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NOTICE: Although audio tapes of all of the substantive session at the Miami Institute currently are only made available to Institute registrants for purchase, the entire proceeding of the Institute, other than the afternoon special sessions, are published annually by Lexis/Nexis. For further information, go to their Web site at http://www.lexisnexis.com/productsandservices. The text of these proceedings is also available on CD ROM from Authority On-Demand by LexisNexis Matthew Bender. For further information, contact your sales representative, or call (800) 833-9844, or fax (518) 487-3584, or go to http://www.bender.com, or write to Matthew Bender & Co., Inc., Attn: Order Fulfillment Dept.,1275 Broadway, Albany, NY 12204

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As we have done in January for the last twenty one years, and again with the permission of the University of Miami School of Law Center for Continuing Legal Education, we will be posting daily Reports to this list containing highlights of the proceedings of the 52nd Annual Philip E. Heckerling Institute on Estate Planning that is being held on January 22-26, 2018 at the Orlando World Center Marriott Resort and Convention Center in Florida. A complete listing of the proceedings and the Institute's 2018 brochure are available at www.law.miami.edu/heckering. **Introduction Part 1** issued on 1/11/18 covered the Institute Opening Reception, its Scope, the Faculty, the Advisory Committee, the Sponsors and the Vendors, plus general information at the end about the Institute. **Introduction Part 2** issued on 1/12/18 contained a complete listing of all of the proceedings of this Institute. This **Report** continues our coverage of the proceedings.

We also will be posting the full text of each of these Reports on the ABA RPTE Section's Heckerling Reports Website, as we have since the 2000 Institute. The Reports from 2000 to 2017 can now be found at URL http://www.americanbar.org/groups/real_property_trust_estate/events_cle/heckerling.htm. In addition, each Report from 2006 to date can also be accessed at any time from the ABA-PTL Discussion List's Web-based Archive that now only goes as far back as January of 2006 and is located at URL http://mail.americanbar.org/archives/aba-ptl.html.

**Announcement:** In Report #5 we referred to the new Leimberg Analyzer suite of web-based products designed for use with new IRC Section 199A. ACTEC Fellow Daniel Evans has recently announced he has created an on-line calculator that shows the impact of the new Tax Cuts and Jobs Act by calculating the federal income tax for both individuals and estates and trusts under both the old law and the new law. For more information, go to http://www.webcalculators.com. Also

**Summary:** This Report #9 contains our coverage of the Thursday morning General Sessions, those being on community property, the Uniform Directed Trust Act, planned giving, and planning for real estate investors.

The next Report #10 will begin our coverage of the Thursday afternoon Special Sessions.

**THURSDAY, JANUARY 25**

9:00-9:50

**Stranger in a Strange Land: Dealing with Foreign and Domestic Community Property Issues in Your State**
People are becoming increasingly peripatetic in today’s mobile society. Sometimes people from different countries marry. Sometimes couples change domiciles. Sometimes individuals have property in more than one country. And sometimes individuals have close family members, even spouses, who live in different countries. This program consider the issues presented when an individual from a community property jurisdiction has connections to a common law property jurisdiction. As usual, this report will cover only the significant highlights of this session.

I. Introduction

The presenter started this presentation with a general synopsis of why community property issues exist and why estate planners do not do a good job of addressing and tracking the issues.

Real estate and the US stock market are attractive investments to people outside of the US. Locally, people are moving more within the US (for example, from high tax to low tax states) which may result in community property to non-community property states or some combination.

There should be conflicts every time an estate plan crosses state lines, but estate planners often don’t think about the issues because the states don’t have walls or noticeable changes in language or other barriers, thus border crossing isn’t noticeable.

The presenter then described the different types of community property systems within and outside of the US.

II. Types of Community Property

Community property is based on one of three systems, UK, Spanish or French systems of property, and each system has different considerations and treatments of property interests.

Even within the US there are different types of community property. There are common law community property states and elective opt-in states. Although only 15% of the states are community property states, those states include California and Texas which means that there is a high population of US residents with community property.

Universal Community is from the old French civil code and provides that upon marriage all of property (even premarital property) is community property. Community of After-acquired property is the typical community property in the States and is also applies to most of Europe and South America. Community on Dissolution is followed in much of
Central America and provides that title controls until the marriage ends. Marriage can end by death or divorce.

The presenter then explained how to determine what law controls the community property issues. The Restatement of Property presumes the character of property stays the same unless there is an agreement to the contrary or it falls into an exemption. The Uniform Disposition of Community Property Rights as Death Act only applies to death transfers; it doesn’t address lifetime transfers. Often to determine which law applies there must be a conflict of laws analysis. This analysis may start with when and where the property interest was acquired, which typically turns on the marriage of the spouses. When determining which law governs the marriage, you have to determine if it is the law of the place of celebration, the domicile at the time of the marriage or the current domicile.

If dealing with international law, you also have to determine whether the property interest in question is similar to a real property interest or a personal property, tangible or intangible interest. Under US law real property interests are generally governed by the law of the location of the property and personal property interests are governed by domiciliary law. Civil law countries do not have real and personal property interests; instead they have movable and immovable property interests. The presenter offered the example of a mortgage being personal property subject to domiciliary law in the US, but in France a mortgage secured by a property interest is an immovable interest that would governed under French law.

III. Tax considerations

Historically, income from community property is taxed equally between the two spouses. Sec 879 provides exceptions for this division of taxable income such that earned community property income typically belongs to the earner and only passive investment income is divided between the spouses.

As for transfer tax considerations, only one-half of the community property is included in the first to die spouse’s estate, so that is only a marital deduction on one-half of the property. No tracing issues regarding the amount each spouse contributed, and the property receives a full basis adjustment at the death of each spouse.

There are some negative issues with community property. Gifting requires spousal consent because the donor spouse does not have sole ownership of property. Divorce typically ends up in a 50:50 split. With respect to transfer taxes, the estate can only deduct 50% of expenses. It may be harder to satisfy the 35% test for closely held business interests for a Sec. 6166 election. Cannot use community property to create GRATs, QPRTS, and term interest with remainder to spouse because this could result in inclusion in the spouse’s estate.

IV Conclusion
The presenter wrapped up this presentation with a few suggested techniques for preserving community property. An accurate accounting and tracing of the couples property and history of ownership is desirable. The accounting should identify premarital and potentially separate property from property acquired during marriage.

The couple could use joint revocable trusts to keep their property interests separate. Assets should not be retitled if the couple moves. A community property agreement may be used to identify community property. The presenter suggested that if a community property agreement is used, it should identify the portion of premarital property that will be treated as community and the portion of marriage property that will be treated as community. It should provide that survivorship rights vest on death and that the terms of the agreement do not apply to divorce.

9:50-10:40

**Trust Administration Takes a Village? The New Uniform Directed Trust Act Paves the Way for Creative and Thoughtful Divided Trusteeship [TRU]**

Presenter: Robert H. Sitkoff
Reporter: Joanne Hindel

The duties and liabilities of directed trustees and trust directors remain a source of confusion. This session canvassed the new Uniform Directed Trust Act, explored how the Act simplifies drafting and administering directed trusts, and highlighted some of the most common and helpful uses of directed trusts in the current planning environment. Here are some of the more significant highlights from this session.

**Part I – Introduction**

Robert Sitkoff served as the chairman of the Uniform Law Commission committee that promulgated the Uniform Directed Trust Act. He started his presentation by stating that directed trusts have remade the field of trust administration.

He said that the fundamental policy question addressed in the Act (UDTA) and arising from the emergence of directed trusts is how the law of trusteeship should be divided among a directed trustee and trust director.

His presentation covered the four areas of improvement developed with UDTA. The first concerns the fiduciary duties of a trust director and a directed trustee. The second addresses the non-fiduciary matters in the subsidiary law of trust administration. The third innovation of the UDTA is to reconcile the law of co-trusteeship with the broad settlor autonomy recognized with respect to a directed trust. The fourth and final innovation is a carefully thought-out system of exclusions that preserves existing law and settlor autonomy with respect to a host of issues that are collateral to the emergence of directed trusts.

**Part II – Scope and Exclusions**
Robert started by saying that understanding the UDTA begins by considering the statute’s scope. The purpose of the UDTA is to promote settlor autonomy by validating directed trusts. The scope of the statute depends largely on which powers qualify as “powers of direction.”

The term "power of direction" includes both a power to direct a trustee to act as well as a power in a director to act on his or her own. The broad definition also covers powers to veto to consent in advance to a trustee’s actions or a power to release a trustee from liability for prior conduct.

The UDTA Committee addressed the issue of enabling versus off-the-rack statutes. Enabling statutes authorize creation of a directed trust by validating terms of a trust that grant to a trust director a power of direction, but they do not prescribe any specific powers by default. Off-the-rack statutes provide for one or more statutory forms of directed trust, with particular sets of powers given to a type or kind of trust director by default. The drafting committee opted for an enabling structure.

There are however exclusions with UDTA where persons holding powers do not come within the definition of trust directors such as nonfiduciary powers of appointment, the power to appoint or remove a trustee or trust director; the power of a settlor over a revocable trust and powers of a beneficiary if exercised solely in the interest of that beneficiary.

**Part III – Allocating Fiduciary Responsibility in a Directed Trust**

The core of the UDTA’s contribution is the act’s allocation in §§ 8 through 11 of fiduciary responsibility among trust directors and directed trustees. The UDTA’s basic approach is to place the primary fiduciary responsibility for a power on the person who holds the power. Thus, if a power belongs to a trust director, then the primary fiduciary responsibility for that power belongs to the director, rather than the directed trustee who merely facilitates the director’s exercise of the power.

The UDTA thus relieves a directed trustee from the full fiduciary duties of a unitary trusteeship, and leaves a directed trustee with only a reduced duty to avoid “willful misconduct” in deciding whether to comply with a director’s directions.

The basic rule of § 8(a) is that “a trust director has the same fiduciary duty and liability” as a “trustee in a like position and under similar circumstances.” A settlor could construct a trust director’s power to be springing.

UDTA § 9(a) says that “the trustee is not liable” for taking “reasonable action to comply with a trust director’s exercise or nonexercise of a power of direction” except as provided in § 9(b). Section 9(b), in turn, provides that a “directed trustee must not comply with a trust director’s exercise or nonexercise of a power of direction ... to the extent that by complying the trustee would engage in willful misconduct.” The UDTA thus generally requires a trustee to comply with a director’s direction and relieves the trustee from liability for so doing, unless by complying with the direction the trustee would engage in willful misconduct, in which case the trustee has a duty not to comply.

**Part IV- Cotrusteeship under the UDTA**

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The UDTA preserves the distinction between a directed trust and a cotrusteeship. Under the UDTA, a “power of direction” cannot be held by a person while the person is serving as a trustee, nor can a person be a “trust director” while the person is serving as a trustee. In consequence, a cotrustee with a power to direct another cotrustee is not a trust director, and the other cotrustee is not a directed trustee. Instead, relations between multiple trustees remain subject by default to the law of cotrusteeship.

Under the UDTA, however, the terms of a trust can opt out of the default law of cotrusteeship, and instead subject cotrustees to the more permissive rules of a directed trusteeship as prescribed by §§ 9, 10, and 11. The drafting committee reasoned that, because a “settlor could choose the more permissive rules of a directed trusteeship by labeling one of the cotrustees as a trust director and another as a directed trustee,” there was little reason not to allow the settlor to apply “the fiduciary rules of [a directed trust] to a cotrusteeship.”

Conclusion

Under the Uniform Directed Trust Act, a power over a trust held by a nontrustee is called a “power of direction.” The holder of a power of direction is called a “trust director.” A trustee that is subject to a power of direction is called a “directed trustee.” The main contribution of the act is to address the many complications created by giving a power of direction to a trust director, including the fiduciary duty of a trust director and the fiduciary duty of a directed trustee.

What’s a Donor to Do? Planned Giving in a Changing Tax Landscape [CHR]
Presenter: Michele A.W. McKinnon
Reporter: Joanne Hindel

This program covered the manner in which donors should approach planned giving under uncertain or new tax laws as well as changes affecting the charitable deduction and their impact on planned giving techniques. It also explored other reasons donors make gifts and whether these considerations are likely to outweigh the new tax limitations in a donor’s gift considerations. This report covers the more significant portions of this session.

Part I – Introduction

Michele started her presentation by saying that millennials are going to change the world. She indicated that the new tax Act will not really change the way donors approach their philanthropy and donors give because they think their gift can make a difference – this resonates with the younger generation.

Part II – Current Income Tax Charitable Deduction Rules
Michele discussed the current income tax charitable deduction rules by reminding the audience that donors must itemize deductions in order to be entitled to an income tax charitable deduction for contributions to qualified charitable organizations. She said that under the new law a donor is generally entitled to deduct the full amount of the contribution up to 60% of the donor’s contribution base for a gift of cash. She also reviewed the top income tax rate for individuals under the new Act ($500,000 at 37%) and for families ($600,000 at 37%).

**Part III – Effects of Tax Reform and Economic Factors on Charitable Giving**

Michele then discussed what effect, if any, Tax Reform has had on charitable giving and determined that basically donors will still want to make charitable gifts. She said that current market conditions should favor charitable giving and in particular tax efficient charitable giving through the use of appreciated property gifts. She also indicated that perceived and real cuts in government funding for certain programs and activities may be a motivating factor for some individuals to increase charitable giving as social needs increase.

Michele discussed why donors engage in philanthropy and said that while many donors are not able to use the income tax charitable deduction due to percentage limitations or other reasons they are still giving. She also reviewed a 2016 U.S. Trust study of high net worth philanthropy which shows that 28% of high net worth individuals plan to increase their giving in the next three years. This same study also revealed that 33% of high net worth individuals participate in impact investing and 34% of these do this in place of some of their charitable giving. She said that the greatest challenge faced by wealthy donors is identifying causes they care about and where to donate. Other reasons donors give include religious reasons, appreciation for a particular organization such as a hospital or college, emotional connection with an organization’s story and mission and in order to share good fortune or give back to the community.

**Part III – Use of traditional planned giving techniques in current tax and economic environment**

Michele concluded her presentation by reviewing some traditional planned giving techniques including gift annuities. She said that in periods of low interest rates, many donors favor the security of fixed payments offered by a charitable gift annuity as well as the simplicity of establishing a gift annuity. She also discussed the gift or a remainder interest in a personal residence or farm and said that these are enhanced by a lower section 7520 rate.

She said that while charitable remainder trusts remain attractive for donors who wish to avoid capital gains on appreciated property, particularly for those facing an income realization event, the low interest rate environment will require the exercise of caution.

**Conclusion**

Michele reiterated her initial emphasis that donors are motivated by more than just tax benefits and estate planners should be having the right conversation with their philanthropically motivated clients.
Dishing the Dirt on Planning for Real Estate Investors

[CHB]
Presenter: Farhad Aghdami
Reporter: Kimon Karas

This program focused on the income tax and wealth transfer tax planning opportunities (and pitfalls) associated with planning for real estate investors, including a discussion of non-tax considerations and obstacles, such as obtaining third-party consents. The program also explored valuation discount planning, freeze, and leveraging strategies for specific types of assets and ownership structures typically found in real estate deals. The report on this session covers the significant details.

Real estate for the owner generates income, depreciation deductions, cash flow, if managed by a professional the losses generated are deductible, through refinancing transactions provide a way for the owner to access appreciation through cash distributions, and when the owner dies he receives a basis adjustment in the asset at death. In today’s environment with high exemptions consider whether a gift with a carryover basis makes sense. Steve Akers has noted that a gift of a $1M asset with 0 basis would have to appreciate to approximately $2.47M (247% of current value) in order for the estate tax savings on future appreciation to start to offset the loss of basis step up for high bracket taxpayers. If real estate is in a valuation discount vehicle, consider unwinding it to position for a basis adjustment.

Valuation issues germane to real estate include the following:

1. Lack of marketability.
2. Lack of control.
3. Fractionalization. Discount applied to ownership of an undivided interest. Partition is the only remedy. A co-owner has the right to use and possess the property so long as interests of other owners are not adversely impacted. See, Estate of Williams, T.C. Memo 1998-59, (court allowed a 44% discount for undivided ½ interest in timberland).
4. Market absorption where seller is forced to sell a large block at one time.
5. When structuring ownership consider discount planning at the outset. For example if client owns both a general and limited partnership interest, for valuation purposes the ownerships will be aggregated and impact the size of the discount.

Valuation discount planning generally includes entity structures such as LLCs and partnerships. See Pierre, where transfers of interests in a single member LLC were treated by the Tax Court as the transfer of LLC interests and not the proportionate interest of the underlying LLC interests. See also, Rev. Rul. 2004-77, where IRS held that where an eligible entity has two owners under local law, but one of the owners is, for federal tax purposes, a separate business entity. See also, Tyler v. Commissioner, T.C. Memo 1998-65, (court allowed a 50% discount for an undivided ½ interest in timberland and held that as a limited partner, the partner was not entitled to participate in net income and losses of the partnership).
purposes, as a disregarded entity, the eligible entity cannot be classified as a partnership and is disregarded as an entity separate from its owner. If the client has a property with a negative capital balance an alternative is to transfer the property to a grantor trust.

Real estate entity should avoid the litany of IRS challenges to LLC or limited partnership planning due to the significant non-tax purposes for creating a real estate entity. If the client is engaging in gift transfer planning, make certain in the gift context to adequately disclose the gift. Generally valuation for the real estate investor is commonly based on appraisals required for loans. If there is a question of value consider using defined value clause or Wandry clause.

Common techniques a real estate investor may use in the family context.

1. Make an outright gift of interest. Easy to accomplish, shifts income and value. Watch Hackl issue if underlying property is not income producing. Consider in that context of adding a put right with the transfer; although that put right will sacrifice some valuation discount.

2. Make a loan to children to give them cash to invest in the entity.

3. Alternatively children borrow from outside 3rd party with parent guarantee of debt obligation. Case law has held that guaranty is not a gift. Service issued a PLR that was later withdrawn, that held a parent’s guaranty of a child’s debt was a gift. The issue of the tax treatment of guarantees is on the 2017-2018 IRS Priority Guidance Plan.

4. Sale to an intentionally defective grantor trust under the authority of Rev. Rule 85-13. Under Rev. Rule 2004-64, grantor’s payment of income tax is not a gift to the trust. Typical arrangement is to provide trust with a 10% seed funding. Trust utilizes cash flow to repay the note. The grantor obtains all of the income tax benefits from the trust. The downside is that there is no basis adjustment. That can be addressed with a substitution power whereby grantor can substitute high basis assets for low basis assets. There is very little by way of case law on this technique. The two cases are Karmazin and Woebling that were settled without addressing the effectiveness of the technique.

5. In order to address the grantor dying with the note, consider structuring the transaction with the grantor retaining either a SCIN or private annuity. Generally these structures will require a risk premium. Estate of Davidson, T.C. No. 13748-13, involved a SCIN, (where IRS argued transfers to SCINs were made based on an unrealistic life expectancy) but the case was resolved by stipulated decision.

Other techniques but not favored by the presenter include a GRAT (creates valuation challenges plus real estate is generally a long term play and GRATs are usually short term to address mortality risk) and BDIT. Another technique that could be used, but does not seem to be that popular which would make sense in the real estate environment is the preferred partnership complying with Section 2701.

Transactions one may wish to consider with a personal residence.
1. Fractionalization, but watch if converting property that qualifies as a tenancy by the entireties ownership that would be creditor protected.

2. Use of LLCs to purchase for privacy purposes

3. Use of residence, vacation home by a child opens up issue of gift. If child is living in a residence owned by parent, consider fractionalizing giving the child a 1% or greater interest. As a tenant in common the child has occupancy rights to the property.

4. Transfer property to a trust for the benefit of the spouse. The transferor spouse, as spouse would have the right to use and occupancy. However, if the beneficiary spouse dies, the donor spouse can no longer reside there rent free. See Rev. Rule 70-155.

5. QPRT, generally better when interest rates are high.

6. Sale/leaseback with a grantor trust. Technique is the sale of residence to a defective grantor trust in exchange for note, followed by a leaseback of the residence for fair market rent.

Considerations as to how a real estate investor will pay estate taxes. Generally real estate owners will not prefer either Sections 6166 or 6161. Problem with Section 6166 is IRS lien that will impact existing credit facilities. Alternative consider a Graegin loan. Most efficient may be to acquire life insurance.

In addition to tax issues with the real estate investor do not overlook non tax issues. Make sure one follows the underlying entity governing documents, i.e. do documents allow transfers, what are transfer requirements. Follow bank and loan agreements where transfer of any size may require advance consent of the lender. A transfer without lender consent may trigger a “bad boy clause”, where the transfer without consent causes allows a nonrecourse loan to be converted to recourse loan.

The Reporters:
Our on-site local Reporters who are present in Orlando in 2018 are Joanne Hindel Esq., a Vice President with Fifth Third Bank in Cleveland, Ohio; Kimon Karas Esq., an attorney with McCarthy, Lebit, Crystal and Liffman Co. LPA in Cleveland, Ohio; Craig Dreyer Esq., an attorney with the Dreyer Law Firm in Stuart, Florida; Herb Braverman Esq., an attorney with Braverman & Associates in Orange Village, Ohio; Kristin Dittus Esq., a solo attorney with offices in Denver, Colorado, Michael Sneeringer Esq., an attorney with Porter, Wright, Morris and Arthur, LLP in Naples, Florida, Michelle R. Mieras, a Fiduciary Risk Manager with Bank of the West in Denver, Colorado, Beth Anderson Esq., an attorney with Wyatt, Tarrant & Combs, LLP in Louisville, Kentucky, Bruce A. Tannahill Esq., a Director of Estate and Business Planning in the Mass Mutual Financial Group in Phoenix, Arizona, and Patrick J, Duffey Esq, an attorney with Holland & Knight in Tampa, Florida.
The Report Editors in 2018 are Joseph G. Hodges Jr. Esq., a solo practitioner in Denver, Colorado, who is the Chief Moderator of the ABA-PTL discussion list. He is being ably assisted in those duties this year by Reporter Bruce A Tannahill Esq.