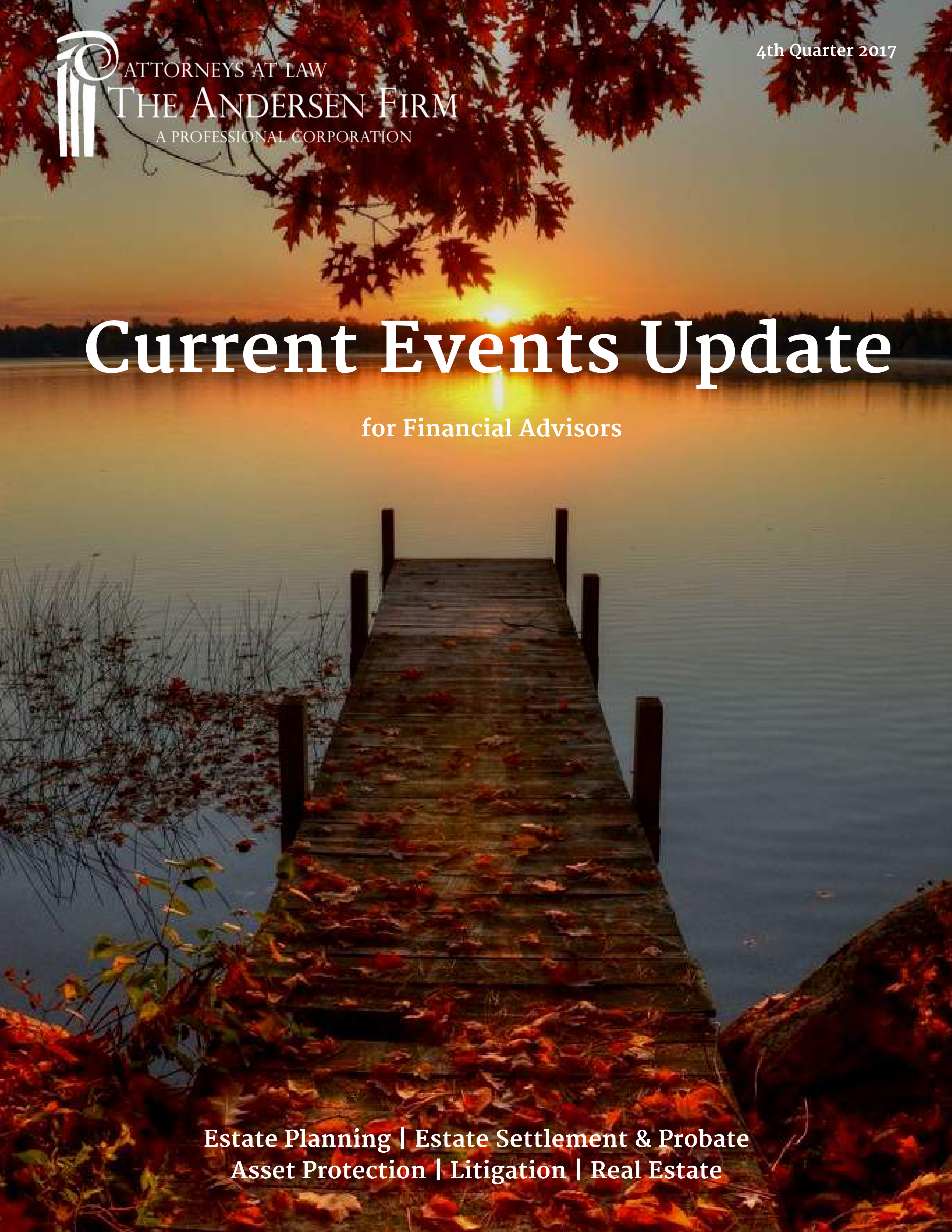

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4th Quarter 2017

Current Events Update

for Financial Advisors

Estate Planning | Estate Settlement & Probate
Asset Protection | Litigation | Real Estate

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FINANCIAL ADVISOR
CURRENT EVENTS UPDATE
FOURTH QUARTER 2017

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on the cover

With National Estate Planning week occurring every fall, and upcoming family gatherings on the horizon, now is the time to talk with family about estate planning. This photo was chosen as it provides us all a glimpse at the beauty of fall.

The photographer is Gary Caldwell.

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laugh for the day

My Living Will

Last night, my kids and I were sitting in the living room and I said to them, 'I never want to live in a vegetative state, dependent on some machine and fluids from a bottle. If that ever happens, just pull the plug.'

They got up, unplugged the computer and threw out my wine!!

What Should Clients Do in Response to TRUMP'S TAX PLAN?

Source: FA Magazine
Carol A. Harrington, Ellen K. Harrison, Carolyn S. McCaffrey

The Trump administration and GOP leaders have unveiled a tax reform plan that contains few surprises, and even fewer details. But there are still things estate planners can do to buttress their clients' estates in the face of possible changes.

The estate tax and the generation-skipping transfer tax are slated for repeal, which is certainly not a surprise considering the proposal has been a longtime goal of the Republican Party and was something President Donald Trump promised during his campaign.

Among the unknowns that advisors will have to contend with: The plan makes no mention of the future of the gift tax. The elimination of the gift tax would likely encourage significant lifetime transfers in trust. These transfers would cause a meaningful erosion of assets potentially subject to future estate taxes. If the gift tax preserved, it may be due to a desire to preserve this possible taxable asset base, although others have suggested that the gift tax is important to prevent income tax avoidance.

Moreover, the plan also does not address basis adjustment at death. This could mean that current law, which generally adjusts basis to date of death market value (a “step-up” or “step-down”), would continue. Presumably, some changes would have to be made to properly coordinate the basis provisions under current law if there is no estate tax. It is also possible that when detailed proposals are made, there could be (1) no basis adjustment at death (“carry-over basis”); (2) a limited basis adjustment at death (basis step up for assets up to the value of the gift and estate tax exemption, currently $5.49 million per person with double that for married individuals); or (3) gain recognition at death.

Because the final form of the tax reform bill is unknown, as is whether it will be adopted at all, maintaining flexibility in estate plans is critical. With the use of a trust protector, another person is granted powers that can be exercised to make certain changes to the principal’s estate plan in response to these changes. In addition a power of attorney could authorize the holder of the power to make transfers of property to revocable trusts and the trust protector could change the terms of revocable trust instruments in a manner that would maximize tax efficiency without changing the basic dispositive plan. Similarly, the independent trustees of an irrevocable trust can be given the power to make changes that would reduce the exposure of trust assets to future taxation. For example, if the estate tax is repealed, giving a trust beneficiary a testamentary power of appointment could provide a means to achieve an asset basis step-up at death.

Although gifts that attract gift tax liability should probably be avoided until the future of the transfer tax system is clear, we think it is important for high-net-worth individuals to continue to implement gift-tax-free transactions that shift property from their estates to trusts for family members. It is possible that estate tax repeal will not be enacted. But even if the estate tax is repealed, lifetime estate planning will continue to be important to individuals who want their children to enjoy some of the family wealth before they die. The parent who wants to continue to contribute to support his or her children after they reach maturity will likely face gift tax consequences unless assets have been shifted to trusts for the children's benefit.

10 ESTATE PLANNING ACTION ITEMS TO DO NOW

The only thing certain used to be death and taxes, but now the taxes are coming into question. President Donald Trump and the Republican-dominated Congress are expected to revamp taxes and maybe change gift and estate tax rules, but no one knows what that will entail or when it might happen.

There will still be taxes, just not all of the taxes we have now. There may be new taxes added and old taxes removed. What we know about taxes is changing.

There is a great deal of uncertainty about particular aspects of the Republican tax proposal—including a replacement tax on the wealthy—and there is already concern about the likely impermanence of any new legislation, These factors highlight the importance of flexibility in preparing an estate plan and proceeding with wealth transfers suited to the current political and economic circumstances.

Even if tax legislation passes, it's likely that the rules of the game will continue to change, perhaps more frequently, going forward. It is essential to stay in the know regarding the potential impact of new laws, in addition to tools currently available to protect your wealth.

The following strategies are good for the long or short term, and most can be used advantageously.

1. Annual Exclusion Gifts

It is still uncertain whether both the estate tax and the gift tax will be repealed. In the past, Congress has avoided taking action to repeal the gift tax, because it prevents individuals from shifting assets to create a loophole to minimize income taxes.

Therefore, you should make annual exclusion gifts to chosen loved ones of $14,000 per recipient, contribute to 529 Plans, and contribute unlimited gifts for the benefit of family members directly to educational institutions and medical facilities.

There has been no discussion about raising the annual gift exclusion amount of $14,000, but taking advantage of the opportunity in 2017 will maximize the potential appreciation on this year's gift before 2018 gifts can be made beginning January 1st of next year.

It is also prudent to consider completing these gifts in trusts, which protect the cash and investments gifted from attack by spouses, lawsuits and creditors, and can allow the donor flexibility to control and access the funds held in trust.

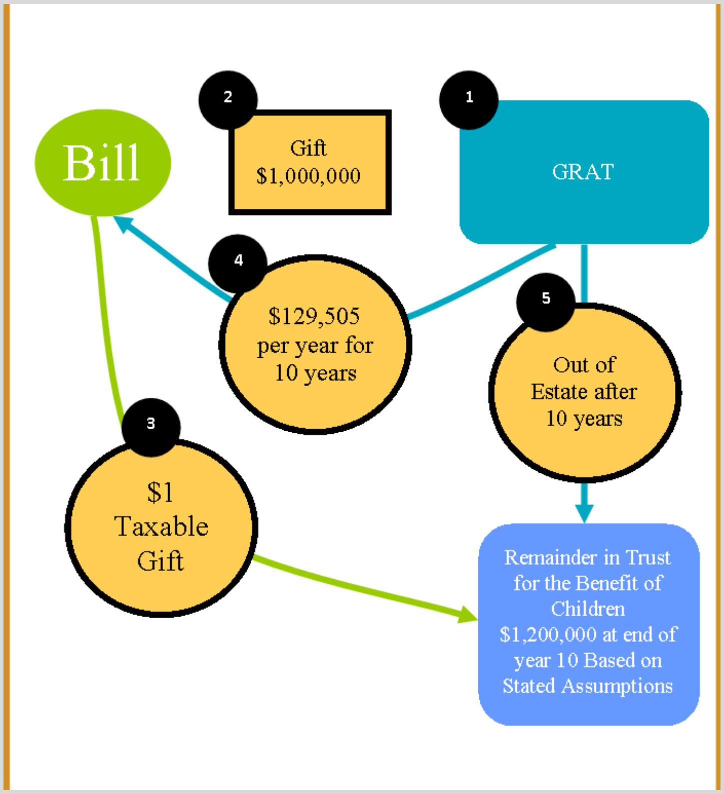
2. Lifetime Exemption Gifts
For the same reason, the $5.49 million lifetime gift exemption should also be utilized. Larger gifts afford a far greater potential for shifting wealth because more assets are available for investment and, therefore, can compound in value to a greater extent.

Again, relying upon an irrevocable trust as the vehicle through which patterned and consistent lifetime gifts are made is one of the most reliable and powerful means of ensuring a legacy of substantial wealth for future generations of the family.

3. **Short-Term And Mid-Term Grantor Retained Annuity Trusts (GRATs)**
The purpose of the GRAT is to make a loan of investment assets to your children or loved ones without using any of your lifetime gift exemption. Your loved ones benefit from any growth above the initial contribution.

Since interest rates remain historically low, it is an ideal time to implement GRATs, especially since there are indications that interest rates will continue to rise in the foreseeable future.

When interest rates are lower, the GRAT pays less back to the grantor, meaning that more assets remain outside of the grantor's estate after the completion of the GRAT term of years.

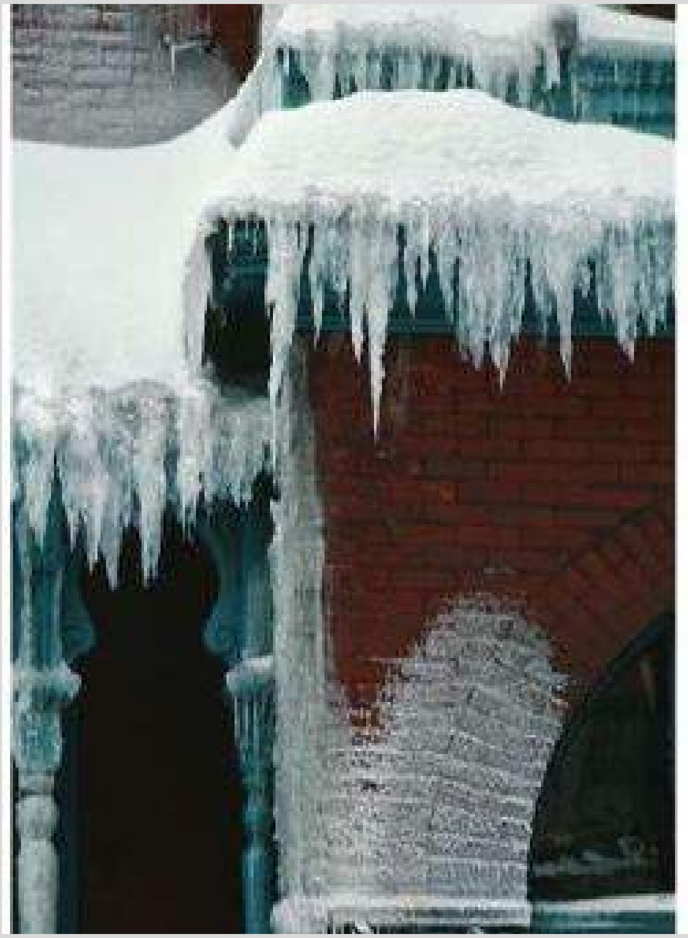


4. Estate Freeze Installment Sales

An installment sale to an intentionally defective grantor trust is a strategy that is comparable to the GRAT and works best with income-producing real estate, interests in a family business, or more illiquid investments with potential for significant future growth. In this form of planning, the investments are sold to an irrevocable grantor trust in exchange for a promissory note.

Since the vehicle is a grantor trust for income tax purposes, no capital gains tax is realized at the time of the transfer. Additionally, since the trust buys the investments for fair market value, no lifetime gift tax exemption is used.

All growth on the investment takes place within the trust and is therefore not taxed as a part of the estate. Many also find this strategy appealing because the revenue or proceeds generated by the investment can be paid back to the original grantor as satisfaction of the debt on the promissory note that the trust is obligated to pay.



5. Family Limited Liability Companies

Proposed IRS regulations were issued in 2016 that would limit discounting of transfers of family business interests. The adoption of these proposed regulations has been delayed and their enforcement could be defunded by Congress, but they are still likely to be adopted by the Treasury for implementation under a future administration.

Therefore, a family limited liability company remains a viable tax minimization strategy. These entities are sophisticated vehicles for centralizing family investments, providing for the orderly transfer of assets, providing asset protection, and expanding family investment opportunities.

Family limited liability companies and their variants may hold family businesses, real estate or other investments. And they can discount the value of the assets because that is seen as the only way people outside the family would buy in, particularly since nonfamily members have no control over what the entity does.

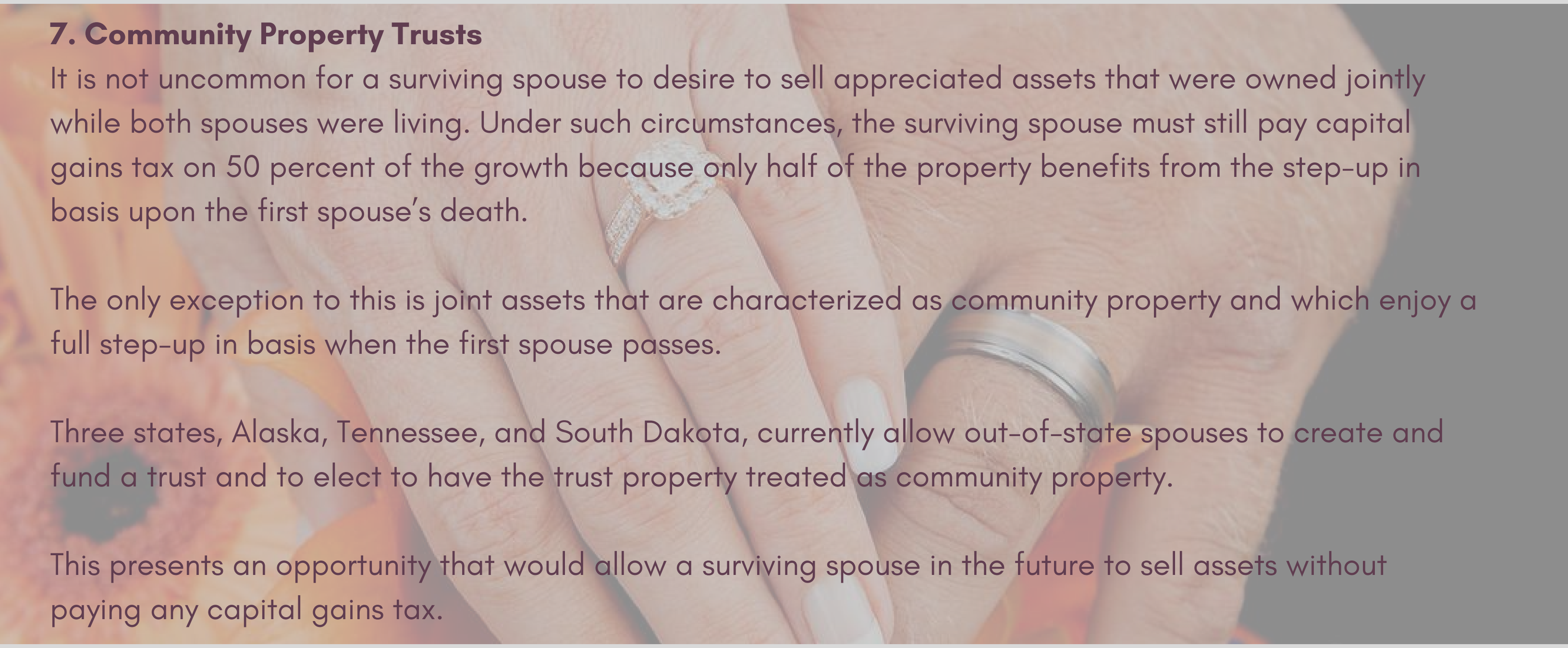
This allows the underlying assets to be shifted without depleting nearly as much of your lifetime gift exemption, resulting in immediate estate tax savings upon the completion of the gift and preserving the exemption for future wealth transfers.

6. Upstream Gifting

Under the current tax laws, a step-up in the cost basis of an asset is granted when an individual passes away, meaning that the surviving family members can sell the asset without realizing any capital gains tax. This benefit is likely to be eliminated if the federal estate tax is repealed.

Furthermore, there are few options for an individual to minimize or eliminate capital gains tax before death. While the step-up in basis remains available, consider giving appreciated assets to a trust specifically designed to cause the assets to be included in a less affluent parent's estate. Inclusion in the parent's estate would allow assets to be sold with minimal capital gains tax consequences within a reasonable period of time during the child's lifetime.

The trust would then ensure that the proceeds would thereafter be held for the benefit of the child's family after the parent's death.



7. Community Property Trusts

It is not uncommon for a surviving spouse to desire to sell appreciated assets that were owned jointly while both spouses were living. Under such circumstances, the surviving spouse must still pay capital gains tax on 50 percent of the growth because only half of the property benefits from the step-up in basis upon the first spouse's death.

The only exception to this is joint assets that are characterized as community property and which enjoy a full step-up in basis when the first spouse passes.

Three states, Alaska, Tennessee, and South Dakota, currently allow out-of-state spouses to create and fund a trust and to elect to have the trust property treated as community property.

This presents an opportunity that would allow a surviving spouse in the future to sell assets without paying any capital gains tax.

8. Charitable Remainder Trusts (CRTs)

Those wishing to sell appreciated assets, liquidate inherited assets that have a carryover basis, and otherwise diversify in a tax-efficient manner will continue to utilize CRTs.

In establishing a CRT, the creator of the trust retains the right to receive an annuity or fixed percentage of the trust assets each year. After the term of years of the CRT or the creator's lifetime, the balance of the CRT assets pass to charitable organizations of your choosing, including a private family foundation.

Since the beneficiaries after the CRT period are not-for-profit organizations, any sale of assets within the CRT does not realize capital gains. The only tax that is due is based on the amount of the annuity transferred back to the individual who funded the CRT.

Many families choose to couple the CRT with life insurance so that the proceeds of the insurance coverage replace the wealth passing to the charities, which would have otherwise been distributed to the family members, after the CRT period.

9. Drafting Flexibility in Core Planning Documents
If the step-up in basis is eliminated by Congress, then the advantages of keeping certain assets inside the estate evaporate. Therefore, without the step-up in basis, it is critical that you have reverse swap powers in the trust provisions, which would allow the swap of low basis, appreciating assets, which are likely to see the greatest appreciation once the assets are inside the trust, in exchange for the trust's high basis assets.

Given the uncertainty of future tax changes and family circumstances, it is also critical for a trust to include limited powers of appointment for the beneficiaries or the trustee, referred to as a decanting. This will allow the beneficiary or trustee to transfer the assets to a new trust that contains the provisions that best reflect the tax laws and your wishes at that time.

By including these authorities in an irrevocable trust, it provides important options for family members to adapt to drama

10. Philanthropic Planning
Rather than making gifts directly to charity, donors are choosing foundations or donor advised funds (DAFs) to maintain some control or full control over making grants as well as taking advantage of the potential benefit of eliminating capital gains and the potential for an immediate tax deduction. Deciding which to use depends on the donors situation and goals.

While DAFs are established quickly, private foundations take longer and require significantly more money as they require IRS approval, creation of a board and other legal actions. Donors using the DAF may advise on the contributions they want to make and the recommendations are typically followed, however, with a private foundation, the donor has the final word on the entire contribution process. Once a DAF is funded, there is no requirement of donations in any amount or time frame, while private foundations must pay out each year 5% of the prior years assets in grants and administrative fees.

With regard to tax deductibility, generally, cash donations to a DAF can be deducted up to 50% of the donor's adjusted gross income. Cash donations to private foundations are deductible up to 30%. Gifts of stock or real property to a DAF can be deducted up to 30% and to a private foundation at 20%.

Either way, your irrevocable contribution grows tax free for future distributions to qualified charities

If you have clients who could use a
Complimentary Estate Plan Review
contact us at 866.230.2206

DISASTER RECOVERY: HOW TO HELP YOUR CLIENTS

The images from Hurricane Irma are still fresh on our screens, and we are reaching out with money, supplies, or time to support those in need. Soon, though, it will be time to step back and think about how we handle these natural disasters more broadly.

What to do if one were to strike your own area, and your own clients? While you can't prevent the next earthquake, nor the next destructive storm like Hurricanes Irma, Harvey, Katrina and Super Storm Sandy, you can help clients be prepared so that if disaster does strike, its recovery can be safer, a bit less bumpy, and at least a little quicker.

Lack of access to important medical information can become a crisis for clients in the immediate aftermath of a disaster, and beyond. In a natural disaster, it's more likely that clients will be treated outside their local network of hospitals and doctors, where their medical records are stored. Moreover, when people are displaced in a disaster, getting refills of their medicines can become a critical, urgent need. Not having all their medications with them, or not having a complete list of their medications with them, can potentially put clients' health at risk rather quickly.

The loss of important legal, financial and insurance papers presents one major problem clients need to overcome in a disaster. And on top of this, not having access to some of these papers can be a multiplying barrier to the recovery effort itself. Proving ownership of a home, the value of one's belongings, the presence of an insurance policy, and the existence of an estate plan, to name a few, can be essential in moving through the disaster recovery process. Any difficulty clients experience in obtaining these documents can add delay to their recovery effort.

Firms can take many approaches to the electronic availability of clients' documents. At one end of the spectrum, some firms simply recommend that their clients create offsite electronic copies of documents, and that's that. The Andersen Firm keeps electronic copies of client documents which can be made available to clients, hospitals, or to other professionals, electronically upon request. If original estate planning documents are destroyed, we are able to recreate those documents for our clients and ensure clients' plans are put back to their original state.

While you can't do anything to help replace the sentimental objects lost in a disaster, there are at least things that we can do as a firm, and that our clients can do as individuals, to preserve the critical information that can help them weather and recover from such a crisis.

WOMEN'S ISSUE

Estate Planning

sources:
Women's Institute for Financial Education
Amy Libertowski, Guest Post, Forbes
American Business Women's Association

Death comes to us all, but on average, women live 4.9 years longer than men. A longer life- expectancy rate means women have additional planning concerns to consider, compared to their male counterparts — for instance, ensuring their assets can last for a longer period, should they ever become widowed.

Some women may also face financial challenges due to shorter work histories, prompted by putting their careers on hold to raise families. This break in pay could reduce the amount of savings these women will accumulate for their retirement; an organized estate plan can help with transferring of those assets.

However, estate planning for women is also to protect all that women have accomplished as individuals. Women have come a long way in the workforce. In 1950, one in three women were part of the labor force. By 2016, that statistic was three out of five, and today in 2017, even more gains have been made in women's leadership.

To further understand why estate planning is a women's issue, it's important to realize how little of an "estate" women were historically "allowed" to have. Even just up until forty years ago, women were still not given the abilities men had to control their own money. It wasn't until 1969 that a U.S. court definitively ruled that labor jobs could not only be given to men, and ruled that firing women from factory work because of their gender was illegal.

We don't want to squander what our fore-mothers gave us, and estate planning is a women's issue because it allows us to protect our hard-won assets. Estate planning allows you to direct where your assets will go and how your healthcare decisions, financial choices, and other important directives are to be made in the event of incapacity or death.

Here are some of the ways in which estate planning benefits women:

Agency and Control Things happen, and you want to be able to keep your property and assets where you want them, without being forced into a decision that would cause a loss of property. Estate planning gives you agency over your healthcare choices and financial decisions. There is no better way to be secure that what you've worked hard for won't be for nothing.

Peace of Mind In the event of incapacity or death, the documents contained in an estate plan will give you a trusted person to make decisions for you. Your living will also contains directives that will tell the hospital and other personnel how to manage your care.

Longevity If you want, you can ensure that your money and property are invested or put into a trust fund that will keep them around for a long time to benefit your daughters and granddaughters.
With the right guidance and team of professionals, you can stay on top of your estate plan and make sure you are ready for whatever the future holds. Here are some important planning tips to keep in mind.

Know your financial assets. It is important to assume an active role in managing your finances. Take inventory of what types of financial assets you own; these might include checking and savings accounts, taxable investment accounts or retirement plan accounts. Make sure you understand how those assets are managed and how they should be distributed at your death.

Protect your financial assets. Make sure your insurance coverage can support your financial needs in case your spouse passes away before you do. Also, consider purchasing insurance on your life to cover any final expenses or estate taxes that might be due at death.

Plan for your financial assets. Essentially, estate planning is a process that allows individuals to create documents reflecting how they want their personal and financial assets to be distributed at their death. By practicing proactive planning, you will gain full control over the disposition of those assets; the process can also include planning for incapacity in case you become physically or mentally unable to make decisions while you're still alive.

The main takeaway

The fact that women are likely to outlive their spouses makes an updated, comprehensive estate plan all the more important. As women, it's crucial that we take an active role in managing our finances, protecting our assets and having a clear plan for distributing those assets in the future.

Estate planning is a women's issue. Make sure that you retain control over your assets and finances by creating an estate plan.

If you have clients who may benefit from a
Complimentary Estate Plan Review
contact us at 866.230.2206.

How to Talk to Parents About Estate Planning

Thanksgiving is a busy and joyful time. As your family comes together to celebrate, you may also want to make time to talk to your parents about estate planning.

It can be difficult to talk to parents about estate planning. For a number of reasons, parents can be reluctant to plan their final affairs. Children are often concerned that broaching the topic will make them seem insensitive or greedy. But the truth is that your parents' estate plan (or lack thereof) can affect you as much as it does them. Talking about estate planning can ease everyone's minds and help ensure a smooth transition when the time comes.

Here are a few tips to help facilitate the discussion.

Start by Talking About Your Own Estate Planning Concerns - A start to the discussion, may be to talk about your own estate planning concerns. Keep the initial discussion about general estate planning topics, and only move to their specific estate plans when the opportunity arises.

There are a number of ways to begin a conversation about estate planning. Here are a few examples:

- Explain that you have talked to someone or read articles recently that prompted you to think about the importance of estate planning.
- Discuss how the turmoil in the economic markets has put some inheritances in jeopardy.
- Talk about how the recent Presidential election and the current political climate could affect gift and estate taxes.
- Mention your goals of avoiding family conflict in your own estate.

Conversations like these provide a low-pressure context in which to discuss estate planning. With a little luck, your parents will open up about their own plans. If not, the conversation will at least give you the opportunity to ask them whether they have thought about these issues for their own estate. At a minimum, the discussion should prompt them to start thinking about the topic.

Make It About Family, Not About Money - Many parents care more about the administrative burdens they leave for their children and family harmony than the specific dollar amount that each heir will receive. Open conversations about estate planning can set family expectations and minimize the risk of conflict after death. And because discussions about family don't carry the same cultural taboo as discussions about money, it is a good idea to keep the focus on maintaining healthy family relationships.

There are a number of ways that family harmony can be disrupted by an estate plan (or failure to plan). For example, choosing the wrong family member to serve as executor or trustee can be a recipe for disaster. If there is conflict between family members, naming one of them in a fiduciary role can bring them further apart, particularly if the fiduciary role involves a lot of discretion. A corporate trustee or more neutral family member may be a better choice.

Planning to avoid family conflict is particularly important in a second-marriage situation. Probate attorneys all have stories about the family train wreck that can occur after the death of a parent who leaves a surviving spouse that is not the parent of his or her children. Special care should be taken in this context to preserve family harmony.

Bringing family concerns to your parents' attention can help them see the bigger picture. A few simple steps taken while your parents are alive can minimize family tension after their death.

Identify the Cause of Procrastination – Sometimes parents just don't want to think about estate planning. If your parents are putting it off, you can help them by addressing the concerns behind their reluctance to plan.

There are a number of reasons that people delay estate planning, including:

- Lack of knowledge regarding the need for estate planning or familiarity with estate planning concepts
- Reluctance to consider their own mortality
- A belief that they don't own enough assets to need estate planning
- Concerns about the cost of estate planning
- A belief that they are too young to need an estate plan
- Concern that the estate planning process might be too complicated

There are easy responses to most of these concerns. If you can identify what is causing your parents to procrastinate, you may be able to encourage them to move forward with their estate planning.

Your Parents' Plan and Your Planning: As you think about your planning, it is useful to factor in any inheritance you might receive from your parents. Knowing how much to expect requires a broader discussion with your parents about estate planning, a difficult topic to broach because it involves two subjects that are very personal and uncomfortable for most people: money and death.

Don't wait for a health crisis: Families that wait too long to talk about inheritances and related issues may not get to talk about them at all. A sudden change in your parents' health or an untimely death can quickly lead to an estate planning nightmare. Ideally you want to broach the estate planning talk before one or both of your parents needs help managing finances or health

"It is so important to discuss estate planning with your parents while they are both mentally healthy," says Joleen Searles, Senior Partner at The Andersen Firm. "If they don't make these decisions until after one of them is incapacitated in some way, quite frankly, it takes many of their choices off the table. Taking an active, compassionate role can prevent a big mess."

SO, HOW DO YOU GET YOUR PARENTS—OR EVEN THE ENTIRE FAMILY—TO START A DIALOGUE ABOUT ESTATE PLANNING?

THE NEXT PAGE PROVIDES A FEW MORE TIPS TO HELP YOU AND YOUR PARENTS START TALKING:

Focus on life, not death

The topics of estate planning and death are, of course, intertwined, but it doesn't mean that death must drive the discussion—in fact, it's best if it doesn't. "It's a challenge, but you really must get the focus off death alone and on life as well when talking about estate planning," says Searles, who is also a member of Wealth Counsel and holds an LL.M. in Taxation. "Emphasize planning to live well versus planning to die well."

Make your parents—and their wishes—the primary focus of the discussion

"The bottom line is that you need your parents to tell you what they want to have done and who they want to do it," says Steve Hartnett, associate director of education, American Academy of Estate Planning Attorneys (AAEPA), San Diego, Calif.

He suggests, "You might want to take a direct approach and say, 'OK, Mom and Dad, here's the problem: I'm just not sure what it is you would like me and/or my siblings to do in the event of an emergency. What documents do we need? Where are they located? Who do you want to take care of what?' Tell them you just want to be absolutely clear about their wishes and that you want to ensure that their goals are met."

Once you learn their wishes, "the reality is that you may not like what your parents choose to do with their money and belongings, but it's their prerogative," says Hartnett. "And because estate plans do not always result in people being treated equally, it's very important—to avoid conflict later—that family members know and understand what plans are in place."

Emphasize the need for PROTECTION FOR THE ENTIRE FAMILY

Having an estate plan helps to protect family members "from creditors, predators and divorcing spouses is paramount," according to Searles, who says the last thing that anyone wants to do is "die intestate" (without a will) because it will result in unnecessary heartache and headaches—and legal fees—for their loved ones.

Encourage your parents to seek advice from an expert

By doing so, you are sending a message that you still trust them to handle their own affairs and perhaps making them breathe easier by knowing you don't want to control the situation. Offer to help them with their search for a qualified attorney. If they have already taken these steps, find out who is on their team.

Be patient—and understanding

Realistically, your first conversation with your parents about estate planning is not going to be your last. It may take several discussions before you make even a little bit of headway with them. And even after your parents have some type of estate plan in place, it doesn't mean that the arrangements they made will remain relevant in the future. Think of it as an ongoing dialogue.

If you feel disingenuous using some ice-breaking strategy, then just be upfront about acknowledging how uncomfortable the topic makes you feel. That alone is an ice breaker.

If you are ready to have the conversation with your parents, or ready to have a conversation about your own estate planning needs, please contact our office at 866.230.2206 to schedule a complimentary estate plan review.

CLARITY ON NEW FEDERAL RULES FOR SPECIAL NEEDS TRUSTS

Special needs trusts have a new level of flexibility and federal officials are working to ensure that state Medicaid directors understand the implications.

Under a law passed late last year, individuals with disabilities can for the first time establish special needs trusts for themselves.

The shift, designed to make saving money easier for those with disabilities, is significant. Previously, trusts had to be created by a third party.

Now, federal Medicaid officials are offering guidance on what the change means for state programs.

"A trust established on or after December 13, 2016, by an individual with a disability under age 65 for his or her own benefit can qualify as a special needs trust, conferring the same benefits as a special needs trust set up by a parent, grandparent, legal guardian or court," wrote Brian Neale, director of the Center for Medicaid and CHIP Services in a letter to state Medicaid directors this month. "The other defining features of a special needs trust remain unchanged."

To qualify as a special needs trust, Neale said that a trust must contain the assets of an individual with a disability who's under age 65, be created for that person's benefit and include a provision that any remaining assets be repaid to the state at the time of that person's death up to the value that the state provided in medical assistance.

In many cases individuals with disabilities face a cap on the assets they can have in their name in order to qualify for Medicaid and other government programs. Special needs trusts are one of a few ways that individuals with disabilities can accrue more assets without losing eligibility.

Allowing individuals to form trusts for themselves "supports the independence of individuals with disabilities," Neale noted in the guidance.

A NEW EXAMPLE OF FAILED DEATHBED TAX PLANNING

ESTATE OF POWELL

It has been 12 years since the Fifth Circuit affirmed the Tax Court's opinion in Estate of *Strangi*, holding that the full, undiscounted value of the assets transferred to a family limited partnership established by a deceased taxpayer was included in the decedent's estate. *Strangi* was a victory for the Internal Revenue Service (IRS) in the family limited partnership area.

The recent Tax Court case of the *Estate of Powell* builds on the rationale established by *Strangi*¸ but ultimately rests on the application of Code § 2036(a)(2). *Powell* held that a power to liquidate a family limited partnership—exercisable by the decedent's agent with other family members—gives the decedent control over possession or enjoyment of the underlying assets transferred to the family limited partnership or the income from it. As a result, the full value of the assets transferred to the family limited partnership are included in the decedent's gross estate. *Powell* also addressed application of Code § 2043 when Code § 2036 is triggered and application of Code § 2038 to a failed gift under a power of attorney.

The rationale of *Powell* represents the latest threat to valuation discounts. If broadly applied in future cases, *Powell* could eliminate many discounts used in valuation planning. This article reviews the case and identifies practical recommendations for valuation planning.

Importantly, this case was reviewed by a majority of the Tax Court.

OVERVIEW OF THE FACTS

The decedent's son made several fundamental mistakes when planning his mother's estate. On August 6, 2008, just nine days prior to her death, while Nancy Powell was hospitalized and in intensive care, her son Jeffrey Powell began his mother's estate planning. He created a limited partnership, NHP Enterprises LP ("NHP"), naming himself as general partner. He then transferred about $10 million in cash and securities from his mother's revocable trust to NHP in exchange for a 99% limited partnership interest.

On August 7, Jeffrey obtained a doctor's note due to his mother's incapacity, allowing him to act as agent under his mother's durable power of attorney for property . He used the power of attorney for property to create a charitable lead annuity trust ("CLAT"), and transferred the 99% limited partnership interest to the CLAT. The CLAT paid the annuity interest to the Nancy H. Powell Foundation for the remainder of his mother's life. The CLAT named Jeffrey and his brother as remainder beneficiaries upon his mother's death.

Jeffrey later filed a gift tax return for the transfer to the CLAT. He determined the value of the 99% limited partnership interest to be $7.5 million after a 25% discount for lack of marketability and lack of control. This resulted in a gift to the reminder beneficiaries of just over $1.6 million. The IRS issued deficiency notices for the gift tax return and the estate tax return.

Estate of Powell v. Commissioner, 148 T.C. No. 18 (2017)
Strangi v. Commissioner, 417 F.3d 468 (5th Cir. 2005)

IRS ARGUMENTS

In its notices of deficiency, the Internal Revenue Service threw the proverbial kitchen sink filled with string provisions at the taxpayer's estate, claiming deficiencies in both estate and gift tax and coincidentally forgetting to credit the taxpayer's estate for the amount of the additional gift tax it had assessed.

The IRS provided the Court with three basic arguments. 1) Under Section 2036(a)(1) and (2), the decedent "retained at her death the possession, enjoyment, or the right to the income from the property she transferred to NHP … or the right, either alone or in conjunction with any person, to designate the persons who shall possess or enjoy the property or the income there from…." 2) Under Section 2038(a), the decedent "retained at her death a power to change the enjoyment of a 99% limited partnership interest in NHP … alone or in conjunction with any other person … to alter, amend, revoke, or terminate …." 3) Under Section 2703(a), "the fair market value is determined without regard to certain rights and restrictions." The arguments under 1) and 2) above were predicated on the fact that the decedent, in conjunction with the general partners, could unanimously agree to dissolve the partnership.

In regard to the transfer of the decedent's limited partnership interest into the CLAT, the IRS pointed out that the power of attorney limited such transfers to the annual gift tax exclusion amount and was, therefore, invalid.

COURT'S ANALYSIS

The tax court determined that the assets gifted to the CLAT were includable in the decedent's estate under IRC §2033 (property in which decedent had an interest) or IRC §2038 (revocable transfers) because Jeffrey exceeded his authority granted under the power of attorney when making the gift.

The underlying cash and securities transferred to NHP for 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 NHP.

The Tax Court found that the exception in IRC §2036 (transfers for full and adequate consideration) did not apply in this case because Jeffrey had no significant nontax reason for the transfer. And the court also found the cash and securities could be includable under IRC §2035 (certain gifts within 3 years of death).

To prevent the double taxation that would have occurred by including the gifted NHP interests and the underlying assets transferred to NHP in the estate, the court found that IRC §2043(a) (allowing an estate to exclude the consideration received for an IRC §2036 or §2035 transfer) applied to the estate tax return.

IMPORTANCE OF TAX COURT'S OPINION

Given the significant errors made in planning the decedent's estate, the Tax Court's outcome is no surprise. So what is it about this case that has led commentators to describe it as "the most important Tax Court case addressing FLPs and LLCs in the context of estate planning? There are two potential reasons: 1) this is the first case where the tax court held IRC §2036(a)(2) applied even though the decedent did not own a general partnership interest; and 2) in dictum, the tax court made some very interesting comments about the potential for double taxation even though it did not apply to the case.

Extending 2036(a)(2) to limited partnership interest

Previous cases that discussed IRC §2036(a)(2) involved decedents who maintained status as a general partner of the family limited partnership (or in the case of *Strangi*, a 47% ownership in the corporation that acted as general partner). Here the decedent owned only limited partnership interests. This case establishes that the applicability of §2036(a)(2) does not depend on the type of ownership interest in the partnership. What matters is the actual powers held by the owner. So while important, the lesson should not be surprising.

Comments on Potential Double Tax

The other important aspect of the *Powell* case is dictum included in the case. The tax court held that the invalid transfer of the limited partnership interests to the CLAT caused the interests to be included in the gross estate. The tax court also held the underlying assets of the limited partnership were included in the gross estate under §2036(a)(2). The reason the estate is not double taxed for the limited partnership interests and the underlying assets of the partnership is because IRC §2043(a) allows an estate to exclude the consideration received for property included in the gross estate under IRC §2036 or §2035.

In *Powell*, the gross estate received consideration – the limited partnership interests – in exchange for transferring the underlying assets of the partnership. So the value of the limited partnership interests were excluded from the estate. Because the assets were transferred to the family limited partnership a week before the decedent died, the court found the value of the limited partnership interest on the date of death equaled the value of the limited partnership interests at the time of the transfer.

The majority opinion could have ended its discussion of 2043(a) at that time, but they didn't. Instead the tax court pointed out that 2043(a) allows the estate to exclude the value of the limited partnership interests at the time of the transfer. Then the tax court speculates that if the limited partnership interests increased in value between the time of the transfer and the decedent's death, the gross estate may have to include the increase in value of the limited partnership interests along with the value of the underlying assets at the time of the decedent's death leading to double taxation. After speculating about this potential, the tax court explicitly stated they are not addressing the issue in this case because it does not apply. But it cannot be clearer that estates that run afoul of IRC §2036 might be at risk under this theory of estate tax inclusion.

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CAREFUL PLANNING

Below are considerations and steps
we take to help clients avoid failed deathbed planning:

Avoid Deathbed Planning When Possible
The timing of the planning makes this a classic case of bad facts making bad law. All of the tax planning and transfers were completed within the week prior to the decedent's death, a mere seven days. The preferred approach would be to plan in advance so as to create a larger gap in time between the estate tax planning transactions and the death of the decedent. This means the planning should occur while the decedent is alive and well, not on his or her deathbed.

Be Able to Substantiate a Business Purpose
The family limited partnership in *Powell* lacked a legitimate business purpose. The family limited partnership only consisted of cash and securities, all owners were family members, and the general partners made no legitimate contribution for their interests. The decedent took back a 99 percent limited partnership interest for contributing $10 million and the decedent's sons took back a one percent general partnership interest for contributing unsecured promissory notes (i.e. nothing of real tangible value). Being able to demonstrate a business interest is important.23 Tax planners can help facilitate this by:

1. Encouraging the family limited partnership to be funded with a diverse set of assets. Property that requires upkeep and management—like rental property—can be ideal.

2. Recommending the general partner take out an interest larger than one percent of the entity. While this would be prudent to apply, the Court did not mention the division of ownership of the entity. This means that it could be interpreted to apply regardless of ownership division.

3. Requiring all contributions to be legitimate and of equivalent value to the amount of equity received for the contribution. An unsecured promissory note may not suffice. If the minority owners do not have capital of equivalent value to contribute, the promissory note should be secured, there should be set payment terms, appropriate rate of interest applied, and actual adherence to the repayment schedule by the notes contributor. Anything less will undermine the legitimacy of the promissory note.

4. Discussing having owners other than family, employees, or any other individual that can be seen as being controlled by the decedent or the decedent's family. This will likely be a very difficult sell to clients because their goal is to keep the wealth within the family unit and having outsiders involved will likely concern them. Including a charity as a beneficiary may help alleviate this concern and accomplish tax objectives.24 This setup provides a very important distinction from *Powell* in that the decedent and his or her family cannot control the liquidation.

Consider the Terms of the Partnership Agreement
In *Powell*, the partnership agreement gave the general partner complete control over timing of distributions and contained no terms limiting the owners' ability to dissolve the family limited partnership. The terms of the partnership agreement should be carefully considered, including any standard boilerplate language. This may be accomplished by having terms which limit distribution and termination so that a non-family member, who cannot be controlled by the decedent or decedent's family, must consent to either action.

This is a perfect opportunity to incorporate a non-family owner of the entity as previously suggested above. If, for example, the partnership agreement required all partners to consent to distribution or liquidation, and at least one partner was a non-family member and not subject to control, then a strong argument may be presented against gross estate inclusion because the power of the non-family member cannot be attributed to the decedent or the decedent's family. The decedent's ability to control the liquidation of the entity and therefore control who will possess or enjoy the assets is negated by using this technique.

Carefully Consider Overlapping Fiduciary Roles

It is also important to consider which individuals will serve in multiple fiduciary capacities. In *Powell*, the decedent's attorney-in-fact was also a general partner the family limited partnership, which he formed by exercise of his power as trustee of the decedent's trust. The individual served as attorney-in-fact, general partner, and trustee. This is problematic. How does one draw a line between the different fiduciary duties? Can a general partner act against the decedent's interest and, at the same time, comply with his fiduciary duty to the decedent under the power of attorney? The solution is simple: use different individuals to serve in different fiduciary capacities (and ideally not all of which are the decedent's family members).

Ensure that the Estate Plan is Coordinated

The final takeaway is the importance of a comprehensive review of the estate plan. The trust terms, the power of attorney, and the partnership agreement should each be carefully reviewed and crafted to permit accomplishing the decedent's goals while minimizing and reducing the exposure of estate or gift tax inclusion. An obvious mistake, like making a transfer that was not permitted under a power of attorney, as in *Powell*, could have easily been avoided with proper counsel. The Court's decision did not turn on this mistake, but it highlights the importance of proper review.

The more we can help distinguish your situation from that of *Powell*, the better chance you have of escaping a similar result.

Estate of Powell v. Commissioner, 148 T.C. No. 18 (2017)

REMEMBER

Noah built the ark before the rain began to fall.

WAITING FOR THE FLOOD COULD DROWN YOUR TAX PLANNING!

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Estate of Powell: Stranger Than Strangi and Partially Fiction
N. Todd Angkatavanich, James Dougherty, Eric Fischer

Practice Areas

ESTATE PLANNING

At The Andersen Firm we have planned for a vast array of estates ranging in size from a few hundred thousand dollars to a hundred million dollars and up, all the while realizing each specific case is different and requires specialized attention.

ESTATE SETTLEMENT & PROBATE

The process of settling an estate can be difficult and emotionally painful for the family and loved ones of the deceased. It is our goal at The Andersen Firm to ensure that the process be handled with compassion, expedience, professionalism, and expertise, while protecting the rights of all parties involved. If the circumstances surrounding a client's estate require probate, our attorneys offer extensive experience in handling the processes and legalities involved.

ASSET PROTECTION

For some, putting an Asset Protection Plan in place is advisable in order to attempt to remove the economic incentive to be sued and also to try and increase the ability to force an early settlement in the event a suit is filed.

LITIGATION

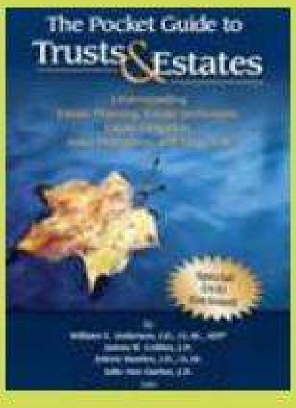
Our attorneys are skilled at handling cases involving estate and trust disputes, civil litigation, commercial litigation, and real estate litigation. Our attorneys draw on a thorough knowledge base of the specific procedures surrounding these issues. The Andersen Firm can efficiently take each case through to completion. Whether you are an individual or a business, defendant or plaintiff, our extensive experience affords our clients the benefit of our counsel.

REAL ESTATE

Our attorneys possess the expertise of being able to draft and review any contract relating to real estate, including but not limited to purchase and sale contracts and addenda, leases with options to purchase, stock purchase agreements, joint venture agreements, mergers and acquisitions, and business purchase agreements.

The Pocket Guide to Trusts and Estates

Bill Andersen and Joleen Searles with Erin Turner and Jerry Saresky have released their collaborative book ***The Pocket Guide to Trusts & Estates: Understanding Estate Planning, Estate Settlement, Estate Litigation and Asset Protection***.



COMMENTS: If you have questions about The Andersen Firm's practice areas, need assistance with continuing education, client seminars, would like to request a copy of The Pocket Guide, or have a question or suggestion about our website, Angela Hooper is our Director of Professional Alliances. Angela welcomes your calls and may be reached at 954.527.8807 or by email at AHooper@TheAndersenFirm.com.

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Thank you for taking
the time to review
this edition.
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Angela Hooper
Director of Professional Alliances
AHooper@TheAndersenFirm.com