Proskauer

Wealth Management Update

January 2024

January 2024 Interest Rates for GRATs, Sales to Defective Grantor Trusts, Intra-Family Loans and Split Interest Charitable Trusts

The January 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 annually) is 4.37%, down from 4.82% in December 2023.

The January 2024 Section 7520 rate for use with estate planning techniques such as CRTs, CLTs, QPRTs and GRATs is 5.20%, down from the 5.80% Section 7520 rate in December 2023.

The AFRs (based on annual compounding) used in connection with intra-family loans are 5.00% for loans with a term of 3 years or less, 4.37% for loans with a term between 3 and 9 years, and 4.54% for loans with a term of longer than 9 years.

REG-142338-07 – Proposed Regulations Related to Donor Advised Funds

On November 13, 2023, the Department of the Treasury and IRS released Proposed Regulation REG-142338-07 under Section 4966; providing guidance related to numerous open-issues with respect to certain tax rules relating to donor advised funds "(DAFs").

Pursuant to §4966(d)(2)(A), a DAF is defined generally as a fund or account (1) that is separately identified by reference to contributions of a **donor or donors**, (2) owned and controlled by a **sponsoring organization**, and (3) with respect to which a donor (or person appointed or designated by such donor) has, or reasonably expects to have, **advisory privileges** with respect to the distribution or investment of amounts held in the fund or account by reason of the donor's status as a donor.

Under the proposed regulations, the definition of a DAF is consistent with the definition under the statute (the same three elements), however, the proposed regulations provide key definitions with respect to specific terms under the Statute.

*Element #1: a fund that is **separately identified** by reference to contributions of a **donor or donors**.*

Separately Identified: The proposed regulations provide that a fund or account is separately identified if the sponsoring organization maintains a formal record of contributions to the fund relating to a donor or donors (regardless of whether the sponsoring organization commingles the assets attributed to the fund with other assets of the sponsoring organization).

If the sponsoring organization does not maintain a formal record, then whether a fund or account is separately identified would be based on all the facts and circumstances, including but not limited to whether: (1) the fund or account balance reflects items such as contributions, expenses and performance; (2) the fund or account is named after the donors; (3) the sponsoring organization refers to the account as a DAF; (4) the sponsoring organization has an agreement or understanding with the donors that such account is a DAF; and (5) the donors regularly receive a statement from the sponsoring organization.

Donor: The proposed regulations broadly define a Donor as any person described in 7701(a)(1) that contributes to a fund or account of a sponsoring organization. However, the proposed regulations specifically exclude public charities defined in 509(a) and any governmental unit described in 170(c)(1). Note: Private foundations and disqualified supporting organizations are not excluded from the definition of a donor since they could use a DAF to circumvent the payout and other applicable requirements.

*Element #2: a fund that is owned or controlled by a **sponsoring organization***. The definition of a sponsoring organization is consistent with §4966(d)(1), specifically, an organization described in §170(c), other than a private foundation, that maintains one or more DAFs.

*Element #3: a fund under which at least one donor or donor-advisor has **advisory privileges**.*

Advisory Privileges: In general, the existence of advisory privileges is based on all facts and circumstances, but it is presumed that the donor always has such privileges (even if no advice is given).

The proposed regulations provide that advisory privileges exist when: (i) the sponsoring organization allows a donor or donor-advisor to provide nonbinding recommendations regarding distributions or investments of a fund; (ii) a written agreement states that a donor or donor-advisor has advisory privileges; (iii) a written document or marketing material provided to the donor or donor-advisor indicates that such donor or donor-advisor may provide advice to the sponsoring organization; or (iv) the sponsoring organization generally solicits advice from a donor or donor-advisor regarding distributions or investment of a DAF's assets.

Donor-Advisor: Defined by the proposed regulations as a person appointed or designated by a donor to have advisory privileges regarding the distribution or investment of assets held in a DAF. If a donor-advisor delegates any of the donor-advisor's advisor privileges to another person, such person would also be a donor-advisor.

Potential Issue related to Investment Advisors: Is a donor's personal investment advisor deemed a "donor-advisor?" Pursuant to the proposed regulations:

- An investment advisor will **not** be deemed a donor-advisor if he or she:
  - Serves the supporting organization as a whole; or
  - Is recommended by the donor to serve on a committee (of more than 3) of the sponsoring organization that advises as to distributions
- However, an investment advisor will be deemed a donor-advisor if he or she manages the investments of, or provides investment advice with respect to, both assets maintained in a DAF and the personal assets of a donor to that DAF while serving in such dual capacity. **This provision, if finalized may have important consequences for fee structures used by supporting organizations since payments from a DAF to an investment advisor who is considered a donor-advisor will be deemed a taxable distribution under §4966**. The IRS is requesting additional comments on this potential issue and is still under consideration.

Exceptions to the Definition of a DAF Under the Proposed Regulations:

- A multiple donor fund or account will not be a DAF if no donor or donor-advisor has, or reasonably expects to have, advisory privileges.
- An account or fund that is established to make distributions solely to a single public charity or governmental entity for public purposes is not considered a DAF.
- A DAF does not include a fund that exclusively makes grants for certain scholarship funds related to travel, study or other similar purposes.
- Disaster relief funds are not DAFs, provided they comply with other requirements.

Applicability Date: The proposed regulations will apply to taxable years ending on or after the date on which final regulations are published in the Federal Register.

Eileen Gonzalez et al v. Luis O. Chiong et al (Sep. 19, 2023)

Miami Circuit Court enters significant judgment for liability related to ownership of golf cart.

Eileen Gonzalez and Luis Chiong and their families were neighbors in a Miami suburb. The families were good friends and had many social interactions. Luis owned a golf cart which he constantly allowed to be driven and used by other people and Eileen's minor children were often passengers on this specific golf cart.

Luis' step-niece, Zabryna Acuna, was visiting for July 4th weekend in 2016. Zabryna (age 16 at that time) visited often and during each visit, she had permission to drive the golf cart. On July 4, 2016, Zabryna took the golf cart for a drive with Luis' son and Eileen's minor children as passengers.

While driving on a public street, Zabryna ran a stop sign and collided with another car which caused all of the passenger to be ejected from the golf cart. Every passenger suffered injuries, however, Eileen's son, Devin, suffered a particularly catastrophic brain injury. This led to an eventual lawsuit.

The Circuit Court ruled that Luis owed the plaintiffs a duty of reasonable care which he breached and was negligent in entrusting the golf cart to his niece who negligently operated it causing the crash and injuries at issue. The Court further held that pursuant to the Florida Supreme Court, a golf cart is a dangerous instrumentality, and the dangerous instrumentality doctrine imposes vicarious liability upon the owner of a motor vehicle who voluntarily entrusts it to an individual whose negligent operation if it causes damage to another.

Ultimately, the Court awarded a total judgment of $50,100,000 (approximately $46,100,000 to Devin and approximately $4,000,000 to his parents).

IR-2023-185 (Oct 5, 2023)

The IRS warns of Art Valuation Schemes (Oct 5, 2023).

The IRS essentially issued a warning to taxpayers that they will be increasing investigations and taxpayer audits for incorrect or aggressively creative deductions with respect to donations of art. Additionally, the IRS is paying attention to art promoters who are involved in such schemes.

The IRS is warning taxpayers to exercise caution when approached by art promoters who are commonly attempting to facilitate the following specific scheme wherein: (i) a taxpayer is encouraged to purchase art at a significantly discounted price; (ii) the taxpayer is then advised to hold the art for a period of at least one year; and (iii) the taxpayer subsequently donates the art to a charity (often times a charity arranged by the promoter) and claim a tax deduction at an inflated market value, often significantly more than the original purchase price.

This increased scrutiny has led to over 60 completed audits with many more in process and has led to more than $5,000,000 in additional tax.

The IRS reminds taxpayers that they are ultimately responsible for the accuracy of the information reported on their tax return regardless of whether they were enticed by an outside promoter. Therefore, the IRS has provided the following red flags with respect to the purchase of artwork: (i) taxpayers should be wary of buying multiple works by the same artist that have little to no market value outside of what a promoter is advertising; and (ii) when the appraisal coordinated by a promoter fails to adequately describe the artwork (such rarity, age, quality, condition, stature of the artist, etc.).

Within the Notice, the IRS details the tax reporting requirements for donations of art. Specifically, whenever a taxpayer intends to claim a charitable contribution deduction of over $20,000 for an art donation, they must provide the following: (i) the name and address of the charitable organization that received it; (ii) the date and location of the contribution; (iii) a detailed description of the donated art; (iv) a contemporaneous written acknowledgement of the contribution form the charitable organization; (v) completed Form 8283, Noncash Charitable Contribution, Section A and B including signatures of the qualified appraiser and done; and (vi) attach a copy of the qualified appraisal to the tax return. They may also be asked to provide a high-resolution photo or digital image.

New York Public Health Law amended to permit remote witnesses for health care proxies (Nov 17, 2023)

An amendment to Section 2981 of New York Public Health Law was signed into law by the governor on November 17, 2023.

Section 2981 was amended to add a new subdivision 2-a, as follows:

2-A. Alternate procedure for witnessing health care proxies. Witnessing a health care proxy under this section may be done using audio-video technology, for either or both witnesses, provided that the following conditions are met:

1. The principal, if not personally known to a remote witness, shall display valid photographic identification to the remote witness during the audio-video conference;
2. The audio-video conference shall allow for direction interaction between the principal and any remote witness;
3. Any remote witness shall receive a legible copy of the health care proxy, which shall be transmitted via facsimile or electronic means, within 24 hours of the proxy being signed by the principal during the conference; and
4. The remote witness shall sign the transmitted copy of the proxy and return it to the principal.

Small Business Succession Planning Act Introduced (Oct 12, 2023)

On October 12, 2023, the Small Business Succession Planning Act was introduced to provide businesses with resources to plan successions, including a one-time $250 credit to create a business succession plan and an additional one-time $250 tax credit when the plan is executed.

Under the proposed Bill, the SBA will provide a “toolkit” to assist **small business concerns** in establishing a business succession plan, including:

1. Training resource partners on the toolkit;
2. Educating small business concerns about the program;
3. Ensuring that each SBA district office has an employee with the specific responsibility of providing counseling to small business concerns on the use of such toolkit; and
4. Hold workshops or events on business succession planning.

Pursuant to the proposed Act, the following credits would be available:

1. $250 for the first taxable year during which the SBA certifies that the taxpayer has: (a) established a business succession plan; (b) is a small business concern at that time; and (c) does not provide for substantially all of the interests or assets to be acquire by one or more entities that are not a small business concern.
2. An additional $250 for the first taxable year which the SBA certifies that the taxpayer has successfully completed the items described above.

Look-back Rule: If substantially all of the equity interests in business are acquired by an entity that is not a small business concern within three-years of establishment of a business succession plan or completion of such responsibilities (as the case may be) the credits will be subject to recapture.

Small Business Concern (defined under Section 3 of the Small Business Act): A business entity that (a) is legal entity that is independently owned and operated; and (b) is not dominant in its field of operation and does not exceed the relevant small business size standard (subject to standards and number of employees provided by the North American Industry Classification System).

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