Proskauer

newsletter

Wealth Management Update

February 2013

in this issue

A monthly report for wealth management professionals.

Edited by **Henry J. Leibowitz**
Contributor: **Jane C. Wang**

As part of our ongoing efforts to keep wealth management professionals informed of recent developments related to our practice area, we have summarized below some items we think would be of interest. Please let us know if you have any questions.

February Interest Rates for GRATs, Sales to Defective Grantor Trusts, Intra-Family Loans and Split Interest Charitable Trusts

The February § 7520 rate for use with estate planning techniques such as CRTs, CLTs, QPRTs and GRATs is 1.2%, which is a slight increase from January's rate of 1.0%. The applicable federal rate ("AFR") for use with a sale to a defective grantor trust, self-canceling installment note ("SCIN") or intra-family loan with a note of a 9-year duration (the mid-term rate, compounded annually) is 1.01%, which is up slightly from the January rate of 0.87%, but still relatively low. Remember that lower rates work best with GRATs, CLATs, sales to defective grantor trusts, private annuities, SCINs and intra-family loans. The combination of a low § 7520 rate and financial and real estate markets which remain undervalued presents a potentially rewarding opportunity to fund GRATs in February with depressed assets you expect to perform better in the relatively near future.

Clients also should continue to consider refinancing existing intra-family loans. The AFRs (based on annual compounding) used in connection with intra-family loans are 0.21% for loans with a term of 3 years or less, 1.01% for loans with a term of 9 years or less, and 2.52% for loans with a term longer than 9 years. Thus, for example, if a 9-year loan is made to a child and the child can invest the funds and obtain a return in excess of 1.01%, the child will be able to keep any returns over 1.01%. These same rates are used in connection with sales to defective grantor trusts.

IRS Issues Revenue Procedure 2013-15

In Revenue Procedure 2013-15, the IRS announced the 2013 inflation adjustments, including the income tax rate schedules, and other tax changes resulting from the American Taxpayer Relief Act of 2012 ("ATRA"). For 2013, the estate tax exemption is $5,250,000, which is an increase from $5,120,000 for 2012. Under ATRA, the estate tax exemption, lifetime gift tax exemption and GST exemption are "unified," and thus, the same amount.

As a reminder, the IRS previously released Revenue Procedure 2012-41, which provides that the annual exclusion for gifts made in 2013 is $14,000, which is an increase from $13,000 for 2012.

Private Letter Ruling 201245004

The IRS ruled that the surviving spouse could disclaim her interest in an Individual Retirement Account ("IRA") even though she had received distributions from the IRA prior to the disclaimer.

The decedent named his spouse as the beneficiary of his IRA. The decedent was receiving required minimum distributions from the IRA prior to his death.

The decedent died survived by his spouse. For two months after his death, the monthly IRA distributions were made and automatically deposited into the surviving spouse's bank account. After those payments were made, the monthly IRA distributions were cancelled. However, the amounts received by the surviving spouse exceeded the required minimum distributions for the year of the decedent's death.

The surviving spouse's attorney-in-fact exercised his authority under the durable power of Attorney and disclaimed the surviving spouse's interest in the balance of the IRA and a proportionate amount of income attributable to such balance.

The IRS ruled that the surviving spouse made a qualified disclaimer, despite accepting automatic distributions which exceeded the required minimum distribution. The IRS cited Revenue Ruling 2005-36, whereby it ruled that receipt of the required minimum distribution constitutes acceptance of that portion of the corpus of the IRA, plus the income attributable to that amount. However, if the beneficiary disclaims the remaining balance of the IRA, then the beneficiary's acceptance of the required minimum distribution does not preclude the beneficiary from making a qualified disclaimer with respect to the balance of the IRA. The IRS found that this case was similar to the one in Revenue Ruling 2005-36.

Estate of Nancy P. Young v. United States (D. Mass., No. 1:11-cv-11829-RWZ, 12/17/12)

In *Estate of Nancy P. Young v. United States,* the District Court upheld a late-filing penalty against an estate whose accountants advised it to file its estate tax return late, believing there would be no penalty since the full amount of the estate tax had been paid.

The decedent died in 2008. The estate submitted timely requests for extensions of time to file and to pay; both of which were granted. The estate paid the estate tax due prior to the extended payment deadline.

The estate was preparing the estate tax return during 2009, in the midst of the recession. The estate believed that the appraised values of its real estate holdings were substantially higher than fair market value and sought reevaluations.

As the extended estate tax return filing deadline approached, the estate had two options: (1) file the estate tax return with the appraised values, and then file a supplemental return later when the real estate holdings were sold; or (2) wait until the real estate holdings were sold, and then file one estate tax return after the filing deadline.

The estate's accountants believed that since the estate already had paid more than its eventual estate tax liability, there would be no penalty for filing late. Therefore, they advised the estate to file one estate tax return after the filing deadline, as one return (rather than two) would simplify the audit process.

The estate followed the accountants' advice and filed one estate tax return after the filing deadline. The IRS assessed the estate with late filing penalties and interest.

The estate argued that it had reasonable cause for filing late because it relied on expert tax advice.

The District Court found that there was not reasonable cause in this case. Here, the estate was fully aware that it legally was required to file the estate tax return by the applicable deadline. The advice that the estate relied on was that (a) there would be no penalty for late filing, and (b) the late filing would be better for the audit process. The District Court cited precedence which held that reliance is not reasonable cause when the taxpayer is advised that the return is due but that the taxpayer need not comply because no penalty would be imposed. In addition, the reliance is not a reasonable cause when the taxpayer decides that the desire to make the audit process easier is more important that his duty to comply with a known filing deadline.

The estate had an obligation to file a timely return with the best information that it had, and it cannot claim reasonable cause based on advice that it was necessary to wait for complete information before filing the return.

The Personal Planning Department at Proskauer is one of the largest private wealth management teams in the country and works with high net-worth individuals and families to design customized estate and wealth transfer plans, and with individuals and institutions to assist in the administration of trusts and estates.

If you have any questions regarding the matters discussed in this newsletter, please contact any of the lawyers listed below:

BOCA RATON

Albert W. Gortz
561.995.4700 — agortz@proskauer.com

George D. Karibjanian
561.995.4780 — gkaribjanian@proskauer.com

David Pratt
561.995.4777 — dpratt@proskauer.com

LOS ANGELES

Mitchell M. Gaswirth
310.284.5693 — mgaswirth@proskauer.com

Andrew M. Katzenstein
310.284.4553 — akatzenstein@proskauer.com

NEW YORK

Henry J. Leibowitz
212.969.3602 — hleibowitz@proskauer.com

Lisa M. Stern
212.969.3968 — lstern@proskauer.com

Philip M. Susswein
212.969.3625 — psusswein@proskauer.com

Ivan Taback
212.969.3662 — itaback@proskauer.com

Jay D. Waxenberg
212.969.3606 — jwaxenberg@proskauer.com

Beijing | Boca Raton | Boston | Chicago | Hong Kong | London | Los Angeles | New Orleans | New York | Newark | Paris
São Paulo | Washington, DC

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