorney that is well-versed in that area of law. **A properly-done plan with adequate documents can save you thousands of headaches and tens of thousands of dollars.**

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