McGUIREWOODS

The Top Ten Estate Planning and Estate Tax Developments of 2015

Prepared for

The Estate Planning Council of Delaware

February 9, 2016

Ronald D. Aucutt

The Top Ten Estate Planning and Estate Tax Developments of 2015

Adapted from:
https://www.mcguirewoods.com/Client-Resources/Alerts/2015/12/Ron-Aucutt-Top-Ten-Estate-Planning-Tax-Developments-2015.aspx

Number Ten
Redstone Cases
The Media Industry and Family Discord Drama

SEASON 1: The Redstone Family and the Formation of National Amusements, Inc. (NAI) (August 1959)

	Michael Redstone ("Mickey")	Sumner Redstone (Mickey's Son)	Edward Redstone (Mickey's Son)
Stock contributed (book value)	$30,328	$18,445	$17,845
Cash contributed	3,000	0	0
Total	$33,328	$18,445	$17,845
Percentage	47.88%	26.49%	25.63%
Shares issued (common stock)	100	100	100
Offices*	President	Vice President	Sec'y-Treas.

The Redstone Family and the Formation of National Amusements, Inc. (NAI) (August 1959), continued

* "Mickey gave Sumner, his elder son, the more public and glamorous job of working with movie studios and acquiring new theaters. Edward had principal responsibility for operational and back-office functions. His duties included maintaining existing properties and developing new properties." (Tax Court Judge Lauber)

  – Today Sumner is the controlling shareholder and executive chairman of Viacom and CBS.

SEASONS 10-13:
Tensions (late 1960s and early 1970s)

- Edward and his wife decided to have their son admitted to a hospital for psychiatric care.
  - Mickey, Mickey's wife, and Sumner opposed that.
  - "in part because they feared it reflected badly on the Redstone family name" (wrote Judge Lauber).
- Edward also began to feel marginalized in the business.
- He quit, demanded possession of the 100 shares registered in his name, and threatened to sell that stock to an outsider if NAI did not redeem it for a fair price.
- But Mickey claimed that at least half of that stock had been held under an "oral trust" for Edward's two children since 1959, reflecting the disproportionate capital contributions.

FINALE: Settlement (June 30, 1972)

- Edward would separate from NAI.
- One-third of the stock registered in his name would be treated as subject to the 1959 oral trust for his children.
- The rest of his stock (66⅔ shares) would be redeemed for $5 million ($75,000 per share).

- Contemporaneously, Edward executed two irrevocable trust agreements, one for each of his children, and transferred 16⅔ NAI shares to each trust.
- Two weeks later, Sumner did the same thing for his two children.

- Neither Edward nor Sumner filed gift tax returns for 1972.

RERUNS: More Litigation (2006-2008)

- Edward's son and the trustees of some trusts argued that more shares should be in trust for Mickey's grandchildren.
- Edward testified that he believed he had been entitled to all 100 shares originally registered in his name.
- Sumner testified that Mickey had never mentioned an oral trust for ***his*** children; he had transferred the shares to the trusts "voluntarily, not as the result of a lawsuit."
  - "I just made an outright gift."
- The court ruled that the plaintiffs had failed to prove that any oral trust ever existed.
- The IRS heard about it and asserted gift tax of $737,625 each against Edward and Sumner for their 1972 gifts, plus penalties.

PAY TO VIEW:
Estate of Edward Redstone v. Commissioner, 145 T.C. No. 11 (Oct. 26, 2015) (Judge Lauber)

- Edward's 1972 transfers were not taxable gifts, but rather transfers in the ordinary course of a trade or business, because they were part of the settlement of a claim of an oral trust that "had sufficient plausibility to generate a great deal of litigation over the course of many years," even though it was rejected by the Massachusetts court 37 years later.
- The IRS argued that Edward's ***children*** had not been parties to the litigation and had not provided consideration.
- But Reg. §25.2511-1(g)(1) tests whether the transfer is made "***for*** a full and adequate consideration," which the court viewed as looking to whether the transferor ***receives*** consideration, not whether the transferees ***provide*** it.

PAY TO VIEW: *Sumner Redstone v. Commissioner*, T.C. Memo. 2015-237 (Dec. 9, 2015) (Judge Lauber)

- The Tax Court found Sumner's 1972 transfers to be gifts:

  "There is no evidence that any dispute existed in 1971-1972 concerning ownership of Sumner's stock or that Mickey was determined to withhold any of Sumner's shares from him.… Because no demand was ever placed on Sumner's shares, no negotiations ever occurred concerning his ownership of those shares. Sumner never filed a lawsuit, and he received no release of claims from Mickey (or anyone else) upon transferring his stock."

- The court found the $75,000 per share redemption price paid to Edward for his shares to be a reliable index of the value of the stock when Sumner made his gifts.
- But the court held that Sumner was not liable for penalties.

Number Nine
Developments Regarding Crummey Powers

Mikel v. Commissioner, T.C. Memo. 2015-64 (April 6, 2015) [also CCA 201208026 (Sept. 28, 2011)]

- In 2007, Mr. and Mrs. Mikel gave property they claimed to have a value of $3,262,000 to a trust in which 60 descendants and their spouses had "Crummey" withdrawal rights.

	$3,262,000
Gift-split	$1,631,000
Annual exclusion: $12,000 x 60	- 720,000
Taxable gift	$911,000
Gift tax lifetime exemption	- 1,000,000
	No tax

Mikel v. Commissioner, continued

IRS Position	Tax Court's Response (Judge Lauber)
Withdrawal rights are "unenforceable and illusory" because disputes can be brought only to a "*beth din*," not to a court.	"A beneficiary would suffer no adverse consequences from submitting his claim to a beth din, and respondent has not explained why this is not enforcement enough."
… and because a beneficiary who filed or participated in a civil proceeding to enforce the trust would be excluded from any further participation in the trust under a "no contest" or "*in terrorem*" clause.	The specific in terrorem provision in this case would not apply to a beneficiary's withdrawal right because it applies only to actions to oppose or challenge discretionary trust distributions.
	Partial summary judgment for Mikels

Other Issues

- Are the Mikels entitled to payment of attorney's fees under section 7430?
  - Judge Lauber said no, finding that the position of the IRS, although unsuccessful, was "substantially justified," in that it had a reasonable basis in fact and law and was justified to a degree that could satisfy a reasonable person. *Mikel v. Commissioner*, T.C. Memo. 2015-173 (Sept. 8, 2015).
- Is the value of the property really only $3,262,000?
  Do all 60 withdrawal rights really count?
  - Yet to be adjudicated, if not settled.

Treasury's Proposal to Limit Crummey Powers

- "Greenbooks" (March 4, 2014, and Feb. 2, 2015) would limit the (currently) $14,000 annual exclusion to:
  - Outright unrestricted gifts.
  - "Tax-vested" one-beneficiary trusts under section 2642(c)(2).
  - Up to $50,000 per donor **(still subject to the $14,000 per donee limitation)** for "transfers in trust (other than to a trust described in section 2642(c)(2)), transfers of interests in passthrough entities, transfers of interests subject to a prohibition on sale, and other transfers of property that, without regard to withdrawal, put, or other such rights in the donee, cannot immediately be liquidated by the donee."

Number Eight
Continued Erosion of the Power of States To Tax Trust Income

Kimberly Rice Kaestner 1992 Family Trust v. North Carolina Department of Revenue, 12 CVS 8740 (N.C. Sup'r Ct. April 23, 2015)

- North Carolina sought to tax the income of a New York trust with a beneficiaries in North Carolina, even though a New York resident was the trustee, all trust records were maintained in New York, the custodian of the trust investments was in Boston, the trust tax returns were prepared in New York, the trustee did not travel to North Carolina, the trustee did not make any distributions to the North Carolina beneficiary, and the beneficiary could not compel the trustee to make a distribution.
- The court held that the tax, as applied to this trust, violates both the due process and commerce clauses of the U.S. Constitution.

Residuary Trust A u/w/o Kassner v. Director, Division of Taxation, 2015 N.J. Tax LEXIS 11, 2015 WL 2458024 (N.J. Sup'r Ct. App. Div. May 28, 2015)

- The trustee of a trust, created under the will of a New Jersey resident, resided in New York and administered the trust outside of New Jersey. The trustee paid New Jersey income tax for 2006 only on income attributable to activities in New Jersey.
- The New Jersey Tax Court rejected the Division of Taxation's contention that the trust was taxable on all undistributed income because it held assets in New Jersey.
- The Appellant Division affirmed, citing the New Jersey "square corners" doctrine that requires the government to deal fairly with its citizens, because the Division of Taxation's published newsletter in 1999 had advised that undistributed trust income would not be taxable if the trustee was not a New Jersey resident and the trust had no New Jersey assets.

Number Seven
More Flexibility in the Support and Administration of Charities

Protecting Americans from Tax Hikes ("PATH") Act of 2015 (part of Public Law 114-113) (Dec. 18, 2015)

- 56 (out of 127) sections deal with "extenders."
- 22 of those make certain "extenders" permanent, including:
  - Charitable distributions from IRAs of individuals over 70½, up to $100,000 per year, without including those amounts in gross income (Act § 112; Code § 408(d)(8))).
  - Favorable rules for contributions of real property for conservation purposes, especially for farmers and ranchers and Alaska Native Corporations (Act § 111; Code § 170(b)).
  - Not reducing the basis in an S corporation shareholder's stock by the unrealized appreciation in property contributed to charity by the S corporation (Act § 115; Code § 1367(a)(2)).

Measure of Section 642(c) Deduction
Green v. United States (W.D. Okla. Nov. 4, 2015)

- Charitable donations by The David and Barbara Green 1993 Dynasty Trust
  - (The Trust owned a 99% limited partnership interest in Hob-Lob Limited Partnership, which owned or operated many Hobby Lobby stores).
  - The Trust made donations of Virginia, Oklahoma, and Texas real estate in 2004.
  - The donees are described in section 170(b)(1)(A).
- The Trust deducted **the adjusted basis** of the properties on its Form 1041.
- And amended the return **exactly three years later** to deduct **fair market value**.

Green v. United States, continued

- The IRS disallowed the refund: “The charitable contribution deduction for the real property donated in 2004 is **limited to the basis** of the real property contributed.”
- The District Court granted summary judgment to the Trust.
- “[S]tatutes regarding charitable deductions … are not matters of legislative grace, but rather ‘expression[s] of public policy’ **to “encourage charitable gifts.”**
- As such, “[p]rovisions regarding charitable deductions should … be **liberally construed** in favor of the taxpayer.”

Green v. United States, continued

- The Government argued that section 642(c) limits the deduction to "any amount of the gross income … paid."
- The court was persuaded by the fact that the properties had been **bought** with gross income.
- The Government argued that gross income does not include unrealized appreciation.
- The court found no limitation to basis in section 642(c).

Green Light for "Mission-Related Investments" Notice 2015-62, 2015-39 I.R.B. 441 (Sept. 15, 2015)

- A "mission-related investment" is intended to produce both a social benefit and an investment return and therefore is not a "program-related investment" exempt under section 4944(c) from treatment as a jeopardizing investment.
- Notice 2015-62 provides that "a private foundation will not be subject to tax under section 4944 if foundation managers who have exercised ordinary business care and prudence make an investment that furthers the foundation's charitable purposes at an expected rate of return that is less than what the foundation might obtain from an investment that is unrelated to its charitable purposes."

Number Six
New Uniform Acts

The Uniform Trust Decanting Act (UTDA) (July 2015)

- Generally allows decanting whenever the trustee has discretion to make principal distributions.
  - Or to create a special-needs trust.
- Notice to beneficiaries is required, but not court approval.
- There is no duty to decant (section 4 of UTDA says), but if decanting is done, it must be done in accordance with the trustee's fiduciary duties.
- Generally decanting may not add beneficiaries.
- UTDA seems carefully structured to avoid tax problems.

- Now we might see a renewal of the Treasury-IRS guidance project on the tax consequences of decanting.

The Uniform Fiduciary Access to Digital Assets Act (UFADAA) (July 2014)

- In July 2014, the ULC approved a Uniform Fiduciary Access to Digital Assets Act (UFADAA) authorizing fiduciaries to access, manage, copy, and delete digital assets.
- Generally, enactment of UFADAA was blocked by internet providers and advocates for personal rights and privacy, in many cases by the use of exaggerated horror stories of the breaches of privacy that UFADAA would allow.
- Some internet service providers even developed and promoted their own very harsh alternative to UFADAA, the Privacy Expectation Afterlife Choices Act ("PEAC Act," pronounced "peace act").

The *Revised* Uniform Fiduciary Access to Digital Assets Act (RUFADAA) (July 2015)

- Renewed discussions resulted in RUFADAA, which original opponents of UFADAA agreed not to oppose.
- RUFADAA generally allows a fiduciary full access to digital assets other than the **content** of electronic communications (unless the user or the court directs otherwise).
- RUFADAA also sets forth a recapitulation of fiduciary duties.

Number Five
Final Portability Regulations

Final Portability Regulations, T.D. 9725, 80 FED. REG. 34279 (June 16, 2015)

- Temporary and proposed regulations had been released June 18, 2012.
- Section 7805(e)(2) requires final regulations in three years.
- Clarified a few matters, but mostly the same.
- Preserved continuous, largely favorable guidance from January 1, 2011.
- Did not address Rev. Proc. 2001-38* and QTIP elections on portability-only estate tax returns.

  * Rev. Proc. 2001-38 applied in PLR 201603004 (Aug. 11, 2015).

  – This guidance will come in due course.
  – QTIP with portability should be confirmed.
  – But there are “hindsight” concerns unrelated to portability.

Number Four
Same-Sex Marriage Recognized as a Constitutionally Protected Right

Obergefell v. Hodges, 576 U.S. ___, 135 S. Ct. 2584 (June 26, 2015)

- Same-sex marriage is a fundamental right.
- The Court's 5-4 decision was exactly two years after its 5-4 decision in *United States v. Windsor*, 570 U.S. ___, 133 S. Ct. 2675 (2013), holding that federal law may not refuse to recognize such a marriage validly performed or recognized under the law of any state.
- *Obergefell* ends one phase of litigation.
- Likely creates –
  - More transitional issues in the short term.
  - More uniformity and simplicity in the long term.

Number Three
Consistency-of-Basis Legislation
Sections 1014(f) and 6035
Notice 2015-57; Form 8971

The Surface Transportation and Veterans Health Care Choice Improvement Act (Public Law 114-41) (July 31, 2015)

- Act Section 2004, “Consistent Basis Reporting Between Estate and Person Acquiring Property from Decedent.”
- Code Section 1014(f):
  - The basis of property received from a decedent may not exceed the value as finally determined for estate tax purposes.
    - If there is no final determination (as in the case of property sold while an estate tax audit is still in progress or, within the statutory period for assessments, has not begun), basis may not exceed the value reported on the estate tax return.
  - But this rule “shall only apply to any property whose inclusion in the decedent's estate increased the liability for the tax imposed by chapter 11 (reduced by credits allowable against such tax) on such estate”
    - Estate below the exemption?
    - Marital? Charitable?

Code Section 6035

- Imposes reporting requirements on every executor who is required to file an estate tax return – that is, in general:
  - If the gross estate plus adjusted taxable gifts exceeds the applicable filing threshold.
  - But also, apparently, under Reg. §20.2010-2(a)(1), if a return is filed only to elect portability.
- The executor must furnish to the IRS and to the recipients of property interests included in the decedent's gross estate a statement setting forth the value of those property interests reported on the estate tax return.
- The statement must be supplemented if value is changed, for example on audit.

Effective Date Issues

- Enacted July 31, 2015.
- Applicable if an estate tax return is filed after that date.
- Requires a report of estate tax values within 30 days after the return is filed.
- August 1 + 30 days = August 31.
- Notice 2015-57, 2015-36 I.R.B. 294 (Aug. 21, 2015) extends due dates to February 29, 2016, and promises guidance by then.
  - Cites section 6081(a), which allows extensions of time only for up to six months except for taxpayers who are abroad.
  - August 31, 2015 + 6 months = February 29, 2016.
  - So this will be the only extension.

Form **8971**
(January 2016)
Department of the Treasury
Internal Revenue Service

Information Regarding Beneficiaries Acquiring Property From a Decedent

▶ **Information about Form 8971 and its separate instructions is at *www.irs.gov/form8971*.**

OMB No. 1545-2264

Check box if this is a supplemental filing ☐

Part I Decedent and Executor Information

1 Decedent's name	2 Decedent's date of death	3 Decedent's SSN
4 Executor's name (see instructions)	5 Executor's phone no.	6 Executor's TIN

7 Executor's address (number and street including apartment or suite no.; city, town, or post office; state or province; country; and ZIP or foreign postal code)

8 If there are multiple executors, check here ☐ and attach a statement showing the names, addresses, telephone numbers, and TINs of the additional executors.

9 If the estate elected alternate valuation, indicate the alternate valuation date: _____

Part II Beneficiary Information

How many beneficiaries received (or are expected to receive) property from the estate? _____ For each beneficiary, provide the information requested below. If more space is needed, attach a statement showing the requested information for the additional beneficiaries.

A Name of Beneficiary	B TIN	C Address, City, State, ZIP	D Date Provided

Notice to Executors:

Submit Form 8971 with a copy of each completed Schedule A to the IRS. To protect privacy, Form 8971 should not be provided to any beneficiary. Only Schedule A of Form 8971 should be provided to the beneficiary. Retain copies of all forms for the estate's records.

Sign Here

Under penalties of perjury, I declare that I have examined this return, including accompanying schedules and statements, and to the best of my knowledge and belief, all information reported herein is true, correct, and complete.

▶ Signature of executor _____ Date _____

May the IRS discuss this return with the preparer shown below? See instructions . . . . . ☐ Yes ☐ No

Paid Preparer Use Only

Print/Type preparer's name	Preparer's signature	Date	Check ☐ if self-employed	PTIN
Firm's name ▶			Firm's EIN ▶	
Firm's address ▶			Phone no.	

SCHEDULE A—Information Regarding Beneficiaries Acquiring Property From a Decedent

► Information about Form 8971 (including Schedule A) and its separate instructions is at *www.irs.gov/form8971*.

Check box if this is a supplemental filing ☐

Part 1. General Information

1 Decedent's name	2 Decedent's SSN	3 Beneficiary's name	4 Beneficiary's TIN

5 Executor's name	6 Executor's phone no.

7 Executor's address

Part 2. Information on Property Acquired

A Item No.	B Description of property acquired from the decedent and the Schedule and item number where reported on the decedent's Form 706, United States Estate (and Generation-Skipping Transfer) Tax Return. If the beneficiary acquired a partial interest in the property, indicate the interest acquired here.	C Did this asset increase estate tax liability? *(Y/N)*	D Valuation Date	E Estate Tax Value *(in U.S. dollars)*
1	Form 706, Schedule _____ , Item _____ Description —			

Notice to Beneficiaries:

You have received this schedule to inform you of the value of property you received from the estate of the decedent named above. **Retain this schedule for tax reporting purposes.** If the property increased the estate tax liability, Internal Revenue Code section 1014(f) applies, requiring the consistent reporting of basis information. For more information on determining basis, see IRC section 1014 and/or consult a tax professional.

From the Instructions for Form 8971 (January 2016)

All property acquired (or expected to be acquired) by a beneficiary must be listed on that beneficiary's Schedule A. If the executor has not determined which beneficiary is to receive an item of property as of the due date of the Form 8971 and Schedule(s) A, the executor must list **all items of property that could be used, in whole or in part**, to fund the beneficiary's distribution on that beneficiary's Schedule A. **(This means that the same property may be reflected on more than one Schedule A.)** A supplemental Form 8971 and corresponding Schedule(s) A should be filed once the distribution to each such beneficiary has been made.

(emphasis added)

From Form 8971, Schedule A (January 2016)

Notice To Beneficiaries:

You have received this schedule to inform you of the value of property you received from the estate of the decedent named above. **Retain this schedule for tax reporting purposes.** If the property increased the estate tax liability, Internal Revenue Code section 1014(f) applies, requiring the consistent reporting of basis information. For more information on determining basis, see IRC section 1014 and/or consult a tax professional.

(emphasis in original)

Number Two
New Leadership in the House of Representatives

- The “regular order” participation and section-by-section attention in the PATH Act was somewhat encouraging.
- Significantly from the standpoint of tax policy:
  - Speaker Paul Ryan chaired the Ways and Means Committee.
  - New Ways and Means Chairman Kevin Brady of Texas has sponsored estate tax repeal bills.
- Following the 2016 election:
  - Republican control of the Senate may or may not survive.
  - But 60 votes is not likely – for either party.
- Repeal of the estate tax would take political capital, which will probably be spent elsewhere.
- So there is probably nothing more that can be done to the estate tax.

Or is there?

Number One
The Administration's Present and Future Assaults on Estate Planning Techniques

Settled and Pending Tax Court Cases

- *Davidson*: SCINs (stipulated decision entered July 6).
  - We learn nothing about SCINs, mortality, or interest rates.
  - Estate has now sued Deloitte Tax LLP for $500 million.
- *Woelbing*: sale to grantor trust (Feb. 29 trial continued).
  - Issues are gift tax valuation, promissory notes valued at zero under section 2702, sold assets subject to estate tax under sections 2036 and 2038, effect of guarantees, estate tax value, and effect of a defined value formula.
- But compare *Estate of Purdue v. Commissioner*, T.C. Memo. 2015-249 (Dec. 28, 2015).
  - To hold and manage marketable securities and a commercial building as a family asset is a "legitimate nontax motive" for transfers to a family-owned LLC, so the value of the LLC assets is not included in the transferor's gross estate.

Administration's Assaults on Estate Tax Planning

- The White House's proposal to tax capital gains at death.
- The Administration's proposals to subject grantor trusts to estate or gift tax.
- Four new projects on the Treasury-IRS Priority Guidance Plan (July 31, 2015):
  - #1 Qualified contingencies in CRATs.
  - #3 Basis of grantor trust assets.
  - #5 Valuation of promissory notes.
  - #8 Defined value formula clauses.
- Valuation discounts under section 2704:
  - Treasury's mixture of hesitancy and boldness.
  - The profession's interest.

Questions or Comments?

Ronald D. Aucutt
raucutt@mcguirewoods.com

www.mcguirewoods.com

See also “Estate Tax Changes Past, Present and Future”
(http://www.mcguirewoods.com/estate-tax-changes)