Proskauer

Wealth Management Update

March 2016

Untitled Document **March Interest Rates for GRATs, Sales to Defective Grantor Trusts, Intra-Family Loans and Split Interest Charitable Trusts**

The March § 7520 rate for use with estate planning techniques such as CRTs, CLTs, QPRTs and GRATs is 1.8%, which is a decrease from January's and February's rate of 2.2%. The March 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 having a duration of 3-9 years (the mid-term rate, compounded semiannually) is 1.47%, down from 1.81%.

The relatively low § 7520 rate and AFRs continue to present potentially rewarding opportunities to fund GRATs in March with depressed assets that are expected to perform better in the coming years.

The AFRs (based on semiannual compounding) used in connection with intra-family loans are 0.65% for loans with a term of 3 years or less, 1.47% for loans with a term between 3 and 9 years, and 2.32% for loans with a term of 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 1.47%, the child will be able to keep any returns over 1.47%. These same rates are used in connection with sales to defective grantor trusts.

IRS Withdraws Proposed Regulations Dealing with Substantiating Charitable Deductions under IRC § 170(f)(8)(D)

IRC § 170(f)(8)(D) requires that taxpayers substantiate charitable deductions of $250 or more by a "contemporaneous written acknowledgment" of the charitable contribution by the donee organization. The "contemporaneous written acknowledgment" must meet certain requirements. On September 16, 2015, the IRS proposed regulations that would have created a form in which the charity had the option of completing and filing with the IRS in the absence of the contemporaneous written acknowledgment.

This new form required charities to report the donor's name, address, and taxpayer identification number to the IRS. After receiving many objections about collecting the donor's taxpayer information and reporting it to the IRS, the IRS withdrew the regulation on January 8, 2016.

The Tax Court prevented taxpayer from asserting collateral estoppel against the IRS and relying on a state court decision in a lawsuit between her and her ex-boyfriend in *Blagaich v. Commissioner*, TC Memo 2016-2 (January 4, 2016)

While Diane Blagaich and Lewis Burns were in a relationship, Lewis gave Diane $300,000 and a corvette. They also entered into an agreement to formalize their relationship and as part of that agreement, Lewis gave Diane an additional $400,000. Months after they executed the agreement, Lewis found out that Diane was cheating on him which subsequently ended their relationship.

Lewis sued Diane in state court for nullification of the agreement and for the return of the money and corvette. The state court ruled that Diane had to pay Lewis back $400,000 (which was connected to the agreement) but the corvette and other cash were treated as gifts from Lewis to Diane.

Lewis then filed a Form 1099-MISC with the IRS reporting that the money he gave to Diane was income to her. The IRS audited Diane's income tax return and asserted that the $700,000 and the corvette should be treated as taxable income to Diane. Diane argued that the corvette and the $300,000 should not be treated as income since the state court held that such items were gifts. Diane further argued that the doctrine of rescission should apply to the remaining $400,000 because the state court required her to pay such amount back to Lewis. Diane's motion for summary adjudication that the IRS is collaterally estopped from litigating the state court's gift finding was denied because Diane failed to demonstrate that the IRS was in privity with a party to the State court action.

Tax Court held that taxpayers were not entitled to a charitable income tax deduction for a donation of a conservation easement because they failed to include a qualified appraisal with their return in *Gemperle v. Commissioner*, T.C. Memo 2016-1 (January 4, 2016)

In 2007, David and Kathryn Gemperle granted to a qualified donee a facade easement on their Chicago residence, which constituted a certified historic structure in a historic district, so that the easement was eligible for classification as a "qualified conservation contribution" within the meaning of I.R.C. 170(f)(3)(B)(iii) and (h)(1).

The Gemperle's obtained an appraisal from an appraiser that valued the easement at $108,000. However, they did not file the appraisal with their income tax returns when claiming the charitable income tax deduction on their 2007 and (as a carryover) 2008 returns.

During trial, the court excluded the appraisal as evidence because the Gemperles failed to list the appraiser as a witness. The IRS argued that the deduction should not be allowed because: (1) the absence of a qualified appraisal; (2) the fact that the façade easement or restriction was neither granted or protected by section 170(h)(5)(A); (3) the Gemperle's failure to include a copy of a qualified appraisal and a completed appraisal summary with the return and (4) the Gemperle's failure to prove that the contribution decreased the value of the house by $108,000. Without analyzing the other issues, the Tax Court denied the Gemperle's charitable income tax deduction because they did not include a qualified appraisal with their income tax returns and also held that an accuracy related penalty also applied.

Related Professionals

- **Jay D. Waxenberg**
  Partner
- **Henry J. Leibowitz**
  Partner
- **Albert W. Gortz**