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Date:	**04-Jun-19**
From:	**Steve Leimberg's Estate Planning Newsletter**
Subject:	**Martin M. Shenkman & Jonathan Blattmachr: Estate Planning Updates and Planning Nuggets January - April 2019**

In their commentary, **Martin Shenkman** and **Jonathan Blattmachr** share with **LISI** members their outline titled "Estate Planning Updates and Planning Nuggets January – April 2019."

Martin M. Shenkman, CPA, MBA, PFS, AEP, JD is an attorney in private practice in Fort Lee, New Jersey and New York City who concentrates on estate and closely held business planning, tax planning, and estate administration. He is the author of 42 books and more than 1,200 articles. He is a member of the NAEPC Board of Directors (Emeritus), on the Board of the American Brain Foundation, and the American Cancer Society's National Professional Advisor Network.

Jonathan Blattmachr is the **Director of Estate Planning** for the **Peak Trust Company**, a **Director** at **Pioneer Wealth Partners, LLC**, a wealth management firm in New York City, and is co-developer with Dallas Attorney **Mike Graham** of **WEALTH TRANSFER PLANNING**, a computer system for lawyers that offers specific client advice and automatically prepares wills, trusts, and other estate planning documents using document assembly.

Click this link to read Marty and Jonathan's commentary: Estate Planning Updates and Planning Nuggets January – April 2019

HOPE THIS HELPS YOU HELP OTHERS MAKE A *POSITIVE* DIFFERENCE!

Martin Shenkman
Jonathan Blattmachr

CITE AS:

Estate Planning Updates and Planning Nuggets
January – April 2019

By: Martin M. Shenkman, Esq. & Jonathan Blattmachr, Esq.

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Updates and Planning Nuggets[1]
January – April 2019
By: Martin M. Shenkman, Esq.

1. 199A QBI Deduction.
    a. Final corrected Code Sec. 199A regulations were issued.[2] The following overview of selected portions of the Final corrected Regulations quotes from the preamble and explains the planning implications for some of the provisions.
    b. The final corrected Regulations provide a succinct overview of 199A: "*Section 199A provides a deduction of up to 20 percent of income from a domestic business operated as a sole proprietorship or through a partnership, S corporation, trust, or estate. The section 199A deduction may be taken by individuals and by estates and trusts. A section 199A deduction is not available for wage income or for business income earned through a C corporation (as defined in section 1361(a)(2)). For taxpayers whose taxable income exceeds a statutorily-defined amount (threshold amount), section 199A may limit the taxpayer's section 199A deduction based on (i) the type of trade or business engaged in by the taxpayer, (ii) the amount of W-2 wages paid with respect to the trade or business (W-2 wages), and/or (iii) the UBIA (unadjusted basis immediately after acquisition) of qualified property held for use in the trade or business (UBIA of qualified property). These statutory limitations are subject to phase-in rules based upon taxable income above the threshold amount*."
    c. Practitioners will have to continue to struggle in many instances with the daunting details, complexities and uncertainties of these regulations. If the so-called Blue Wave continues in 2020 and there is a change in administration in Washington, the favorable tax rates for corporations may be changed and. if so, the purpose of 199A[3], to put non-C corporations somewhat on parity, will be eliminated. That might lead to the repeal of 199A. So, an issue practitioners must address is not merely planning for 199A, but whether the cost of that planning is worthwhile to the clients affected given what might be uncertainty about the survival of the provision. In any event, 199A is set to sunset (that is, be eliminated) after 2025 even if there is no change in the administration in Washington.
    d. "*However, taxpayers may rely on the rules set forth in §§1.199A-1 through 1.199A-6, in their entirety, or on the proposed regulations under §§1.199A-1 through 1.199A-6 issued on August 16, 2018, in their entirety, for taxable years ending in calendar year 2018*." Thus, on 2018 returns can be based on either the proposed Regs or these final corrected Regs.
    e. "*The purpose and scope of the proposed regulations and these final regulations are also to determine when to treat two or more trusts as a single trust for purposes of subchapter J of chapter 1 of subtitle A of the Code (subchapter J). These final regulations are not intended to address section 643 in general*." The

[11] Unless otherwise indicated, "Section" and "Code Sec" refer to sections of the Internal Revenue Code of 1986 as amended.
[2] RIN 1545-BO71.
[3]Any reference to 199A is to Section 199A.

final regulations continue a focus on restricting the use of trusts to circumvent the taxable income threshold under 199A. However, as noted below the Final Regs significantly change the approach to 643(f) and the examples from the Proposed Regs were eliminated, thus providing less guidance.

f. An important focus of the 199A Regs, especially the final corrected Regs, is eliminating what the IRS perceived as abuses practitioners had discussed with the use of multiple non-grantor trusts to secure 199A deductions when the taxpayer herself may not have qualified. "*Part I of subchapter J provides rules related to the taxation of estates, trusts, and beneficiaries. For various subparts of part I of subchapter J, sections 643(a), 643(b), and 643(c) define the terms distributable net income (DNI), income, and beneficiary, respectively. Sections 643(d) through 643(i) (other than section 643(f)) provide additional rules. Section 643(f) grants the Secretary authority to treat two or more trusts as a single trust for purposes of subchapter J if (1) the trusts have substantially the same grantors and substantially the same primary beneficiaries and (2) a principal purpose of such trusts is the avoidance of the tax imposed by chapter 1 of the Code. Section 643(f) further provides that, for these purposes, spouses are treated as a single person*."

g. The Final Regs merely reiterate the 643(f) Code provisions for multiple trusts here and near the end of the Regs. The examples from the Proposed Regs have been eliminated. It would appear that if the strictures of Code Section 643(f) can be avoided, the multiple trust rule will not apply but the anti-avoidance rules of the Final Regs will still have to be grappled with.

h. In determining the 199A deduction practitioners have to identify a "trade or business" from which qualified business income ("QBI") is generated. The Final Regulations provide: "*The calculation of QBI and therefore, the benefits of section 199A, are limited to taxpayers with income from a trade or business. Section 199A and its legislative history, however, do not define the phrase "trade or business." The proposed regulations define trade or business by reference to section 162. Section 162(a) permits a deduction for all the ordinary and necessary expenses paid or incurred in carrying on a trade or business…However, because many taxpayers who will now benefit from the section 199A deduction are already familiar with the trade or business standard under section 162, using the section 162 standard appears to be the most practical for taxpayers and the IRS...Specifically, for purposes of section 199A and the regulations thereunder, §1.199A-1(b)(14) defines trade or business as a trade or business under section 162 (section 162 trade or business) other than the trade or business of performing services as an employee*."

i. The definition of a trade or business under Section 162 does incorporate a large existing body of law, but also leaves substantial uncertainties, e.g. when leased real estate will qualify, and much complexity, e.g. calculations, aggregation and more. The Final Regs confirm that the trade or business test under Section 162 is a factual determination and Treasury did not choose to provide any additional guidance.

j. The Final Regulations refer to case law as to the definition of what constitutes a trade or business, citing one case in particular: "*Because there is no statutory or regulatory definition of a section 162 trade or business, courts have established* *elements to determine the existence of a trade or business. The courts have developed two definitional requirements. One, in relation to profit motive, is said to require the taxpayer to enter into and carry on the activity with a good faith intention to make a profit or with the belief that a profit can be made from the activity. The second is in relation to the scope of the activities and is said to require considerable, regular, and continuous activity. See generally Commissioner v. Groetzinger, 480 U.S. 23 (1987) Id. at 35*."

k. The factual determination of whether there is a trade or business requires a profit motive and considerable, regular and continuous activity. Considerable, regular and continuous under Section 162 does not require the level of involvement necessary to constitute material participation under Section 469. Clients should be advised to make a point of creating corroborating evidence that these criteria are met if there is any question as to qualification. Section 162 is a narrower definition of trade or business than Section 469 discussed below. For real estate the Section 469 classification is irrelevant, and the taxpayer will have to prove that the real estate rises to the level of a Section 162 trade or business.

l. Whether real estate rental activities rise to the level of a trade or business remains uncertain. The Final corrected Regulations provide some guidance on this: "*In determining whether a rental real estate activity is a section 162 trade or business, relevant factors might include, but are not limited to (i) the type of rented property (commercial real property versus residential property), (ii) the number of properties rented, (iii) the owner's or the owner's agents day-to-day involvement, (iv) the types and significance of any ancillary services provided under the lease, and (v) the terms of the lease (for example, a net lease versus a traditional lease and a short-term lease versus a long-term lease)*."

m. Landlords will have to maintain time logs for themselves and vendors. For landlords the above factors provide a non-exclusive list of some of the considerations in evaluating the facts and circumstances under Code Sec. 162. Residential property, perhaps in particular a vacation home used in part by the taxpayer, may be less likely to meet the trade or business test than might a lessor of a commercial property, e.g. a warehouse. It certainly fails the safe harbor below. The number of units rented, services provided, lease terms, and other factors will be relevant. For landlords, reserving some services and, perhaps, even expenses may help meet the requirements. Lease terms should be reconsidered and negotiated differently if the taxpayer is willing to do so. For example, taking a higher rent but retaining the burden of some expenses may be preferable for meeting the Section 162 test. Landlords whose rental endeavors are in the gray zone of uncertainty as to whether they meet the criteria of constituting a trade or business should consider maintaining a diary of each activity done. It might be better to engage in different activities on different days to increase the days for which entries are made to enhance the appearance of continuous involvement. Corroboration will be important. Perhaps a landlord should visit the rental property monthly or quarterly and take videos of the property to corroborate the site visit and review. Note that the provisions of the Final Regs below suggest that travel to and from the property are not counted. That is rather odd as many vendors charge travel time. For example, a plumber may charge travel time as well as time on the job site. Would the hours billed by an independent vendor not be counted below towards the 250?

n. A special safe harbor has been provided to help taxpayers determine when a rental real estate enterprise may be treated as a trade or business solely for purposes of Section 199A.[4]

o. "*Under the proposed safe harbor, a rental real estate enterprise may be treated as a trade or business for purposes of section 199A if at least 250 hours of services are performed each taxable year with respect to the enterprise. This includes services performed by owners, employees, and independent contractors and time spent on maintenance, repairs, collection of rent, payment of expenses, provision of services to tenants, and efforts to rent the property. Hours spent by any person with respect to the owner's capacity as an investor, such as arranging financing, procuring property, reviewing financial statements or reports on operations, planning, managing, or constructing long-term capital improvements, and traveling to and from the real estate are not considered to be hours of service with respect to the enterprise. The proposed safe harbor also would require that separate books and records and separate bank accounts be maintained for the rental real estate enterprise. Property leased under a triple net lease or used by the taxpayer (including an owner or beneficiary of an RPE [relevant passthrough entity]) as a residence for any part of the year under section 280A would not be eligible under the proposed safe harbor. A rental real estate enterprise that satisfies the proposed safe harbor may be treated as a trade or business solely for purposes of section 199A and such satisfaction does not necessarily determine whether the rental real estate activity is a section 162 trade or business. Likewise, failure to meet the proposed safe harbor would not necessarily preclude rental real estate activities from being a section 162 trade or business*."

p. Landlords should keep diaries of services. When a contractor or agent is hired now, landlords will have to have the vendor indicate not just the price but also the hours worked so that this forms a record to corroborate the 250 hours. Note that the time spent with respect to an improvement appears to be excluded from the 250-hour safe harbor count. However, with many real estate projects, how can one differentiate an improvement from a repair, the time for which would appear to count towards the 250-hour safe harbor? How much patching of a parking lot may occur before it is equivalent to a capital improvement? Separate books and bank accounts may be onerous and unreasonable, even impractical for some real estate taxpayers. It is common to use a common paymaster, or one management LLC to incur and handle all maintenance and administrative costs. This is often done through one bank account to minimize paperwork. It would appear that to qualify for the safe harbor that such practices could no longer be used.

q. The Final corrected Regulations removed the examples from the Proposed Regs and might eliminate some confusion those examples caused, but no new illustrations leave open much uncertainty about the qualification of rental real estate as a trade or business.

r. The Final corrected Regs have rules for aggregation of trades or businesses. *"[The] rule also allows taxpayers to aggregate their trades or businesses with the*

[4] Notice 2019-07, 2019-XXX IRB XXX.

leasing or licensing of the associated rental or intangible property if all of the requirements of proposed §1.199A-4 are met." Note that these special rules permit the aggregation of a business and a rental activity that does not rise to the level of a Code Sec. 162 trade or business. This related party leasing rule is an exception to the general Section 162 definition of a trade or business adding to the layers of complexity. See also the rules for SSTBs (specified service trades and businesses) as to aggregation that prevents an SSTB from having a related rental operation qualify for Section 199A. Note that Code Sec. 469 has provisions requiring that rental to a related party, e.g. a dentist rents a building that lease payments will be characterized as active to avoid transmuting active income from the practice into passive rental income. Consider the complexity this all creates.

s. The need to maintain separate books and records was also addressed further in the Final corrected Regulations: "*…a taxpayer can use different methods of accounting for separate and distinct trades or businesses and specifies two circumstances in which trades or businesses will not be considered separate and distinct. Section 1.446-1(d)(2) provides that no trade or business will be considered separate and distinct unless a complete and separate separable set of books and records is kept for such trade or business*. "Separable" suggests that separate books need not be kept so long as the records are separable. Nonetheless, given the comments on separate books and records (see above for example) consideration should be given to maintaining separate books. For a single entity to have separate trades or business they must have complete and separable books and records, meet the requirements of being able to use different methods of accounting, and that not result in income not being clearly reflected.

t. The Final corrected Regulations prohibit treating an endeavor as a trade or business, and hence prevent a Section 199A deduction if Form 1099 reporting requirements are not met. "*…taxpayers should consider the appropriateness of treating a rental activity as a trade or business for purposes of section 199A where the taxpayer does not comply with the information return filing requirements under section 6041*." Code Sec. 6041 provides in part: *"(a) Payments of $600 or more. All persons engaged in a trade or business and making payment in the course of such trade or business to another person, of rent, salaries, wages, premiums, annuities, compensations, remunerations, emoluments… shall render a true and accurate return to the Secretary, under such regulations and in such form and manner and to such extent as may be prescribed by the Secretary, setting forth the amount of such gains, profits, and income, and the name and address of the recipient of such payment*." Failing to issue Forms 1099 would disqualify a trade or business that has surmounted the Code Sec. 162 trade or business definition from claiming a deduction under 199A.

u. Disregarded entities raise issues in the application of the Section 199A rules. The Final corrected Regulations provide: "*The proposed regulations do not address the treatment of disregarded entities for purposes of section 199A…trades or businesses conducted by a disregarded entity will be treated as conducted directly by the owner of the entity for purposes of section 199A*." Note that the trade or business of a disregarded entity will be treated as if directly operated by the owner of the entity However, does that suggest that, if rental real estate endeavors that are held in disregarded LLCs, will they be treated as conducted directly by the owner of the LLC? That might be necessary in order for the aggregate of the endeavors to rise to a level of a trade or business. But if the endeavors of each LLCs rental are not themselves not sufficient to rise to the level of a trade or business, will this "look-through" rule not be triggered? Consider the potential arbitrariness of this and other rules below. If an LLC elected to be taxed as other than a disregarded entity, it would not be able to avail itself of this rule. If one developer had each property held in a separate brother-sister LLC, those would be disregarded entities and, perhaps, the developer would be treated as operating the properties directly. Consider a second developer using a very common structure of having a management entity that owns 1% of each property LLC so that there are multiple members and, perhaps, better asset protection. But now each LLC is not a disregarded entity and if the activities of each property entity do not arise to the level of a trade or business, can they be aggregated? But the LLC activities would not be treated as if conducted directly by the developer for Section 199A purposes.

v. Section 199A provides for harsher penalties, all of which seems rather unfair given the daunting complexity and uncertainty of the 199A rules. "*Section 6662(a) provides a penalty for an underpayment of tax required to be shown on a return. Under section 6662(b), the penalty applies to the portion of any underpayment that is attributable to a substantial underpayment of income tax. Section 6662(d)(1) defines substantial understatement of tax, which is generally an understatement that exceeds the greater of 10 percent of the tax required to be shown on the return or $5,000. Section 6662(d)(1)(C) provides a special rule in the case of any taxpayer who claims the section 199A deduction for the taxable year, which requires that section 6662(d)(1)(A) is applied by substituting "5 percent" for "10 percent*." The harsher Section 199A application of the underpayment penalty remains so if the tax due exceeds 5% (not the general 10%) of the tax due on the return an understatement penalty may be applied. Practitioners should caution clients about this when taking positions concerning Section 199A that are not certain.

w. The 50% of wages (or 25% of wages and 2.5% of UBIA) test might result in some clients restructuring business operations to enhance their Section 199A benefit. This should all be considered in the analysis of any estate plan as it might affect a range of planning issues. "*The definition of W-2 wages includes amounts paid to officers of an S corporation and common-law employees of an individual or RPE. Amounts paid as W-2 wages to an S corporation shareholder cannot be included in the recipient's QBI. However, these amounts are included as W-2 wages for purposes of the W-2 wage limitation to the extent that the requirements of §1.199A-2 are otherwise satisfied*." Consider whether this creates an incentive to restructure an entity as an S corporation to enhance the 199A deduction. If that is done, consider the client's estate plan. Do current entity owners include, or might planning to secure the temporary estate tax exemption result in, trusts owning interests in the entity? If so, do those trusts meet the requirements to own S corporation stock? Does the clients will include appropriate S corporation provisions for QSSTs and/or ESBTs? Have the disadvantages of S corporations as to refinancing, etc. been considered?"

x. There was some uncertainty as to the treatment of property contributed to an entity in terms of determining the amount to consider for UBIA. The Final corrected Regulations provide: "…*qualified property contributed to a partnership or S corporation in a nonrecognition transaction should generally retain its UBIA on the date it was first placed in service by the contributing partner or shareholder. Accordingly, §1.199A-2(c)(3)(iv) provides that, solely for the purposes of section 199A, if qualified property is acquired in a transaction described in section 168(i)(7)(B), the transferee's UBIA in the qualified property is the same as the transferor's UBIA in the property, decreased by the amount of money received by the transferee transferor in the transaction or increased by the amount of money paid by the transferee to acquire the property in the transaction*." Practitioners will have to obtain basis information on assets contributed to entities. This is in addition to the need to maintain separate records to reflect the 10-year minimum life for UBIA, etc. How can practitioners handle these additional recordkeeping requirements?"

y. The Final Regs provide a more favorable rule for like kind Code Sec. 1031 exchanges generally continuing to use the UBIA of the property given up in the exchange adjusted for boot.

z. "…*section 743(b) basis adjustments should be treated as qualified property to extent the section 743(b) basis adjustment reflects an increase in the fair market value of the underlying qualified property*." This is a favorable change made in the Final Regs and will be helpful to estates, and in other circumstances. Practitioners should be mindful to address whether the governing documents for the entity involved provide the client/estate the right to require a basis adjustment. If the decedent was not a controlling partner or member there may be no ability to force the partnership to make the election absent a provision in the governing instrument.

aa. "*The preamble to the proposed regulations provides that for property acquired from a decedent and immediately placed in service, the UBIA generally will be its fair market value at the time of the decedent's death under section 1014…The final regulations provide that for qualified property acquired from a decedent and immediately placed in service, the UBIA of the property will generally be the fair market value at the date of the decedent's death under section 1014*." This is important for estate planning and helpful in context of the focus on basis maximization. Further, the regulations provide that a new depreciable period for the property commences as of the date of the decedent's death.

bb. Real estate and business aggregation rules are important for determining whether a real estate activity arises to the level of a trade or business. The Final corrected Regulations provide: "*A rental real estate enterprise that meets the safe harbor described in Notice 2017-07, released concurrently with these final regulations, may also be treated as trades or businesses for purposes of section 199A. Additionally, the rental or licensing of property if the property is rented or licensed to a trade or business conducted by the individual or an RPE which is commonly controlled under §1.199A- 4(b)(1)(i) is also treated as a trade or* *business for purposes of section 199A*." This is the exception and aggregation rule. If a developer has net leased properties that would not qualify, but a management company, would the Section 199A results change if the properties were overleased to the management entity then subleased to the third parties? Would the overlease meet the requirements above? In addition to these requirements, the items must be effectively connected to a trade or business within the United States as described in Section 864(c).

cc. Reasonable compensation and what wages qualify for the 50%/25% tests are important for many taxpayers. The Final corrected Regulations provide: "*Section 199A(c)(4) clearly excludes reasonable compensation paid to a taxpayer by any qualified trade or business of the taxpayer for services rendered with respect to the trade or business from QBI. These amounts are attributable to a trade or business and are thus qualified items…in determining taxable income for the taxable year. In addition, reasonable compensation paid to a shareholder-employee is included as W-2 wages for purposes of the W-2 wage limitation to the extent that the requirements of §1.199A-2 are otherwise satisfied. Further, guaranteed payments and payments to independent contractors are not W-2 wages and therefore, cannot be counted for purposes of the W-2 wage limitation*." These provisions were continued from the Proposed Regs and in some instances may favor use of an S corporation so that the amount of wages can be planned, subject to requirements of reasonable compensation, to maximize the Section 199A deduction with consideration to the 50% or 25% of W2 wage adjustment.

dd. Considerable uncertainty, and risk, remain for the determination of what constitutes "reasonable compensation". The Final corrected Regulations provide: "*A few commenters were concerned about whether tax return preparers would have the responsibility to closely examine whether compensation paid to a shareholder of an S corporation is reasonable before calculating the section 199A deduction, and whether tax return preparers could be subject to penalties….Providing additional guidance with respect to what constitutes reasonable compensation for a shareholder-employee of an S corporation or application or non-application of assessable penalties applicable to tax return preparers is beyond the scope of these final regulations*." Treasury refused to act in regard to this issue. Practitioners might face potential problems if clients take positions that are rejected on audit and the client incurs penalties under the tougher Section 199A 5% rule discussed above. What can, or should, practitioners do to protect themselves? One practical issue is that given the change in the tax dynamics some taxpayers may pay wages that differ from what was done historically. For example, a taxpayer may have paid low or no wages from an S corporation to minimize payroll taxes. Post Section 199A that same taxpayer may want to pay a greater wage to increase the Section 199A deduction with consideration to the 50%/25% wage computation. So, the new wage may not be consistent with historic wages. Might that raise the audit profile on a return? How can the disparity of historic and current wages be explained? Will taxpayers pay practitioners to document or justify the wage changes?

ee. How income and expenses are allocated among different businesses is critical to the Section 199A results. The Final corrected Regulations provide: "*Whether* *direct tracing or allocations based on gross income are reasonable methods depends on the facts and circumstances of each trade or business. Different reasonable methods may be appropriate for different items. Accordingly, the final regulations retain the rule in the proposed regulations. However, once a method is chosen for an item, it must be applied consistently with respect to that item. The Treasury Department and the IRS continue to study this issue and request additional comments, including comments with respect to potential safe harbors*." Allocations between multiple trades or business must be consistent, made using reasonable methods, is based on facts and circumstances, clearly reflect income and expenses, and may be direct tracing or allocation by gross income. These parameters provide little practical guidance and practitioners will have to document whatever methods they use. It appears that allocations are made among "trades or businesses." Does that mean that, if a real estate rental does not rise to the level of a trade or business, that allocations cannot be made?

ff. Family attribution can be important to the determination of the Section 199A deduction and whether businesses can be aggregated...*" The final regulations address these recommendations by requiring that the same person or group of persons, directly or by attribution through sections 267(b) or 707(b), own 50 percent or more of each trade or business. A C corporation may constitute part of this group*." This broadens the attribution rules from what the Proposed Regs contained.

gg. *"To determine whether trades or businesses may be aggregated, the proposed regulations provide that multiple trades or businesses must, among other requirements, satisfy two of three listed factors, which demonstrate that the businesses are part of a larger, integrated trade or business. These factors include: (1) the businesses provide products and services that are the same (for example, a restaurant and a food truck) or customarily provided together (for example, a gas station and a car wash); (2) the businesses share facilities or share significant centralized business elements (for example, common personnel, accounting, legal, manufacturing, purchasing, human resources, or information technology resources); or (3) the businesses are operated in coordination with, or reliance on, other businesses in the aggregated group (for example, supply chain interdependencies)... this test is based on all the facts and circumstances*." This is a common theme of the Regs… facts and circumstances tests. This, while reasonable, does not provide the type of guidance practitioners would often prefer.

hh. "…*aggregation should be allowed at the entity level. Accordingly, the final regulations permit an RPE to aggregate trades or businesses it operates directly or through lower-tier RPEs*." If a subsidiary entity that holds intangible property rights licensed to the main entity does not rise to the level of a trade or business, then it appears that it may not be aggregated.

ii. The sale of insurance may avoid the taint as an SSTB. "*Overall the Final Regs provide valuable leniency to those selling insurance. However, insurance consultants should be careful to delineate what ancillary or other services they provide as those may be tainted as an SSTB. Perhaps the insurance and non-insurance financial related activities should be separated into different* *businesses. If an insurance consultant charges for time, not a commission, that revenue might be subsumed under the consulting category above or the finance category here*." Later the Final Regulations provide: "*…commission-based sales of insurance policies generally will not be considered the performance of services in the field of investing and investing management for purposes of section 199A*." If a wealth adviser earns fees on investment product, e.g. 1% AUM and the adviser includes in the array of services offered estate planning and insurance planning, might that change the result? What if a financial planner charges hourly as a fee only adviser on services rendered and also sells an insurance policy? Is that something other than a purely "commission-based" fee?"

jj. "*…the final regulations provide that if a trade or business provides property or services to an SSTB and there is 50 percent or more common ownership of the trade or business, the portion of the trade or business providing property or services to the 50 percent or more commonly-owned SSTB will be treated as a separate SSTB with respect to related parties*." This is a harsh rule that makes it quite difficult for a professional tainted as an SSTB, e.g. an attorney, to have a related party lease and not have that related entity also tainted as an SSTB. Planning is still feasible, if acceptable to the taxpayer. If three attorneys who are not related jointly purchase a building and lease it to their respective practices, that would not meet the 50% common control test and would not have the rental activity tainted as an SSTB. But now, under the Final Regs. the real estate safe-harbor would have to be met and that could pose a problem in qualifying as a trade or business to obtain the Section 199A deduction.

kk. ESBTs will have one threshold amount for Section 199A purposes. The Final Regulations provide: "*an ESBT being two separate trusts for purposes of chapter 1 of subtitle A of the Code (except regarding administrative purposes), the S portion and non-S portion...Although an ESBT has separate portions, it is one trust. Therefore, in order to provide clarity, the final regulations state that the S and non-S portions of an ESBT are treated as a single trust for purposes of determining the threshold amount*." This change in the Final Regs seems reasonable and merely closes what some might have viewed as a loophole.

ll. There were concerns with the how the Proposed Regulations treated trusts and in particular in that they ignored the DNI deduction. The Final Regulations restored more reasonableness to this: "*Multiple commenters suggested that distributions should not be counted twice in determining whether the threshold amount is met or exceeded, saying this is counter to the statute and beyond the regulatory authority of the Treasury Department and the IRS. Further, sections 651 and 661 are fundamental principles of fiduciary income taxation...The Treasury Department and IRS agree with the commenters that distributions should reduce taxable income because the trust is not taxed on that income. The final regulations remove the provision that would exclude distributions from taxable income for purposes of determining whether taxable income for a trust or estate exceeds the threshold amount. The final regulations specifically provide that for purposes of determining whether a trust or estate has taxable income that exceeds the threshold amount, the taxable income of the trust or estate is determined after taking into account any distribution deduction under sections 651 or 661*." This is a very significant and favorable change made by the Final Regs that addresses a concern raised on the Proposed Regs. Trusts will deduct distributions/DNI shifting taxable income to the beneficiaries receiving distributions. This will permit planning to spread taxable income as between a complex or non-grantor trust and the beneficiaries of that trust, perhaps enabling increasing the Section 199A deduction at both the trust and beneficiary level.

mm. Trust allocations to beneficiaries for Section 199A purposes remain a consideration. The Final Regulations provide: "*the final regulations continue to require that a trust or estate allocates QBI (which may be a negative amount) to its beneficiaries based on the relative portions of DNI distributed to its beneficiaries or retained by the trust or estate*." The election to treat distributions after year end, the 65-day rule, as from the prior year may be important to planning."

nn. The Final Regulations attempt to quash the ability to use non-grantor trusts to circumvent the Section 199A threshold limitation and take a harsher view then the Proposed Regulations had. "*The final regulations clarify that the anti-abuse rule is designed to thwart the creation of even one single trust with a principal purpose of avoiding, or using more than one, threshold amount. If such trust creation violates the rule, the trust will be aggregated with the grantor or other trusts from which it was funded for purposes of determining the threshold amount for calculating the deduction under section 199A*." The Final Regs take a more stringent view of trusts used to circumvent the taxable income threshold under 199A so that even a single trust can be disregarded if it is created or funded to avoid the rule. For practitioners that created a non-grantor trust for this purpose, it should be evaluated to determine the impact.

oo. The Final Regulations eliminate examples and discussions that the Proposed Regulations had contained concerning the use of multiple trusts to plan around the taxable income threshold for Section 199A purposes. The Final Regulations have deferred back to the statute, Code Sec. 643(f) on multiple trusts. "…*the Treasury Department and the IRS have removed the definition of "principal purpose" and the examples illustrating this rule that had been included in the proposed regulations, and are taking under advisement whether and how these questions should be addressed in future guidance. This includes questions of whether certain terms such as "principal purpose" and "substantially identical grantors and beneficiaries" should be defined or their meaning clarified in regulations or other guidance, along with providing illustrating examples for each of these terms. Nevertheless, the position of the Treasury Department and the IRS remains that the determination of whether an arrangement involving multiple trusts is subject to treatment under section 643(f) may be made on the basis of the statute and the guidance provided regarding that provision in the legislative history of section 643(f), in the case of any arrangement involving multiple trusts entered into or modified before the effective date of these final regulations*." The examples that raised concerns and the principal purpose test from the Proposed Regs have been eliminated in the Final Regs but practitioners have little more to rely on with respect to how multiple trusts will be treated other than the bare language of Code Sec. 643(f).

2. Aging and Elder Abuse Statistics.

a. "*Senior citizens may lose nearly 25 times more to scammers than what is reported, according to a report by Comparitech, a consumer research organization based in the U.K. Instead of the 200,000 cases of elder financial abuse that are reported annually to U.S. authorities, the actual number may be as high as 5 million, with losses of $27.4 billion a year, not the $1.17 billion that is officially reported, said Paul Bischoff, researcher and editor of Comparitech, which focuses on consumer issues in the United States, Canada and the United Kingdom*."

b. "A lot of the financial abuse is perpetrated by family members or people the elderly trust, so they are reluctant to report it; they may be ashamed they got scammed, or they may not realize it," *Bischoff said*.

c. "*Statistics on the real numbers surrounding elder financial abuse vary by organization, but experts agree it is a serious problem that is debilitating to seniors. An earlier report from the New York City Department for the Aging and Cornell University done in 2011 estimated that only one in 23 cases is reported*."

d. "*Comparitech estimated one in 10 people in the United States over the age of 65 falls victim to elder fraud in the last year. The average loss per case based on numbers reported to state Adult Protective Services organizations is $2,415*."[5]

e. Practitioners in all the allied professions need to make later life planning and planning with safeguards to minimize the risks of elder financial abuse, a standard part of the planning process. Common planning steps for aging, like preparing a durable power of attorney, need to be rethought in light of these risks. What safeguards can be built in to a durable power and all other aspects of the plan? What monitor relationships external to the document can be created for the client? Might a revocable trust with a trust protector and co-trustees provide a better set of checks and balances? A planning team of independent experts provide additional checks and balances, but that team and its functioning preferably should be addressed in advance of an issue.

f. "*Comparitech estimates 5 million cases of elder fraud occur in the US annually resulting in $27.4 billion in losses. Elder fraud, also called elder financial abuse or elder financial exploitation, is defined as the misappropriation or abuse of financial control in a relationship where there is an expectation of trust, resulting in harm to the elderly victim. More than 200,000 scams and financial abuse cases targeting the elderly are reported to authorities every year, and most experts agree that's just the tip of the iceberg. Our estimates show $1.17 billion in damages are reported to authorities, but the real figure likely dwarfs that amount when factoring in unreported elder fraud.*" [6]

g. The impact of elder financial abuse, inheritance abuse and all these matters is staggering. Traditional estate planning in many ways still seems mired in the historic view of intact families in first marriages and family loyalty that in many situations is inappropriate or simply does not exist. The common approach of

[5] Karen Demasters, "Elder Financial Abuse Much Worse Than Reported, Study Says," Financial Adviser Online, Apr 19, 2019.

[6] Paul Bischofftech, "Elder Financial Abuse in Each State," Financial Adviser online, Apr 17, 2019.

naming spouse then children in age order as agents perhaps should be discussed in detail with clients along with other planning options.

3. ## Aging and Infirm Clients.

a. Clients are aging and the incidence of elder financial abuse, and the permutations it can take, are growing as well. A recent article illustrated what appears to be a common occurrence which it dubbed "inheritance exploitation:"

b. "*After a live-in caretaker was hired to care for his mother full-time, the woman's step-son and other family members were allegedly denied access to their loved one, locked out of the family home and written out of estate planning documents that had originally named them as heirs. By the time the step-son sued for breach of fiduciary duty and financial elder abuse, the caretaker had already pocketed some $5 million, according to a lawsuit filed in the Superior Court of California in Alameda. Although the case against the caretaker was privately settled in mediation last month, the attorney for the plaintiffs, Michael Hackard, warned that cases of inheritance exploitation like this one are on the rise*."[7]

c. The statistics of those potentially at risk is alarming: "*The number of boomers in their 60s with living parents has risen since 1998 to about 10 million, according to an Urban Institute analysis of University of Michigan data. The Alzheimer's Association estimates that 5.7 million Americans are living with Alzheimer's*."[8]

d. The article continues on to discuss the role that financial advisors can serve in protecting clients from elder abuse. There is no question that wealth advisers can serve a vital role in protecting clients with these challenges, but to do so more needs to be done then typically occurs. Addressing how that role can be enhanced, and the role of other advisers on the planning team, can reduce the risks of "inheritance exploitation" and elder financial abuse generally.

e. Financial professionals can restrict distributions from accounts if they have a reasonable belief that the client/account owner is being subjected to financial exploitation under FINRA Rule 2165.[9] The FINRA rule also appropriately broadens the discussion to include not just elderly clients (which most articles unfortunately restrict their discussion to) but clients with other health or cognitive challenges that make them susceptible to abuse. "*…the term "Specified Adult" shall mean: (A) a natural person age 65 and older; or (B) a natural person age 18 and older who the member reasonably believes has a mental or physical impairment that renders the individual unable to protect his or her own interests*."

f. The FINRA rule permits placing a temporary hold on disbursements from the accounts of customers who are believed to be at risk. "*The member [financial adviser] reasonably believes that financial exploitation of the Specified Adult has occurred, is occurring, has been attempted, or will be attempted; and The*

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[7] Juliette Fairley, "What Advisors Can Do About Inheritance Exploitation," Financial Adviser, February 25, 2019 https://www.fa-mag.com/news/what-advisors-can-do-about-inheritance-exploitation-43495.html?section=101&page=2 .

[8] Id.

[9] http://finra.complinet.com/en/display/display_main.html?rbid=2403&element_id=12784.

member, not later than two business days after the date that the member first placed the temporary hold on the disbursement of funds or securities, provides notification orally or in writing, which may be electronic, of the temporary hold and the reason for the temporary hold to: (i) all parties authorized to transact business on the Account, unless a party is unavailable or the member reasonably believes that the party has engaged, is engaged, or will engage in the financial exploitation of the Specified Adult; and (ii) the Trusted Contact Person(s), unless the Trusted Contact Person is unavailable or the member reasonably believes that the Trusted Contact Person(s) has engaged, is engaged, or will engage in the financial exploitation of the Specified Adult; and… The member immediately initiates an internal review of the facts and circumstances that caused the member to reasonably believe that the financial exploitation of the Specified Adult has occurred, is occurring, has been attempted, or will be attempted. (2) The temporary hold authorized by this Rule will expire not later than 15 business days after the date that the member first placed the temporary hold on the disbursement of funds or securities, unless otherwise terminated or extended by a state regulator or agency of competent jurisdiction or a court of competent jurisdiction, or extended pursuant to paragraph (b)(3) of this Rule."

g. To best equip a financial adviser to provide this safety net, a number of prerequisites need to be addressed. The adviser must have names and contact data for trusted contact persons to reach out to. But there are many more practical steps that can be taken that too often are not addressed in the planning process. Many of these steps are non-technical practical steps that the entirety of the client's planning team can foster. But these steps are rarely within the primary purview of any single adviser and are not the traditional planning steps most advisers take. But to combat the growing epidemic of financial abuse of elderly and infirm clients need more.
h. Planning considerations:
    i. The key step is changing the dialogue. There is not nearly enough focus in financial and estate planning discussions on later life planning. Nor is there the collaboration amongst different professionals robust enough to foster a true team effort in this regard.
    ii. Many clients have many accounts scattered at many institutions. This makes each account less significant to the financial adviser at each firm. It exponentially increases the number of advisers and accounts to address making identification of an issue more difficult. To protect against elder abuse, it may be safer to consolidate accounts at one or two institutions and deepen the relationship with the adviser at the firm (or if really necessary limited numbers of firms) so that the adviser has more contact, more knowledge and hence opportunity to react to a potential elder abuse. This is a difficult or impossible task for a financial adviser to accomplish because the client may view the recommendation to consolidate accounts with that adviser as self-serving. However, if the client's other advisers

encourage consolidation (e.g. the CPA, estate planning attorney, etc.) that recommendation may have more impact.

iii. Get a real financial plan based on a realistic budget completed by the financial adviser. That can provide a touchstone to evaluate suspect transactions. Without a budget and financial plan only the most egregious distributions might be identifiable as inappropriate. For example, a wire transfer of $100,000 to a Caribbean account pertaining to a supposed lottery winning might be identifiable in all instances. However, if a care worker or family member were to take an elderly client to the cash ATM machine several times a week and slowly pilfer money in that manner, would that be noticeable? Perhaps, not without a budget to compare to historic cash withdrawals. Too many people do not address the fundamental basics of planning which are critical to protecting clients as they age or deal with other health challenges.

iv. Automate every financial transaction feasible. If most bills are automatically charged to credit cards, credit cards automatically paid from a checking account, and deposits automatically made to the same account a number of protective benefits can be achieved. First, the number of bills, checks and other financial records that arrive by mail can be drastically reduced. That leaves less information for bad actors to abuse. Automating financial transactions reduces the amount of work necessary to pay bills and make deposits, thereby permitting more attention to be given to oversight then working in the financial weeds.

v. Automate accounting records on a computer program, e.g. Quicken, so that a CPA or other independent or trusted person can monitor activity remotely. Consider if feasible having an independent firm, e.g. a CPA firm, handle bill pay. That provides a check and balance and independent oversight.

vi. Encourage clients to use a more robust revocable trust in lieu of relying on a durable power of attorney. Powers of attorney often have one person named agent to act on behalf of the client. That can foster financial abuse if the agent is the person who turns out to be the bad actor. A revocable trust can offer a number of safeguards. You can incorporate co-trustees. While this can be done in a durable power of attorney (and perhaps should be), other steps can include appointing in the trust document a trust protector. This is a person, who may be designated to act in a fiduciary capacity (and under some state laws fiduciary status is the only result), who can be given the authority to remove and replace the trustee if anything is suspected, demand an accounting from the trustee, and more. Other commentators suggest that the trust protector be expressly designated as acting in a non-fiduciary capacity (if state law permits, and if not creating situs and specifying governing law of a jurisdiction that does permit non-fiduciary capacity for the protector). Having a protector as a check and balance for the trustees or co-trustees can be helpful especially for a settlor facing health, cognitive or other challenges caused by aging, or otherwise. Also, consider assigning the revocable trust a separate tax identification number so that accounts are not under the client's Social Security number to make it more difficult for bad actors to identify the account.

vii. Involve family and others in developing a financial and legal safety net. For example, once financial accounts have been consolidated, have a consolidated statement sent to the client. This can make it easier for even a client with some degree of challenges to stay in control longer as one composite statement of all accounts with that institution can be far simpler to understand than a dozen or more different statements from different institutions. Then have a trusted family member, or if affordable, the client's independent CPA, receive duplicate copies of that statement. If a family member is named, consider naming a person who is not the agent under the client's power of attorney nor the successor trustee of the revocable trust.

viii. If appropriate to the plan, have consistency between all dispositive documents. The distributions under a will or revocable trust, if agreeable, can match the beneficiary designations under IRA, qualified plans and insurance policies, and so forth. That consistency sets a pattern that could be important if someone endeavoring to commit inheritance extortion or another type of financial abuse is able to have the client change an account title (e.g., to POD to the perpetrator), change a will, etc. Also, consider re-signing the will or revocable trust a few months after the initial document is signed. Add a bequest to a new charity to show that the client considered the document and made a change, but the dispositive scheme other than that remains intact. Consider having different witnesses. That too can create a history corroborating intent.

i. Financial abuse of the elderly or infirm appears to be more rampant than statistics can ever identify. So many of these acts are difficult or impossible to identify. Determining whether an elderly parent intended to give more money to a child who claims to have been a caregiver, or whether the purported caregiver was abusing the elderly parent, are difficult to differentiate. Taking proactive steps earlier on, with a collaborative team, looking at practical not just technical implications of planning, can provide more security.

4. Asset Protection - IRA.

a. A bankruptcy court has held that, where a taxpayer withdrew money from his IRA and rolled over part of those funds into another IRA within 60 days, then filed for bankruptcy, the rollover sum was an exempt asset for bankruptcy purposes.[10]

[10] In re: Jones, (Bktcy Ct IL 4/15/2019), 123 AFTR 2d ¶ 2019-620.

b. The facts in this case are rather bizarre but illustrate the protection an IRA can afford from an asset protection perspective. The debtor took $50,000 out of his IRA, commingled the funds with his other assets, and spent $30,000 on lottery tickets (what else would you buy with your IRA funds?) Within the 60-day rollover period he deposited $20,000 into another IRA. Later that year he filed for Chapter 7 bankruptcy and the Court held that the $20,000 was exempt from the reach of creditors as a rollover of his IRA. The funds did not lose their exempt status merely because the debtor took them out of his IRA. They remained a qualified retirement asset because they were rolled over in the requisite time period.
c. Reg. Sec. 1.408-4(b) provides for a 60-day rollover rule and allows the funds distributed from an IRA to be paid back "from the same amount of money and any other property."

5. Assisted Suicide.

a. New Jersey recently enacted right to die or assisted suicide legislation making New Jersey the eighth jurisdiction in the US to permit assisted suicide. This is a slowly growing trend of states enacting such legislation. The New Jersey law is reviewed below as a new development, and then a broader discussion of assisted suicide legislation follows.
b. The preamble to the bill proposed provides insights into the right to die movement and the realities of the legislation enacted in other states.
   i. "*Recognizing New Jersey's long-standing commitment to individual dignity, informed consent, and the fundamental right of competent adults to make health care decisions about whether to have life-prolonging medical or surgical means or procedures provided, withheld, or withdrawn, this State affirms the right of a qualified terminally ill patient, protected by appropriate safeguards, to obtain medication that the patient may choose to self-administer in order to bring about the patient's humane and dignified death;*
   ii. *Statistics from other states that have enacted laws to provide compassionate aid in dying for terminally ill patients indicate that the great majority of patients who requested medication under the laws of those states, including more than 90% of patients in Oregon since 1998 and between 72% and 86% of patients in Washington in each year since 2009, were enrolled in hospice care at the time of death, suggesting that those patients had availed themselves of available treatment and comfort care options available to them at the time they requested compassionate aid in dying*;
   iii. *The public welfare requires a defined and safeguarded process in order to effectuate the purposes of this act, which will*;"

c. On April 12, 2019, New Jersey passed "Aid in Dying for the Terminally Ill Act."[11] This will permit:
    i. An adult, defined as 18 or older
    ii. Resident of New Jersey. This might preclude a transfer of a patient from a state not permitting assisted suicide into New Jersey to avail himself or herself of the New Jersey statute.
    iii. Who is mentally capable (means having the capacity to make health care decisions and to communicate them to a health care provider, including communication through persons familiar with the patient's manner of communicating if those persons are available).
    iv. Who is terminally which means that the patient is in the terminal stage of an irreversibly fatal illness, disease, or condition with a prognosis, based upon reasonable medical certainty, of a life expectancy of six months or less. A patient shall not be considered a qualified terminally ill patient until a consulting physician has: examined that patient and the patient's relevant medical records; confirmed, in writing, the attending physician's diagnosis that the patient is terminally ill; and verified that the patient is capable, is acting voluntarily, and has made an informed decision to request medication that, if prescribed, the patient may choose to self-administer.
    v. Whose attending physician has determined to be terminally ill as defined.
    vi. Who has made an informed decision. This means a decision by a qualified terminally ill patient to request and obtain a prescription for medication that the patient may choose to self-administer to end the patient's life in a humane and dignified manner, which is based on an appreciation of the relevant facts and after being fully informed by the attending physician of:
        1. The patient's medical diagnosis.
        2. The patient's prognosis.
        3. The potential risks associated with taking the medication to be prescribed;
        4. The probable result of taking the medication to be prescribed; and
        5. The feasible alternatives to taking the medication, including, but not limited to, additional treatment opportunities, palliative care, comfort care, hospice care, and pain control.
    vii. To obtain self-administered medication to terminate her life.

d. Time delays are built into the statute to prevent an unintended action. the patient shall make two oral requests and one written request for the medication to the patient's attending physician, subject to the following requirements:
    i. At least 15 days shall elapse between the initial oral request and the second oral request;

[11] P.L. 2019, Ch. 59. Introduced in 2018 as Assembly, No. 1504.

ii. At the time the patient makes a second oral request, the attending physician shall offer the patient an opportunity to rescind the request.
iii. At least 15 days shall elapse between the patient's initial oral request and the writing of a prescription.

e. The health care agent is not authorized to make or rescind the request for such self-administered medication.
f. Hawaii. he “Our Care, Our Choice Act” was into law in 2018 making Hawaii the seventh U.S. jurisdiction to pass an assisted suicide statute.[12] The new law became effective January 1, 2019.
g. While the phrase itself may evoke strong emotions on each side of the issue, “assisted suicide” is a concept that every practitioner must understand. When a client faces a diagnosis of a terminal illness, especially one anticipated to be rife with pain and suffering, practitioners may be called upon to engage in a conversation about the options, one of which for the client may include assisted suicide. Any advice given to clients as to end of life decisions should be based upon the developments in this area. As the population ages and medical technology continues to advance, the conscious decision of those with terminal conditions and severe pain and/or the loss of quality of life, to choose whether to end their lives, will sadly occur more frequently. Practitioners may for personal, religious or other reasons choose not to counsel a client on pursuing assisted suicide, but knowledge of the topic may be important to that discussion and the recommendations to other advisers. But while some states have moved in the direction of permitting assisted suicide, other states have moved in the opposite direction prohibiting assisted suicide.
h. Colorado passed Proposition 106, the End of “Life Options Act,” on November 8, 2016. States that permit what many refer to as “legal suicide “include: California, Colorado, Hawaii, New Jersey, Oregon, Vermont, and Washington. Montana has a court decision that is viewed as permitting similar actions.
i. Legal suicide is when, after complying with strict procedures, a dying and suffering client may obtain prescription medication to end his or her life in a less painful manner. A few states permit this process, but only for terminally ill individuals who have less than a six-month life expectancy. Common requirements of these laws may include:
    i. The patient must personally make the request of his or her physician for self-administered aid-in-dying medication.
    ii. Be a resident of the state permitting this. This requirement is an important part of planning that those living in other states should address, and preferably as early as possible after obtaining a diagnosis of the terminal condition.
    iii. Be an adult, which is generally age 18 or older.

[12] HB 2739.

iv. Communicate an informed decision to health care providers. Thus, an agent under a health care proxy may not be permitted to do this for a client.
v. Diagnosed to have a terminal illness with a prognosis of six months or less to live.
vi. The dire health status must be confirmed by two physicians, including the client's primary physician and a second, consulting physician.
vii. Confirmed as being mentally capable to make this decision by two physicians. They must specifically conclude that the client understands the consequences of the decision.
viii. Confirmation that the decision is deliberate. This is accomplished by requiring the client to make two oral requests, at least fifteen days apart, and one written request, that are specific as to what is being requested, to the client's primary physician. Clients should be encouraged to discuss these wishes in person with their physicians. Regardless of the physician's response, the client should request that the physician to record the request in the client's medical record. This request should constitute the first oral request under the law. Advise the client to obtain a copy of that record (patient chart) to have proof of the request. The written request must also be witnessed by at least two other persons who meet certain requirements.
ix. After all prerequisites are met, some states require a waiting period before the prescription can be written. Some states require that a final attestation form be completed 48 hours before taking the medication to provide yet a further waiting period for the client to reconsider.
x. Death certificates will list the cause of death as the person's terminal illness, not physician-assisted suicide. If this is an important consideration for the client, verify that the laws of the state under consideration provide for this.

j. If a client has been diagnosed with a terminal illness, faces the prospect of severe pain, loss of quality of life, and wishes to avail himself of the assisted suicide laws in one of these states, it may be prudent to move to a state permitting assisted suicide to have the availability of this option if chosen. That move should be made while there is capacity to effectuate establishing residency in the chosen state and to carry out the requirements above which require sufficient capacity over a period of time to corroborate understanding and intent. Of course, consideration must be given to other effects of changing residence, such as income and estate taxation.
k. Be certain that the client understands and considers that this option may violate religious beliefs of the faith the client has adhered to. It may also deeply offend and upset family and friends. Encourage the client to discuss the entire matter with any religious advisers, mental health professionals and others.

l. The California, Colorado, Oregon, Vermont, and Washington Death with Dignity laws allow mentally competent, terminally ill adult state residents to voluntarily request and receive a prescription medication so they can die in a peaceful, humane manner in a place and time of their choosing. Death with Dignity is one of many end-of-life care options available. Montana does not have a statute that codifies the right to assisted suicide. In 2009, Montana's Supreme Court ruled that there is nothing prohibiting a physician from prescribing medication to hasten the patient's death.

m. In contrast to the discussions in the preceding section, New York held that statutes criminalizing assisted suicide are constitutional. The court determined that such restriction do not violate the due process or equal protection clauses. While the court stated that anyone, regardless of physical condition, if competent, can refuse unwanted lifesaving medical treatment that does not extend so far as to permitting assisted suicide. The court found a legitimate state purpose to guard against misuse or abuse of assisted suicide and preserving life. The New York Court held: "Although New York has long recognized a competent adult's right to forgo life-saving medical care, we reject plaintiffs' argument that an individual has a fundamental constitutional right to aid-in-dying … We also reject plaintiffs' assertion that the State's prohibition on assisted suicide is not rationally related to legitimate state interests."[13]

n. A tangential issue worth noting is a case addressing an action for the "wrongful prolongation of life.[14] The Koener case presented a novel question and a sensible resolution. The plaintiff's decedent had signed a "do not resuscitate" and "do not intubate" directive at Morristown Medical Center. This was known to the hospital, her physicians, and nurses. She was 89 years old and living in an assisted living community. When undergoing a Doppler procedure at the hospital, she went into cardiac arrest. Despite the orders, she was resuscitated and lived another six months. Unfortunately, she was then intubated, had daily pain from an arthritic condition, difficultly with breathing from an end-stage lung disease, chest pain, bowel and bladder problems, depression and dementia, incidents of falling, and a stroke making it difficult to communicate, speak and eat. Defendants' motion for summary judgment was denied, and they moved for reconsideration, claiming that the New Jersey Advance Directive for Health Care Act, N.J.S.A. 26:2H-73, immunized them when lifesaving care is administered in violation of a health care directive. In 2016, the judge, drawing on concepts found in "wrongful birth" cases, had found that a cause of action existed here for "wrongful prolongation of life." He likewise now rejected the alleged statutory bar to the claim. The act, he noted, immunizes medical personnel and institutions from civil and criminal liability when the patient's directive is carried out, not when it is ignored. The act protects "for actions performed in good faith and in accordance with the provisions of this act to carry out the terms of an advance directive."

[13] Sara Myers et al., Eric A. Seiff, et al., v. Eric Schneiderman, 2017 NY Slip Op 06412, Sept 7, 2017.

[14] Koener v. AHS Hospital Corp. (MRS-L-2983-13).

(N.J.S.A. 26:2H-73(c), emphasis added). The judge found that the decedent's rights were violated when she "lived an additional six months in a diminished condition that included unwanted pain and suffering." The court relied on the Supreme Court's wrongful life cases in the opinion's extended analysis, a view that certainly may be seen as an imperfect analogy. It concluded that the decedent "had a well-established right to reject lifesaving treatment," and that the damages for the finite period could be assessed by a jury. This right was violated, causing her pain and suffering. In this situation, the courts should provide refuge for the injured party, or, as here, her estate.

o. Questions come to mind. What if the directives had in their extended texts a waiver of claims such as these? May the statutory absolution be contractually expanded? Would such language be given effect? Would public policy preclude it? Can next of kin override the directives and agree to indemnify the providers against claims such as these? Such issues must await later decisions; but this case appears to be a step in elucidating this expanding area of tort law.

6. C Corporations.

a. Consent dividend.

i. With the rush to C corporation status in light of the low 21% federal corporate tax rate, the personal holding company ("PHC") tax could be a significant concern for some C corporations. A recent letter ruling is relevant to those that that have C corporations involved in their planning.[15] For many decades, until limited liability companies ("LLCs") became quite mainstream, the use of S corporations was popular in the context of family transactions. S corporations, unlike C corporations, permit the flow through of income to the shareholders. However, they are subject to a number of stringent restrictions which often constrained estate planning, e.g. only specified trusts may hold S corporation stock. While C corporations may have become more popular because of the new favorable tax break, that is unlikely to reduce significantly the number of S corporations involved in family estate and other plans.

ii. First, some background on the PHC tax and some of the means to avoid it.

iii. The PHC tax, imposed under Section 541, was enacted decades ago, at a time when the marginal corporate tax rate was well below the individual top income tax rate. The purpose was to prevent taxpayers from accumulating income inside a C corporation at a lower tax rate. The PHC tax had remained academic for many years because the corporate tax rates exceeded the top rate applicable to individuals. The 2017 tax act flipped the relationship of corporate and individual tax rates with the well publicized 21% corporate tax rate. The result of this, the nearly forgotten PHC tax again became relevant. As a result of the new relationship between the maximum individual rate at 37% (or 40.8% if the 3.8% NIIT

[15] PLR 201901002, Feb. 4, 2019 (not precedent).

is applicable) and the maximum corporate of 21% there is now a significant incentive to hold cash and investment assets inside a C corporation rather than distribute them. Many taxpayers have modified existing entities into C corporations or have created them. One risk of using C corporations in this manner is the exposure to the PHC tax.

iv. The tax is assessed under IRC Sec. 541, which provides: "*541 - Imposition of personal holding company tax -In addition to other taxes imposed by this chapter, there is hereby imposed for each taxable year on the undistributed personal holding company income (as defined in IRC Sec. 545) of every personal holding company (as defined in IRC Sec. 542) a personal holding company tax equal to 20 percent of the undistributed personal holding company income*."

v. The aggregate of the 20% PHC rate and the regular corporate rate of 21% is 41%, hardly a significant penalty (unless the second tax on distributions to shareholders on dividends from the C corporation are factored into the analysis).

vi. Personal holding company income ("PHCI") is determined by taking specified deductions from the C corporation's income. PHCI may include the following (but there are a host of exception and special rules): dividends, rents, mineral, oil and gas royalties, amounts received from contracts for personal services, income reported by a corporate beneficiary of an estate or trust, etc.

vii. A personal holding company must meet an income and ownership test. The income test requires that PHCI comprises 60% or more of its adjusted ordinary gross income for the year. The ownership test requires that for the last half of the tax year more than 50% of the stock is owned directly or indirectly by five or fewer individuals. Constructive ownership rules apply. IRC Sec. 544. These will attribute to a particular shareholder shares in the C corporation that are owned by controlled entities, etc.

viii. So, if a C corporation passes the income and ownership test it could be subject to an additional 20% tax. So, planning can be done to avoid or fail the ownership or income test. For example, a C corporation could buy a business that produces significant gross income to enable the post-sale corporation to fail the 60% of income test. But what if a C corporation meets both tests? Can something be done to avoid paying the additional 20% PHC tax? Yes, the corporation may be able to pay a dividend to its shareholders to avoid the penalty tax. More specifically, the PHC can pay what is known as a "deficiency dividend" and avoid the PHC tax. See IRC Sec. 547.

ix. This recent ruling pertained to this process. In Private Letter Ruling 201901002, the IRS granted a C corporation an extension on the period of time during which it could make the election to pay a consent dividend and avoid the PHC tax.

x. The IRS granted the C corporation a 60-day extension to make the election for a consent dividend under Code Section 565 (which permit the corporation a deduction for such dividends). The rationale for the leniency was that the corporation made reasonably good faith reliance on its accountant who had not properly advised it. The accountant had evaluated the corporation's PHC tax at the consolidated return level and concluded that PHC tax did not apply. The accountant also failed to advise the taxpayer that it was necessary to make the consent dividend election.

xi. The election is made by filing with the Form 1120 "U.S. Corporation Income Tax Return:"

1. Schedule PH.
2. Form 972 – "Consent of Shareholder to Include Specific Amount in Gross Income".
3. Form 973 – "Corporation Claim for Deduction for Consent Dividends."

7. Charity – Post-Death Valuation of Donation.

a. What value should be placed on charitable bequests? A recent case addressed this issue, and an article in the literature raised some important questions about the finding in the case. Before addressing the case some background on valuation considerations will be presented.

b. The value of property donated to charity should be based on its fair market value which is often determined by appraisal. A not uncommon valuation issue is what happens when the valuation obtained is altered or contradicted by later events. In the case of estate tax valuations, for charitable purposes or otherwise, what is the impact of post death events?

c. In valuing estate assets, practitioners need to be cautious concerning post death sales. In the Noble case the Court held that a post death sale of a closely held stock position was determinative of the value of the stock on the decedent's estate tax return. In contrast another case reached the opposite result. In another case, the valuation of property that comprised a charitable deduction considered post-death events.

d. A recent case considered the impact of post-death events on the determination of an estate tax charitable contribution deduction finding that the post-death events should be applied to modify the valuation determined at the date of death. The Dieringer v. Com'r, case was initially decided by the Tax Court in 2016 and was recently affirmed by the Ninth Circuit.

e. Stock in a closely held business was bequeathed to a charitable foundation. An appraisal was obtained as of the decedent's date of death.

f. After the decedent's death, another appraisal was completed, and the decedent's shares were redeemed by the company. In the post-death appraisal, the appraiser was instructed to consider minority interest and other discounts that might affect the decedent's shares, and those were determined by the appraiser to be substantial. While the estate claimed a charitable contribution, deduction based on the date of death value the Court held that the post-death events had to be considered and a lower value, therefore, had to be used for the contribution.

g. A charitable contribution deduction cannot exceed the value of the property received by the charity. While that is generally determined based on the value of the property included in the decedent's gross estate at the date of death, that is not always the case.
h. Similar to the facts in other recent cases that have been resolved unfavorably to the taxpayer, in the instant case the decedent's son was executor, trustee of her trust, trustee of the foundation, and a shareholder and officer in the company. In those capacities he controlled all sides of the transaction and orchestrated a redemption based on a valuation reflecting a minority discount but claimed a charitable contribution on a valuation not reflecting a discount.
i. An accuracy related penalty was imposed and upheld by the Court.
j. The estate tax charitable deduction was reduced to the price at which stock specifically bequeathed to the private foundation was subsequently redeemed by the family's closely held business. The stock redemption price was determined based upon the application of multiple valuation discounts. While the tax result of the case was a substantial reduction in the originally claimed estate tax charitable deduction, the economic result was that the foundation received much less value that it would have received had the redemption never occurred. Commenters have questioned a number of aspects of this case including the liability of the foundation for selling shares at a discount and the control the key persons exercised over all aspects of the transactions.

8. Charity – Section 501(c)(4).

a. Section 501(c)(4) organizations provide interesting planning opportunities. Before examining a recent case addressing Section 501(c)(4), first some background on these unusual organizations will be considered.
b. A Section 501(c)(4) organization is defined as civic leagues etc. operated exclusively for social welfare. Section 501(c)(4) are organizations which are not organized for profit and which are organized solely for the promotion of the public welfare.
c. Section 501(c)(4) organizations are allowed to promote in political actions so long as that is not their "primary purpose". What constitutes political campaign intervention, and what is the threshold for the amount of intervention that can be performed before it becomes the corporations "primary purpose" and therefore become a violation is not clear. The IRS uses a facts and circumstances test to determine if an action is considered political activity- but that test remains vague and open to interpretation and has come under criticism.
d. An organization is operated exclusively for the promotion of social welfare if it is "primarily engaged" in promoting the common good and general welfare of the community.[16] Advocating for a particular social issue by sending mailings and

[16] Reg. Sec. 1.501(c)(4)-1(a)(2)(i).

paying for advertising can be an acceptable social welfare activity. But direct involvement in political matters is not.[17]

e. In a recent case, the IRS denied recognition of an organization as a Code Sec. 501(c)(4) social welfare organization. The Court held that the organization did not have standing to challenge of IRS's test for determining whether it operated exclusively for the promotion of social welfare.[18]
f. A Code Sec. 501(c)(4) organization that spends funds to influence the selection, nomination, election, or appointment of any individual to any federal, state, or local public office is subject to income tax. The tax is based on the lower of the amount spent on these purposes or the investment income the organization earned in the year.[19]
g. The IRS has provided guidance on the income tax implications of such political campaign activity.[20] IRS uses a similar "facts and circumstances" test to determine if an applicant seeking tax-exempt status under Code Sec. 501(c)(4) is primarily a social welfare organization that will qualify, or if instead the organization is excessively involved in political campaign matters so that it should not qualify.
h. Factors that the IRS might consider as indicating political activity include the following:
    a. The communication identifies a public candidate.
    b. The timing of the communication coincides with an election.
    c. The communication targets voters in a particular election;
    d. The communication is not part of an ongoing series of substantially similar advocacy communications by the organization on the same issue.
i. Factors that the IRS might consider as indicating social welfare activity include the following:
    a. The communication identifies specific legislation outside the control of the organization, that it is trying to influence.
    b. The communication identifies the candidate solely as a government official who can act on the public policy issue.
    c. The communication identifies the candidate solely in the list of key or principal sponsors of the legislation.
j. The facts in the instant case in brief were as follows. Freedom Path applied for recognition as a social welfare group under Code Sec. 501(c)(4). The IRS concluded that many of the organization's communications were political campaign activities and that it was not being operated primarily for the promotion of social welfare. The IRS denied the application based on a facts and circumstances analysis of the organization's advertisements and other documents.

[17] Reg. sec. 1.501(c)(4)-1(a)(2)(ii)).
[18] Freedom Path, Inc., (CA5 1/16/2019) 123 AFTR 2d 2019-466.
[19] IRC Sec. 527(f)(1).
[20] Rev Rul 2004-6, 2004 IRB 328.

The organization challenged Rev. Rul. 2004-6 as so vague and inhibiting of its First Amendment rights that it was unconstitutional.

k. The district court held that Rev. Rul. 2004-6 was not unconstitutional. The organization appealed to the Fifth Circuit which concluded that the organization did not have standing to bring the suit so that it did not address the merits of the challenge.

9. Charity – House Donation.

a. Overview.

i. This rather detailed case is quite fact specific but offers valuable lessons on several important charitable giving topics that have much wider applicability. There is a detailed discussion of what is required to constitute a qualified appraisal, with a number of points of what not to do in an appraisal for a charitable donation if you want it to be respected. Another key issue was the receipt of a quid-quo-pro benefit that disallowed a portion of the taxpayers' hoped for deduction. There is also a discussion of the rules on donations of a partial interest that stresses the importance of understanding applicable state law. These are all valuable lessons for donors, advisers and charities alike.[21]

b. Facts Generally.

i. Taxpayers donated a house, personal property in the house, and cash to a charity, Second Chance, Inc.

ii. In April 2011, the taxpayers purchased real property which included a remodeled house in good condition. Later, they identified defects with the house and sought to have it demolished so they could build a new house on the property.

iii. Taxpayers hired a builder to demolish the house and to build a new residence. Prior to the demolition, the taxpayer contacted the charity about donating the house. The charity takes apart homes, salvages building materials, fixtures, and furniture and thereby provide employment to the disadvantaged and training. On December 1, 2011 the taxpayer signed a contract with charity for this work in deconstructing their house.

iv. The charity advised the taxpayers that they could claim an income tax deduction for the value, as determined by a qualified appraiser, of the salvaged property that was received by the charity's warehouse.

v. The taxpayers were also supposed to donate $20,000 in cash to the charity to offset the charity's anticipated costs of the project.

vi. The taxpayers hired appraisers to value the house and personal property. The appraiser used a sales comparison approach to value the house based on its highest use which the appraiser determined was based on keeping the house intact and moving it to another site for use as a residence. A second appraisal was premised on a conveyance of the entire house to the

[21] Lawrence P. Mann et ux. v. United States, No. 8:17-cv-00200.

charity and used the estimated cost to reconstruct the house to determine value.

vii. On December 1, 2011 the taxpayers signed an agreement with the charity conveying all of her rights, title, and interest in "the improvements, building and fixtures located on the Premises" to the charity. There is no evidence that this agreement was recorded.

viii. The charity estimated that the deconstruction of the house would yield items with a fair market value of at least $150,000, but kept no records, as it had indicated it would, of the salvaged items.

ix. On their 2011 tax return the taxpayer deducted $675,000 which was the appraised fair market value of the house as a residence to be used intact at another location. When the IRS rejected that deduction amount, the taxpayers re-filed their 2011 tax return claiming a $313,353 deduction, based on the appraised deconstructed value of the house as calculated in their second appraisal based on the cost to build the house.

c. Partial interest issue.

i. The IRS went further and asserted that no deduction of any amount was permitted under Code Section 170 for a partial interest in a house. The taxpayers asserted that they had donated a discrete and separable interest in the house.

ii. The determination as to whether the interest donated is the taxpayers' entire interest and hence deductible, or rather is a partial interest and not deductible, is a question of federal law but the answer to may depend on state law property rights.[22]

iii. State law in this case provides that recorded ownership is what governs the determination of who owns an interest in real property. So, the contract the taxpayer signed with the charity, because it was not recorded, did not satisfy this requirement. So, while the taxpayers could sever the ownership of the house from the land to have donated an entire interest in that severed interest in the house, because it was not recorded that severance did not occur. So, the court viewed the taxpayer's donation as comparable to the taxpayer having given a mere license to the charity to use the house for salvage and training. This was merely a partial interest in the property and did not qualify under Code Sec. 170(f) as a charitable contribution.

d. Appraisal issues.

i. The IRS also took issue with the amounts the taxpayers had tried to claim for the donation. The property to be donated was not moved to a new location and used as a house which the first appraisal presumed. Instead, the property was dismantled as part of a training exercise so only salvage value remained. The IRS analogized the case to another

[22] US v. Craft, 535 U.S. 273, 278 (2002).

case where a taxpayer donated a house to the fire department to burn down as part of a training exercise. In that case the taxpayer tried to value the donation as the difference in the value of property as the value of the land with the house and the value of only the land. The Court held that was incorrect since the house was burned down as a condition of the donation, and that fact had to be considered.[23]

ii. The second appraisal obtained by the taxpayers did not fare much better than the first. The Court held that since the deconstruction process would necessarily destroy components of the house only those that remained after the training exercise was complete could be valued for donation purposes. That would be more than a house donated to a fire department to be burned down, but less than the value of reconstructing the house as the appraiser had assumed.

iii. The IRS also denied the taxpayer's deduction for the donation of personal property in the house because the appraisal was deficient. Any donation of non-marketable property of more than $5,000 must be accompanied by a qualified appraisal. Code Sec. 170(f)(11). A qualified appraisal must specify the valuation approach used. The taxpayer's appraisal did not indicate the specific methodology used for appraising each item. It only provided fair-market values for several items. The appraisal indicated that the values should be reduced by costs incurred and estimated depreciation but only did so in a haphazard manner.

e. Donations should be offset by benefit received.

i. The IRS further attacked the taxpayer's deductions on the basis that they received a benefit, or quid quo pro, for the purported donation. The benefit was that the charity demolished the house which they not only wanted demolished, but for which they consulted with a builder about demolishing it before arranging with the charity to do so.

ii. The Court held that the taxpayers gave a required cash contribution to the charity in order to secure the charity's agreement to accept its donation of the house and its contents. The court did not find that the taxpayers did so not to secure some tangible goods or service in return, but to secure the ability to donate to a charitable cause and to obtain a tax deduction, which is not a specific benefit negating the deduction. The IRS argued that the benefit of the cash donation was the deconstruction of the house. But the Court reasoned that the taxpayers had already executed agreements transferring ownership of the house to the charity so that the deconstruction benefited the charity not the taxpayers. The Court also found in the instant case the taxpayer did not avoid all demolition costs as a result of the arrangement with the charity.

10. Charity – Conservation Easement.

[23] Rolfs v. Commissioner, 668 F.3d 888 (7th Cir. 2012).

a. A deduction for a conservation easement was denied.[24] To qualify as conservation easement under Code Sec. 170 the real property must be subjected to a perpetual use restriction. In the instant case the developer had reserved the right to identify the location of a future structure within the conservation area. The Court held that specifically defined use restriction on the real property had to exist when the easement was donated. The permission to locate a development within that area at a later date prevented a precise delineation of the restriction.

11. Charity – Private Foundation Self-Dealing.

a. The Code imposes an excise tax on certain acts of self-dealing, between a private foundation and disqualified persons.[25] Taxpayers with private foundations that have not been as careful as, perhaps, they should have been in operating the foundation in strict conformity with the tax requirements should review foundation activities with their advisers and be proactive about correcting any issues. The lists below might well indicate that the IRS has identified common foundation problems and is looking to identify other taxpayers violating the rules.

b. A self-dealing transaction must be corrected. This includes filing Form 4720 – "Return of Certain Excise Taxes on Charities and Other Persons Under Chapters 41 and 42 of the IRC," and the required excise tax must be paid.

c. Hot button issues to be considered with respect to private foundations and disqualified persons include the following:
    i. A self-dealing transaction occurred, but no Form 4720 was filed.
    ii. Loans were made from the foundation to a disqualified person.
    iii. The foundation's property was used by a disqualified person.

d. The IRS has set forth rules taxpayers should follow to correct a self-dealing transaction.[26] It has also provided the following guidance for its auditors for identifying self-dealing transactions:

e. Th IRS has suggested several audit tips to be followed by agents examining possible self-dealing transactions. These include:
    i. Investigate records of the private foundation to identify transactions between the foundation and disqualified persons.
    ii. Review contracts, meeting minutes, interviews, personnel and payroll records to identify such transactions.
    iii. Review balance sheets.
    iv. Review assets listings and depreciation schedules.
    v. Determine the location of all assets, even fully depreciated ones, and identify who is using them.
    vi. If the foundation owns real property, determine whether disqualified persons might be using it for hunting or other personal uses.

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[24] 151 TC No. 14 Pine Mountain Reserve, LLP.
[25] IRC Sec. 4941.
[26] Reg. §53.4941(e)-1(c).

vii. If there are fully depreciated vehicles, might a disqualified person be using one? Perhaps the IRS is endeavoring to identify a vehicle that since fully depreciated might be viewed inappropriately as one which a disqualified person might use.
viii. If the foundation owns artwork, confirm where it is listed as being held on the foundation's books (e.g., in "storage") and also determine where it is actually being held. Might art be in a disqualified person's residence or business?
ix. If fully depreciated assets were disposed of, determine if they still had value. How and to whom were the disposed of? Were they given to a disqualified person? Perhaps the IRS is endeavoring to identify asset values inappropriately transferred to a disqualified person.
x. Tour buildings and real estate assets to determine how and who is using them. Might a disqualified person be using it?
xi. Review rental agreements, sales contracts, agreements, etc. Be alert for "side deals" between a foundation and a disqualified person.

f. Practitioners might consider informing clients of these hot button issues and warn them that if there are any possible transactions that might fall within the ambit of the above list that they should set up an appointment to review these.

12. Charity - Remuneration.

a. The IRS issued guidance on excess renumeration paid by exempt organizations.[27]

13. Clawback of Temporary Exemption.

a. Regulations were issued confirming that a taxpayer's use of the temporarily enhanced gift tax exemption will not result in a recapture or clawback when the exemption declines.[28]
b. These Regulations provide favorable results assuring no clawback of the current high temporary exemption if it is used.
c. In computing the amount of Federal gift tax to be paid on a gift or the amount of Federal estate tax to be paid at death, the gift and estate tax provisions apply a unified rate schedule to the taxpayer's cumulative taxable gifts and taxable estate on death to arrive at a net tentative tax. The net tentative tax then is reduced by a credit based on the applicable exclusion amount ("AEA"), which is the sum of the basic exclusion amount ("BEA") under Code Sec. 2010(c)(3) and, if applicable, the deceased spousal unused exclusion ("DSUE") under Code Sec. 2010(c)(4).
d. What is the manner in which the calculations will be made to avoid a clawback? Start with gross estate inclusive of adjusted taxable gifts. Calculate a tentative estate tax. Subtract a hypothetical gift tax (using rates in effect at the date of death) but using the basic exclusion amount ("BEA") at the time of the gift. That was $11.4 million. Adjustments for deductions should be made. Subtract deductions- and calculate estate tax due and apply credits. Most would have

[27] Notice 2019-9.
[28] Prop. Regs. 20.2010-1(c); Reg-106706-18.

thought the issue was how the gift tax was calculated, but the proposed Regs address this at the last stage of the calculation. Use the higher of the BEA that applied at the time the gifts were made, or at the time of death.

e. **Example**: The taxpayer makes a $9 million gift sheltered by the gift tax exemption in 2019. The taxpayer then dies after 2025 when the exclusion has dropped to $5M inflation indexed. Use the BEA to determine how much estate tax credit the estate is to receive. This is the BEA used in determining the gift exclusion at the time the gift was made, which was $9 million or the BEA at death. So, assume BEA is $9 million and prevents decedent from paying estate tax on a gift made when exclusion was higher.

f. The "off the top" gift tax issue was negatively resolved. Assume that a taxpayer makes a gift of $5M in 2019 and makes no further gifts. If the taxpayer dies after 2025 and the enhanced exclusion no longer provides benefit, some had speculated that the gift would be deemed to have been made off the top of the exclusion amount possibly have left the remaining exclusion intact, but that was not addressed in the proposed Regulation and it appears the intent was to negate the ability to make a gift of the top portion of the exclusion (i.e. the temporarily enhanced exclusion) and retaining intact (i.e., intact after the reduction in the exclusion amount) the remaining exclusion. This does not seem feasible. The fact that a bottom tier of exemption may not be preserved suggests that taxpayers who cannot afford to make sufficient gifts to use both spouses' full exemptions, might instead consider the merits of having just one spouse use all of his or her exemption and have the other spouse retain his or her entire exemption intact. This one-spouse-gifts approach might for some clients provide a net better result.

g. For example, what if the wife died during period of higher exemption, e.g. in 2019, and the surviving husband calculated his DSUE off that larger amount? Thereafter the surviving spouse dies after exclusion has declined. Does the surviving spouse on death get the DSUE based on the larger amount that existed with the first spouse died? Should it be the DSUE calculated at the time of the first spouse's death? Yes, so the surviving spouse should obtain the benefit of the larger DSUE (i.e., based on the temporary high exemption that existed when the first spouse to die passed).

h. The fact that the clawback issue has been resolved should serve as a strong incentive for "moderate" wealth clients ("moderate" relative to the current high exemptions) should be encouraged to plan now, certainly before 2026 when the exemption is going to decline, but perhaps even before the 2020 election. If the "blue wave" of the 2018 mid-term election continues, the exemption amount could be reduced before the 2026 scheduled halving of the exclusion. For example, the estate tax proposal by Bernie Sanders in S. 309 proposed a mere $1 million gift exemption and a $3.5 million estate tax exemption, much less than the 2026 anticipated reduced amount. Practitioners should proactively educate and encourage clients to plan and avoid a repeat of the 2012 deluge of clients trying to get planning done just prior to a possible change in the exemption. Also, consider more robust planning than many executed in 2012. Gifts should not only be made in trust and not outright, but for many clients gifts to trusts that they can access such as non-reciprocal spousal lifetime access trusts or domestic asset protection trusts. See comments below concerning the Wacker case and the reciprocal trust doctrine.

i. This Regulation begs the question for many clients "what are you waiting for?" With the risks to the estate tax of the so-called Blue Wave continuing in 2020, and the proposal made by Senator Bernie Sanders (discussed later in more detail in this monograph) clients of even "moderate" wealth should be investigating transfers to reduce their estates now.

14. Connecticut.

a. Connecticut has proposed a change in its estate tax.[29]

b. "*Sec. 4. Subdivision (2) of subsection (e) of section 12-391 of the general statutes is repealed and the following is substituted in lieu thereof (Effective from passage):*

   i. *(2) (A) For a nonresident estate, the state shall have the power to levy the estate tax upon all real property situated in this state and tangible personal property having an actual situs in this state.*

   ii. *(B) For real property and tangible personal property owned by a pass-through entity, the entity shall be disregarded for estate tax purposes and such property shall be treated as personally owned by the decedent if (i) the entity does not actively carry on a business for the purpose of profit and gain, (ii) the ownership of the property by the entity was not for a valid business purpose, or (iii) the property was acquired by other than a bona fide sale for full and adequate consideration and the decedent retained a power with respect to or interest in the property that would bring the real property situated in this state or the tangible personal property having an actual situs in the state within the decedent's federal gross estate. For purposes of this subparagraph, "pass-through entity" means a partnership or an S corporation, as those terms are defined in section 12-699, or a single member limited liability company that is disregarded for federal income tax purposes.*

   iii. *(C) The state is permitted to calculate the estate tax and levy said tax*

   iv. *to the fullest extent permitted by the Constitution of the United States*."

c. The concept of disregarding a partnership or other pass through entities to tax real estate is an expansion of Connecticut's ability to tax real and tangible property of non-residents for estate tax purposes. Other states have similar provisions to pierce entities that hold real estate.

[29] S.B. No. 1090 [cga.ct.gov] (Raised) An Act Concerning The Department Of Revenue Services' Recommendations For Tax Administration.

d. For many years, it appeared as if the trend were for states to reduce or eliminate state estate taxes, but that trend may be reversing with Connecticut, New York and California (see other updates in this article) moving in the opposite direction. This, as pointed out in the discussion of Sanders estate tax proposal, may be part of a movement overall towards more restrictive and costly estate taxes reversing the recent trends on both federal and state levels. "Support for raising taxes is widespread, according to a new poll, which found that 76% of registered voters want the wealthiest Americans to pay more."[30] That is a statistic that should alarm those of wealth and motivate them to plan now before the current favorable transfer tax environment is changed adversely.

15. Deaf Clients.

a. There are more than 2.2 million people who are considered deaf living in our country.[31]

b. It is suggested that communication is the biggest hurdle. "*Communication is dependent on a gamut of variables. For one, it may depend on whether the person was born deaf or lost their hearing later in life. Additional accommodations should be made when working with a couple where one is deaf and the other is hearing…It quickly became clear to me that written communication or closed captioning isn't sufficient. The deaf community typically uses ASL, which is very different from spoken English — or any other language. Additionally, many of the common terms and concepts we use in our industry do not exist in ASL*."

c. Typing in a Word document on a smart board or larger monitor may be useful. Secure interpreters for meetings with deaf clients.

16. Decanting.

a. Decanting has become so popular and talked about that it is almost surprising to see a case challenge an attempt to decant. It shouldn't be. It is not uncommon that once a planning technique takes hold clients will push the edges seeking to expand the scope of what is possible.

b. In a recent Nevada, the Court considered a district court order granting a motion to decant half of a trust's assets from a charitable trust into a new charitable trust. The Nevada Supreme Court reversed the order denying the right to decant. The facts in the case included that the trust instrument required unanimous vote of the trustees to make a distribution. Only one of the two co-trustees wanted to decant 50% of the trust into a new trust. That new post-decanting trust would continue the purpose of the transferor trust but just one trustee as the sole trustee. The transferor trust would retain 50% of the assets and have the other co-trustee solely

[30] http://fortune.com/2019/02/04/support-for-tax-increase-on-wealthy-americans-poll/

[31] Matthew Phillips, "Voices This client community isn't underserved. It's ignored," Apr 8 2019, https://www.financial-planning.com/opinion/how-financial-advisors-can-help-deaf-clients?utm_campaign=Apr%208%202019-ria_iq&utm_medium=email&utm_source=newsletter&eid=1e37f45019da92648262289efc5464d1

in charge. The court determined that the requirement of the governing instrument for both trustees to agree had to be met.[32]

17. Estate Tax Proposal – Bernie Sanders.

   a. However, the "theme" of the Sanders tax proposal above, Warren's proposal, the California consideration of enacting an estate tax with a 40% tax rate with a $3.5 million exemption, New York enacting a mansion or millionaires' tax, and so on, might start to all suggest a pattern that practitioners should be aware of and proactively advise clients to plan for.
   b. Congressman Bernie Sanders' proposed tax act, entitled "For the 99.8 Percent Act," S. 309 116th Cong. (2019) (the "Act") should concern everyone with wealth and their advisers.[33] While few, if any, believe the estate tax bill proposed by Sanders could be enacted with the current Trump White House and a Republican Senate, practitioners should take heed of the intent behind the proposals made in the Act. While one might dismiss this as mere electioneering by Sanders, be careful as this proposal might be a glimpse as to what could occur if the so-called Blue Wave (that is, the Democrats winning both Houses of Congress and the White House) from the 2018 mid-term elections continues through the 2020 election. It is worthwhile noting that many of the Sanders proposals have been made in the past by others.
   c. Why Practitioners Should Care.
      i. While there may currently be a Federal estate tax and gift tax exemption of $10 million inflation adjusted (currently $11.4 million in 2019) that does not mean practitioners should be unconcerned with planning for clients with lower level of value of assets than the current exemption. The bill proposes a dramatic reduction in the exemption and restriction or elimination of several of the most powerful planning tools in an estate planners arsenal.
      ii. Some ultra-wealthy clients have appeared to plan with renewed vigor since it became clear that President Trump was unable to repeal the estate tax. In contrast, many moderate wealth clients ("moderate" relative to the current exemptions) say in the $5 million to, perhaps, $40 million wealth range, appear to have neglected planning as not really relevant to them. That could prove a costly mistake depending on the outcome of the 2020 election. Is it really worth the risk? Most clients do not find dealing with estate planning particularly enjoyable, so practitioners must educate them as to the risks this mere Sanders' proposal that is unlikely to get enacted may mean for their future. It is relatively simple and inexpensive for a married couple to create, for example, non-reciprocal SLATs (spousal lifetime access trusts) and make gifts of, perhaps, $10 million each under

[32] In the Matter of the Fund for the Encouragement of Self Reliance, An Irrevocable Trust, 135 Nev. Adv. Op. No. __ (March 21, 2019).
[33] Shenkman, Tietz, and Blattmachr, "Bernie Sanders Estate Tax Proposal: Might it Foreshadow Future Dem Proposals?" Leimberg Information Services, Inc. April ___, 2019.

current tax law. If legislation similar to Sanders proposal is enacted, as a result of a Democratic sweep in 2020, the same couple might face a daunting task to shift wealth, and the cost of doing so could be dramatically greater. Even if a client guesstimates only a 10% likelihood of both events occurring (a Democratic sweep and a Sanders-like estate tax change being enacted), isn't it worthwhile to plan and avoid that risk? Modern trust planning techniques provide an array of options to permit a client to benefit from assets transferred to completed gift trusts that can use exemption. These include: DAPTs, hybrid-DAPTs where someone in a non-fiduciary capacity can name the settlor as a beneficiary, special powers of appointment to direct a trustee to make a distribution to the settlor, variations of non-reciprocal SLATs, loan powers, floating spouse-clauses, etc. If clients can have access to the assets transferred, what is the impediment to proceed with planning in light of the risks posed by Sanders proposal? Other than the cost of the planning, there may be no substantive downside of planning now versus waiting and facing a potentially dramatically more limited planning regime? In fact, because effective estate tax planning although always requires assets be removed from claims of the client, this planning may benefit him or her, as well as his or her family. That may be a calculus many moderate wealth clients have viewed quite differently with the current high exemptions. But that perspective should be reexamined.

d. Overview of Sander's Proposed Act.

   i. Senator Sanders has proposed a tremendous increase in the estate tax, with the Act reducing the Federal estate tax exemption from the current $11.4 million to the $3.5 million level that existed in 2009. Some have argued to make it even smaller. The Act would also impinge upon the ability of clients to make lifetime gifts, reducing the lifetime (gift tax) exemption to a "mere" $1 million. For those in the moderate wealth range, considered in this case to be $3 million + this could be significant and a dramatic change from the current planning environment. For the wealthy, the dollar value of the exemption is critical. Too many wealthy clients, however, have been adopting a "wait and see" planning tactic, choosing to sit back and rely on the high current $11.4 million per person exemption, assuming the exemption as making the estate tax irrelevant to them. Sanders' announcement and the provisions of the bill should be a wakeup call for those clients, as well as for practitioners. It should be a call to action for clients to use their exemptions and use it wisely (discussed below), before it disappears even faster than it was slated to do so under the Tax Cuts of Jobs Act of 2017 (reducing by half to $5 million, inflation adjusted, in 2026) if there is a sufficient Democratic shift in Washington.

   ii. Senator Sanders also proposed in the Act raising the estate tax rates with a maximum rate of 77% for estates over $1 billion. As a perspective, do not view that as too radical as that was the rate on estates above $10 million until 1977. For the uber wealthy, the marginal rate is the biggest fear as at high wealth levels the exemption becomes rather insignificant. At that level of wealth, estate planning has never really been only about the exemption, as even the current high amounts are relatively insignificant to the very wealthy. The marginal estate tax rate is really critical in terms of the estate tax pain felt by these clients.

iii. The proposed changes are much tougher on clients than just the lower exemptions and the rate increases may indicate. Sanders' changes include restrictions on the use of valuation discounts, grantor retained annuity trusts ("GRATs"), and more techniques that have been the grease for many estate plans completed up to this point. The proposed restrictions on planning techniques may have an incredibly negative impact on the ability of very wealthy taxpayers to shift wealth to future generations without significant wealth transfer tax. So, the clients at this level of wealth should really be planning with vigor and not wait to see what might occur in 2020 or beyond. If one opts to wait, clients and practitioners might face a scenario similar to the end of 2012. There was considerable worry at the end of 2012 that the estate tax exemption would drop from $5 million to $1 million in 2013. Taxpayers lined up outside their planners' offices hoping to get work done in time. Due to waiting until it was almost too late, some taxpayers had too little time to consider the implications of planning. In addition, compressed 2012 planning schedules increased the risk of causing step-transaction doctrine issues because there often could not be much time between different actions or transfers. The 2012 rush resulting in some cases where planning that really didn't serve the client's needs as they might have hoped was created, as there just wasn't enough time for clients to absorb ideas or planners to compete forecasts or other steps a calmer planning schedule would have permitted. Also, if you wait to the last minute, what if there is a Democratic victory and the effective date of new tax legislation is so soon after the election that it precludes clients from completing any of the planning they wish to do? Consider the effective dates of Sanders' proposed changes to the estate tax rules, which are proposed to be effective for anyone dying after December 31, 2019. Wait and see might be the strategy most clients wish to employ, but it could also be a costly mistake.

e. Again, why wait? With modern trust drafting techniques, practitioners can craft plans that allow clients to have the ability to perhaps benefit in some manner from assets transferred out of their estates. This might include in the use of non-reciprocal spousal lifetime access trusts, some control over investments in a fiduciary capacity (as the investment advisor of a directed trust), and other steps that traditional trust drafting which was less flexible did not afford. So, pose the question to your clients: why wait?

f. How Sanders' Act Would Change Planning.

i. Here are some of the changes in the Act and what they might mean to planning if some variation of each change is enacted:

ii. Exemption: The proposed $3.5 million exemption would greatly reduce the ability of wealthy people to shift wealth out of their estates, or into protective structures that may limit the reach of divorcing spouses or claimants. This might mean that there is a great advantage for clients to using the current $11.4 million exemption now, or as much of it as possible, before a change is enacted. For clients of moderate wealth ("moderate" relative to the current exemption amount) consider that they might be able to make a simple gift to a trust to accomplish much of the asset protection, estate tax planning, succession planning and other goals that client has. Waiting might necessitate the use of much more costly and complex planning, and some of those same techniques are also curtailed under the Act as proposed.

iii. **<u>Example</u>**: Doctor Jane has $6 million in savings, $1 million in a house and $2 million in a retirement plan. As a surgeon she is worried about malpractice risks. She is also concerned about what might change with the estate tax rules if the political winds blow in another direction. She would like to remove $5 million from the reach of claimants and the estate tax. If she created a self-settled domestic asset protection trust ("DAPT") today she can gift $5 million to the trust by transferring securities (e.g., ACAT, using the Automated Customer Account Transfer system) securities to her new trust, and signing any documents needed to confirm the gift being made. If the exemption drops to $3.5 million that would limit what could be transferred to the trust, and the excess above $3.5 million would be more difficult to transfer given the other restrictive changes proposed in the Act. It might no longer be practical to do so at that point. So why wait?

iv. Credit Shelter Trusts and One-Fund QTIP Trusts: Years ago, the default or common estate plan for married couples might have been to fund a credit shelter trust to the largest amount that would not generate a state or federal estate tax. As the exemption grew, the default plan for married couples evolved to a so-called one-fund QTIP that might have provided the surviving spouse the right to disclaim into a family (or credit shelter) trust, or, perhaps, give an independent (according to some views) executor the right to elect the portion of the QTIP qualifying for the marital deduction thereby shifting funds to a credit shelter trust. A drop in the exemption to a $3.5 million level might suggest that reverting back to the historic default plan will prove better for many clients.

v. Credit Shelter Basis Planning Risk: Practitioners have been helping advise and guide clients on terminating credit shelter trusts or distributing appreciated assets out of a credit shelter trust to garner a basis step up on the death of the surviving spouse. If a Sanders type bill is enacted after the

2020 election that could prove a costly mistake. While terminating or distributing assets out of a credit shelter trust to gain a basis step up might be advantageous with an $11.4 million exemption it could prove to be a very costly gambit if the surviving spouse dies after the exemption drops.

vi. Gift Exemption: As mentioned above, the Act also would reduce the gift tax exemption (how much you can gift during your lifetime without a current gift tax) to a $1 million. That would inhibit a lot of the common planning techniques practitioners use today.

vii. Clawback:

1. It seems that the Bill is attempting to honor any prior use of the unified credit, even though the credit would be significantly reduced under the Bill. The Act might propose that if a client make gifts this year to use their current high $11.4 million exemption, there will be a penalty for that with the gifts "clawed" back into their tax calculation. If that were to be enacted, it might already be too late to plan. Again, while few if any practitioners believe that the Act will be passed with a Republican Senate and Presidency, the changes proposed, like these gift tax changes, would radically restrict planning. This clawback proposal, if this is the correct interpretation, is important to communicate to clients.
2. The question of whether the Sanders proposal would cause a clawback or not seems to turn on the reduction as applied to the phrase "the amount of tax computed under subsection (b)." Starting with a "prejudice" that the bill wanted total claw back and, therefore, it could be assumed that the term "tax" was the gift tax credit calculated under Section 2001(b). In other words, it would be assumed that the reduction in "tax" was not addressed to the net estate tax computed under Section 2001(b) but rather the gift tax offset (credit) computed under that section which is subtracted from the estate tax otherwise calculated under the section.
3. One colleague wrote concerning the possible claw back: "*I keep reading and reading the language and propose new subsection (h) to Section 2001 which adds an "adjustment to reflect changes in exclusion amount." I've gone over it and over it. At first, I computed the estate tax on an included gift using rates at the date of gift but then realized subsection (g) would require the use of rates at the date of death. At least, I think that's what subsection (g) requires. The addition of subsection (d) to section 2502 and particularly (4) which defines 'applicable exclusion amount' confused me since that same phrase is used in the estate tax adjustment paragraph. When I tried to insert the gift application exclusion amount from 2502, I end up with a credit – money back to the estate – which obviously was not intended. I've come around*

to the view that the new 2001(h) is really designed to avoid clawback, but …" While the language may be unclear, certainly from a planning perspective the earlier planning is completed perhaps the better.

4. Many likely assume that they can wait until after the 2020 election and then, based on the election results, determine whether or not to incur the cost and hassles of planning. But if this type of provision is replicated in future legislation it might negate the ability to plan effectively after new estate tax legislation is proposed if there is a Democratic sweep. This is a risk that clients should weigh carefully. For example, it is common to transfer assets to a DAPT before marriage to backstop a prenuptial agreement or in lieu of a prenuptial agreement. That type of planning would have to rely on incomplete gift trusts or may no longer be feasible with such a low gift exemption. Also, if the gift exemption is reduced to $1 million, the ability of clients to leverage wealth out of their estates, to implement asset protection planning, to safeguard assets for matrimonial purposes, etc. could all be severely hindered. Practitioners must also consider the range of other restrictions proposed in the Sanders' Act. If GRATs, discounts, and other techniques are also proscribed as proposed in the bill, the ability to plan around a $1 million exemption will be more limited than it had been in the past years when the $1 million exemption was law. Then, discounted FLP (family limited partnership) interests inside GRATs, "rolling" GRATs, etc. all facilitated wealth transfers "around" the low $1million exemption. If a sweeping change as Sanders has proposed is enacted, the prior means of dealing with a low exemption will largely not be available.

viii. Upstream Planning: Many practitioners have touted the use of "upstream" planning to salvage otherwise unusable exemptions that elderly relatives of clients have. For example, if a parent has an estate of only $4 million, the parent's child could create a trust with $7 million, and give parent a general power of appointment ("GPOA") over that trust. That GPOA could require the consent of a non-adverse party, could be crafted as a limited power of appointment and someone could hold the right to convert it to a GPOA, etc. The intent of the plan was that parent's estate would include the assets in the trust and those assets would garner an estate tax free adjustment (hopefully step-up) in income tax basis on parent's death. If the exemption is reduced to the $3.5 million as in the Sanders' Act, most or all upstream planning would be obviated. If that occurs practitioners might want to review that planning to be certain that the estate inclusion in the upstream plan does not inadvertently trigger an unintended estate tax on the senior generation's death. While many such upstream plans were likely crafted to only include in the senior generation's estate an amount that does not trigger an estate tax, the more prudent course of action would be to confirm that. Clients who only recently had planning updated to address the inclusion of GPOAs to a higher generation will likely be frustrated by the yo-yo tax law changes and ongoing planning updates. Indeed, a safe alternative to granting the parent a GPOA would be to give the parent a limited power of appointment which the parent could exercise at death to trigger the application of Section 2041(a)(3), the so-called Delaware Tax Trap which causes property subject to the special power to be included in the estate of the power holder. If there would be no tax benefit by causing the assets to be included in the estate of the parent, the parent would forego triggering the trap.

ix. Grantor Trusts: The heart of many estate plans for years has been the creation of grantor trusts. The bill would include in client's taxable estates all assets held by trusts that are grantor trusts, reduced only by taxable gifts made to the trusts. These are trusts whose assets are treated as owned for income tax purposes by the settlor who created the trust. Currently, this income tax characterization for a trust permits a GRAT to pay its annuity to the settlor with appreciated assets, without causing gain recognition. In addition, the creator of the trust will report any income attributable to the trust on their own tax return, therefore paying the income tax on trust income, permitting greater growth of wealth inside the trust. It also permits the client to sell assets to the trust without recognition of gain due to that sale and shift growth outside the client's estate. These sales, often done for a note issued by the trust, have been a mainstay of planning in the estate planner's arsenal. Consider: What if you added to any new trusts you draft for your clients (or old trusts that you decant into new trusts) a provision that says if the assets of the trust will be included in the clients estate then effective one-day before the clients death, the trust shall convert to non-grantor and all power holders of the trust that are holding powers that could taint or characterize the trust as a grantor trust agree that those powers or rights will be extinguished. Might that work as a safety net just in case you don't have the time or ability to affirmatively turn off grantor trust status just before a client's death? The answer based upon the language in the Act seems to be no: if the grantor trust status ends during the grantor lifetime, he or she will be deemed at that time to have made a gift of everything in the trust other than the amount of taxable gifts made to the trust.

x. GST Tax: Another foundation of planning has been to shift value to an irrevocable trust and allocate generation skipping transfer ("GST") tax exemption to the trust. Properly done under the current system, the value of assets in that GST exempt trust, no matter how much they appreciate, should never be subject to the transfer taxation system. The compounding of wealth outside the estate tax system can provide incredible wealth shifting opportunities. When this is coupled with a long-term trust (a so-called dynastic trust), wealth can compound outside a client's estate forever. The Act appears to limit the application of the GST exemption to a maximum of 50 years. Indeed, it seems that the trust may not last more than 50 years. That change would hinder this type of planning and might result in a costly tax after 50 years of a trust's existence. If a change along the same lines as this proposal is enacted, but if it "grandfather's" existing trusts (i.e., the new restrictions only apply to trusts formed after the new law), many people, even those of moderate wealth, might benefit from creating long-term dynastic trusts now.

xi. GRATs: Grantor Retained Annuity Trusts ("GRATs") are a planning tool long favored by practitioners. A key benefit of GRATs is that clients can create these trusts to shift wealth out of their estates without using any (or any material) part of their gift tax exemption, to the extent the assets in the trust grow at a rate above the so-called Section 7520 rate (a relatively low rate the IRS announces each month). Many, perhaps most, GRATs were structured by practitioners as so-called zeroed out GRATs. This meant that the annuity payment the trust made to a client as the grantor creating the trust equaled (or almost equaled) the value of assets gifted to the trust. Upside appreciation (above the rate of return the IRS required be used in the technique) would inure to the beneficiaries of the GRAT with no gift tax cost. The bill's proposal almost certainly would eliminate the viability of this technique in many cases by requiring a minimum 10 year term for any GRATs created after the enactment of the bill. If a client does not outlive the term of the GRAT, some or all the assets (generally) are included in the client's estate. That would dramatically increase the risk of a GRAT not succeeding. There is also a minimum required gift amount (equal to 25% of the amount contributed to the trust), effectively removing the ability to have a "zeroed out" GRAT (that is, one that produces no significant taxable gift). These two changes could potentially make GRATs impractical for very wealthy taxpayers that have traditionally used GRATs when they no longer had gift tax exemption remaining. It would also seem to eliminate the commonly used technique of "rolling-GRATs", where practitioners would create a 2 year GRAT and the client would "re-GRAT" each annuity received to a new GRAT and continue to shift appreciation beyond the Sec. 7520 rate out of the estate taxation system.

xii. Discounts: Valuation discounts would be severely restricted under the Act, e.g. not permissible in a family planning context and would come into effect upon passage of the Act. Comparison may be given to the proposal in Connecticut discussed above.

xiii. **Example**: Client wants to gift $18 million of interests in LLCs that own neighborhood shopping centers. If these are non-controlling interests, then under current law the interests might be valued after a valuation discount at perhaps $11 million. At the current gift tax exemption, the client might be able to simply gift all these interests to a trust for descendants. The discount in value is due to the interest she or he may transfer does not control the LLCs and cannot dictate when a distribution is made or when the LLC might be liquidated. If the client waited until after the bill is enacted, or a similar proposal is enacted, the elimination of discounts might reduce the percentage that can be gifted. If the exemption is lowered as well, even less can be transferred tax free. This is all potentially even worse still. Based on some recent case law developments (such as Estate of Powell v. Commissioner, 148 TC—No. 18 (2017)), the IRS might argue that if she retains any interests in the LLCs after the transfers are made, that the client "in conjunction with" others (i.e., those to whom the interests are gifted) controls the LLC and, therefore, even the interests which client thought he or she transferred end up included in his or her taxable estate. The lower exemption and restriction or elimination of discounts will make it more difficult for clients to shift remaining equity positions out of their estate under a Sanders' estate tax regime to avoid the reach of Estate of Powell.

xiv. Crummey Powers: Another common planning tool has been for clients to make gifts to trusts from which a class of beneficiaries can withdraw a pro-rata portion of the gift made by the grantor, up to the annual gift exclusion amount for that beneficiary. (The power of withdrawal is known as a Crummey power and it allows gifts to the trust to qualify for the gift tax annual exclusion under Section 2503.) This has facilitated the ability for clients to make large gifts to a trust, e.g. used to buy and hold life insurance, and not incurring any gift tax cost by reason of the gift. The bill has proposed eliminating this technique. If this applied to all trusts after enactment, the results could eliminate the common Irrevocable Life Insurance Trust ("ILIT") which has been ubiquitous in estate plans. Practitioners might discuss with their clients implementing an ILIT so it is in place before any changes are made to existing law, in case existing trusts are grandfathered (i.e., exempted from the new change). Clients might also consider making large gifts now (using that exemption that might also disappear) so that they won't have to rely on annual gifts to fund their life insurance premium payments.

xv. **Example**: Client has a typical ILIT with Crummey powers. Premiums are $75,000/year and are easily covered by the annual demand powers available to children and grandchildren who are beneficiaries of the trust. But if a Sanders' type law is enacted and Crummey powers prospectively eliminated (even for trusts predating the law change) the client will not be able to fund premiums without incurring a costly current gift tax cost. The client might be able to transfer a sufficient amount of marketable securities to the trust now, using his or her exemption, so that the future premiums can be paid from a combination of the income and principal of the gift made. It might also be worthwhile if this is pursued to inquiring as to the results of prepaying future premiums currently to minimize future income tax costs to the client.

xvi. **<u>Example</u>**: Since GRATs are also on the chopping block, a wealthier client who does not have adequate exemption remaining to complete a large gift as in the prior example, might create and fund a GRAT now that will pour into the ILIT (a common approach when exemptions were lower for a non-GST exempt ILIT). The GRAT could be planned to endeavor to shift value to the ILIT to avoid the gift tax issues if Crummey powers are in fact eliminated. This type of GRAT/ILIT plan might also be structured in a different manner than such plans had been historically. The traditional GRAT/ILIT plan would have entailed creating a two year GRAT with the ILIT as the beneficiary. Each time an annuity payment was made the client would re-GRAT the annuity into a new GRAT also benefiting the ILIT. But if GRATs are slated for restriction as in the Sanders' bill then perhaps a tier of GRATs with different terms might be created now, before the new GRAT restrictions are enacted, so that the existing GRATs may be grandfathered and continue to fund insurance premiums for years to come despite the restriction on Crummey powers.

g. Don't Dismiss the Sanders Proposal.

i. If you think that Sanders's proposals in the Act are just an inconsequential flash, think again. Many aspects of Sanders's proposal discussed above are not new and should not be a surprise to practitioners. Democratic candidates have long called for restrictions that would make the estate tax harsher. For example, President Obama's Greenbook proposals consistently proposed the reduction of the estate tax exemption to $3.5 million, but that was only a small part of the get-tough-estate tax plan he had proposed. Many of the commonly used estate planning strategies discussed above, such as grantor retained annuity trusts ("GRATs") that can shift value out of a client's estate to the extent that the growth in those assets exceed a mandated federal interest rates, note sale transactions to grantor trusts (the client sells a non-controlling interest in an asset whose value is discounted because of the lack of control and marketability of that assets to lock in not only the discounts but future post-sale growth), and much more were proposed to be curtailed in similar ways to those proposed in the Sanders' bill. Whoever helped craft the proposals understood many of the tax planning strategies the wealthy use to shift assets outside their estates. These and other changes from the Obama

White House appear to be part of the playbook for Sanders and other Democratic nominees.

h. Additional Planning Steps to Consider Now

    i. Following are a list of planning steps practitioners might propose to their wealthy and mega-wealthy clients, along with some of the reasons why planning should be pursued sooner rather than later. But keep in mind if the bill was made law tomorrow (unlikely) clients could already be out of luck. So, while there is certainly no means of predicting what might, or might not happen, practitioners should consider advising clients to at least review with their entire planning team whether they should accelerate their planning and get it in place now.

    ii. QTIPs: Marital trusts such as Qualified Terminable Interest Property ("QTIP") trusts are taxed in the estate of the surviving spouse. This technique is commonly used by practitioners and many have made this the default plan for many clients. However, if a much lower exemption is enacted through the Act, those clients with QTIPs could be exposed to the potential of a high tax cost. Consider implementing a disclaimer of part of the income interest in the QTIP now for clients currently with a QTIP trust created by a deceased spouse. That disclaimer could trigger a deemed gift of all of the QTIP assets (principal). That would use up part of the exemption the surviving spouse has before the law might reduce his or her exemption. It is not clear whether a change in the law might affect the unused exemption of the first spouse to die (called the Deceased Spouse Unused Exemption, or "DSUE"). Another approach might be to distribute out of the QTIP assets to the surviving spouse if the QTIP trust terms permit such a distribution, and have the surviving spouse gift those assets to, for example, a self-settled domestic asset protection trust ("DAPT") of which he or she can be a beneficiary. If a QTIP is not a GST exempt trust, consider creating a Sec. 678 grantor trust and shifting value out of the QTIP via a note sale to that new trust. Under the current law there are numerous options for practitioners to employ for their clients, but those clients may have to get them while they still can.

    iii. Crummey Trusts: Many irrevocable trusts, including the typical life insurance trust or ILIT, are based on the premise of making annual gifts that qualify for the (now $15,000) gift tax annual exclusion. But that the administration required to take advantage of this technique certainly can be a hassle: consistent gifts, writing checks, issuing annual demand notices (Crummey powers). Clients have consistently commented on their distaste of the steps required. Consider suggesting to clients that they make a big gift to the trust now (and file a gift tax return for that gift) that will cover what would have otherwise been annual gifts for a long time and dispense with future annual administrative hassles. If future laws lower the exemption or reduce annual gift exclusions, such as the proposals in the

Act, this kind of simplification likely would not be possible. If the Act removes the ability to use Crummey powers, clients will not be able to fund this type of trust the way they have in the past. Suggest to clients that they implement simplifying steps while they still can. In addition, practitioners might want to consider suggesting to clients decanting (merging) the existing old Crummey trust into a new trust that provides more flexibility.

iv. Split-Dollar/Note Sales: Many wealthy taxpayers, who can barely be considered wealthy now relative to the high temporary exemptions, engaged in split-dollar life insurance plans, note sale transactions, and other techniques to shift wealth out of their estates. The result is an existing trust that owes money to those clients for the purchase of assets (e.g., an interest in a family business), or on a note secured by life insurance. A simple gift to the trust within the parameters of the current high exemption might be used to unwind that old plan and simplify ongoing plan administration. But keep in mind that Sanders' bill if enacted as proposed, might clawback these 2019 transfers. While no one can determine what future legislation might do, it may well prove advantageous to have clients make these transfers and unwind the planning by using exemption while they still have it.

v. DAPTs/SLATs: Domestic asset protection trusts ("DAPTs") are trusts the clients create that they are a beneficiary of. Spousal lifetime access trusts ("SLATs") are trusts the clients create that their spouses are the beneficiaries. The key of these trusts for planning now is that clients may still benefit from assets they shift out of their estate. There are lots of options (and risks) with either of these techniques, but the key is that for most clients access is critical to have the ability to gift away sufficient assets to use most/all of their exemptions. Both of these types of trusts, if they succeed, might provide the client with access to the assets transferred. If the techniques are successful, assets might be moved outside the clients estate and be out of the reach of their creditors, but they may benefit from the trust if they need to.

i. Ancillary Planning Considerations Favoring Earlier Planning

  i. In formulating planning for clients, practitioners may consider some of the following concepts:

  ii. Step-Transaction Doctrine: If there are a sequence of steps in a plan that are not independent, the IRS might disregard them and collapse the plan into a single event, potentially causing an adverse result inconsistent with why the planning was initially completed. Although one court approved a short time period between transfers it is certainly preferable to begin planning earlier and have more time, and independent economic events, between transfers.

iii. **Example**: Wife gives $5 million of assets to her husband, who the next day gifts those assets to a trust that benefits the donor/wife (e.g., a spousal lifetime access trust or SLAT). The IRS might disregard the intervening step of the gift to the husband, and the husband's gift to the trust, therefore just treating the transaction as if the wife gave the assets directly to the trust. If she has already used her gift tax exemption, that could trigger a gift tax. If instead of the clients waiting to the last minute to complete planning, consider if the wife gave the gift to husband now in early 2019. Those funds are then commingled with the husband's assets and invested, perhaps, even using a different asset allocation. Then, more than a year from now in 2020, husband makes a gift to the trust. The intervening time, the fact that the transfers occurred in different tax years, and the investment with other assets, might all serve to reduce the risk that a step-transaction challenge can be successfully argued by the IRS. However, waiting might harm the client's planning.

iv. Reciprocal Trust Doctrine: In certain situations, a trust created for one taxpayer by another will be treated as created by the other if the taxpayer has created or creates a trust for the person who created the trust under what is known as the "reciprocal trust doctrine." One of the factors that can serve to differentiate trusts each spouse creates for the other and avoid the application of the doctrine is creating them at different times. The earlier the planning process is begun; the more time remains to differentiate the two trusts by time. For clients waiting until the last minute (however that may be determined) this differentiating feature will be sacrificed.

v. Asset Protection: Every doctor, attorney, accountant, and really every professional, board of director member, real estate developer, etc. should be concerned about liability exposure. Society seems to be getting meaner and more litigious as time progresses. The current large gift and estate tax exemptions make it easy for clients to transfer assets into protective irrevocable trust structures (whichever trust "flavor" that is chosen). If clients do not take advantage of the current exemptions while they are still in effect, the opportunity might be lost and at that point only more complex, costly and risker options may remain to shift wealth into protective structures.

vi. Suboptimal Trusts: Many old trusts are not optimally drafted, some have mistakes, many were created when planning styles were different (e.g. distribute assets at age 30 outright instead of keeping them in long term trusts), they may not have allocated GST exemption, and so on. Practitioners should suggest to clients that they allow you their advisors to do housekeeping now, while there's large gift and GST exemptions in case they are needed cleanup. For example, if clients decant (merge) an old suboptimal trust into a better drafted more modern trust consider making a late allocation of GST exemption to that trust. That means allocating some of the client's $11.4 million GST exemption to that trust now (rather than when a gift was first made years ago to the old trust). This late allocation might enhance the overall benefits of the trust in that it may then be outside the transfer tax system for as long as the trust lasts.

vii. While the bill proposed by Senator Sanders is unlikely to be enacted for some time, or ever, it is a clear indication of the direction in which Sanders and, perhaps, others in the Democratic party might wish to see the estate taxation system move. Clients can be advised that they can either wait and see and hope, or they can act now and take proactive steps in case any of the concepts proposed in the bill become reality. The latter certainly may prove more prudent.

18. Estate (Wealth) Tax Proposal – Elizabeth Warren.

a. Elizabeth Warren proposed a new wealth tax on wealthy Americans which most dismiss as impossible to enact or administer.
b. Warren had proposed an annual wealth tax on Americans with more than $50 million in assets at a rate of 2%, and 3% for over $1 billion.
c. This tax was estimated to affect only 75,000 families.

19. Estate Tax Proposal - California.

a. On March 26, 2019, California Senate Bill 378 was introduced to create a California estate tax with an exemption of $3.5 million. The proposed California estate tax phases out at the current federal estate tax exemption amount of $11.4 million to avoid subjecting a California resident to both federal and state estate tax. The tax rate would be a very high 40%.[34] The state estate tax would be deductible for Federal estate tax purposes so that, with a 40% Federal tax rate, the net "cost" of the California 40% estate tax would be 24%.
b. The taxes collected will be used to mitigate wealth concentration, i.e. to alleviate the so-called "wealth gap" and would fund a new "Children's Wealth and Opportunity Building Fund." To fund services that directly address and alleviate socio-economic inequality and build assets among people who have historically lacked them, including helping low income children build wealth through savings accounts.
c. The average white family has over 40 times more wealth than the average black family, and over 20 times more wealth than an average Latino family.[35] The goal of this tax is to address this disparity.

20. Ethics.

a. A recent American Bar Association publication reminded its readers that the ABA Standing Committee on Ethics and Professional Responsibility's Formal Opinion, Rule 1.4, requires that lawyers "self-report" to a current client if they have erred

[34] "Senator Wiener Introduces California Estate Tax Proposal to "Fund Programs Reducing Wealth Inequality," Mar 26, 2019, https://sd.senate.ca.gov/news/20190326-senator-wiener-introduces-california-estate-tax
[35] Id.

in the client's representation and if the error is material. The test is whether a disinterested lawyer would conclude that the error is reasonably likely to harm or prejudice the client; or is of such a nature that it would reasonably cause a client to consider terminating representation even in the absence of harm or prejudice.

b. What is an "error?" Is having created a credit shelter trust that now loses basis step up possibilities and no longer provides any estate tax benefit an "error"? It would seem that it is not an error, but how would it be characterized?

c. Self-reporting is a concerning concept. When might a practitioner undertake self-reporting? Perhaps, an independent attorney should be retained to guide the attorney as to whether or not self-reporting is required. Communication with the attorney's malpractice carrier before the reporting may be necessary under the policy or at least be wise to do.

21. Family Structure and Estate Planning.

a. Commentators have addressed for years the evolving American family unit and that the historic assumptions on which much of estate planning was premised, applies to a smaller segment of the population. That trend continues and below is yet another societal change that practitioners should be mindful of when assisting clients.[36]

b. The Van Dam article cited in the footnote below suggests that many middle aged parents, referred to as "the middle generation" have been devasted by opioid abuse and other substances. The result is that the middle generation's children are increasingly being raised by grandparents. "It's a responsibility that many didn't expect and weren't prepared for. Retired folks find themselves trading their sedans for minivans, moving out of their adult-only communities and searching for work to cover the expenses that come with raising a child."

c. For those affected the impact is far reaching. Financial plans need to be completely revised using new budgets reflective of the new financial responsibilities for one or more grandchildren. Will the grandparents be able to designate guardians for their grandchildren if the parents are assumed not sufficiently responsible to do so? This might require a formal adoption of the grandchildren. What becomes of legal documents? The need to provide succession of trustees to provide for and assist the grandchildren may change significant components of the grandparents planning documents. Issues of who should be appointed in various positions may change dramatically. The common default of many to name an adult child will not be viable if that adult child is struggling with addiction or other issues. Will it still be appropriate to name other children (siblings of the addicted child) in fiduciary positions or will the conflicts make this unpalatable? Perhaps, those affected might default to naming institutional trustees?

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[36] Andrew Van Dam, "How these grandparents became America's unofficial social safety net," Washington Post, March 23, 2019, at https://www.washingtonpost.com/us-policy/2019/03/23/how-these-grandparents-became-americas-unofficial-social-safety-net/?utm_term=.5fba3728e783&wpisrc=nl_evening&wpmm=1

22. FBAR.

a. The IRS has been pursuing with vigor those not reporting foreign bank accounts and other assets as required. In a recent case, the IRS was permitted to assess higher penalties where it found the taxpayer willfully failed to report foreign accounts.[37]
b. The maximum penalty assessed was 50% of the foreign account balance.
c. Some background first. U.S. citizens and resident aliens, including those with dual citizenship, have an annual April 15 deadline to e-file their annual Report of Foreign Bank and Financial Accounts (FBAR) if they have a foreign bank or financial account. In general, the filing requirement applies to anyone who had an interest in, or signature or other authority, over foreign financial accounts whose aggregate value exceeded $10,000 at any time during 2018. Because of this threshold, the IRS encourages taxpayers with foreign assets, even relatively small ones, to check if this filing requirement applies to them. The FBAR filing, Form 114, must be filed electronically with the Financial Crimes Enforcement Network (FinCEN). In addition, Form 1040, Part III of Schedule B asks about the existence of foreign accounts, such as bank and securities accounts, and usually requires U.S. citizens (and Alien Residents) to report these items for the country in which each account is located. Also, separate from the foreign accounts reporting requirements above, certain taxpayers may also have to complete and attach to their return Form 8938, Statement of Specified Foreign Financial Assets. Generally, U.S. citizens, resident aliens and certain nonresident aliens must report specified foreign financial assets on this form if the aggregate value of those assets exceeds certain thresholds.[38]
d. The facts in the case suggest why the IRS was not found to have abused its discretion in assessing harsher penalties:
    i. The taxpayer knew she had funds in foreign bank accounts.
    ii. She did not report the interest on those foreign bank accounts. Her income tax return reflected no foreign interest.
    iii. She managed her foreign accounts with the help of her overseas bankers.
    iv. She did not maintain the account in her own name.
    v. She hid the account from the IRS by not investing in U.S. securities
    vi. She failed to tell her accountant that she had a foreign bank account.
e. Practitioners may wish to discuss with or advise clients about the importance of complying with foreign reporting requirements and the harsh potential impact of failing to do so.
f. One of the confusing issues for many taxpayers is whether they have to file to report foreign accounts that they have no financial interest in if they have signature authority over those accounts. After all, it's not their interest to report. For example, if a taxpayer owns a foreign account and gives a family member a

[37] Kimble, FedCI., Jan. 2, 2019.
[38] IR-2019-63, Apr. 4, 2019.

power of attorney that governs that account, the agent under the power of attorney has no economic interest over the account but does have signature authority.

g. The filing deadline has been extended for such individuals.[39]

23. Financial Planning Costs.

a. Many wealth advisers bundle planning services together with their asset management fee. Once a client pays the asset management fee the array of services from tax and estate planning to a comprehensive financial plan are all inclusive. But that is not the only approach, and that approach might be changing to charging additional fees for add-on services.

b. How much does it cost to get a comprehensive financial plan?[40] "*The average cost for a standalone comprehensive financial plan is $2,400 (up from $2,200 in a 2012 study from the Financial Planning Association). Notably, though, our research finds that more and more advisory firms who offer financial plans actually are charging for them separately – rather than merely bundling the plan into their AUM fees – and in fact there is a growing rise of financial advisors who are charging for financial plans solely in a "fee-for-service" manner (hourly fees, monthly subscription fees, or annual retainer fees), rather than blending fees with AUM at all*."

c. "*…the biggest driver of financial planning fees is not the cost… clients with more financial means to pay for a financial plan tend to pay more for a financial plan. Opening a debate of whether more affluent clients pay more for financial plans simply because they can afford to do so, because they tend to use more experienced advisors with deeper expertise (even if "the plan" itself is the same), or simply because their higher net worth and affluence means they perceive more value in the financial plan, to begin with*."

d. "*…more recent 2017 study on the fees that advisors charge, by Bob Veres, included 956 advisors at RIAs and broker-dealers and similarly found that while the AUM model remains dominant (even amongst those who deliver financial planning and not "just" investment management), the trend in overlapping fees has continued. Specifically, Veres found that more than half of financial advisors doing financial planning (nearly 55%) were charging an AUM fee as well as a separate financial planning fee, and that charging only AUM fees is actually only done by a minority of advisors*."

e. What might this mean for allied professionals? Perhaps, attorneys and CPAs should unbundle planning from other services. Perhaps, attorneys should charge a planning fee that similarly considers the net worth of a client and be separate from the billing for drafting or compliance work.

[39] FinCEN Notice 2018-1, Jan. 4, 2019.

[40] Meghaan Lurtz, "How Much Does A (Comprehensive) Financial Plan Actually Cost?" Apr 8, 2019 Nerd's Eye View by Michael Kitces, https://www.kitces.com/blog/average-financial-plan-fee-hourly-retainer-aum-plan-cost/?utm_source=Nerd%E2%80%99s+Eye+View+%7C+Kitces.com&utm_campaign=cbc109e3b8-NEV_MAILCHIMP_LIST&utm_medium=email&utm_term=0_4c81298299-cbc109e3b8-57068781

24. Fraud.

a. "*Retirement account scams made up 9 percent of non-credit card fraud last year, up from 3 percent in 2017*."[41]

b. Practitioners in all disciplines should review the risks of identity theft, fraud, elder financial abuse, etc. with clients. This should be an integral part of wealth management and planning for aging. Consider:

   i. Discuss with clients involving an independent CPA to monitor accounts and maintain books and records for them if they reach an age or have health challenges such that they cannot do so themselves.

   ii. Clients might involve an agent under a durable power of attorney or co-trustee on a revocable trust earlier. Traditional agents and successor trustees only become involved when a problem occurs, or the client/principal/grantor is incapacitated. That is often too late as by that point considerable financial damage may have already been done. Perhaps advisers and clients alike should rethink document structure and use and involve fiduciaries at an earlier point in time to perhaps prevent the abuse that might be triggered waiting for incapacity.

   iii. Advisers should review the manner in which clients pay bills, the number of accounts and different institutions they have and seek to help clients streamline their financial affairs and infuse checks and balances, e.g. a trust protector on a revocable trust.

   iv. A simple precaution can be to have duplicate copies of an aging or infirm client's monthly statements sent to a trusted party (ideally a CPA but if not, perhaps a family member who is not the agent under the power of attorney or successor trustee under the revocable trust).

   v. See the discussions above under planning for aging clients.

25. Gift Tax – Protective Claim for Refund.

a. A taxpayer can file a protective claim for a refund for gift taxes.[42] While the gift tax law does not permit filing a protective refund claim and the IRS, it does not prohibit such a filing. Therefore, the IRS in the recent CCA 201906006, saw no basis to deny it.

b. Background.

   i. There are several authorities addressing filing a protective refund claim, but none addressed doing so in the context of a gift tax.

   ii. The IRS noted that a prior CCA 200938021 discussed protective refund claims.

   iii. The Internal Revenue Manual I.R.M. 21.5.3.4.7.3.1 explains protective refund claims.

   iv. The requirements for a protective refund claim was set forth in U.S. v. Kales, 41-2 USTC ¶9785, 314 U.S. 186.

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[41] Michael Thrasher, "Brokerage and Retirement Account Fraud Jumped in 2018," Mar 08, 2019.

[42] Code Sec. 6402; CCA 201906006, Mar. 11, 2019.09

c. The Chief Counsel ruled that there was no basis for denying the protective refund claim for gift tax in CCA 201906006.

26. GST Allocation.

a. A taxpayer can allocate increased GST exemption to modify the inclusion ratio of a trust created in a prior year.[43]

b. Taxpayers should evaluate old trusts that are not GST exempt, or which have an inclusion ratio of more than zero, to determine if they should use current elevated GST exemptions in a late allocation to make that trust GST exempt. Often irrevocable life insurance trusts ("ILITs") were structured not to be GST exempt. This was common for term policies since a death benefit is collected in fewer than 2% of term life insurance policies. So, when the GST exemption was limited to $1 million, many ILITs were intentionally not allocated GST exemption as it might have been wasted. But if the client's wealth is such that the exemption is unlikely to be used perhaps making a late allocation to the trust to make it GST exempt may be worthwhile. This might be followed by a decanting of the trust to a newer trust that has longer term provisions. For example, if the old ILIT distributed all trust corpus to the beneficiary at age 35, extending the term of the trust for the beneficiary's lifetime (for example, by decanting), or as long as the rule of perpetuities permits, may be worthwhile as well. Considering that some tax proposals (e.g. Bernie Sanders's bill, S. 309), call for the elimination of Crummey powers, capping the duration of a GST exempt trust to 50 years, and reducing the exemption, this type of planning may be valuable for clients who feel that under the present system transfer tax planning is irrelevant to them. Perhaps, it is not.

c. It may be appropriate to note that allocating GST exemption to a pre-existing long term trust would appear not to fall under the 50 year maximum that S. 309 would prescribe.

27. GST Automatic Allocation.

a. Taxpayers often neglect to address the GST automatic allocation rules. This certainly is due in part to the complexity of the rules and, perhaps, that many professional advisers are not as informed as they should be on these matters but nonetheless assist clients in preparing Forms 709 gift tax returns. In this particular letter ruling the IRS granted an extension of time for the taxpayers to opt out of the GST automatic allocation rules.[44] Specifically, the decedent's spouse was granted a 120 day extension of time to elect under Code Sec. 2632(c)(5) out of the GST automatic allocation rules for gifts made in years 2017 to an irrevocable trust.

b. On a date prior to December 31, 2000, the Donor created an irrevocable trust, for the benefit of a child and the child's issue ("Trust"). Thus, the trust could have GST implications. Prior to December 31, 2000, Donor and Spouse made gifts to Trust but did not allocate their GST exemptions to it. Subsequent to December 31,

[43] Joint Committee on Taxation's Blue Book for the Tax Cuts and Jobs Act Footnote 372, p. 89.
[44] PLR 201903006, Sept. 24, 2018, Release Date: 1/18/2019.

2000, Donor made gifts to Trust in Years 2 through 17. Donor and Spouse retained the Tax Department of Company to advise and prepare their Year 2 through 17 Forms 709 reporting the Year 2 through 17 transfers to Trust. Although Donor and Spouse did not intend for GST exemption to be allocated to the Year 2 through 17 transfers, Company's tax professionals failed to advise Donor or Spouse of the rules under Code Sec. 2632(c) regarding the automatic allocation of GST exemption and the ability to elect out under Code Sec. 2632(c)(5) and they did not do so. Tax Department discovered these errors upon review of the Forms 709.

c. Code Section 2632(a)(1) provides that any allocation by an individual of his or her GST exemption under Code Sec. 2631(a) may be made at any time on or before the date prescribed for filing the estate tax return for such individual's estate.

d. Under the so-called automatic allocation rules, Code Sec. 2632(c)(1) provides that if any individual makes an indirect skip during such individual's lifetime, any unused portion of that individual's GST exemption is treated as allocated to the property transferred to the extent necessary to make the inclusion ratio for such property zero. This includes any transfer of property to a "GST trust," as defined in Code Sec. 2632(c)(3)(B). A GST trust is a trust that could have GST potential with respect to the transferor unless the trust satisfies any of the exceptions listed in Code Sec. 2632(c)(3)(B)(i)-(vi).

e. The opt out provision under Code Sec. 2632(c)(5)(A)(i) provides that an individual may elect to have the automatic allocation rules of § 2632(c)(1) not apply to an indirect skip, or any or all transfers made by such individual to a particular trust. Section 2632(c)(5)(B)(ii) provides that the election may be made on a timely filed gift tax return for the calendar year for which the election is to become effective.

f. Reg. Sec. 26.2632-1(b)(2)(iii)(A)(2) provides that a transferor may prevent the automatic allocation of GST exemption (elect out) with respect to any transfer constituting an indirect skip made to a trust.

g. Reg. Sec. 26.2632-1(b)(2)(iii)(B) provides that to elect out, the transferor must attach an election out statement to a Form 709 filed within the time period provided in Reg. Sec. 26.2632-1(b)(2)(iii)(C).

h. Section 2642(g)(1)(B) provides that in determining whether to grant relief and extend the time for the election out to be made, the Secretary shall take into account all relevant circumstances, including evidence of intent contained in the trust instrument or instrument of transfer and such other factors as the Secretary deems relevant. For purposes of determining whether to grant relief, the time for making the allocation (or election) shall be treated as if not expressly prescribed by statute.

i. Notice 2001-50, 2001-2 C.B. 189, provides that, under Section 2642(g)(1)(B), the time for allocating the GST exemption to lifetime transfers and transfers at death, the time for electing out of the automatic allocation rules, and the time for electing to treat any trust as a GST trust are to be treated as if not expressly prescribed by statute. The Notice further provides that taxpayers may seek an extension of time to make an allocation described in Section 2642(b)(1) or (b)(2) or an election described in Section 2632(b)(3) or (c)(5) under the provisions of Reg Sec. 301.9100-3.

j. Reg. Sec.301.9100-1 through 301.9100-3 provide the standards the Commissioner will use to determine whether to grant an extension of time to make an election. Reg. Sec. 301.9100-2 provides an automatic extension of time for making certain elections. Reg. Sec. 301.9100-3 provides the standards used to determine whether to grant an extension of time to make an election whose date is prescribed by a regulation (and not expressly provided by statute). In accordance with Code Sec. 2642(g)(1)(B) and Notice 2001-50, taxpayers may seek an extension of time to make an allocation described in Code Sec. 2642(b)(1) or (b)(2) or an election described in Code Sec. 2632(b)(3) or (c)(5) under the provisions of Reg. Sec. 301.9100-3.

k. Reg. Sec. 301.9100-3(a) provides, in part, that requests for relief subject to Reg. Sec. 301.9100-3 will be granted when the taxpayer provides the evidence to establish to the satisfaction of the Commissioner that the taxpayer acted reasonably and in good faith, and the grant of relief will not prejudice the interests of the Government. Good faith exists if the taxpayer reasonably relied on a qualified tax professional, including a tax professional employed by the taxpayer, and the tax professional failed to make, or advise the taxpayer to make, the election.

28. Guardianship Abuse.

a. An organization called CEAR, Center for Estate Administration Reform, is advocating for reforms to better protect vulnerable adults, and their estates, in probate and guardianship adjudication. An adult guardianship order removes a person's rights, decision making ability, and estate granting them to a third party.[45] The action is traumatic or worse to the alleged incapacitated person as he or she, and his or her estate, become the property of the guardian. Fraudulent guardianships describe those who fraudulently petition the court to gain control of a person and that person's estate in denial of federal and state statutes, estate documents, and often the emotional objections of the quite articulate vulnerable adult and their family. Trustees of family trusts are often targeted by the process.

b. The National Center for State Courts reports that 1.3 million American adults were under guardianship in 2015 and 176,000 were added to the rolls that year. This is only an estimate as most states do not keep records on those conscripted into guardianship. Estimates by the Federal Reserve and Metropolitan Life reported in 2015 that the average 75 year old has a net worth of $300,000. Using these estimates substantiates that nearly $300 billion in assets are controlled by guardians and approximately $50 billion in new assets are obtained each year.

[45] See https://www.cearjustice.org/about-us/ .

The numbers are growing 10-15% per annum due to the aging baby boomer generation and the growth in dementia related diseases.

c. CEAR[46] refers to this as "estate trafficking" and calls it "the crime of the 21st century."

d. Perhaps, these tragedies are another reason to rethink planning for aging. Clients should put in place a comprehensive plan, perhaps including a funded revocable trust with various built in safeguards (e.g., co-trustees, a monitor, organized financial team, etc.). Health care proxies can include recommendations of persons to be appointed as guardians. While not binding on a court, they might prove persuasive. Steps should be taken to avoid these issues.

e. Consider these comments in light of the discussions above under "Fraud" and "Aging."

29. IRA – Secure Act.

a. Proposals have been made to modify and enhance retirement savings. The so-called "Secure Act," is a proposal that many might consider likely to be enacted in 2019.[47]

b. Proposed changes include eliminating the age limit on IRA contributions, deferring the Required Minimum Distributions ("RMDs") from age 70½ to age 72. The revenue costs of these changes intended to deal with the realities of longevity would be paid for by restricting stretch IRAs as to successor beneficiaries, a revenue raiser that has been discussed for many years.

c. The implications of this while important to many may not change most planning techniques but rather will affect more detailed decisions and likely will have a meaningful impact on financial forecasts for aging clients that avail themselves of the new rules, if enacted.

d. Consider the impact of such a change on Qualified Charitable Distributions ("QCDs")? Might deferring the age for RMDs also defer the age for QCDs? Also, paying qualified plan and IRA proceeds (other than a Roth IRA) to a charitable remainder trust described in Section 664, which is income tax exempt, likely will be considered.

30. IRA – Division.

a. The IRS evaluated the tax consequences of a division of an IRA.[48]

b. In the letter ruling, the decedent's estate was the sole beneficiary of an IRA.

c. The IRA was divided, through a trustee-to-trustee transfer, into inherited IRAs for each of the beneficiaries, percentages.

d. The IRS held that this did not result in taxable distributions or payments.

e. The beneficiaries were also permitted to take required minimum distributions ("RMDs") from each of their inherited IRAs and the amount required to be taken

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[46] https://nyam.org/institute-urban-health/research/center-evaluation-and-applied-research/

[47] H.R. ___ Setting Every Community Up for Retirement Enhancement (SECURE) Act of 2019.

[48] LTR 201909003, Apr. 1, 2019.

from each inherited IRA could be determined independently of the RMDs of the other beneficiaries.

f. The division of the IRA through a trustee-to-trustee transfer into inherited IRAs was not a transfer under Code Sec. 691(a)(2) causing recognition of the income in the accounts.

31. IRA – 60 Day Rollover Requirement.

a. A surviving spouse will be treated as having acquired an IRA directly from the deceased spouse, not from the decedent's estate or testamentary trust.[49]

b. Although the trust was designated as the beneficiary of the IRA, the trust disclaimed its interest in the IRA and it passed to the decedent's estate. Further, to get the IRA to the surviving spouse, the decedent's child and several grandchildren disclaimed their interests in the IRA. The net result of all of these steps was that the surviving spouse was entitled to the IRA as the beneficiary of the estate.

c. Because the taxpayer was entitled to the IRA as the beneficiary of the estate, then, the surviving spouse was the individual for whose benefit the IRA was maintained and was permitted to roll over the IRA to one or more IRAs established and maintained in her own name. Code Sec. 408(d)(3)(A)(i).

d. See the discussion of In re: Jones, (Bktcy Ct IL 4/15/2019), 123 AFTR 2d ¶ 2019-620 under "Asset Protection" of an IRA rollover, above.

32. Life Insurance – Reporting.

a. The 2017 tax act included new rules on life insurance reporting and also the determination of the income tax basis for a life insurance policy. Proposed regulations (which do not have the force of law as final or temporary ones do) discussing these rules were issued.[50]

b. The 2017 tax act changes included, among others, the following. New tax reporting rules for life settlement transactions were enacted. Reporting requirements apply in the case of the purchase of an existing life insurance contract in a reportable policy sale and the act imposed reporting requirements on the payor in the case of the payment of reportable death benefits. (A reportable policy sale means the acquisition of an interest in a life insurance contract, directly or indirectly [such as through a partnership], if the acquirer has no substantial family, business or financial relationship with the insured apart from the acquirer's interest in such policy.) The reporting requirement applies to every person who acquires a life insurance contract, or any interest in a life insurance contract, in a reportable policy sale during the taxable year. This is the acquisition of an interest in a life insurance contract, directly or indirectly, if the acquirer has no substantial family, business, or financial relationship with the insured (apart from the acquirer's interest in the life insurance contract). An indirect acquisition

[49] LTR 201901005, Feb. 4, 2019.

[50] Prop Reg REG-103083-18; Prop Reg § 1.101-1, Prop Reg § 1.6050Y-1, Prop Reg § 1.6050Y-2, Prop Reg § 1.6050Y-3, Prop Reg § 1.6050Y-4.

includes the acquisition of an interest in a partnership, trust, or other entity that holds an interest in the life insurance contract. Under the reporting requirement, the buyer reports information about the purchase to the IRS, to the insurance company that issued the contract, and to the seller. The information reported by the buyer about the purchase is: (1) the buyer's name, address, and taxpayer identification number ("TIN"), (2) the name, address, and TIN of each recipient of payment in the reportable policy sale, (3) the date of the sale, (4) the name of the issuer, and (5) the amount of each payment. The statement the buyer provides to any issuer of a life insurance contract is not required to include the amount of the payment or payments for the purchase of the contract. On receipt of a report described above, or on any notice of the transfer of a life insurance contract to a foreign person, the issuer is required to report to the IRS and to the seller: (1) the name, address, and TIN of the seller or the transferor to a foreign person, (2) the basis of the contract (i.e., the investment in the contract within the meaning of IRC Sec. 72(e)(6)), and (3) the policy number of the contract. When a reportable death benefit is paid under a life insurance contract, the payor insurance company is required to report information about the payment to the IRS and to the payee. Under this reporting requirement, the payor reports: (1) the name, address and TIN of the person making the payment, (2) the name, address, and TIN of each recipient of a payment, (3) the date of each such payment, (4) the gross amount of the payment (5) the payor's estimate of the buyer's basis in the contract. A reportable death benefit means an amount paid by reason of the death of the insured under a life insurance contract that has been transferred in a reportable policy sale.

c. A second change made by the 2017 tax act pertains to the determination of the basis of a life insurance policy. In Revenue Ruling 2009-13, 2009-21 IRB 1029, the IRS had ruled that income recognized under IRC Sec. 72(e) on surrender to the life insurance company of a life insurance contract with cash value is ordinary income. In the case of sale of a cash value life insurance contract, the IRS ruled that the insured's (seller's) basis is reduced by the cost of insurance (not defined), and the gain on sale of the contract is ordinary income to the extent of the amount that would be recognized as ordinary income if the contract were surrendered (the "inside buildup"), and any excess is long-term capital gain. Gain on the sale of a term life insurance contract (without cash surrender value) is long-term capital gain under the ruling. The Act overrules the above and provides that, in determining the basis of a life insurance or annuity contract, no adjustment is made for mortality, expense, or other reasonable charges incurred under the contract (known as "cost of insurance"). This change specifically reverses the position of the IRS in Revenue Ruling 2009-13 that on sale of a cash value life insurance contract, the insured's (seller's) basis is reduced by the cost of insurance.

d. IRS has issued proposed regs on the new information reporting obligations for reportable policy sales of life insurance contracts and payments of reportable death benefits. The proposed regs also provide guidance on the amount of death benefits excluded from gross income under Code Sec. 101 following a reportable policy sale.

e. In Notice 2018-41, 2018-20 IRB 584, IRS delayed the new information reporting obligations for certain life insurance contract transactions under Code Sec. 6050Y until final regs are published.
f. The proposed regulations specify the manner and time at which the information reporting obligations must be made.

33. Loans – Can you "Step" or Defer Interest?

a. Assume a client is going to engage in a note (that is, installment) sale to a grantor dynasty trust (which some -call Intentionally Defective Irrevocable Grantor Trust or "IDIGT" although the result will be the same even if the trust is not intentionally made to be a grantor trust). But the entity whose interests are being sold has current cash flow needs for business research and development. As a result, distributions will be difficult/limited for several years.
b. Might the purchasing trust backload the scheduled payment dates of the interest that accrues under the term of the note? So, during the first X years of the note, the purchaser will pay interest every year at a rate of say 1%. The remaining and unpaid 2% interest (assuming a 3% AFR) will compound at the same 3% AFR rate until it is paid. Thus, the note will have negative amortization during the first X years of its term. After the first X years, the purchasing trust will pay the full interest that accrues every year on a current basis (or if advisable from a cash flow perspective another "step" in rate can be used). During the remaining term of the note, the purchaser also will pay the compounded shortfalls in interest payments that arose during the first X years of the note.
c. Because the debtor trust under the note, the purchaser will not have sufficient cash flow to currently pay all the interest that accrues during the first X years of the note, it might be argued that the purchasing trust could be characterized as "thinly capitalized." So, practitioners considering such a note structure should confirm and corroborate that thin capitalization is not an issue as that might undermine the validity of the debt itself and hence the transaction. Thus, there should be no issue as to whether the note will be respected as debt or whether it could instead be characterized as equity. The issue of the trust not being "thinly capitalized" will depend on a current balance sheet of the trust reflecting the current appraised value of assets it owns.
d. The delayed payment during the first X years of the note of the interest that accrues should not by itself cause the note that the purchaser gives to the seller to be recharacterized (e.g. as an invalid indebtedness, a gift, as equity instead of debt, etc.).
e. Using variable interest should not itself undermine the validity of a note. If a loan requires payments of interest calculated at a rate of interest based in whole or in part on an objective index or combination of indices of market interest rates (e.g., a prime rate, the applicable federal rate, the average yield on government

securities as reflected in the weekly Treasury bill rate, the Treasury constant maturity series, or LIBOR (London interbank offered rate)), the loan will be treated as having sufficient stated interest if the rate fixed by the index is no lower than the applicable federal rate (1) on the date the loan is made, in the case of a term loan, and (2) for each semiannual period that the loan is outstanding, in the case of a demand loan.

f. For term loans, determining the appropriate AFR is simply the use of an interest rate that is equal to the AFR with the same compounding period for the month in which the loan is made. For sale transactions the appropriate AFR is based not on the term of the note, but on its weighted average maturity.

g. Code Sec. 7872, which created new rules for the tax treatment of loans with below-market interest rates, went into effect on June 6, 1984. The scope of this code section and its application for gift tax purposes were addressed in Frazee. The Tax Court determined that the Code Sec. 7872 applicable federal rate ("AFR"), and not the Code Sec. 483(e) six-percent interest rate, was controlling for gift tax valuation purposes. Accordingly, because the intra-family sale of real property in Frazee was not a bona fide arm's-length transaction free of donative intent, the court held that the excess of the face amount of a note bearing seven-percent interest over its recomputed present value, using the applicable federal rate for long-term loans, constituted a gift of interest.

h. Code Sec. 7872 applies to any transaction that (1) is a bona fide loan, (2) is below market, (3) falls within one of four categories of below-market loans, and (4) does not qualify for one of several exceptions. The four categories are loans (1) from a donor to a donee, (2) from an employer to an employee, (3) from a corporation to a shareholder, and (4) with interest arrangements made for tax avoidance purposes [Code Sec. 7872(c)].

i. Code Sec. 7872(a)(1) recharacterizes the below-market-rate demand loan as a two-step transaction:

j. The lender treated as having transferred on the last day of the calendar year an amount equal to the forgone interest (the prevailing federal rate of interest less the loan's actual interest rate) to the borrower; and

k. The borrower/trust is then treated as retransferring that amount back to the lender as imputed interest.

l. What if the loan provides adequate interest so that it is not a below-market loan? There is no forgone interest to report under Code Sec. 7872. But if the note provides for the interest to accrue and is not paid, the original issue discount (OID) rules will apply. The OID rules do not apply merely because interest that is to be paid currently is not paid. They only apply where there is accrual/deferral by the terms of the note. The OID rules would have the taxpayer report a pro rata amount of the overall mount of the OID over the life of the loan using a constant yield method under the Regulations under Code Sec. 1272. But on a sale to a grantor trust the OID complications appear to be obviated at least until grantor trust status terminates. So, while these rules should apply, they should have no income tax significance.

m. Different variations can be devised based upon needs of the parties. Consider:
   i. Have interest accrue at different rates during the term of note instead of being paid at different rates. To clarify, the above discussion concerns accruing interest ratably over the note, just providing for payment at a different schedule.
   ii. Pay interest that cannot be paid in cash by issuing a note from the borrower/trust for any unpaid interest. There does not seem to be any consistency in views as to whether this will make the note more problematic to support on audit. One view is that there is nothing prohibiting paying a note interest payment in-kind, e.g. with another note. The opposing view is that this might make the transaction appear uneconomic in contrast to "baking in" the cash flow considerations from inception, e.g. with a stepped note.

34. Loans - Bad Debts and Valid Indebtedness.

a. The issue in question in this case was whether or not an LLC would be entitled claim a deduction for a worthless debt. The court found that the indebtedness was bona fide[51] The existence of a bona fide debt is a critical issue in many estate planning transactions. A common technique during periods of low interest rates is for a senior generation to loan funds to a younger generation and for that younger generation to invest and earn the difference on the spread of the investment return over the anticipated much lower minimum interest rate (AFR) that has to be charged. Another common transaction is for a taxpayer to sell an asset likely to appreciate to a grantor trust. Typically, the buying trust has inadequate resources to pay for the asset, so it issues a note. The validity of that note is critical to the transaction being respected. There are a many other common estate planning transactions dependent on a debt being respected. This recent case evaluates a number of the factors that should be considered in structuring loan transactions, especially related party and family transactions.

b. Factors the court considered with respect to the debt in question included:
   i. The debt was evidenced by a promissory note.
   ii. The note had a fixed maturity date.
   iii. The rate of interest on the note was set at an above market rate.
   iv. The lender intended to collect the debt, believed that the borrower would repay the debt, and had the legal right to enforce collection of the debt.
   v. If there was a default, a higher default interest rate would apply, and the debtor would be entitled to attorney fees to collect.
   vi. The debt, however, was unsecured.
   vii. The repayment of the debt was not limited to solely the income from the borrower.

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[51] 2590 Associates, LLC, TC Memo. 2019-3, Dec. 61,404(M), Feb. 1, 2019.

viii. The borrower was not thinly capitalized. There was an appraisal by an unrelated lender indicating that the borrower had substantial equity.

c. Practitioners should consider communicating to clients the requirements for a valid debt. In many instances, clients making intra-family loans, or loans between related entities, ignore some important formalities. A reminder to adhere to the requirements is always useful.

35. Longevity.

a. "*The number of U.S. billionaires has grown swiftly of late. There were an estimated 747 of them in North America in 2017, up from 490 in 2010, according to a study. At the same time, long-term economic data suggest the 10-figure crowd and those just behind them control ever-larger pieces of the economic pie. The wealthiest 1 percent control 37.2 percent of the country's personal wealth, while the bottom 50 percent control nothing*."[52]

b. "*Longevity can be critical to the growth and long-term success of such family business interests, said Jonathan Flack, who leads PricewaterhouseCoopers's U.S. Family Business unit. In earlier eras, longer lifespans were driven by declining child mortality. In the past 50 years, the driver has been older people living longer. Men in the top one-fifth of America by income born in 1960 can on average expect to reach almost 89, seven years more than their equally wealthy brethren born in 1930. (Life expectancy for men in the bottom wealth quintile remained roughly stable at 76*.)"

c. Consider what the above longevity statistics mean to planning. Using table life expectancies will understate actual life expectancy for the wealthy clients almost all advisers serve. Also, in the discussion of societal goals and the estate tax, the shocking statistics of expanding life expectancy for the wealthy and stagnant life expectancy for the lower tiers of wealth may well serve as an incentive for the proposals of universal health care to be paid for by a harsh estate tax. See the discussions above how most Americans believe the wealthy should pay more tax. If the difference in life expectancies becomes more widely known it may only serve to fuel the desires of many Americans to address wealth disparity through tax law changes, etc.

d. "*The state of diminished capacity isn't going to be a bright line," she explained, given the vagaries of such diseases as dementia or Alzheimer's. In the past, an aging tycoon may have relied on a trustee or family friend to make the call. Nowadays, the rich are planning for the possibility of a slow decline, making use of vehicles to transfer wealth or fund philanthropy while keeping control longer. And for protection, Glasgow said, the rich are introducing clauses in wills that require heirs to produce two, or even three, doctors who agree they are unfit to*

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[52] Simone Foxman, "U.S. Billionaires Are Living Longer Than Ever, Making Heirs Wait," Apr 3, 2019, Bloomberg, https://www.wealthmanagement.com/high-net-worth/us-billionaires-are-living-longer-ever-making-heirs-wait?NL=WM-07&Issue=WM-07_20190408_WM-07_984&sfvc4enews=42&cl=article_6_b&utm_rid=CPG09000005740948&utm_campaign=19709&utm_medium=email&elq2=d0c17deacd1a4f95910e5e559dc3c857

administer their own estate. One client stipulated that only a court could determine whether he was mentally incapacitated, she said."

e. Longevity planning for clients is clearly a significant part of what practices should encompass.

f. There is already a growing wave of concern in the country about "perks" of the uber-wealthy. Longer life expectancy is likely to exacerbate that issue.

36. Malpractice – Risk Disclosure.

a. A recent malpractice complaint filed in New Jersey might have significant implications to estate planners in all disciplines regardless of the details of the case or its ultimate disposition.[53] One of the issues raised in the case is whether in fact the practitioners apprised the clients of the relevant risks of the transactions involved. The clients claim they were not informed. Perhaps many practitioners discuss risks at meetings with clients but never formalize them in writing. Whether that lack of formalization is due to the desire to minimize the memorialization of issues that the IRS might identify, or because the client is reluctant to incur yet more fees to memorialize what was said, practitioners might wish to reevaluate their practices and take a more proactive approach to informing clients in writing of the risks associated with much of estate planning.

b. Estate Planning Is By Nature Uncertain

    i. The tax laws are always in flux. Almost every new administration in Washington proposes and often enacts changes in the tax laws. President Obama's Greenbook proposals recommended a $3.5 million exemption, severe restrictions on GRATs and a myriad of other planning techniques, could have dramatically changed the outcome of many estate tax plans. President Trump almost repealed the estate tax but was forced to settle for doubling the already historically high exemption amount. The next administration might reverse the path and make the estate tax very harsh. And no one should forget 2010, the year with no estate tax?

    ii. Uncertainty is part of the fabric of the estate planning process. Clients must understand and accept this. But perhaps, again regardless of the outcome of this particular case, the point for practitioners to consider is how might standards of practice be changed to assure clients are made aware of these risks that every estate planner understands, and how can that be corroborated?

c. Every form of tax planning is always subject to risks that the law may change, economic assumptions underlying the planning may change, client goals may evolve, family dynamics can transform, and any of the myriad of other assumptions underlying any plan can change. Clients must be charged with some knowledge of what they are doing when it comes to planning. Clients should be held responsible to understand that there are risks inherent in any planning and it

[53] https.1/www.law.cornlnjlawjouma/12019/02/04//owenstein-faces-malpractice-lawsuit- over-creation-of-dynasty-trustl.

is there decision whether or not to accept those risks (known and unknown) and pursue planning. No client should be permitted to feign ignorance of fundamental aspects of planning.

37. Matrimonial – Alimony Termination.[54]

a. A husband's obligation to pay alimony was terminated by the court noting the following facts: Payor was seventy-five years old. His health had declined, he had cardiac problems, a pacemaker, was hospitalized for cardiac arrhythmia, and took thirteen medications.
b. The court determined to terminate alimony on the basis of the payor's retirement was found to be supported by sufficient credible evidence.
c. When completing a financial or estate plan, how long should an obligation to pay lifetime alimony be presumed to continue? That may be critical to the planning. Considering the standards of the above case is it ever reasonable to assume that alimony will assuredly cease?

38. New York.

a. New York had a rule recapturing or "clawing-back" gifts made within three years of death. Prior to the 2014 changes to New York's estate tax, residents could make large inter-vivos gifts and reduce their New York estate tax. New York had a temporary gift recapture (clawback) but it was extended through the end of 2025. The gift recapture did not apply to gifts of non-New York real and tangible personal property, or to those dying after 2018. The clawback was reinstated retroactively to January 1, 2019 (but excluding gifts during the two weeks from January 1-15, 2019) and will now continue through the end of 2025. Those subject to New York estate tax should consider the impact of this when planning large gifts to use the current high temporary federal exemption amount.
b. New York got whipsawed on an estate that did not file a federal estate tax return.[55] The facts in the case succinctly were that the husband died in New York in 2010 when there was no federal estate tax. A New York QTIP election was made but no federal estate tax return was filed so no federal QTIP election was made. The wife, as surviving spouse, died in 2014 in New York. A resident gross estate is defined as federal gross estate. But because the husband died in 2010 when there was no federal QTIP election, the court held that the QTIP assets could not be included in federal gross estate and could not, therefore, be included in her New York gross estate. New York has passed legislation providing that regardless as to whether the first to die spouse's estate was required to file a federal estate tax return, if that spouse's estate filed a New York estate tax return that made a QTIP election, the New York surviving spouse has to include that property in her New York gross estate. This is effective for estates dying on or after on or after April 1, 2019.

[54] Frangipani v. Frangipani, New Jersey App. Div., February 19, 2019.
[55] In re Estate of Seiden, NYLJ 10/12/18 p.23 Col. 5.

c. New York's so-called millionaire tax was extended to 2024.[56]

39. Partnership - 754 Elections.

a. Increasing income tax basis has become the focus of much of estate planning. When assets are held in a partnership, or in a limited liability company taxed as a partnership, the full benefit of the income tax basis step up is not achieved unless the partnership can increase its inside basis as to the asset involved. But to accomplish this the partnership must make an election to adjust its basis under Code Sec. 754.
b. This election must be made in a written statement that is filed with the partnership's timely filed return (including any extension) for the tax year during which the distribution or transfer occurs. Reg. Sec. 1.6031-1. The statement must include the name and address of the partnership, and a declaration that the partnership elects under Section 754 to apply the provisions of Section 734(b) and Section 743(b). If a valid election has been made under Section 754 for a preceding taxable year and not revoked a new election is not required to be made. The election must be signed by any one of the partners.
c. The IRS granted an extension of time for a partnership to make the basis adjustment election.[57]
d. In the ruling the taxpayer had inadvertently failed to file a timely election to adjust the basis of a partnership property. The IRS found that the taxpayer acted reasonably and in good faith and permitted the election.

40. Probate – Estate Tax Liability

a. Recipients of an estate's assets were liable for federal estate tax.[58]
b. The decedent owned property jointly with his children and prior to death also transferred property to a grandchild. The estate tax return was not filed until almost eight years following death. The beneficiaries had made a few payments towards the estate tax liability, but it remainder largely unpaid.
c. For there to be transferee liability, the IRS show that the estate tax was not paid and that the transferee/beneficiary received property that was included in the gross estate. Code Sec. 6324(a)(2).
d. The forgiveness of a loan between the decedent and the grandchild was a transfer within three years of death and included in the gross estate under Code Sec. 2035 upon which no estate tax was paid. The decedent had retained a life estate in the family farm so that it was included in the gross estate under Code Sec. 2036.
e. Each beneficiary was held liable for his or her proportionate amount of the estate tax.

41. Probate – Estate Tax Liability.

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[56] Samuel Steinberge, "N.Y. Extends Its "Millionaire Tax' The "temporary" tax got new life," Apr 09, 2019. https://www.forbes.com/sites/ashleaebeling/2019/04/09/new-yorks-temporary-millionaire-tax-extended-5-more-years/#115a847359bd
[57] LTR 201852013, Feb. 4, 2019.
[58] U.S. v. Ringling, 123 AFTR2d 2019-XXXX (DC SD 2/21/19).

a. In an action to collect estate tax from the heirs of an estate, the 10th Circuit held that the transferee-liability claim under Code Sec. 6324(a)(2) was timely.[59]
b. Background. Code Sec. 6502(a) provides the general rule that, where the assessment of any tax has been made within the period of limitation, such tax may be collected by levy or by a proceeding in court, but only if the levy is made or the proceeding begun within 10 years after the assessment.
c. If the estate tax due is unpaid, a transferee such as a beneficiary, who received property that is included in the gross estate under Code Sec. 2034-2042, is personally liable for the unpaid estate tax.[60]
d. The assessment of unpaid tax against a beneficiary must be made within one year after of the assessment period against the estate.[61]
e. Decedent died testate in 1991. Decedent died leaving four children who were the beneficiaries against whom the IRS sought to impose the liability for unpaid estate taxes. Most of the estate consisted of stock in a hotel business and the estate elected to defer estate tax under Code Sec. 6166. Assets of the estate passed to a trust which was later liquidated pursuant to an agreement that acknowledged the deferred estate tax. The estate paid much of the estate tax but failed to pay it all. The IRS maintained that the executors were liable under USC 3713(b). The executors could not avoid liability for unpaid tax by the contract signed with the beneficiaries terminating the trust to which the residuary estate was distributed. The court found that the 10 year statute of limitations in Code Sec. 6502(a) applied and was suspended because the estate deferred estate tax under Code Sec. 6166.
f. The taxpayers argued that, even if a Code Sec. 6166 election suspended the limitations period for the estate, the limitations period set out in Code Sec. 6901(a) governed transferee liability; the taxpayers argued the government never timely and properly assessed them by following the procedure set out in Code Sec. 6901(a). The court held for the IRS.

42. Probate – Estate Tax Liability.

a. The Second Circuit has affirmed the Tax Court's denial of tax deductions claimed by pension beneficiaries on their individual return for funeral and estate administration expenses of the deceased pensioner. [62]
b. Taxpayer received gross distributions as the beneficiary of her father's retirement plan. The taxpayer paid various expenses related to her father's death and the administration of his estate, including funeral expenses and professional fees. She claimed deductions relating to these as an estate tax deduction on Schedule A, Itemized Deductions.
c. The court disallowed the itemized deductions for funeral expenses and estate administration fees. Code Sec. 262 provides that no deduction is permitted for

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[59] U.S. v. Johnson, (CA10 3/29/2019) 123 AFTR 2d ¶2019-565.
[60] Code Sec. 6324(a)(2).
[61] Code Sec. 6901.
[62] Harrell v. Comm., (CA2 3/13/2019) 123 AFTR2d ¶2019-505

personal expenses except as expressly provided in the Code. Funeral expenses are personal expenses, which are allowed only to the estate under IRC Sec. 2053. The claimed deductions of estate administration expenses against income in respect of a decedent ("IRD") were also disallowed as not authorized by IRC Sec. 691(b), which limits those deductions to trade or business expenses, interest, taxes, investment expenses, and depletion.

d. The 2nd Circuit Court of Appeals affirmed that the funeral and estate expenses were personal, living, or family expenses, which may not be deducted on an income tax return unless specifically permitted.

43. Probate – Estate Tax Liability IRD.

a. The Tax Court denied an income tax deduction (reported as a miscellaneous itemized deduction on the heir's Form 1040, Schedule A) for the estate tax attributable to predeceased father-in-law.[63] The taxpayer claimed the deduction based on the Federal estate tax attributable to distributions she received from inherited IRAs and an annuity. She had received the distributions on the death of her husband.

b. While Code Sec. 691(a) provides that income in respect of a decedent (IRD) is includible in gross income and a deduction is permitted for the estate tax attributable to that IRD, the taxpayer did not demonstrate that there was any tax paid on her husband's estate.

44. QTIP.

a. The executor was granted an extension of time to make a qualified terminable interest property ("QTIP") election under Code Sec. 2056(b)(7).[64] The executor hired an attorney to prepare the estate's Form 706, but the estate was believed to be less than the basic exclusion amount so no QTIP election was made. However, after the estate tax return was filed an additional asset was discovered that made the estate taxable and hence the need for a QTIP election.

45. QDOT.

a. The IRS granted an extension of time for a Qualified Domestic Trust ("QDOT") to notify the IRS of a beneficiary's citizenship.[65]

b. The trustees of a QDOT were granted an extension of time to file Form 706-QDT and certify that the decedent's surviving spouse had become a U.S. citizen. At the time of the decedent's death, the spouse was not a citizen of the U.S. The spouse established a QDOT under Code Sec. 2056A and funded it with assets that would have passed outright to the spouse from the decedent's estate.

46. Rental expenses.

a. This case discusses the denial of a taxpayer's claimed rental expense deductions but has an interesting and important discussion of deduction of personal expenses,

[63] Jill Schermer v. Commissioner, No. 12182-17, T.C. Memo 2019-28 (4 April 2019).
[64] PLR 201903014, Feb. 18, 2019.
[65] PLR 201903012, Feb. 18, 2019.

such as legal fees. This is a matter that affects many estate planners as clients often pay estate planning expenses from entities and other sources to endeavor to claim a deduction.

b. The Tax Court has denied a taxpayer's deductions for rental expenses and legal and professional fees.[66] Many of the denied deductions seemed personal in nature, the Court noting that many pertained to the client's child's divorce.

c. Code Sec. 162(a) allows a deduction for ordinary and necessary expenses paid or incurred in carrying on a trade or business. Code Sec. 212 allows a deduction for ordinary and necessary expenses paid or incurred in connection with an activity engaged in for the production of income.

d. The deductibility of legal fees depends on the origin and character of the claim for which the legal fees were incurred. Does the underlying claim have sufficient nexus to the taxpayer's business or income-producing activities so that it can be deducted under either 162 or 212? The Supreme Court held that whether legal fees are deductible expenses or nondeductible personal expenses depends upon whether the claim arises in connection with profit-seeking or personal activities of the taxpayer.[67] This is known as the "origin of the claim" test.

e. Code Sec. 262(a) denies deductions for personal, living, or family expenses.

f. Code Sec. 6001 requires taxpayers to maintain sufficient records to establish the amount and purpose of a deduction.

g. In the Sholes case the taxpayer did not produce any invoices from lawyers that explained the nature of the services performed. No invoices produced contained a description of the services that would allow allocation between personal and business expenses.

h. If the origin of the claim was a divorce, the legal expenses would not be deductible even if the result affected income-producing property.

47. S Corporations - ESBT.

a. Proposed Regulations, effective January 1, 2019, were issued that provide that a nonresident alien beneficiary of an ESBT is subject to income tax.[68] Prior to the 2017 tax act, nonresident aliens ("NRA") were not permissible beneficiaries of an ESBT. Post-2017 tax act a nonresident alien individual still cannot be a direct shareholder of an S corporation or it disqualifies the S corporation. The 2017 tax act change the law to permit a non-resident alien to be a current beneficiary of an ESBT without causing disqualification of the S corporation election.

b. A trust can be both a grantor trust and an ESBT. If a trust qualifies as both, in whole or part, the grantor trust rules trump the ESBT rules. If a non-resident alien were allocated income under the grantor trust rules, in certain instances that might result in avoiding of income tax. For example, if the NRA was domiciled in a country with an income tax treaty, the treaty might result in that income not being

66 Sholes, TC Memo 2018-203.
67 Gilmore, (S Ct 1963) 11 AFTR 2d 758.
68 REG-117062-18, Apr. 18, 2019.

subject to income tax. Similarly, if an NRA were allocated under the grantor trust rules foreign source income, or income not effectively connected with the conduct of a U.S. trade or business, that income might avoid taxation as well.

c. The proposed regulations require that certain S corporation income of an ESBT must be included in the S portion of the ESBT income, and not allocated to an NRA as an owner under the grantor trust rules.

48. Tax Identification Numbers.

a. Effective May 13, 2019 only a responsible party can obtain a Tax Identification Number ("TIN"). A responsible party must be an individual who themselves has a TIN.

b. Entities will be prohibited from using their own EINs to obtain additional EINs.

c. The new requirement will apply to both the paper filed Forms SS-4 as well as online applications.

49. Trusts - Companies.

a. US Trust is no longer.

b. "U.S. Trust, Bank of America's private bank which caters to ultra-high net worth clients, will become Bank of America Private bank, and Merrill Lynch Private Banking & Investment Group will become Merrill Private Wealth Management, dropping the "Lynch" in its name."[69]

c. Remarkable. What does this mean as to the value of other venerable names in the estate planning community?

50. Trusts – QDOT.

a. The IRS granted an extension of time to file that a Qualified Domestic Trust ("QDOT") beneficiary had become a U.S. citizen. [70]

51. Trusts – Grantor Trusts.

a. The circumstances did not cause the grantor of the trust to be treated as the owner of any portion of the trust as long as the trust was a domestic trust and the Power of Appointment Committee ("PAC") remained in existence.[71] The PAC members did not have the power exercisable by themselves to vest trust income or corpus in themselves, so none of the members were treated as owners of the trust under Code Sec. 671. The circumstances did cause administrative controls to be considered exercisable primarily for the benefit of the grantor. The powers held by the PAC members under the grantor's consent power were exercisable only in conjunction with the grantor so that the PACC committee members were not deemed to possess general powers of appointment. Moreover, in each case, the powers held by the committee members were not general powers. Accordingly, in

[69] https://www.cnbc.com/2019/02/25/reuters-america-update-3-bank-of-america-drops-merrill-lynch-name-in-rebranding-effort.html?__source=iosappshare%7Ccom.apple.UIKit.activity.CopyToPasteboard .
[70] PLR 201903012.
[71] PLR 20198003-20198008, Mar. 25, 2019.

each case, any distribution made from the trust to a beneficiary, other than the grantor, did not constitute gifts by the PAC members, but rather by the grantor.

52. Trusts - Qualified Disability Trusts.

a. The 2017 tax act provided that the personal exemption for a taxpayer has been suspended, as they are for most trusts and estates, other than qualified disability trusts which effectively will enjoy an exemption of $4,150 in 2018.[72]
b. The qualified disability trust exemption, from 2018 through 2025, is not subject to phaseout.

53. Trusts – State Taxation.

a. The U.S. Supreme Court granted certiorari on January 11, 2018 to hear a case involving the issue as to whether a state can tax a trust's income solely on the basis of an in-state beneficiary.[73]
b. The issue in Kaestner and other cases is whether, if a trust has limited contacts with a state, will those contacts suffice for that state to tax the income of that particular trust? The question is particularly nettlesome with respect to a state's income taxation of undistributed income of a trust.
c. In Kaestner, the current beneficiary resided in North Carolina, and that was enough for the state to assert the right to taxation. However, the North Carolina Supreme Court held that it violated the Constitution to tax the trust's undistributed income. The court referenced Quill and minimum contacts that might be required to be able to tax a trust. Important to the analysis was that the trust was a separate taxpayer from the beneficiaries who lived in North Carolina. Kaestner, the settlor of the trust, was a New York resident. The trustee initially was a New York person and later changed to Connecticut. The contingent beneficiaries were not in North Carolina. Was that enough to establish the minimum contacts necessary so that North Carolina could subject the trust to income taxation? The case made an analogy to an entity. A beneficiary might be analogous to a shareholder. That should not be enough.
d. Another noteworthy state trust income taxation case similarly held that there were insufficient contacts with the state of Minnesota and the Minnesota Supreme Court held that taxing the trust also violated due process.
e. The recent Wayfair[74] case may also have an effect on these and other cases addressing the state income taxation of trusts. The Supreme Court concluded that a state can require companies to collect a sales tax. The taxpayer had no physical presence in most states so does that mean those states cannot require that they collect sales tax? The Supreme Court held that physical presence is not the right test with the internet and electronic commerce. As a result, there no longer is a requirement to have physical presence. Wayfair overturned the Quill case which

[72] https://www.irs.gov/forms-pubs/qualified-disability-trust-exemption-not-subject-to-phaseout.
[73] Kimberley Rice Kaestner 1992 Family Trust v. North Carolina Dept. of Revenue, 814 S.E.2d 43 (N.C. June 8, 2018), aff'g 789 S.E.2d 645 (N.C. App. 2016).
[74] Need cite. I will find and add.

had required physical presence to charge sales tax. In Quill, the court found that the sales tax requirements did not violate the due process clause. It found that a volume of mailings into the state satisfied due process.

f. The relevance of Wayfair and Quill to the determination of state income taxation of trusts could be significant in that Quill, now superseded by Wayfair, had been cited in many of the recent federal income tax cases in terms of the requisite minimum contacts for state taxation of trusts. So, the Wayfair analysis may now be the relevant litmus test instead of Quill and that might impact the outcome. In the Wayfair case, how did they establish substantial nexus? Companies in other states will be required to collect sales tax if they have 200 or more separate transactions, and $100,000 of sales, in the state. If Quill, which required physical presence, has been overruled by Wayfair, will trust taxation change?

g. On April 19, 2019 oral arguments were presented to the United States Supreme Court in the case. The Supreme Court is being requested to address, on due process grounds (not commerce clause grounds), whether a North Carolina statute permitting that state to tax a trust on a contingent beneficiary/resident's share of the undistributed trust income when there is limited nexus to the state. Neither the settlor nor the trustee is a resident of North Carolina, and the trust has no contact with North Carolina other than the residence of the beneficiary.

h. Here is a link to the audio of the arguments: https://www.supremecourt.gov/oral_arguments/audio/2018/18-457 .

54. Wandry – Reconsider Classic Wandry Clauses in light of Powell?

a. Many practitioners believe a Wandry clause provides security to deflect a valuation challenge by the IRS of a transfer to, for example, an irrevocable trust.[75] Other practitioners might view the protection as less secure. An illustrative Wandry clause is below:

b. **Sample Clause**: "*I have this day executed this Declaration of Gift and separate Assignments and Stock Powers Separate from Certificates (the "Assignment") transferring (the "Transfer") shares of stock (the "Gift Shares") bearing the following values, as of the date of this transfer, to the Client-Name 2018 Irrevocable Trust ("Trust"): Dollar Number ($___________.00) value of the shares of Common Stock, no par value, of Entity-Name Corp., a State-Name corporation ("Entity-Name") (the "Entity-Name Gift Shares"). The Transfer of the Gift Shares to the Trust is intended to constitute, and constitutes, the complete and irrevocable gift of all of the aforementioned Gift Shares. The Transfer is made by way of gift and without any consideration. I have had a good-faith determination of such values made by an independent third-party professional experienced in such matters and appropriately qualified to make such a determination. Based on such determination, the number of shares constituting the Entity-Name Gift Shares is ______Number shares. Nevertheless, if the IRS challenges such valuation and a final determination of a different value is made*

[75] Wandry et al., 103 TCM 1472, CCH Dec. 59,000(M), TC Memo. 2012-88.

by the IRS or a court of law, the number of gifted Shares shall be adjusted accordingly so that the value of the number of Shares of each entity gifted to the Trust equals the dollar amount set forth above, in the same manner as a federal estate tax formula marital deduction amount would be adjusted for a valuation redetermination by the IRS and/or a court of law. I declare under the penalties of perjury that the foregoing is true and correct and further declare that this Declaration of Gift is being executed effective as of the date of the signature below."

c. There might be a different variation of a Wandry clause that might be useful in certain circumstances. In particular, if the transferor must transfer all shares at the closing, can the typical Wandry clause be improved upon? What might be dubbed a "two-tiered Wandry" may provide a planning solution. A "two-tier Wandry" arrangement would consistent of a two-part transaction: a traditional Wandry transfer, followed by a simultaneous sale of any shares (or other assets) left by the Wandry adjustment clause if it is triggered. There may be income tax or contractual reasons for the need to transfer all equity. The problem with a Wandry clause is that it could leave shares in the selling taxpayer or trust's hands, which may not be desirable for business or personal reasons. This could create uncertainty with respect to the trust's ESBT status if all S corporation shares are sold but the operation of a Wandry clause results in shares having remained in the trust. For example, does the ESBT election end when all shares are sold? If so what occurs when it is later determined that S corporation shares are held in the selling trust? The second tier of the Wandry arrangement would consist of a second sale of any shares, effective as of the same date as the primary Wandry sale, that remain in the selling taxpayer or trust's hands. The price for this second sale, if any, would be for a price equal to the gift tax value as finally determined. This second tier Wandry sale would be supported by a note for that on which interest would accrue from closing and be made current within a specified time period, e.g., 90-days of the final determination.

d. The two-tier Wandry, i.e. a traditional Wandry adjustment mechanism coupled with a sale of any interests left in the transferor's hands may have another use post-Powell/Cahill.

e. Code Section 2036 provides that if the decedent could have pulled the 2036 "strings" "alone or in conjunction with any other person" the entity interests will be included in the estate.

f. In Powell[76], the decedent's son made several fundamental mistakes when planning his mother's estate. While it's no surprise that the Tax Court ruled against the estate, the Tax Court's reasoning on at least one point was novel. After summarizing the case, the errors made in planning the decedent's estate, including misusing a power of attorney, engaging in aggressive last-minute planning, not having a business purpose for a family limited partnership, and running afoul of IRC §2036 will be reviewed. The discussion will cover the Tax Court's extension

[76] Estate of Powell v. Commissioner, 148 T.C. No. 18.

of IRC §2036(a)(2) to limited partnership interests and the possibility of double taxation (or an increased step up in basis) in FLP inclusion cases.

g. The underlying cash and securities transferred to the limited partnership interests were includable in the estate under IRC §2036(a)(2) (transfer with right to designate enjoyment of the property) because the decedent had the ability, when acting along with her sons, to dissolve the FLP. The Tax Court found that the exception in IRC §2036 (transfers for full and adequate consideration) did not apply in this case because son Jeffrey, acting as attorney in fact, had no significant nontax reason for the transfer. Thus, in some instances the decedent's retained right to control "in conjunction with" could undermine the planning. How far this concept will be interpreted to extend is unclear, but the later Cahill case expanded the same reasoning of Powell to a split-dollar insurance contract.[77]

h. The court in Cahill focused on this requirement and noted that the decedent (really through his son as trustee of the revocable trust) had the right to terminate the split-dollar agreements in conjunction with the trustee of the MB Trust (the ILIT). That, in the Court's view, satisfied the Section 2036 and 2038 requirements because the two trustees could have, in the court's view, merely terminated the split-dollar agreement and the Revocable Trust would have received the cash value of the policy. The estate's counter to this was that it would not make economic sense for the ILIT to allow termination of the split-dollar agreements since that would harm the beneficiaries of the ILIT. However, the son and his descendants were the beneficiaries. The estate argued that such a termination was so unlikely that the termination rights had no value as of decedent's date of death. On this basis, the estate contended that the value of decedent's interests in the split- dollar agreements was limited to the value of decedent's death benefit rights. The difference between the two was dramatic.

i. Code Sec. 2036 can apply to include in the value of the gross estate the value of:
    i. All property that the decedent had transferred during lifetime [The Cahill Court viewed the transfer of the premium payments from the Survivor's trust (the decedent's revocable trust) to the ILIT as constituting the property transferred],
    ii. Over which the decedent retained for life the right, alone or in conjunction with another person, to designate the person or persons who shall possess or enjoy the property or the income therefrom. The Cahill Court viewed the right of the Survivor's Trust and the ILIT together to terminate the IGSD agreement as the right "in conjunction with another" to designate who would enjoy the property, i.e. the cash value resulting from the premiums paid.

j. A response to this uncertain and potentially expansive view of Code Sec. 2036(a)(2) might be to reconsider the traditional Wandry adjustment mechanism and use a different approach to assure that no equity remains with the transferor in

[77] Lee Slavutin, Richard Harris & Martin Shenkman, "Intergenerational Split Dollar - Recent Adverse Decisions in Morrissette and Cahill, Where Do We Go from Here?", LISI Estate Planning Newsletter No. 2651 (July 17, 2018).

order to assure that the transferor cannot "in conjunction with" control any of the entity interests transferred. This could take the form of a more robust price adjustment mechanism where all interests are transferred with the excess interests being transferred to a non-taxable receptacle (GRAT, marital trust, charity, or incomplete gift trust). Another alternative is to structure a two-tier Wandry. Under this latter approach any equity that is not transferred to, for example, the buying trust, would be sold pursuant to a sale contract executed the same day as the primary gift or sale that is subject to a Wandry clause. The sale price under that contract would be the gift tax value as finally determined for Federal gift tax purposes. While that may make what was a simple Wandry adjustment more complex, perhaps it can deflect an expansive Powell/Cahill challenge by assuring no equity remains with the transferor.

55. Wealth Transfers.

a. "*The amount of inherited wealth up for grabs is staggering and getting larger. In a U.S. High-Net-Worth and Ultra-High-Net-Worth Markets 2018 report, Cerulli Associates estimated that $68 trillion is transferring over the next 25 years to heirs and charities, an amount significantly higher than earlier estimates (known as "The Great Wealth Transfer").*
b. *While studies differ on the percent of beneficiaries firing their advisors when the estate transfers, most agree that advisors who ignore the inheriting generation, including spouses, are at a greater risk of losing them. Yet most advisors aren't engaging the beneficiaries.*
c. *Cerulli reported that 45% of high-net-worth practices have had limited interactions with their clients' children, while only 59% have established relationships with clients' spouses*."[78]
d. The implication of the statistics and the discussion in the article is that all practitioners should endeavor to open dialogues not just with clients, but with client heirs. This is something wealth management firms appear to routinely address. Attorneys and CPAs, with hourly billing models and practices that tend to be more focused on compliance and document creation appear to have done much less. Those practice models need to evolve.
e. The take home messages to estate planners and all allied professionals is that apart from the vicissitudes of the tax system there should be more emphasis on building relationships with heirs and helping clients and their heirs focus on the impact of wealth transition.

56. Wealth Managers – Time Allocations.

[78] Carol A. Sherman, "The Great Wealth Transfer Wake-Up Call," Apr 12, 2019 https://www.wealthmanagement.com/high-net-worth/great-wealth-transfer-wake-call?NL=WM-27&Issue=WM-27_20190420_WM-27_894&sfvc4enews=42&cl=article_11_b&utm_rid=CPG09000005740948&utm_campaign=19878&utm_medium=email&elq2=a9d40e9addb14f2da4938fb30bdf44f7

a. Advisers divide their time as follows: 55.3% client facing activities including meeting time with current clients, acquisition of new clients, client services and plan preparation. 21.2% administrative activities such as compliance, back office matters, etc. 17.4% investment management including research, due diligence and asset management, and 6.1% professional development.[79]
b. The Morningstar monograph asks: “But if you could choose, would you rather spend more time with clients, building stronger relationships and looking for opportunities to increase your assets under management? Some advisers are doing just that by turning over the labor-intensive tasks of investment management – everything from establishing an asset allocation strategy and implement portfolio decision to providing risk management and ongoing oversight – to a third party investment management firm.”
c. These statistics and the prospect of outsourcing investment management raise a host of fascinating questions for the entire profession. Consider:
    a. The Morningstar monograph wisely suggests that wealth managers focus on what is most important to their business and where they add the most value to clients. That may not be in the tedium of the weeds of investment management but in client interaction, holistic planning, and keeping the plan on track. This is a profound paradigm shift that all advisers need to consider. How much time does an attorney spend drafting documents rather than interacting with a client to determine whether their plan is on track, what issues might exist and more? For attorneys that have not automated their practices and begun outsourcing not essential tasks, they should take heed.
    b. If wealth managers spend 55.3% of their time in client facing activities how can CPAs, attorneys and perhaps other advisers ever hope to develop the deep relationship with clients that a wealth adviser can? They probably can’t. What does that mean for referrals, client relationships and so much more?
    c. If wealth advisers only spend 17.4% of their time on wealth management, and may in greater numbers now outsource that, what does that mean to the professional advisor team? Estate planning attorneys often lament that wealth advisers usurp their role and their work. The Ceruli statistics seem to suggest why that is possible, and the Morningstar report suggests that it will expand. What are estate planners doing about this?
    d. If wealth advisers only spend 17.4% of their time on wealth management, and may in greater numbers now outsource that, what does that mean to the client? What is it that a client believes he or she is paying for? Will this reality change that? Might clients rethink their relationship with

[79] Morningstar issued a report “Five Ways Portfolio Outsourcing May Help Grow Your Practice” https://www.morningstar.com/lp/five-ways-outsourcing-can-grow-your-practice February 16, 2019 citing The Ceruli Report, Advisor Metrics 2017, Adviser Attributes, Chapter 5, p. 131, quoted on page 2 of the Morningstar monograph.

wealth advisers if such a small percentage of time is spent on actual investment management and that in fact more and more of that may be outsourced? Might clients opt to hire unbundled lower cost investment advisers and hire other professionals as they require services rather than pay a larger AUM fee to a wealth adviser? Consider the percentage of time that CPAs spend on tax compliance and attorneys on document drafting? No doubt the percentages are dramatically greater, thereby reducing the potential abilities of CPAs and attorneys to build the same strength in their client relationships that wealth advisers build.

e. If wealth advisers spend about 6% of their time on professional development, assuming a 2,000-hour year that is about 120 hours/year. That might be three times what some other professionals might spend based on continuing education requirements for other professionals. If that is the case, might that mean that wealth advisers are spending substantially more time learning than their peers in other allied professions? With such rapid changes in technology, tax laws, the economy and so forth, might that imply an edge that wealth advisers have and are adding to as compared to other advisers?

d. There are other interesting data presented in this monograph that should be considered in light of this discussion. Wealth management firms and trust companies routinely appear to limit their liability for estate planning. See the discussion under the "Malpractice" category. It appears common, perhaps the norm, for wealth advisers and trust companies to maintain that they do not provide legal or tax services, that somehow those services are solely within the purview of the attorney and CPA. Yet wealth advisor firms routinely meet with clients and discuss tax and estate planning. It also appears based on other discussions in this monograph that wealth advisers are increasingly charging additional fees for planning services. Is it possible for wealth advisers to limit the scope of their liability, and charge additional fees, for work that CPAs and attorneys have traditionally done? Yes. What does this mean to the professional generally? What must CPAs and attorneys do to maintain their client relationships and contacts?

57. Wealth Managers – Who is the Estate Planner?

a. A recent article points out how far some wealth managers will go to usurp the role of estate planners and why multidisciplinary teaming is so difficult to accomplish. The real tragedy is that this type of overreach will expose financial advisers to liability, it destroys the checks and balances and sharing of ideas a collaborative planning team can provide and hurts clients.[80]

[80] "Voices Client tragedy, a phone call and an advisor's tough job," By Carolyn McClanahan January 30 2019, 5:20pm EST https://www.financial-planning.com/opinion/financial-advisors-and-living-wills-advanced-care-directives?utm_campaign=Jan%2031%202019-daily&utm_medium=email&utm_source=newsletter&eid=1e37f45019da92648262289efc5464d1

b. “Managing investments is easy. Taking care of clients in their most acute time of need is hard. A recent tragedy concerning a client vividly brought home this reality.”
c. Here’s the planning situation the financial adviser paints. What’s wrong with this picture? “*The call came on a Wednesday morning. A client visiting her sister out of state had become acutely ill and uncommunicative. She was rushed to the emergency department by ambulance. Her partner, scrambling to get a flight to be with her, called us to let us know what happened. By the evening our client was in the intensive care unit, still uncommunicative. Her condition quickly worsened. Her partner arrived and it was determined our client would need to be placed on a ventilator or she would die. At this point, the hospital asked for documentation showing that our client’s partner was indeed the health care surrogate. All of our clients have an electronic vault containing their important documents. The problem? The client’s partner couldn’t remember how to get in the vault. She texted us and asked us to fax the living will and health care surrogate document to the hospital and we promptly obliged*.”
d. The client called her financial adviser to get a copy of her living will, not the attorney who drafted it and more likely understood the issues involved better.
e. The article continues: “*Our client, a delightful spitfire, had suffered serious health issues in the last three years. Although she was still enjoying life, she was losing her verve. In our last conversation about advance directives, she made it perfectly clear that if she had a serious health event that was going to kill her, she wanted to be kept comfortable and have as peaceful a death as possible. Her partner participated in these meetings and agreed to support her wishes. The client also shared her wishes with her entire family…. I gently reminded her of our advance directive conversations through the years*.”
f. So, the financial planner, without the attorney, met with the client and her partner to discuss end of life decisions excluding the attorney. The newest member of the planning team, especially for ill or aging clients, is a care manager. If the client had had these issues for three years, why was a care manager not involved? Albeit in the instant case the author of the article, a brilliant financial planner, has a medical background and may have had the expertise to address the issues involved. But that is a rare situation and not one that would be appropriate for most financial advisers.
g. “Attorneys complete living wills and health care surrogate documents but they don’t make the time for education about how to actually prepare for a serious health event. Advisors can take this advance directive planning a step further by helping the client document their desired quality of life in the event they can no longer speak for themselves due to a health condition.” So, attorneys don’t take the time to discuss the decisions in the documents they prepare? Perhaps, one of the issues is how planners bill versus attorneys. This is an issue that rankles most attorneys and too often is used by financial planners to usurp the role of the attorney. A dangerous practice for clients. The financial adviser who bills an asset

management fee has that fee subtracted as a line item in a lengthy monthly statement. The estate planning attorney on the other hand sends a bill for which the client has to write a check. What the financial adviser should be doing if he or she cared about her client is insisting that the client include the attorney, CPA, insurance consultant and other advisers in annual reviews, but too often they don't. As this article corroborates many financial advisers believe that they have the knowledge to handle all of these areas. While some firms have extensive expertise, many do not have the same breadth of knowledge. But this conduct can prevent a client team from being formed and can harms the client by having less than the most knowledgeable adviser involved.

h. "*As my client's story shows, people need someone to initiate the discussion, get the documents in place, codify the quality-of-life discussion, know where the documents are located and provide access when required. This is not something doctors or attorneys do*." Seriously?

i. Another article cited the growth in estate planning services provided by wealth management firms: "*So it's not surprising that 45 percent of wealth management firms now offer estate and succession planning as primary services, up from 37 percent just a year ago, according to Cerulli Associates. The data provider estimated that demand for these capabilities will continue to snowball: Over the next 25 years, $68 trillion of wealth will be transferred in the U.S. alone*."[81]

58. Wealth Management – Fees.

a. "*Cerulli found that clients have gradually been paying more attention to the fees advisors are charging them. The firm's surveys show that the percentage of investors who believe the advice they receive is either free or who are unsure of what they pay has gone from 65 percent in 2011 to 42 percent in 2018. Advisors apparently know what's going on: 75 percent of those surveyed told Cerulli that prospective clients are more sensitive about fees than they were five years ago. About 42 percent of advisors also expect their fees to decline, mainly because of the growth of robo-advisors. At the same time, clients are more willing to pay for financial advice, with 53 percent saying in a survey last year that they were willing to pay for financial investment advice, up from 38 percent in 2009. About 76 percent of investors agreed that the value they receive from financial advisors is worth the expense, the survey found*."[82]

b. How should advisers structure fees? How can advisers demonstrate a value add for the fees charged?

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[81] Simone Foxman, "U.S. Billionaires Are Living Longer Than Ever, Making Heirs Wait," Apr 3, 2019, Bloomberg, https://www.wealthmanagement.com/high-net-worth/us-billionaires-are-living-longer-ever-making-heirs-wait?NL=WM-07&Issue=WM-07_20190408_WM-07_984&sfvc4enews=42&cl=article_6_b&utm_rid=CPG09000005740948&utm_campaign=19709&utm_medium=email&elq2=d0c17deacd1a4f95910e5e559dc3c857

[82] Raymond Fazzi, "Clients Get More Savvy When It Comes To Advisor Fees," Financial Adviser, Apr 4, 2019, https://www.fa-mag.com/news/clients-get-more-savvy-when-it-comes-to-advisor-fees-44187.html?section=43&utm_source=FA+Subscribers&utm_campaign=7dc7289891-FAN_AM_Send_021318_A-B_Split_COPY_01&utm_medium=email&utm_term=0_6bebc79291-7dc7289891-222625781

59. Wealth Management – Who Are Clients.

a. "The average age of wealth management clients now stands at 64, according to data from global consulting firm Simon-Kucher & Partners…"[83]
b. What type of work and planning do clients at this age require?
c. "It's just plain silly," advisor Randy Bruns of Model Wealth in Downers Grove, Illinois, says of using the AUM fee model with younger clients. "*On one end you have millennials with serious financial planning needs, and a pricing structure that cannot serve them. And on the other end, you have clients paying tens of thousands of dollars just because they've saved well. Less wealthy consumers are penalized for having not yet saved, and wealthy consumers are penalized for decades of saving. It's so strange. And it can lead to some terrible advice as well, simply because of conflicts inherent to the AUM pricing structure*.'"[84]
d. In reality, this type of adjustment might happen as some firms do discount the AUM fee as assets increase above certain breakpoints. Perhaps the key issue is identifying the right adviser for the right client so that there is a match of services to the client needs as well as a rationale for the overall fees to the services provided. One of the questions prospective clients should ask is not what the minimum AUM fee is but rather what the firm's client sweet spot as that is might be the level and nature of services the firm endeavors to provide.

60. Wealth Management – Withdrawal Rates.

a. "*A confluence of factors like increasing longevity, historically low interest rates and high stock prices are prompting some advisors to rethink this entire subject. Some are concluding that clients who want to be sure they don't outlive their money probably need to consider a withdrawal rate closer to 3% than the traditional 4% or 4.5%.*"[85]
b. If this is correct it has a profound influence on planning, the use of dynasty trusts, and more. If a practitioner is going to project funds required to be retained accessible to a client so that the funds that can be moved outside of the estate and, perhaps, depending on the technique selected, outside of the client's reach. If forecasts are completed to determine whether life insurance should be purchased to insure the premature death of a spouse with respect to a non-reciprocal SLAT plan, a lower feasible withdrawal rate will affect the amount of life insurance that might be advisable. In fact, if a 3% withdrawal rate is correct (and there are many articles suggesting more complex and potentially higher distribution rates), perhaps, every client's estate, financial and insurance plan should be revisited.

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83 Amanda Schiavo, "Advisors should change fee structures to attract next-gen clients, https://www.financial-planning.com/news/financial-advisors-should-change-their-price-module-to-attract-new-clients?utm_campaign=Jan%2012%202019-weekend&utm_medium=email&utm_source=newsletter&eid=1e37f45019da92648262289efc5464d1, Jan 7 2019.

84 Id.

85 Evan Simonoff, "Withdrawal Rates For Asset Preservationists," Apr 1, 2019, https://www.fa-mag.com/news/withdrawal-rates-for-asset-preservationists-43966.html

Certainly, a lower withdrawal rate might be used in sensitivity analysis for forecasts.

61. ## Valuation – Gift Tax Value Closely Held Business.

a. The value of closely held stock transferred to family members was determined by considering comparable companies and applying relevant discounts.[86] The closely held stock was owned primarily by the donors' family, directors, and employees. There was an established price the sale and purchase of shares owned by non-family members, but no set price for shares transferred to family members. The company bylaws included a provision that the family was limited to transferring stock by gift, bequest, or sale to other family members. The donors gave minority shares to their children and grandchildren in three years, which were reported on gift tax returns. The court discussion is instructive as to what factors make an appraisal report useful, or not.

b. "*The U.S. District Court – Eastern District of Wisconsin issued an important decision in Kress v. U.S. in which Chief Judge William C. Griesbach relied largely on the findings of the taxpayers' experts to value gifts of minority interests in a Subchapter S corporation (S corp) operating company, Green Bay Packaging, Inc. (GBP). In those experts' reports, a Subchapter S corp was first valued on a C corporation (C corp) equivalent basis, which included tax-affecting the entity's earnings, followed by quantitative and qualitative adjustments to address whether any economic adjustment/benefit should be ascribed to the Subchapter S election (the C to S method).*"[87]

c. The Court found the IRS appraisal lacking because: it failed to consider comparable companies under the market approach, did not address the impact of the economic recession, improperly valued nonoperating assets.

d. The Court found one of the taxpayer's appraisal reports useful because: it used accurate projections, accounted for the effects of the recession, relied on management interviews, prior year reports, and the analysis of guideline companies to choose the best comparable companies.

e. The IRS argued, and the Court agreed that the taxpayer's appraiser incorrectly evaluated the family transfer restriction in calculating the discount for lack of marketability. Code Sec. 2703 permits consideration of a restriction only if it meets three criteria: (1) it is a bona fide business arrangement; (2) it is not a device to transfer property to a decedent's family members for less than full and adequate consideration; and (3) it includes terms that are comparable to similar arm's-length arrangements. The taxpayer's appraiser did not address nor meet the third prong of the test.

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[86] Kress, DC Wis., Mar. 28, 2019.

[87] Todd G. Povlich, "A Breakthrough in S Corporation Valuation," Apr 05, 2019 https://www.wealthmanagement.com/high-net-worth/breakthrough-s-corporation-valuation?NL=WM-27&Issue=WM-27_20190408_WM-27_695&sfvc4enews=42&cl=article_2_b&utm_rid=CPG09000005740948&utm_campaign=19711&utm_medium=email&elq2=9eb9c45b72f14c5781f06d797f974297

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