# Introduction, Pt. 1

A complete listing of the proceedings and speakers is available on **the Institute's Web site**

As we have done in January for the last ten 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 41th Annual Philip E. Heckerling Institute on Estate Planning that is being held January 8-12, 2007 at the Orlando World Center Marriott Resort and Convention Center in Orlando, Florida, a new venue for the Institute this year. A complete listing of the proceedings and speakers will be published here later and is also available on the Institute's Web site at http://www.law.miami.edu/heckerling.

Our on-site local reporters who are present in Orlando this year are Gene Zuspann Esq. of Zuspann & Zuspann in Denver, Colorado, Herb Braverman Esq.of Walter & Haverfield, LLP in Cleveland, Ohio, Merry Balson Esq.of Wade, Ash, Woods, Hill & Farley in Denver, Colorado, Paul Hood Esq. of L. Paul Hood Jr. (APLC) in Mandeville, Louisiana, Joanne Hindel Esq. of Fifth Third Bank in Cleveland, Ohio. Jason Havens Esq. of Havens & Miller PLLC in Destin, Florida. Alan Rothschild Esq. of Hatcher, Stubbs, Land, Hollis and Rothschild, LLP in Columbus, Georgia, and Kimon Karas Esq. of McCarthy, Lebit, Crystal and Liffman Co., LPA in Cleveland, Ohio. The editor again this year will be Joseph G. Hodges Jr. Esq, a solo practitioner in Denver, Colorado, who also is the Chief Moderator of the ABA-PTL List.

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**Scope of the Institute:**

The Heckerling Institute on Estate Planning is the nation's leading conference for estate planning professionals. The program is designed for sophisticated attorneys, trust officers, accountants, insurance advisors, and wealth management professionals who are familiar with the principles of estate planning.

• The recent developments panel on Monday afternoon, featuring three of the nation's foremost estate planning experts, will guide you through the year's most significant developments in estate planning, including the latest developments on the tax front.

• Our general session lectures, which begin on Tuesday morning and continue throughout the week, will provide in-depth analysis of topics of timely interest to experienced estate planners.

• On Wednesday and Thursday afternoons, a wide variety of workshops, panel discussions, and case studies will examine and provide practical guidance on sophisticated estate planning techniques, including our popular series on planning with financial assets. Sessions in the financial assets series are designated:

• A second series of afternoon programs will focus on trust and estate litigation, including an update on FLP audit and litigation issues and a session on reducing the risk of malpractice claims. The series will also include a full afternoon session on a new simplified trial resolution process to resolve disputes that cannot be successfully mediated. Sessions in the litigation series are designated:

• Our fundamentals program is of interest to not only entry-level practitioners, but also to experienced planners who would benefit from a thorough review of three important topics. The programs will cover selected wealth transfer tax issues, buy-sell agreements, and Subchapter K.

As the largest gathering of estate planning professionals in the country, the Institute offers a unique opportunity to exchange ideas, to network and to review the latest in technology, products and services displayed by over 100 vendors in an exhibit hall dedicated entirely to the estate planning industry.

Our new headquarters hotel, the Orlando World Center Marriott Resort & Convention Center, offers nearly 2,000 hotel rooms as well as expanded meeting and exhibit space. Please join us in Orlando, January 8 -12, 2007, to take advantage of this exciting event!

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# Introduction, Pt. II

A complete listing of the proceedings and speakers is available on **the Institute's Web site**

As we have done in January for the last ten 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 41th Annual Philip E. Heckerling Institute on Estate Planning that is being held January 8-12, 2007 at the Orlando World Center Marriott Resort and Convention Center in Orlando, Florida, a new venue for the Institute this year. A complete listing of the proceedings and speakers will be published here later and is also available on the Institute's Web site at http://www.law.miami.edu/heckerling.

Our on-site local reporters who are present in Orlando this year are Gene Zuspann Esq. of Zuspann & Zuspann in Denver, Colorado, Herb Braverman Esq.of Walter & Haverfield, LLP in Cleveland, Ohio, Merry Balson Esq.of Wade, Ash, Woods, Hill & Farley in Denver, Colorado, Paul Hood Esq. of L. Paul Hood Jr. (APLC) in Mandeville, Louisiana, Joanne Hindel Esq. of Fifth Third Bank in Cleveland, Ohio. Jason Havens Esq. of Havens & Miller PLLC in Destin, Florida. Alan Rothschild Esq. of Hatcher, Stubbs, Land, Hollis and Rothschild, LLP in Columbus, Georgia, and Kimon Karas Esq. of McCarthy, Lebit, Crystal and Liffman Co., LPA in Cleveland, Ohio. The editor again this year will be Joseph G. Hodges Jr. Esq, a solo practitioner in Denver, Colorado, who also is the Chief Moderator of the ABA-PTL List.

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In Introduction Part I we summarized the Scope of the Institute, introduced the Faculty for 2007, and listed the Institute's Director and the members of the Advisory Committee.

In this Introduction Part II we are listing the Substantive Program Schedule and Highlights so everyone will know what sessions will be presented next week and when and approximately when the various Reports on the same can be expected to appear on the ABA-PTL discussion list.

**2007 HECKERLING SUBSTANTIVE PROGRAM SCHEDULE AND HIGHLIGHTS:**

**Monday, January 8**

7:00 a.m.

Registration

9:00 a.m. – 12:15 p.m.

OPTIONAL PRE-CONFERENCE FUNDAMENTALS PROGRAM

Wealth Transfer Tax: Selected Issues, Surprising Results

Jeffrey N. Pennell

Beneath their superficial simplicity, many wealth transfer tax provisions present quirky refinements that challenge our understanding of the actual operation of these complex and poorly-integrated rules. This session explores the obvious and less-than-obvious fundamentals that must be mastered to become a veteran estate planner.

2:00 – 2:10 p.m.

Introductory Remarks

Tina Portuondo, Institute Director

2:10 – 5:15 p.m.

Recent Developments – 2006

Steve R. Akers Carlyn S. McCaffrey and Louis A. Mezzullo

Materials by Richard B. Covey and Dan T. Hastings

6:00 – 7:00 p.m.

Complimentary Reception for Registrants

**Tuesday, January 9**

9:00 – 9:50 a.m.

GRATs vs. Installment Sales to IDGTs: Which is the Panacea or are They Both Pandemics?

Jonathan G. Blattmachr

How do GRATs stand up against installment sales to grantor trusts? Although GRATs are touted as a “heads I win, tails, I can't lose” strategy, incorrect resolution of unanswered questions about GRATs could be devastating. Understanding the economics is also critical to success. Learn which assets, which structure and why.

9:50 – 10:40 a.m.

Financial Engineering Meets Estate Planning

S. Stacy Eastland

This session will explore the ins and outs of modern financial engineering, including the use of derivatives in hedging and modernization of a client’s highly appreciated, marketable assets. The use of derivatives during estate administration and the use of interfamily derivatives to shift wealth from one generation to the next will also be covered.

10:50 – 11:40 a.m.

“Free” Life Insurance: Really a Free Lunch or a Prelude to Acid Indigestion?

Stephan R. Leimberg

An exploration of the convergence of ethics, law, and life insurance, what “works” and what’s “right”, and an examination of how the more we forget (or never learn) the lessons of the past, the more often they will be revisited upon us – and our clients.

11:40 a.m. – 12:30 p.m.

What Have They Done to Our Benefits? An Update on Recent (and Prospective) Developments in Estate and Distribution Planning for Retirement Benefits

Natalie B. Choate

What Congress, the courts, and the IRS have done to (or for) our clients' retirement benefits recently, including: which trusts must be amended due to Rev. Rul. 2006-26; 2006 PLRs; which clients should adopt the new Roth 401(k) plans; how increasing Roth plan availability affects estate planning; and what's next (charitable IRA rollovers anyone?).

2:00 – 2:50 p.m.

Yesterday’s FLP: Fabulous Locked-In Profits or Finally Losing Pizazz?

Ronald D. Aucutt

Has case law reassured us that we have been “doing family limited partnerships right,” so that only sloppy FLPs should expect any problems? Or has the IRS finally found the Achilles’ heel of a technique it equates with bogus discounts? This presentation will boldly ponder those questions and their implications.

2:50 – 3:40 p.m.

Succession Planning – The Need For Both A Belt and Suspenders – Coordinating the Estate Plan with the Corporate Documents

Jonathan C. Lurie

The succession plan involves a combination of estate planning and corporate documents that need to be coordinated. This session will explore how to best coordinate the estate planning documents, which may include an irrevocable trust, with the business documents necessary to implement the plan.

3:50 – 4:40 p.m.

Avoiding Malpractice Claims Against Estate Planning Counsel: How Your Actions Can Exacerbate, Mitigate, or Eliminate Your Exposure

Kevin S. Rosen

Estate planning lawyers face the greatest exposure to malpractice claims. These claims do not arise solely from substantive errors. Rather, the overall relationship with the client poses a veritable malpractice minefield. Learn how to identify and mitigate these risks and otherwise put yourself in the best position to defend against the increasingly inevitable lawsuit.

4:40 – 5:30 p.m.

Charting a Course for Convenience or Incapacity –New Aids to Navigation in the Uniform Power of

Attorney Act

Linda S. Whitton

This session will highlight the innovations and default rules of the new Uniform Power of Attorney Act, and analyze their implications for principals, agents, and the persons who deal with agents.

**Wednesday, January 10**

9:00 – 9:50 a.m.

Navigating the Landmines in Charitable Gift Planning: Legislation, Lawsuits, and Personal Liability

Kathryn W. Miree

The charitable landscape has never been more tumultuous. This session focuses on how to plan charitable gifts with recent and proposed legislative changes, how to ensure gift intentions withstand institutional and programmatic changes, and how to avoid the increasing potential for personal liability in post-gift management.

9:50 – 10:40 a.m.

Estate Planning and Compliance after the Final (or re-proposed) GSTT Qualified Severance Regs (if they are issued) OR Generation-Skipping for the Charitably Inclined Grandparent

Pam H. Schneider

If the Service has issued final (or re-proposed) GSTT Qualified Severance Regulations, this session will discuss how these regulations will change the way we plan and the forms we file with the IRS. If this life changing event has not happened, this session will instead discuss the intersection between popular planned giving techniques and the generation-skipping transfer tax as well as the synergies available to a client with both generation-skipping and charitable goals.

10:50 a.m. – 12:30 p.m.

Question & Answer Session

Steve R. Akers Carlyn S. McCaffrey and Louis A. Mezzullo

2:00 – 5:15 p.m.

FUNDAMENTALS PROGRAM – (Runs concurrently with the Special Sessions) The Blount True-th about the Family Business: Tax and Non-Tax Considerations in Drafting Buy-Sell Agreements

Howard M. Zaritsky and Farhad Aghdami

The favorable income tax rates for both dividends and capital gains have temporarily simplified some aspects of planning for business buy-outs, but questions remain. This program examines the key issues in planning a buy-sell agreement, including: Where and how should one document the restrictions? What types of transfers should be restricted? How can one best assure favorable income tax treatment and full recovery of basis? How best to fund the buy-out? What are the estate, gift, and GST tax ramifications? How should the agreement restrict competition by former owners? How should it change control from a strict one-share, one-vote regimen? All this, and forms too.

2:00 – 3:30 p.m. Special Sessions I

I-A – Current Issues Involving Family Limited Partnerships and LLCs

John W. Porter

A discussion of the federal estate and gift tax issues involving family limited partnerships and limited liability companies. The discussion will include IRS and taxpayer positions regarding these entities, recent valuation and Section 2036 case law, and tips for dealing with disputes regarding these entities.

I-B – What the Heck-erling is Happening with Life Insurance?

Stephan R. Leimberg, Lawrence Brody and Charles L. Ratner

The panelists will further discuss stranger owned (a.k.a investorinitiated) life insurance and 2006 life insurance cases, rulings, and legislation including Dow Chemical (insurable interest), Chawala (insurable interest), Grassley/Baucus Excise Tax (CHOLI), Blount (impact of corporate owned life insurance on valuation), PLR 200606027 (transfer for value), PLR 200603002 (transfer tax implications of intent vs. policy facts), DOL Advisory Opinion 2006-03A and more.

I-C – Navigation without a Compass – Charitable Planning in 2007

Kathryn W. Miree and Jerry J. McCoy

Donors and donees today must react to a changing landscape. Actual and proposed legislation would provide new incentives but impose added burdens. Conventional planning approaches must be reconsidered and some adjustments will be necessary. These concerns, and appropriate reactions, will be discussed in this interactive session.

I-D – One Size Fits All – Tailoring a Form Power of Attorney to Meet Individual Client Needs

Linda S. Whitton and William LaPiana

Using the new Uniform Power of Attorney Act statutory form as a model, this session will offer drafting strategies for customizing a form power of attorney.

I-E – When Trusts Are Not Enough – Strategic Family Plans Also Require a Strategic Structure: The Private Trust Company

John P.C. Duncan, Michael R. Conway, Bryan R. Dunn and Sara S. Hamilton

The panel will share their experiences with families using private trust companies (“PTCs”) to place and keep the family at the helm to guide the family’s strategic plan across generations. The PTC’s role in tax risks and benefits management, and the best chartering states will also be explored.

3:45 – 5:15 p.m. Special Sessions II

II-A – Defense Strategies, Risk Management, and Evolving Theories and Trends in Malpractice Claims Against Estate Planning Counsel

Kevin S. Rosen, Pamela A. Bresnahan and Mary Beth S. Robinson

Where are the malpractice risks when performing estate planning work?How are they changing? The answers are far broader than knowing the substantive law. Client identification, unrecognized conflicts, and evidentiary disputes are a few examples of the other factors that create risks for estate planning lawyers. Learn how best to position yourself to avoid these risks and how your actions will be portrayed in malpractice litigation from experienced trial counsel who defend these claims and malpractice insurance claims counsel who manage them.

II-B – What Yesterday’s FLP Calls For: Rejoicing or Repairing?

Ronald D. Aucutt and Daniel H. Markstein, III

This session will examine family limited partnerships at the crossroads and explore how to distinguish the success stories from the disasters waiting to strike. The panel will offer suggestions on how to secure the successes and repair the wrecks, with an eye particularly on practical dilemmas and tax traps.

II-C – Emerging Issues Under the Twin UPIAs

Susan Porter and Alan S. Acker

This workshop will address the interplay between the Uniform Prudent Investor Act and the Uniform Principal and Income Act. The session will explore common issues which arise concerning investments and allocations of receipts and disbursements, including practical considerations regarding the power to adjust and the unitrust regime.There will be an emphasis on drafting recommendations which can achieve greater flexibility and overcome some of the drawbacks under the model statutes.

II-D – More on the Generation-Skipping Transfer Tax

Pam H. Schneider and Carol A. Harrington

This session will further explore issues concerning planning with the generation-skipping transfer tax.

II-E – GRATs vs. Installment Sales to Grantor Trusts vs. Direct Gifts: What Do the Numbers and Theory Say?

Jonathan G. Blattmachr, Robert A. Weiss and Diana S.C. Zeydel

This session will discuss “intimate” details of selected sophisticated estate and gift tax planning arrangements including GRATs, installment sales to grantor trusts and gifts. It will discuss theory, the legal risks (and how to minimize those risks) and will present a “Monte Carlo” analysis projecting the after-tax benefits. The session will consider the wealth retained by the senior generation, management of wealth for successor generations, and the impact of generation-skipping transfer and income taxes.

FIN

Thursday, January 11

9:00 – 9:50 a.m.

Not My Fault - The Devil Made Me Do It!

Responsibilities and Liabilities of a Directed Trustee

Dennis I. Belcher

Grantors frequently divide a trustee's duties, particularly where the investments are concentrated. One trustee has custody of the assets and another (often an investment committee or a trust advisor) has the authority to direct investments. This presentation will cover the allocation of trustee responsibilities, the duties and potential liability of directed trustees, the steps to minimize directed trustee liability, and the effect of exculpation provisions.

9:50 – 10:40 a.m.

Waste Not, Want Not – Creative Use of General Powers of Appointment to Fund Tax-Advantaged Trusts

John F. Bergner

This presentation will analyze several recent Internal Revenue Service letter rulings endorsing the use of general powers of appointment to fund tax-advantaged trusts. The program will discuss planning techniques that can be built upon these rulings, review the tax and non-tax risks, and provide sample forms designated to accomplish the planning goals while minimizing risks.

10:50 – 11:40 a.m.

The Perfect Storm: How the Confluence of Tax Planning and the Ethics Rules Can Sink the Estate Planner, the Fiduciary and the Estate Plan

Mary Ann Mancini

This program will examine the state and federal ethical rules an estate planner or fiduciary must address when engaged in tax planning, including the preparation of tax returns for a trust or estate. Although no definitive answers will be provided (because there aren't any), means of protecting the estate planner and the fiduciary from the anger of beneficiaries, a state ethics committee and/or the Office of Professional Responsibility will be discussed.

11:40 a.m. – 12:30 p.m.

Simplified Trial Resolution: High Quality Justice in a Kinder, Faster Environment

Robert W. Goldman

This program will provide an overview of a new trial resolution process developed by the American College of Trust & Estate Counsel ("ACTEC"). After reviewing and discounting traditional forms of arbitration, ACTEC has developed a new way to resolve disputes that cannot be successfully mediated. Litigation is inevitable, but slogging through the overworked, time consuming judicial process is no longer required.

12:45 – 1:45 p.m.

Florida Insurance: Issues Relating to Unauthorized Entities

Attendance at this session is required for all insurance professionals seeking continuing education credit in Florida.)

2:00 – 5:15 p.m.

FUNDAMENTALS PROGRAM – Making "Friends" with Subchapter K (Runs concurrently with the Special Sessions)

Richard B. Robinson

The estate planner's encounters with Subchapter K are not limited to FLPs. Questions regarding the formation, operation and liquidation of partnerships and limited liability companies are everyday occurrences when doing estate planning for a family business. This program will give you the basic tools to spot the issues and provide answers.

2:00 – 3:30 p.m.  Special Sessions III

III-A – Simplified Trial Resolution from an Estate Planner's Point of View

Robert W. Goldman, Bridget A. Logstrom, John T. Rogers, Jr. and Bruce M. Stone

Strategies for protecting your client's estate for the intended beneficiaries with the new simplified trial resolution process developed by ACTEC.

III-B – It All Starts When the Participant Dies: The Executor's Guide to Post-Mortem Compliance and Planning for Retirement Benefits

Natalie B. Choate

Everything you need to know to advise executors and beneficiaries regarding inherited retirement benefits: post-mortem rollovers, Roth conversions; estate taxes: how to pay; valuation discounts; AVD issues; the IRD deduction; disclaimers; plan-to-plan transfers; surviving spouse under age 59½; cleanup strategies if decedent named no beneficiary; six differences between an inherited and a regular IRA; and problems with the plan administrator.

III-C – Directed Trustees, Co-Trustees, and Successor Trustees – Fiduciary and Regulatory Issues

Dennis I. Belcher, David H. Pankey and Ann Hart Wernz

Corporate trustees are increasingly using third party investment managers to manage funds either as a directing trustee or a co-trustee, and trustees are changing more frequently. The panel will discuss regulatory and fiduciary risks in using third party investment managers, practical problems with multiple trustees, and liability issues for successor trustees.

III-D – Coordinating Business and Succession Plans

Jonathan C. Lurie

This session will explore how to coordinate the business and estate planning documents to effectuate the succession plan.

III-E – The Ethical Rules of Circular 230 and the Estate Planner and Fiduciary

Mary Ann Mancini and Cono R. Namorato

The panelists will discuss how the ethical rules of Circular 230 impact the manner in which an estate planner and/or a fiduciary addresses tax issues when advising an estate planning client or administering a trust or estate.

III-F– Planning with Derivatives and Structured Products

S. Stacy Eastland and George F. Albright, Jr.

The session will examine case studies in which financial engineering turbo-charges estate planning.

3:45 – 5:15 p.m.  Special Sessions IV

IV-A – Simplified Trial Resolution from a Litigator's Point of View

Robert W. Goldman, Bridget A. Logstrom, John T. Rogers, Jr.and Bruce M. Stone

Strategies for implementing a simplified trial resolution clause in a will or a trust and for working with estate planners to protect the intent of the testator/settlor.

IV-B – The Ethics of Asset Protection Planning – An Oxymoron?

Alexander A. Bove, Jr., Matthew P. Matiasevich, Jay D. Adkisson and Gideon Rothschild

A panel presentation/debate examining the sometimes conflicting ethical and practice issues faced in asset protection planning when representing clients with situations ranging from no foreseeable problems to existing claims and investigations against them. Do the attorney's responsibilities and exposure to professional, civil, or even criminal liability change as the client's situation becomes more egregious? The panelists will review and comment on the challenging practical, ethical, and philosophical issues surrounding this troublesome area of the law.

IV-C – It Is Better to Give and Then Receive – Is the IRS' Favorable Analysis Correct?

John F. Bergner and Mitchell M. Gans

This panel will provide a more detailed analysis of the potential benefits and risks of using general powers of appointment to fund tax-advantaged trusts. The presentation will review several planning situations in which the IRS letter rulings may be helpful; analyze the tax, legal and practical issues and the IRS reporting requirements; and review sample forms that may be used to implement this planning.

IV-D –Death, Dirt & Duties: Estate Planning for Real Estate Transfers

Wendy S. Goffe and Scott B. Osborne

This panel will deal with selected issues that arise in the context of estate planning with real property, including the personal residence gain exclusion, title insurance, like kind exchanges, planning for gifts to individuals as well as charities, and conservation easements.

IV-E– A Holistic Approach to Analysis of Private Annuity Trusts to Defer Capital Gains, Including Exit Strategies

Jerome M. Hesch and Kevin McGrath

Sellers may rejoice at the deferral of capital gains afforded by the sale of appreciated property to a non-grantor, private annuity trust, but there is no joy in the income tax treatment to the purchaser. This session will address the negative income tax aspects and other tax issues that must be considered in evaluating a proposed private annuity transaction. What if the private annuity sale is a done deal? Exit strategies to minimize the negative income tax consequences to the purchaser will be evaluated.

Friday, January 129:00 – 9:50 a.m.

The Inheritance Threat That Dares Not Speak Its Name: Financing the Cost of Long-Term Care

Richard L. Kaplan

This session explores the financing of long-term care in the context of preserving assets for surviving heirs. Subjects include the limited coverage provided by Medicare and “medigap” policies, but the principal focus will be the cataclysmic changes to Medicaid enacted in February2006 and their implications for long-term care insurance.

9:50 – 10:40 a.m.  From NASCAR Condominiums to Private Mausoleums: Keeping the Vacation Home in the Family

Wendy S. Goffe

As the proportion of wealth invested in family recreational property increases, issues relating to keeping the property in the family take on a new significance. Deep feelings arise when family members are forced to deal with questions about how to share responsibilities and benefits of ownership. This presentation examines why the family cabin (of any value) is so important in our society, the types of conflicts that arise when families try to hold onto property, methods for transferring ownership to charity and the next generation, and methods of management and organization to maintain harmony once the property has been passed down.

10:50 a.m. – 12:00 noon

There’s Got to be a Morning After: What We Have Learned and What to Do with It

Mark B. Edwards

After five days of study, you might feel that you suffer from information overload. To help you, we will wrap up the week’s presentations, put what we have learned in the context of our day-to-day practice using a hypothetical fact situation, and focus on practical issues.

The End

**GENERAL INFORMATION ABOUT INSTITUTE:** Inquiries/Registration: Philip E. Heckerling Institute on Estate Planning University of Miami School of Law Center for Continuing Legal Education P.O. Box 248087 Coral Gables, FL 33124-8087 Telephone: 305-284-4762 / FAX: 305-284-6752 Web site: www.law.miami.edu/heckerling E-mail: heckerling@law.miami.edu

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# Introduction

A complete listing of the proceedings and speakers is available on **the Institute's Web site**

As we have done in January for the last ten 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 41th Annual Philip E. Heckerling Institute on Estate Planning that is being held January 8-12, 2007 at the Orlando World Center Marriott Resort and Convention Center in Orlando, Florida, a new venue for the Institute this year. A complete listing of the proceedings and speakers will be published here later and is also available on the Institute's Web site at http://www.law.miami.edu/heckerling.

Our on-site local reporters who are present in Orlando this year are Gene Zuspann Esq. of Zuspann & Zuspann in Denver, Colorado, Herb Braverman Esq. of Walter & Haverfield, LLP in Cleveland, Ohio, Merry Balson Esq.of Wade, Ash, Woods, Hill & Farley in Denver, Colorado, Paul Hood Esq. of L. Paul Hood Jr. (APLC) in Mandeville, Louisiana, Joanne Hindel Esq. of Fifth Third Bank in Cleveland, Ohio. Jason Havens Esq. of Havens & Miller PLLC in Destin, Florida. Alan Rothschild Esq. of Hatcher, Stubbs, Land, Hollis and Rothschild, LLP in Columbus, Georgia, and Kimon Karas Esq. of McCarthy, Lebit, Crystal and Liffman Co., LPA in Cleveland, Ohio. The editor again this year will be Joseph G. Hodges Jr. Esq, a solo practitioner in Denver, Colorado, who also is the Chief Moderator of the ABA-PTL List.

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The start of the 41th Institute is only two days away now and, as we prepare for that, we want to pass along a few news items we have received recently or need to broadcast.

**Institute Opening Reception**

The Heckerling Institute staff reminds everyone to attend the Complementary Reception for Registrants that will be held in the exhibition hall at the Marriott from 6:00 to 7:00 p.m. on Monday evening. This is a don't miss function - plenty of food and lots of things to drink, plus a great place to meet and make friends with a lot of people.

**News from the Exhibit Hall:**

The vendor's list this year has significantly expanded and includes the following (in alpha order) that may be of particular interest to many of our readers. Most of these vendors will be covered in more depth in later Reports as the Institute progresses:

ABA Section of Real Property, Probate & Trust Law Academy of Special Needs Planners Advanced Settlements, Inc. Air Planning Alaska Trust Company American Association of Attorney _ CPA's American Endowment Foundation American Guaranty & Trust Company American Society of Appraisers Antiquorum Auctioneers Aon Private Risk Management Appraisers & Planners, Inc. Ashar Group, LLC Ashton Group Asset Management Advisors Atlantic Trust Private Wealth Management Attorney's Will Registry Balsam Settlement Management LLC Bank of America Bayview Financial Exchange Services BNA Tax Management, Inc. Bonhams & Butterfields Brentmark Software, Inc. BRIDDGE ART STRATEGIES, LTD. CCH Charitable Trust Administration Company Christiana Trust Christie's Citigroup Trust Commonwealth Trust Company Community Foundations of Florida ComStock Valuation Advisors, Inc. Connect2A Coventry Crawford & Company Credit Suisse Deutsche Bank Private Wealth Management Donlevy_Rosen & Rosen, PA Doyle New York Eidelman Associates _ WINDRAFT Empire Valuation Consultants LLC Equity Trust Company Estate Valuations & Pricing Systems, Inc. EstateWorks Exeter 1031 Exchange Services FAMILIY OFFICE Services Corporation FASTER Systems, LLC Fast_Tax Fidelity Charitable Services Fiduciary Trust Company International Financial Data Service Fine Art Capital First Capital Surety & Trust Company First PREMIER Bank, Trust Department Firstat RN Care Management Services FMV Opinions, Inc. Fort Pitt Capital Group Foundation Source FREEMAN'S Auction House Gillett Publishing LLC Goldman Sachs Trust Company Gurr Johns Masterson, Inc. Harris Private Bank Harvey E. Morse, P.A. Hays Companies Hemisphere Real Estate Heritage Auction Galleries Heritance System by DataTech Software HSBC Private Bank Insurance Strategies Group LLC InterActive Legal Systems International Genealogical Search Investment Scorecard Incorporated Investors Bank & Trust Company John Hancock Life Insurance Company U.S.A. LAWGIC LLC Lawyer's Weekly, Inc. Leslie Hindman Auctioneers LexisNexis Life Insurance Settlements, Inc. Lucion Technologies M.J. Bohan Co., Inc. Management Planning, Inc. Marcum & Kliegman LLP MassMutual Financial Group Medicaid Practice Systems Mellon's Private Wealth Management Group Mercer Capital Merrill Lynch Millea Bros. Ltd. Nadeau's Auction Gallery Inc. National Philanthropic Trust New York Private Bank and Trust Newman + Cohen Financial Management NIXON PEABODY FIDUCIARY SERVICES Northern Trust Company Paul Comstock Partners PDI Global, Inc. PENSCO Trust Company PinnacleCare Plexus Financial Technologies LP PPC Private Asset Management Real Automation Solutions Riava Realty Advisors Rochdale Offshore Investment Management Rockefeller Philanthropy Advisors RSM McGladrey, Inc. Rumson Capital LP Schumacher Publishing, Inc. Schwab Fund for Charitable Giving Sherwood Partners, LLC Skinner, Inc. Sotheby's, Inc. South Dakota Trust Company, LLC and South Dakota Planning Company LLC Southpac Group Stack's Rare Coins State Street Global Advisors Succession Capital Alliance The Bank of New York _ Directed Trust Services The Insurance Design Center, LLC The Lackner Group, Inc. The Shafe Group, Inc. The InsuranceAdvisor.com Thomson RIA Thomson West Trugman Valuation Associates, Inc. Trusts & Estates U.S. Trust and Practical Drafting ® University of Miami Vanguard National Trust Company Wachovia Exchange Services Wachovia Trust Wealth Manager WealthCounsel Willamette

Management Associates Willis Private Client Group Wyoming Bankers Association _ Trust Committee Yellowstone Trust Administration

Below is information that will be included at the end of each Report due to its importance and in case any of our readers need to contact the Institute or someone who is there while the Institute is progressing.

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# Report #1 (Monday & Tuesday)

A complete listing of the proceedings and speakers is available on **the Institute's Web site**

As we have done in January for the last ten 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 41th Annual Philip E. Heckerling Institute on Estate Planning that is being held January 8-12, 2007 at the Orlando World Center Marriott Resort and Convention Center in Orlando, Florida, a new venue for the Institute this year. A complete listing of the proceedings and speakers will be published here later and is also available on the Institute's Web site at http://www.law.miami.edu/heckerling.

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This Report contains coverage of most of the Tuesday morning and afternoon Sessions. Since the Report on the Monday afternoon Recent Developments session has not been turned in yet, we are going ahead with the publication of these Tuesday Reports now.

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Financial Engineering Meets Estate Planning - Derivatives and Structured Products Tuesday Morning, January 9, 2007
Presenter: S. Stacy Eastland

Reporter: Joanne Hindel Esq. of Fifth Third Bank in Cleveland, Ohio

Mr. Eastland, who followed Jonathan Blattmachr, started off by saying that he remembered Ed McMahon from the Johnny Carson show saying that one should never follow an animal or children’s act.

He then said that he would describe financial planning products that work well with GRATs and IDGTs and hoped that we would find them easier to understand than the Iraq policy and Texan.

Mr. Eastland started off by describing the vocabulary used by financial engineers including the definitions for a call option; a call spread option; a put option and a put spread option. He pointed out that buyers of call or call spread options assume that a stock will go up whereas buyers of put or put spread options assume that a stock will go down in value.

He then discussed key tax law considerations that affect the integration of financial engineering with estate planning by reviewing the tax treatment with respect to call options held by an investor and the tax treatment with respect to the owner of the put. Mr. Eastland also discussed how the writer of a put or call is taxed.

The focus of Mr. Eastland's presentation centered around situations that allow for the integration of financial engineering with estate planning and post mortem planning.

Situation 1: Using financial engineering to hedge or monetize a dominant single stock position in an integrated estate plan

Mr. Eastland briefly described the effect of diversification of a single stock position and the possible strategies an investor might consider to accomplish diversification. He pointed out that for the individual investor who wishes to benefit his family there are two primary taxes on capital: capital gains taxes and transfer taxes.

He then posed the following examples for this situation:

1. Contributing highly appreciated marketable stock to a partnership and then selling the limited partnership for a note to a grantor trust for the benefit of the grantor's family.

The following questions were addressed in connection with this example:

Is the grantor entitled to a valuation discount for the sale of the limited partnership interest to the grantor trust? Will the grantor owe any tax on the sale of the partnership interests to the trust? Will the grantor owe any gift tax because of the effective payment of income tax on the trust income that is accruing for the benefit of the trust beneficiaries?

Mr. Eastland then discussed the answers; the grantor will be entitled to a valuation discount for the sale of the partnership interest but will not owe any tax on the sale or any gift tax. He concluded this example with a brief discussion of the advantages of this technique (immediate liquidity and simplicity and economically superior if there is a declining market value associated with a single stock position) and also pointed out the considerations (immediate tax burden and no opportunity to take advantage of the investor's charitable intent).

2. Transferring highly appreciated stock to a family limited partnership that then creates a 20 year CRUT in which the partnership has a 90% actuarial interest and the charity has a 10% actuarial interest. The trustee of the CRUT sells the stock and the grantor then transfers her limited partnership units to a GRAT and receives annuity payments for the transfer.

Here too, Mr. Eastland discussed the advantages:additional contributions, possibility for trust distributions to keep pace with inflation and a current income tax deduction for the grantor. He also pointed out that, depending upon investment performance, under the tiered income rules when the trust terminates approximately 40% to 60% of the inherent “old” capital gains and the assets contributed to the CRUT will not be subject to capital gains tax. Also, the remaining inherent capital gains will be subject to capital gains, but it is tax deferred. Depending upon the term of the unitrust it is tax deferred for as long as 20 years.

He also listed the considerations inherent with this example (unfavorable tax treatment of distributions of a CRUT and inability for a CRUT to own any unrelated business income investments). He also indicated that the need to value the CRUT assets annually may present additional administrative burden to the trustee and may be costly and there are certain prohibited party transactions. Capital gains tax rates may also increase in the future so it is possible that some of the capital gains deferral could be taxed at a higher rate.

3. Four individuals contribute assets to an Exchange Fund Partnership which is designed to last 20 years. All the individuals contribute their interests in the partnership to a family limited partnership and then sell the FLP to a grantor trust. When the partners withdraw their pro-rata shares from the partnership they incur no capital gains at the time of their withdrawal and have achieved a diversified portfolio.

Mr. Eastland discussed the advantages of this example (effective non-charitable technique if markets are rising and many investment firms market the exchange fund partnership to multiple clients and collect many public securities upon formation) and the considerations (lack of liquidity and financial management fees and exchange fund partnerships also have a limit on the number of shares of any particular stock they will accept. So, for a client with substantial holdings the manager of the exchange fund partnership may not be in a position to accept all of that client’s holdings or even a majority of that client’s holdings). He also pointed out that if a client wants a relatively small portion of his assets in index type funds, this is not an appropriate technique for that client.

4. The dominant owner of a partnership is considering either a cashless collar or a prepaid variable forward contract. The partnership is considering borrowing against its hedged position and reinvesting the proceeds of that loan. Once the transactions are complete, the owner will transfer her limited partnership positions to a grantor trust.

Mr. Eastland discussed the advantages and considerations for both the cashless collar and the prepaid variable forward contract and then concluded with the following observations:

If the client wishes to allocate a portion of her asset allocation to domestic index funds, then the exchange fund solution might be the best choice. If she has some deferred charitable intent, then the partnership CRUT technique might be the best. If she has a bullish feeling about her stock, then she might wish to consider the prepaid variable forward contract and if she does not have a bullish feeling about the stock, she should consider simply selling her stock to meet liquidity needs.

Mr. Eastland reviewed a chart that examined the examples posed assuming that the client lived in New York and died in the 20th year. He concluded by pointing out that the reason why the various techniques produce a better result for the client's family has little to do with the total income taxes saved but rather the reason why the techniques are efficient and produce a superior result is because of the investment opportunity cost associated with those income taxes.

Situation 2: Integrating Financial Engineering with GRATs

After discussing a number of aspects of GRATs including their valuation advantages, synergy with other techniques, comparatively low hurdle rate, high leverage, non-recourse risk to remaindermen and financial reasons why a GRAT may not succeed, Mr. Eastland reviews examples of financial engineering with GRATs.

1. Grantor wishes to compare the possible results from entering into a variety of private derivative transactions with his spouse. He also wants to compare transactions in which his spouse takes her position and contributes it to a second GRAT.

Mr. Eastland reviewed charts contained in his outline to analyze this example and concluded that significant results will be attained even if only one GRAT is utilized in either the private call spread transaction or the private put spread transaction. He also analyzed the tax outcome and possible legal outcome by a court of having the spouse then take her part of the family's hedged position in the stock and contribute that to another GRAT.

2. Grantor uses cash to enter into a call spread transaction and then transfers his call spread position to a GRAT. The GRAT is very successful over the annuity period and it then terminates in favor of a grantor trust held for the benefit of the grantor's children. The grantor then transfers a part of his closely held business to the grantor trust in exchange for the cash in that trust.

Mr. Eastland pointed out that this technique is very useful because of the power to substitute with a grantor trust without income tax consequences.

3. Grantor and his spouse use their positions with respect to a cashless collar with GRATs.

Mr. Eastland commented that in order to avoid the reciprocal trust doctrine being applied, it may be necessary to have different beneficiaries for the two GRATs that the Grantor and his spouse create.

4. Same facts as in #2 but the Grantor and his spouse also enter into a call spread transaction using different GRATs for stock .

5. Daughter owns a significant position in a stock and mother, who also owns a significant position, tells daughter that she would be happy to purchase a contemplated call option from daughter. Are there income tax or gift tax consequences to this transaction? What if mother decides to contribute her call option to a GRAT in which the remainderman is a trust in which the daughter is a discretionary beneficiary?

Mr. Eastland discusses aspects of these additional two examples as well.
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Investor Initiated Life Insurance: Really a "Free Lunch" or Prelude to Acid Indigestion? Tuesday Morning, January 9, 2007 Presenter: Stephan R. Leimberg

Reporter: Kimon Karas Esq. of McCarthy, Lebit, Crystal and Liffman Co., LPA in Cleveland, Ohio.

Mr. Leimberg discussed Investor-Initiated Life Insurance, the last portion of the outline, although the early part of the outline that was not discussed is a very comprehensive overview of the "insurable interest" rules in life insurance.

Investor Owned Life Insurance--referred to as Stranger Owned Life Insurance also "SPIN" Life Insurance.

The concept is not new. The early "free insurance" case is Warnock v. Davis, U. S. Sup Ct (1881). A substantial amount of insurance was purchased on the life of Henry Crosser through a group of investors who agreed to pay all premiums and costs with respect to the policy with no outlay made by Mr. Crosser. The investors were to receive 90% of the proceeds and Mr. Crosser's wife, 10%. Citing insurable interest requirements the Supreme Court ruled the arrangement was void. For there to be an insurable interest there must be a "reasonable expectation of advantage or benefit from the continuance of the (insured's) life." The Court held there was no fraud or deception but there was no  rights the investors had no to the policy proceeds. The Court held there was nothing wrong with financing premiums or assignment of the policy, but the assignment was valid as to the investors only for the sums advanced.

The issues relate to the following: Market finance principles, insurance, tax and property laws.

Mr. Leimberg described this form of insurance as a beneficiary looking for an insured rather than an insured seeking a beneficiary.

Questions for the advisor include is the concept legitimate and should the client do it.

Mr. Leimberg raised as concerns compared to the general principles for acquiring insurance based on insured's need, here the acquisition and amount of insurance is driven by the investors with the ultimate goal to sell the policy to a settlement company.

SOLI is based on two concepts: life insurance premium financing and life settlements

Investor Initiated Free Insurance is not a static concept. There is no single program; promoters are constantly changing the names and features so that each arrangement must be examined on its own.

The process includes the following:

1. Insured provides the authorization for release of medical information to determine if one "qualifies" for the program and in return, the insured receives two years free life insurance, up front cash payment (11/2 to 3% of the death benefit) and a profit from the expected sale of the policy.

2. Insured is examined by life settlement company's experts to determine if prospective insured is a candidate (ie a sound investment).

3. Special purpose lender makes a loan to a non-grantor irrevocable trust.

4. Trust collaterally assigns the policy to the lender.

5. After 24 months (period coincides with the investors' needs to meet both the policy's incontestability period and avoid the state's "wet ink" insurance laws regulating the premature sales of policies to settlement companies, the insured selects the following:

a. Repays the loan and all costs; b. Sells the policy to a life settlement company; or c. Transfers the policy the lender in full satisfaction of the loan.

The parties to the transaction include the following: The insured, the insurer, the investors, special purpose lenders, the settlement company, the insured's advisors and the broker. By the way the broker obtains two commissions on the initial sale of the policy and then the subsequent sale to the settlement company if that is the exit mechanism selected.

The Risks.

Uses insured's amount of available life insurance--insured loses the ability to acquire insurance if needed later.

The rebate/sweetner given to insured to enter into the program may be illegal or if not, certainly income.

May trigger both income and gift tax. Some authorities believe this is split dollar.

If trustee returns the policy to the lender there is possible forgiveness of debt.

A sale of the policy leads to additional questions as to how much gain, what is the trust's basis (is the basis reduced by the cost of insurance), if so, policy's basis may be close to zero. Since trust has no other assets who pays the tax? Will IRS pierce trust and tax the insured?

Insurer possibly may rescind the policy if it believes the policy was applied for under false pretenses.

Possible lawsuit by investors against the insured if the insurer denies payment and the investors do not receive expected benefit.

The settlement company does not purchase the policy or offers a significant reduction from what was originally anticipated.

If there is a real need for insurance why let a stranger receive the benefit?

Finally as Mr. Leimberg states, the "Ickyness" factor. The insured hopes to live a long time. The investor has no control over who owns the policy and more importantly the investors' return varies inversely with the number of years he lives. The tension is as stated by Michael Nelson, that the third party owner benefits from the death of the insured. On the other hand sound underwriting is that the owner of the policy and the insured are better off if the insured continues to live.

SOLI has been described by Barry Flag as "mortality futures" transaction. The insurer is calculating life expectancy one way and the investors in another way. The shorter the insured lives the greater the return for the investors. The investors return is dependent up the present value of the death benefit outweighing the present value of the acquisition costs.

Recent developments.

New York General Counsel Opinion issued July 9, 2006. The Office of General Counsel of New York State Department of Insurance opined that "free insurance" was not insurance as there was no valid "insurable interest." The opinion examined the true substance of the transaction and not its form. "..procurement of insurance solely as a speculative investment for the ultimate benefit of a disinterested third party."

New York Life and Annuity Corporation filed suit on July 5, 2006 to rescind a sale of a policy.

Similar to the position in New York, the states of Utah in Utah Insurance Department Bulletin 2006-03 and Louisiana in Louisiana Insurance Department Bulletin 06-05 ruled that stranger investor policies violated the state's insurable interest rules.

Mr. Leimberg concluded by saying because of the many unanswerable questions with investor-initiated "free insurance" it should give all advisors pause in this area. =================================================== ==========================

What have they done to our benefits? An update on recent developments in Estate and Distribution Planning for Retirement Benefits Tuesday morning, January 9, 2007 Presenter: Presenter: Natalie B. Choate, Esq.

Reporter: Merry Balson Esq.of Wade, Ash, Woods, Hill & Farley in Denver, Colorado

Ms. Choate started the session by reviewing a few recent pronouncements by the IRS. In 2006, the IRS finally gave practitioners some guidance regarding questions that had been pending for many years. First, in Chief Counsel Memorandum 2006-44020 the IRS addressed the problem of funding a pecuniary bequest by transferring an interest in an IRA to a beneficiary. Here, a trust made $100,000 pecuniary bequests to charities. The trustee, who had been named as beneficiary of an IRA, requested that the IRA provider transfer $100,000 IRA to the charities, hoping that a charitable deduction would be available to protect the IRA from income tax. In this CCM, the IRS said this would not work, and instead, held that the transfer of an IRA to a pecuniary fixed dollar legatee in satisfaction of a pecuniary bequest triggered the immediate realization of income under 691(a)(2). Ms. Choate notes that while the CCM went too far, its holding may be correct. Because the trustee had a choice of assets to use to satisfy the bequest, the direction to transfer the IRA could be considered an assignment of income under 691(a)(2). Section 691(a)(2) provides that after death of the IRA owner, the underlying income of the IRA is immediately realized when the IRA is transferred unless the transferee is entitled to the IRA under the will or trust. Note that the IRS supported the CCM by citing a 60 year old case that doesn't even mention 691(a)(2). Estate planners need to deal with this issue in their drafting. If the document requires the charitable bequest be satisfied by transferring a portion of the IRA, Ms. Choate believes the transfer should not trigger recognition of income because the document requires the transfer and the transferee is entitled to the IRA. The lesson here is that if there will be substantial pecuniary bequests (e.g., marital deduction formulas) and IRA benefits will be payable to a trust, practitioners must consider the income issues and work around them if possible.

Second, the IRS issued an unpublished Technical Advice Memorandum addressing the "life insurance subtrust". These subtrusts occur where an IRA owner holds a life insurance policy inside the retirement plan, using the plan assets to pay the premiums. Ms. Choate noted that this is not usually recommended if there are other options. A subtrust is created by the retirement plan to keep the policy out of the owner's estate under the theory that this might avoid incidents of ownership by the insured. Plans engaged in this activity for years, with no guidance from the IRS, until now. In September 2006, in this unpublished TAM provided to a single taxpayer, the IRS took the position that the subtrust disqualified the plan, based on a very old revenue ruling dealing with the incidental benefit rule. That rule says that if a plan benefit cannot be used to provide retirement benefits, the plan is disqualified. While there may be a way to draft around this, Ms. Choate believes use of subtrusts for insurance is too risky, and she suggests people stay away from these. The TAM noted that a person may irrevocable designate a beneficiary without disqualifying the plan. The TAM is discussed in more detail in Steve Leimberg's Employee Benefits and Retirement Planning Email Newsletter - Archive Message #385 (September 19, 2006) and in a Tax Notes article in December 2006.

Third, in Revenue Ruling 2006-26 the IRS rejected the Uniform Principal and Income Act (UPIA) provisions regarding income for marital deduction purposes. The UPIA provides that 10% of a minimum required distribution is income and that the balance is principal. The IRS held that the UPIA 10% rule cannot be used to determine income of a marital deduction trust. If this rule is used, the trust will not qualify for the marital deduction. This ruling does not require rewriting of all trusts. However all marital trusts that will receive retirement benefits should requires the distribution of all trust income, and all income from the IRA to qualify for the marital deduction. Income from the IRA is either internal trust accounting income (e.g., the interest and dividends are identified within the IRA and distributed as income) or a unitrust percentage between 3 and 5%.

Congress has passed 3 pieces of legislation recently affecting retirement benefits:

1. Pension Protection Act (PPA) of 2006. This Act contains two provisions that affect retirement benefits. First, up to $100,000 can be transferred from an IRA of a person over age 70 1/2 to a §501(c)(3) public charity in a direct trustee to trustee transfer. This provision is sometimes referred to as the charitable rollover. This provision only applies for 2006 and 2007, and applies only to IRAs, not to other types of retirement plans. Private nonoperating foundations, donor advised funds, split interest gifts and supporting organizations do not qualify for the charitable rollover provisions. Ms. Choate suggests that if a client is going to make a charitable gift using IRA money, the charitable rollover is the preferable method. The advantages of the charitable rollover over a withdrawal by the participant followed by a contribution to the charity are numerous. First, for very low income taxpayers, a withdrawal of IRA assets will increase taxable income which can increase taxability of social security payments, while a direct transfer avoids this increase. Second, alternative minimum tax is impacted when IRA assets are withdrawn because that amount is added to gross income and can affect the phase out range and reduce the taxpayer's available exemption. Third, the charitable rollover is a deduction in addition to the regular percentage limitations for charitable deductions, and can be beneficial for those clients who want to make additional gifts. Fourth, a withdrawal followed by direct contribution to the charity will increase the taxpayer's income, which can have the effect of reducing the taxpayer's available itemized deductions by up to 2%.

The charitable rollover is best for two main groups of people: (1) older clients who do not need the money or the hassle of IRAs, and want to give money to charity now rather than waiting until death; and (2) the average Joe/Jill who is retired, over 70 1/2, and makes charitable gifts, can use this as a way to fully or partially satisfy their minimum required distributions while satisfying the charitable gift at the same time.

One problem with the PPA is that no one asked the IRA providers what they thought of the charitable rollover, and they may be setting some minimum rollover amounts to avoid multiple small gifts from IRAs. Additionally, there has been some confusion about the $100,000 limitation on the charitable rollover and a person's required minimum distribution. While the charitable contribution can satisfy the required minimum distribution, the limitation on the charitable rollover does not change a person's required minimum distribution.

Effective January 1, 2007, the PPA gives a nonspouse beneficiary the ability to rollover inherited retirement benefits after the participant's death to an inherited IRA. The process is as follows: nonspouse beneficiary inherits a 401(k) plan; beneficiary opens an inherited IRA titled in the same manner as the inherited 401(k); and, the then beneficiary directs the 401(k) plan to send the funds by direct plan to plan transfer to the new inherited IRA. This provision is long overdue, because although the tax law has permitted payout of an inherited 401(k) over the beneficiary's life expectancy, plans were not required to offer this payout option, and most did not offer this extended payout and instead offered only a lump sum distribution. Note that this provision will not enable you to fix the beneficiary designation after client dies, but Ms. Choate will address post mortem fixes in the special session on Thursday.

2. Tax Relief and Health Care Act of 2006. This law was passed in late December 2006 and is not in the outline. The Act created a new tax free transfer from IRAs called the qualified health savings account contribution. The provision allows a one time tax free transfer from an IRA to a health savings account (HSA). An HSA is a tax free account that can be used to pay medical expenses if you have a high deductible health plan. A high deductible health plan is generally one that has a deductible of not less than roughly $1,100 and a deductible or out of pocket limit of not more than $5,000. Roughly $3,000 can be contributed to an HSA and that account can later be used to pay medical expenses. The contributions to an HSA are tax deductible on the front end, and distributions from the HSA for medical expenses are tax free. The Act made HSAs easier to get. However, if you are over age 65 you will not qualify because Medicare is not a high deductible health plan. Steve Leimberg's newsletter (cited above) today includes an article by Natalie Choate providing additional details on HSAs. At this time, Ms. Choate sees no benefit to the ability to make a distribution from an IRA to an HSA. The only group to benefit under this rule are persons under 59 1/2, who want an HSA, but have no other assets to fund the HSA. Email Ms. Choate at author@ataxplan.com if you have other ideas about how this new provision could be used.

3. Tax Increase Prevention and Reconciliation Act of 2005 (TIPRA). This Act encouraged conversions from to Roth IRAs. Under Roth IRA rules, income tax is paid on contribution into the plan, but all future distributions are tax free and there are no minimum required distributions during life. Currently, the attractiveness of Roth IRAs is limited in two primary ways: (1) the price of the conversion is high because the tax must be prepaid on the contribution to the plan, thus, low income taxpayers cannot afford to convert; and (2) no conversions are allowed unless the taxpayer's income is under approximately $100,000 (the "income test"), thus, high income taxpayers (who can afford the tax) are prohibited from participating in conversions. Under TIPRA, starting in 2010, there will be no income test for IRA conversions.

Additionally, as of 2006, anyone who has a 401(k) or 403(b) plan can now elect to have their cash or deferred contributions allocated to a Roth 401(k) (also referred to as a "designated Roth account") rather than a regular plan. There is no income test for this, therefore if clients have a small business, they may want to adopt a 401(k) plan and a Roth 401(k) to take advantage of these provisions. There are many considerations to take into account when determining whether to convert to use a Roth 401(k) and Ms. Choate ended the session with the following comments she has heard

from clients, attorneys and other planners highlighting those considerations: 1. client is concerned the investments may depreciate after conversion to a Roth 401(k) and he/she will lose money; 2. client distrusts government, and believes they may change the law and make Roth plans taxable; 3. client wants the current tax deduction of a traditional 401(k); 4. client already has significant traditional retirement plans and wants to diversify into a Roth; 5. client wants to pack the retirement plan by putting the full deferral amount into the Roth plan and pay the taxes with other non-retirement assets which increases total value of the plan; 6. client believes it is easier to pay the taxes now when he/she is still working, and that tax payments during retirement may be more difficult; 7. clients spend assets that are not in a retirement plan so they will be advised to fund these plans; 8. client believes that the tax rates are low now, but as the baby boomers start to retire the tax rates will increase to pay for necessary services for them; and, 9. client will not pay tax now to convert because they believe the baby boomers by virtue of their sheer numbers have such influence over Congress that they will be able to affect change to the retirement plan rules and convince Congress to make all pensions tax free.
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Avoiding Malpractice Claims Against Estate Planning Counsel Tuesday afternoon, January 9, 2007 Presenter: Kevin Rosen

Reporter: Alan Rothschild Esq. of Hatcher, Stubbs, Land, Hollis and Rothschild, LLP in Columbus, Georgia

Opening thoughts: Juries predisposed against attorney In conflicts of interest area, if there is any uncertainty, situation will be construed against the attorney. Client identification is key. No such thing as the family lawyer. The engagement letter is the key protection against malpractice in the estate planning area – who you do and don’t represent.

He noted that estate planning malpractice claims present unique problems because claims may not arise until years, or even decades, after the alleged malpractice occurred.

Privity – General rule is that attorney owes a duty of care only to the client with whom attorney stands in privity of contract. Starting in 1950/60’s, courts began to relax the privity requirement to malpractice claims by estate beneficiaries.

Lucas case (California Supreme Ct. 1961) allowed narrow exception to privity rule – six point, balancing of factors test: extent to which the transaction was intended to benefit the plaintiff; forseeability of harm to plaintiff; degree of certainty of harm; closeness of connection between defendant’s conduct and the injury; policy of preventing future harm; and whether imposing liability placed undue burden on legal profession.

Florida-Iowa Rule – a narrower cause of action approach than the balancing of factors test. Also adopted in Colorado, Michigan and Wisconsin. Here, a beneficiary may maintain cause of action only if the client’s intent, as expressed in estate planning documents, was frustrated.

Strict Privity – In some states, lack of privity still acts as bar to legal malpractice claim against estate planning attorney by beneficiary – unless attorney acts with intent to harm.

When does duty to client end? Not as estate planning case, but cited Georgia case where court found attorney liable for not renewing UCC filing. Like conflicts, if unclear, will likely be construed against attorney. ABA suggests writing understanding when duty ends.

Cause of Action – where beneficiary has standing, must prove four elements:

1. existence of duty
2. breach of that duty
3. proximate cause – the breach must have caused the harm
4. actual injury

Examples of duty – to inquire as to heirs at law; prepare will in accordance with client's wishes; to advise correctly about legal implications; to know and research law.

Ten common risk situations in estate planning field:

Attorney naming himself/herself as fiduciary Requiring drafting attorney be engaged to represent estate Bond letter that attorney will advise estate Understanding duties and obligations as attorney for fiduciary Spousal and family representation Very old/ill testator & caregiver Estate administration – multiple clients Unauthorized practice of law – this area capturing attention of bar groups, plaintiff attorneys and criminal enforcement agencies, recent NC case where GA lawyer prosecuted for work for NC client. Actions post-mortem contrary to decedent's intent/actions Competency of client

Protections – Document, document, document – in writing, including extent of representation; testator's intent; issues discussed with client; research done. Contemporaneous documentation of research and advice may lead to "judgmental immunity" which is a key defense, allows for summary judgment and case doesn't go to jury.

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Charting A Course for Convenience or Incapacity - New Aids to Navigation in the Uniform Power of Attorney Act Tuesday afternoon, January 9, 2007 Presenter: Prof. Linda S. Whitton

Reporter: Alan Rothschild Esq. of Hatcher, Stubbs, Land, Hollis and Rothschild, LLP in Columbus, Georgia

The presenter of this session, Prof. Linda Whitton, Professor at Valparaiso Law School, is Reporter for the Uniform Power of Attorney Act. Large portion of the written outline was the November 27, 2006 version of the Uniform Power of Attorney Act with prefatory note and comments which is available at the NCCUSL website – http://www.nccusl.org/.

Reasons for uniform power of attorney effort raise competing interests - POA must be acceptable to those relying upon it, protect the principal from abuse, yet must also protect agent who takes actions on behalf of principal.

Greatest challenge – making acceptable to person/institution relying upon – they demand to be protected for doing so. Act contains protections for good faith acceptance of acknowledged POA (Section 119). Also contains protection for legitimate refusal to accept POA. No liability for refusing unacknowledged POA. Two alternative provisions in uniform act -- Alternate A (120(b)) contains six safe harbors for refusal. Alternate B provides only protection for refusal of non-statutory form POA.

Liability for unreasonable refusal (120) – time limits for decision to accept (7 business days); may not require additional or different form; liability for refusal to accept – court mandated acceptance/attorneys fees & costs.

Presently, unclear under most states' laws what fiduciary duty means in the context of a POA. The uniform act contains a list of default rules/duties (Sections 111-118) which can be altered through contrary language in the POA. Certain mandatory rules also in uniform act.

Any important concept is the protection of the principal's previously expressed choices (114). Standard for agent conduct is principal's expectations – best interest standard applicable only if expectations not known. Agent must cooperate with health care agent. Has to preserve estate plan to extent known and in principal's best interest.

Agent's authority continues after later court appointment of a fiduciary unless court limits or terminates agent's authority.

Protecting the principal – valid POA can be refused by person who suspects principal is victim of abuse. Generally, no duty to account, but a governmental agency with authority to protect welfare may request an accounting from agent. Unless POA states otherwise, spouse will cease to be agent upon filing of action to dissolve or annul marriage.

Hot powers – express language required in POA to create, amend, or revoke inter vivos trust, to make a gift (statutory limits in 217 unless POA specifies otherwise), change rights of survivorship, create or change beneficiary designation;

delegate authority granted to agent under the POA; waiver of principal’s right to be a beneficiary of a joint and survivor annuity, exercise of fiduciary powers that the principal has authority to delegate, disclaimer of property, including a power of appointment.

Questions: Is there HIPAA language for access of medical info? – yes, in109 & 213. Brokers require medallion guarantee, would this address? Yes, if state enacts, only acknowledgement required. Can agent do will for principal under uniform act? No.

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News From The Exhibit Hall - none tonight - this is already long enough

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Our on-site local reporters who are present in Orlando this year are Gene Zuspann Esq. of Zuspann & Zuspann in Denver, Colorado, Herb Braverman Esq. of Walter & Haverfield, LLP in Cleveland, Ohio, Merry Balson Esq.of Wade, Ash, Woods, Hill & Farley in Denver, Colorado, Paul Hood Esq. of L. Paul Hood Jr. (APLC) in Mandeville, Louisiana, Joanne Hindel Esq. of Fifth Third Bank in Cleveland, Ohio. Jason Havens Esq. of Havens & Miller PLLC in Destin, Florida. Alan Rothschild Esq. of Hatcher, Stubbs, Land, Hollis and Rothschild, LLP in Columbus, Georgia, and Kimon Karas Esq. of McCarthy, Lebit, Crystal and Liffman Co., LPA in Cleveland, Ohio. The editor again this year will be Joseph G. Hodges Jr. Esq, a solo practitioner in Denver, Colorado, who also is the Chief Moderator of the ABA-PTL List.

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GENERAL INFORMATION ABOUT INSTITUTE: Inquiries/Registration: Philip E. Heckerling Institute on Estate Planning University of Miami School of Law Center for Continuing Legal Education P.O. Box 248087 Coral Gables, FL 33124-8087 Telephone: 305-284-4762 / FAX: 305-284-6752 Web site: www.law.miami.edu/heckerling E-mail: heckerling@law.miami.edu ==========================================

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Brought to you by the ABA-PTL Discussion List Moderators.

# Report #2

A complete listing of the proceedings and speakers is available on **the Institute's Web site**

As we have done in January for the last ten 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 41th Annual Philip E. Heckerling Institute on Estate Planning that is being held January 8-12, 2007 at the Orlando World Center Marriott Resort and Convention Center in Orlando, Florida, a new venue for the Institute this year. A complete listing of the proceedings and speakers will be published here later and is also available on the Institute's Web site at http://www.law.miami.edu/heckerling.

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This Report contains coverage of the Monday afternoon session on Recent Developments - 2006 and the Tuesday sessions on GRATS vs. Installment Sales to IDGTs, Yesterday's FLP, and Succession Planning

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Recent Developments - 2006 Monday afternoon, January 8, 2007 Presenters: Steve Akers , Carlyn McCaffery and Lou Mezzullo , again utilizing the materials prepared by Richard B. Covey of Carter, Ledyard and Milburn and Dan T. Hastings of Skadden, Arps, Slate, Meagher & Flom.

Reporter: Paul Hood Esq. of L. Paul Hood Jr. (APLC) in Mandeville, Louisiana

Akers led off with a statement that estate tax repeal "is as dead as dead can be." He reviewed the various reform bills that have been introduced during the past year. He expects to see little action until 2009 with exemptions in the $3.5-5 million range. Mezzullo predicted a rate of 35% and an exemption of $3.5-5 million range. McCaffery cautioned against defining bequests based upon definitions set out in the Code, which may well change substantially, and she reminded all to put property in trust as opposed to outright legacies because there may still be a gift tax without a substantial estate tax.

McCaffrey reviewed the 2006-2007 Treasury/IRS Priority Guidance Plan. She also reviewed the new private annuity trust proposed regulations under IRC Sec. 1001. She is anticipating comments to those proposed regulations that will suggest installment sale income tax treatment.

Mezzullo then reviewed the Pension Protection Act of 2006 provisions applicable to estate planning. The IRC Sec. 529 plan legislation has been made permanent. He also discussed the modified provisions pertaining to conservation easements under new Internal Revenue Code Sec. 170(h), which elevated the deduction limitation from 50% to 100% and that lengthened the carryforward period from five to 15 years for conservation easements.

He cautioned against making fractional interest gifts in artwork due to the limitation on the deduction of a retained interest in that artwork as well as the recapture provisions of the income and gift tax benefits.

Akers then discussed the Senda decision out of the Tax Court and the Eighth Circuit, principally the integrated transaction doctrine. In light of this decision, Akers cautioned against making gifts too soon after formation of the entity, but Mezzullo disagreed.

Akers then discussed the discount case: the district court decision in Temple v. U.S. He indicated various surveys, informal and formal, of discounts for FLP's with marketable securities that range from 25-40%, with discounts being curiously higher at the audit level as opposed to the appeals or trial level.

Akers then discussed the Rosen case, an IRC Sec. 2036(a)(1) decision. He cautioned all to make pro rata distributions. In Korby, there is an appeal to the U.S. Eighth Circuit in another FLP/IRC Sec. 2036 case in which the taxpayers lost.

The conversation then turned to the Fifth Circuit decision in McCord, which involved a gift of all of the senior generation's interests in the FLP. The panelists seemed to all be in agreement that transactions that look like the one in McCord will pass muster (although Mezzullo admitted that he has never used a defined value gift), despite the seeming lack of discussion of the public policy and other issues pertaining to defined value gifts. Mezzullo pointed out the new draft Form 706, which asks if the decedent ever owned or ever sold an interest in an FLP or LLC to essentially a grantor trust.

McCaffery then discussed the Focardi case, which held that the revocable spousal annuity was not a "qualified interest" for purposes of the GRAT rules under IRC Sec. 2702. She also discussed deferred payment GRATs and parallel GRATs as possible planning techniques, which, if drafted correctly, can provide GST Tax leveraging.

After the break, McCaffery then took up a discussion of the history of the GST Tax as well as some planning opportunities with respect to that tax, including using a GRAT, a sale of a GRAT remainder interest as well as a lifetime QTIP in connection with a GST Tax transfer to leverage the GST Tax exemption.

Akers then proceeded to discuss the few valuation cases there were in the past year, beginning with the Huber decision. In the Kohler decision, Akers pointed out that there was a $100 million difference between the value as stipulated by the taxpayer as opposed to that of the IRS. He emphasized how important it is to have a good appraisal and to shift the burden of proof to the IRS.  Mezzullo then discussed the Amlie decision.

Mezzullo discussed new Rev. Rul. 2006-26 in the area of IRAs being made payable to QTIP trusts, which replaces Rev. Rul. 2000-2 and that obsoletes Rev. Rul. 89-89.

The panel concluded with a discussion of patents on estate planning techniques.

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GRATs vs. Installment Sales to IDGTs: Which is the Panacea or are They Both Pandemics? Tuesday morning, January 9, 2006 Presenter: Jonathan G. Blattmachr

Reporter: Reporter: Paul Hood Esq. of L. Paul Hood Jr. (APLC) in Mandeville, Louisiana

Blattmachr led off by pointing out that he had a co-author of his Heckerling materials: Diana S.C. Zeydel of the Miami office of Greenberg Traurig, P.A. He cautioned all at the outset that it is virtually impossible to make an "apples to apples" comparison in comparing GRATs to installment sales to intentionally defective grantor trusts (IDGTs).

His materials begin with some general gift tax valuation principles and an observation that the GRAT works when appreciation exceeds the IRC Sec. 7520 rate. However, Blattmachr highlighted three exceptions to that general rule: (1) where a special or disparate valuation factor such as a blockage discount comes into play, (2) where GRAT assets experience large losses before even larger gains and (3) parallel GRATs.

Blattmachr compared the complexities of the GRAT to those of the installment sale to the IDGT, noting that different people find each technique more complex than the other. He pointed out two "basic" questions about GRATs: namely, how small can the remainder in a GRAT be (despite the Walton decision, Blattmachr doesn't zero out a GRAT-he creates a gift equal to .001 of the fair market value of the GRAT property) and how short a GRAT may last. He included language to assist with both of these uncertainties that he referred to as the "Zeydel formula".

Blattmachr cautioned all to observe the formalities of a GRAT, e.g., timely making the annuity payments, in order to avoid an IRS argument that the GRAT is disqualified, which would result in a gift of the entire value of the property put into the GRAT. He indicated that his firm offers clients a GRAT compliance service to make sure that the GRAT stays qualified.

He discussed some remaining issues pertaining to the viability of installment sales to IDGTs, namely, the applicability of IRC Secs. 2701 or 2702 to the technique, whether the IDGT assets are includible in the grantor's estate if the grantor dies while the note is outstanding, the effect of the techniques if it is not administered in accordance with its terms and whether gain is recognized by an installment sale of appreciated assets (Blattmachr emphatically says no).

Blattmachr went on to compare and contrast the two techniques where the grantor dies during the term of the GRAT/installment sale as well as some GST Tax differences between the two techniques. He then discussed the risks of an inadvertent gift with each of the techniques, which he pointed out could be ameliorated through the use of a defined value formula, creation of a 10% remainder or a disclaimer. His materials suggest that the risk of a large inadvertent gift may be greater for the installment sale to an IDGT than for a GRAT. He pointed out that the installment sale offers a lower interest charge (IRC Sec. 7520 rate as opposed to the IRC Sec. 1274 rate for installment sales) as well as a greater opportunity for leverage.

He introduced the concept of using a Monte Carlo simulation to assist in the comparison and design of either technique. Blattmachr makes several conclusions. First, he believes that a direct gift may be better than either technique if very significant appreciation is expected. Second, the installment sale may produce better results than a GRAT if return exceeds the IRC Sec. 7520 rate. Third, the installment sale may be better adept at capturing outperformance as well as for mitigating the effects of underperformance. Fourth, Blattmachr observed that the short term GRAT utilizing the 105 day payment delay rule can be more beneficial than the installment sale in some instances.

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"Yesterday's 'FLP': 'Fabulously Locked-in Profits'? Or 'Finally Losing Pizzazz" Tuesday afternoon, January 9, 2007
Presenter: Ronald D. Aucutt

Reporter: Reporter: Paul Hood Esq. of L. Paul Hood Jr. (APLC) in Mandeville, Louisiana

Aucutt began with a fair market value of FLP hypothetical. He made brief mention of a possible revival of the step transaction doctrine in Senda v. Commissioner, T.C. Memo 2004-160, aff'd., 433 F. 3rd 1044 (8th Cir. 2006). Aucutt then went through the "dirty dozen" IRC Sec. 2036 cases.

He then discussed the factual timeline in Bongard v. Commissioner, 124 T.C. 95 (2005), which was not appealed. Aucutt highlighted Judge Laro's "checklist" for why the transfer of assets to the FLP was not a bona fide sale for adequate and full consideration for purposes of IRC Sec. 2036(a)(1) in his opinion in Rosen v. Commissioner, T.C. Memo 2006-115, which IRS examiners and reviewers have essentially begun using as an audit checklist.

Aucutt set out some lessons from Estate of Strangi v. Commissioner (often referred to as "Strangi II"), T.C. Memo 2003-145, and his outline contains a list of the "badges" of a kind of retained interest and control. He discussed the uncertainties that clients have relative to the applicability of IRC Sec. 2036, and he reviewed possible legislative and regulatory preemption. Aucutt believes that Treasury has enough legislative authority to successfully deal with FLP's in IRC Sec. 2704(b)(4).

As possible options for potentially problematic FLP's, he suggested termination (but he cautioned against ignoring the income tax consequences) as well as having clients give up control of the FLP.

Aucutt concluded with a discussion of the applicability of IRC Sec. 2035 to interests in FLP's. He suggested limiting distribution powers in FLP's/LLC's to an ascertainable standard as a possible way around IRC Secs. 2035/2036.

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Succession Planning - The Need For Both A Belt and Suspenders Coordinating the Estate Plan with the Corporate Documents Tuesday afternoon, January 9, 2007 Presenter: Jonathan C. Lurie

Reporter: Gene Zuspann Esq. of Zuspann & Zuspann in Denver, Colorado

Mr. Lurie's presentation concerns the integration of the client's estate plan with Buy-Sell agreements and other corporate documents. Many problems arise because the attorney preparing the corporate documents and the attorney preparing the estate plan do not consult with each other and the results can be confusing or disastrous.

Some of today's presentation set out questions and issues, the answers to be presented at the breakout session tomorrow.

He cautioned that where both a trust agreement or estate plan and a buy-sell agreement (BSA) are in place, that the BSA must anticipate changes in the trustee or the beneficiaries. The trust must be drafted to take into account permitted transferees - parties that may receive stock or ownership in the business approved by the BSA. The BSA may specify the terms under which a trustee may continue to hold the business interest after the death of one of the parties.

He then discussed some areas that are often not addressed in the documents.

- How with the burden of death taxes be handled?

- May the estate defer taxes? The BSA may cause acceleration of taxes under §6166 because of a forced sale of business interests.

- If the tax allocation clause is not considered, a person not receiving the business may be burdened with the estate tax.

Marriage and domestic partnerships:

- There are often issues about ownership of the business between spouses. The spouse who started and operates the business may not own all of the stock and is often indignant that the other spouse must be involved in the negotiation and drafting of the BSA.

- Divorce should be one of the triggering events in a BSA. If the asset is S-Corp stock, one alternative is to make the spouse's stock non-voting. This still meets the one class of stock requirement in the S-Corp laws.

- The client should also be cognizant of the impact of a post death divorce - a possibility in some states. In some cases, the family business is dealt with in a premarital agreement.

- In QTIP trusts, the spouse must be given the right to make the assets in the trust productive. The BSA may cause a loss of the marital deduction if this is not provided.

The BSA must meet the Chapter 14 requirements.

The agreement must be comparable to other agreements negotiated in an arms-length transaction, it must not be a device to transfer property to the decedent's family for less than full and adequate consideration in money or monies worth, and it must be a bona fide business arrangement. Some issues that arise are whether counsel was consulted during the negotiation of the agreement and whether an appraiser was used to determine the value of the business.

The BSA may use a formula to determine value, but these must also meet the Chapter 14 tests. John recommends that you must involve experts to determine the operation and design of the formula and the agreement must be arms-length.

The agreement must be drafted taking into consideration the estate tax apportionment provisions that are applicable, either in the governing instrument or by statute. These can impact a party to the agreement that is not an heir or beneficiary of the decedent. Mr. Lurie said that some people suggest giving the buyer the right to participate in the audit negotiations, however, he suggested a better solution is to create a fund for the purpose of paying the taxes, possibly funded with life insurance. Also, another issue involves of what happens if the BSA is disregarded for estate tax purposes. The attorney must remember that the purchaser may not be involved in the estate tax audit.

He discussed the use of a trust protector. The trust protector would not act in a fiduciary capacity. The trust protector would have powers to change the trust, change the jurisdiction of the trust or change the trustee. The trust must provide for the compensation of the trust protector, as well as issues involving removal of the protector and replacement on resignation. The desire is to give the trust protector the powers needed to accomplish the client's goals without giving too much power. The document needs to provide a system of checks and balances.

In drafting the BSA, consideration should be given to requiring arbitration or mediation.

All BSAs should include an exit strategy. John likes the Biblical method - one party divides the assets into two pools and the other party chooses which pool of assets it will receive.

The attorney should realize that some plans provide for continued control of the business when a prudent person would not.

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News From The Exhibit Hall

All of the major players are here and all seem to have their usual space and configuration.

Thomson West has much of the center of the room.  They have a large area that has been decorated and includes a plush astro turf carpet.  Don Kelly is here and is demonstrating his IEP program.

Mark Gillette is here with the GEMS product that does everything but the Form 1041.

Vince Lackner is here with his 6-in-1 full line of estate administration programs, including the Form 1041.

WTP has several bays and a pretty good staff.  Nicole Splitter, (not her current name - she is remarried) is here and seems to be with WTP.  She was with U.S. Trust until it abandoned (sold) its software products.  Jonathan Blattmachr no doubt will be frequenting this boot to do demos of WTP, which is a HotDocs-based DAE.

Jane Shuck is still with Brentmark.  Natalie Choate mentioned during her presentation that she would be at the Brentmark booth, presumably to push sales of her book, Life and Death Planning for Retirement Benefits (6th Edition).

A problem with the configuration this year is that the attendees have no reason to pass by the vendors unless they specifically go to the exhibition area.  You arrive at the conference rooms before the exhibitor area and all refreshments are set up outside of the conference rooms.  The advantage of the Fontaine Bleu was that almost everyone walked through the exhibitor area several times a day.  We will be curious to see what the vendors have to say about this later this week.

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Our on-site local reporters who are present in Orlando this year are Gene Zuspann Esq. of Zuspann & Zuspann in

Denver, Colorado, Herb Braverman Esq. of Walter & Haverfield, LLP in Cleveland, Ohio, Merry Balson Esq.of Wade, Ash, Woods, Hill & Farley in Denver, Colorado, Paul Hood Esq. of L. Paul Hood Jr. (APLC) in Mandeville, Louisiana, Joanne Hindel Esq. of Fifth Third Bank in Cleveland, Ohio. Jason Havens Esq. of Havens & Miller PLLC in Destin, Florida. Alan Rothschild Esq. of Hatcher, Stubbs, Land, Hollis and Rothschild, LLP in Columbus, Georgia, and Kimon Karas Esq. of McCarthy, Lebit, Crystal and Liffman Co., LPA in Cleveland, Ohio. The editor again this year will be Joseph G. Hodges Jr. Esq, a solo practitioner in Denver, Colorado, who also is the Chief Moderator of the ABA-PTL List.

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**Heckerling Institute 2007**
Reports from the event, as posted to the ABA-PTL List Serve

# Report #3

Each report can also be accessed at any time from the ABA-PTL Discussion List's **Web-based Archive**

As we have done in January for the last ten 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 41th Annual Philip E. Heckerling Institute on Estate Planning that is being held January 8-12, 2007 at the Orlando World Center Marriott Resort and Convention Center in Orlando, Florida, a new venue for the Institute this year. A complete listing of the proceedings and speakers will be published here later and is also available on the Institute's Web site at http://www.law.miami.edu/heckerling.

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This Report contains coverage of the Wednesday sessions on Charitable Gift Planning, Estate Planning and Compliance after the Final GSTT Qualified Severance Regs, Current Issues Involving FLPs, Power of Attorney Forms and Private Trust Companies.

In addition, since this Report includes a report on the Kathryn Miree charitable law session, we are sending copies of this Report to the GIFT-PL and PG lists.

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Navigating the Landmines in Charitable Gift Planning: Legislation, Lawsuits and Personal Liability Wednesday morning, January 10, 2007 Presenter: Kathryn Miree

Reporter: Alan Rothschild Esq. of Hatcher, Stubbs, Land, Hollis and Rothschild, LLP in Columbus, Georgia

Kathryn Miree, a planned giving consultant based in Birmingham, AL, presented this Wednesday morning program on a variety of charitable gift planning issues. Kathryn opened by noting that the publicity of donor and exempt organization malfeasance and the related press, governmental and public reaction had greatly alternated the planning giving landscape over the last decade.

She reviewed the United Way/Aramony scandal in 1992 and its lingering impact; Hawaii's Bishop Estate; and New Era Philanthropy's pyramid scheme. Kathryn then summarized the series of Congressional hearings since June, 2004. She particularly noted the Senate Finance Committee's Staff Discussion Report issued just before the June, 2004 SFC hearings – the legislative agenda it contained and how many of its proposals that had already been adopted. These include the American Jobs Creation Act of 2004, which contained new rules on vehicle and intellectual property donations; the Katrina Emergency Relief Act that temporarily allowed cash donations up to 100% of AGI to public charities (but not, as a precursor to future legislation, donor-advised funds, supporting organizations or private foundations); and the Pension Protection Act of 2006 (discussed below).

The speaker then reviewed a number of charitable giving statistics, including Bank of America's 2006 Study of High Net Worth Individuals which found 98% of high net worth individuals give to charity, 16% had donor-advised funds and 20% have private foundations. Kathryn emphasized the size and amount of charitable giving, particularly by high net worth individuals, create a significant potential client base.

Miree then turned to a broad overview of the few benefits to charitable giving and a number of major reforms/restrictions on charitable giving and exempt organizations contained in the Pension Protection Act of 2006: · Most dramatic revision to charitable provisions of IRC since 1969 · Good news – three tax incentives (all of which expire 12/31/07) § Tax-free transfer of IRA to charity – only age 70 ½ and older eligible, capped at $100,000 year, only to public charities, not donor-advised funds, support orgs or private foundations § More favorable basis rules of gifts made by S corporations § Expansion of deduction limitations for conservation easements

Much greater bad news in the new law:

- Increase and extension of excise taxes – most private foundation penalties doubled; private foundation taxes on excess business holdings extended to donor-advised funds and many supporting organizations § Rules for easements in Historic Districts tightened § Limits placed on deductions for gifts of distressed clothes and property § New substantiation rules for gifts of $250 or more § New rules for gifts of fractional interests in tangible personal property – particularly damaging to museums

- Charities must report life insurance holdings

Other changes under PPA of 2006, including those impacting donor-advised funds and supporting orgs are to be covered in afternoon break out session.

The Treasury is also studying insurance ownership by charities; abuse and minimum distribution issues related to donor-advised funds and supporting organizations. Miree predicted that we have only seen the first wave of charitable legislation, more is to come. But at this point, somewhat surprisingly, private foundations look like a more preferred form of grant-making entity than donor-advised funds or supporting organizations – for example, they can make grants to individuals and pay reasonable compensation to family members.

Miree next turned her discussion to endowment gifts. As the numbers of large, permanent gifts have increased, so have the problems. Miree briefly discussed the Barnes Foundation gift and the Robertson – Princeton dispute, which to date has cost many millions in attorneys fees.

Although it won't avoid all disputes, Miree suggested a written gift agreement would avoid many legal problems and strained donor relationships. In her experience, only about 10% of endowment gifts are documented by a gift agreement. A well drafted agreement will address such issues as the donor's goals, a "Plan B" if the original purpose cannot be carried out, and standing to sue. On the standing issue, states are divide on the issue – some allow donor to file sue to enforce gift, others, consistent with common law, say the power is vested only in the attorney general. The present version of UMIFA (1972) does not really address. The recently adopted successor law, UPMIFA, contains greater flexibility in the release or modification of endowment funds, it is still no substitute for a gift agreement.

Finally, Miree shared her views on post-gift liability for the management of charitable gifts. She noted that 38% of charitable remainder trusts name individual unrelated trustees and 18% name family members. In her experience, CRT's are rarely administered properly by individuals, just as private foundations often operate incorrectly, such as paying for charitable dinners. She suggested planners consider naming corporate trustees more frequently for charitable trusts to ensure the complex rules are followed.

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Estate Planning and Compliance after the Final GSTT Qualified Severance Regs Wednesday morning, January 10, 2007 Presenter Pam Schneider

Reporter: Kimon Karas Esq. of McCarthy, Lebit, Crystal and Liffman Co., LPA in Cleveland, Ohio.

The topic was to address the final or reproposed regulations regarding qualified severance. Since no regulations had yet been issued Ms. Schneider discussed the interplay between GST planning and charitable planning.

Ms. Schneider started her presentation with an overview of the GST definitions which are important in understanding and planning with the GST provisions.

Interest in a trust. A charity has an interest in a trust if it has a present right to receive income or corpus from the trust or if it is the remainder beneficiary of a qualified charitable remainder trust or a pooled income fund.

Skip persons. A trust is a skip person only if persons with interests in the trust are skip persons (individual assigned to a generation that is two or more generations below that of transferor) or if no persons have interests in the trust and no distributions can be made from the trust to non-skip persons. A charity is a non-skip person.

When dealing with trusts, the skip person rules relating to trusts, rather than that of individuals applies, even if the individual has the absolute right to withdraw trust property. Trust is not definitively defined for GST purposes and can include any arrangements (except estates) that have the same effect as a trust, such as life estate, remainders, estate for years, insurance and annuity contracts. Ms. Schneider identified certain split interest arrangements that are not trusts which could create traps where there are transfers to skip persons such as charitable gift annuities or gifts of remainder interests in personal residences. What is not answered is where the tax is paid from in those cases.

Ms. Schneider next reviewed the inclusion ratio requirements. The inclusion ratio is 1 minus the applicable fraction. The numerator being the GST exemption allocated the transfer and the denominator being the value of the property transferred. Ms. Schneider cautioned that with charitable transfers the denominator is reduced by estate or gift tax charitable deductions chargeable to the property.

Ms. Schneider posited whether a late allocation can be made. She suggested that it may be a possible planning opportunity with a high unitrust or annuity trust payment where the value of the trust is expected to decline prior to the GST event occurring.

Ms. Schneider discussed charitable lead trusts. A charitable lead trust will never be a skip person and hence no direct skip can be made to it. On the termination of the lead interest a taxable termination or distribution will probably occur. If no particular charity is entitled to the lead interest, arguably no one had an interest during the lead period and thus there was no interest to terminate and thus a taxable distribution occurs on the distribution to the skip person. This was the result in the Robertson v. U.S. case. The significance of the Robertson case is that the trust terminated in 2001 but the distribution was not made until 2002. Because GST rates fell between the years in question (55% v. 50%) there was considerable GST savings if the result were that the termination was treated as a taxable distribution in the year of the distribution

The issue centers around when the distribution is deemed to have occurred, when the beneficiary becomes entitled to the property or when actual distribution is made? Ms. Schneider citing Reg. Section 26.2612-1(f), Ex 13, states the time of the distribution controls.

Ms. Schneider suggests as a planning alternative in designing non-GST exempt charitable lead trusts terminating in favor of a skip person it is advisable not to designate a particular charitable beneficiary and to continue the trust property in trust with discretionary distributions to skip persons (and authority to make direct payments of medical and tuition expenses).

GST allocations are made to charitable lead unitrusts at the time of the initial transfer whereas with lead annuity trusts one cannot determine the GST amount cannot be determined until the end of the lead period. The denominator is the value of the property at the end of the lead period and there is no credit for the charitable deduction.

Can there be a negative rate? No, if the fraction results in a negative the result is a zero inclusion ratio. Can the negative rate be purged by adding property or combining trusts? Ms. Schneider believes that is possible to add property to the trust to get to a zero value.

Ms. Schneider compared GRATS with CLAT. A CLAT is not subject to ETIP so she suggests a client charitably inclined client should consider a CLAT to replace charitable gifts the client might otherwise make.

Choice between CLAT or CLUT. No easy answer. CLUT advantages are inclusion ratio can be determined and the charity shares in appreciation and depreciation in the assets. The advantage to the CLUT is the family benefits from growth (detriment of depreciation).

Ms. Schneider concluded with a discussion of combining charitable planning with ensuring funds for the education and health of descendants. She discussed Section 2611(b) the exclusion for transfers that if made by an individual during life would not be treated as gifts under Section 2503(e) relating to transfers for tuition or medical expenses.

Suggestions were

1) giving an interest in a trust to a charity or

2) making sure that no one has an interest in the trust initially and that the only distributions from the trust that can be made are to skip persons in the same generation and to charities.

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Current Issues Involving FLPs and LLCs Wednesday afternoon, Special Session 1-A, January 10, 2007 Presenter: John Porter

Reporter: L. Paul Hood Jr. (APLC) in Mandeville, Louisiana

Porter began by emphasizing that preparation for the transfer tax dispute begins in the estate planning phase. He reviewed the various arguments that the IRS has used or is using to battle FLP's.

The first argument was lack of economic substance. Porter noted that the IRS really doesn't make this argument much anymore, especially where the FLP is validly created and validly existing under state law after the Tax Court's decision in Strangi II.

The second argument was IRC Sec. 2703. Porter pointed out that the IRS was using this argument now, especially where the FLP agreement contains a buy-sell or right of first refusal provision. Porter informed all that he tried a case last spring that is awaiting decision, Holman v. Commissioner, Docket No. 007581-04, that involved a right of first refusal. The facts involved a Minnesota entity. Porter used a Minnesota lawyer as an expert to testify that the terms of the right of first refusal are commercially comparable. The IRS countered with a Minnesota law professor as its expert witness.

The third IRS argument was gift on formation of the FLP. Porter noted that this argument went back to the 1997 TAMs, and he further noted that the IRS made this argument (in the form of the integrated transaction argument) in both Shepard and Senda (where there was eight days between formation of the FLP and the gift). He advised that good formation facts (partners take back proportionate interests, capital accounts are maintained and liquidation was to be made in accordance with capital account balances) pretty well defeat the gift on formation argument. Porter stated that the IRS really is not using this argument much anymore, except in egregious situations. He offered a number of suggestions to avoid this argument. First, he suggested maintenance of contemporaneously prepared financial records to reflect the initial capital accounts and to not wait for the initial FLP income tax returns. Second, he suggested waiting six months to one year between formation of the FLP and gifting of FLP interests, although he agrees with Lou Mezzullo that waiting one day between formation/funding and gifting should be sufficient.

The fourth IRS argument was IRC Sec. 2036(a)(1), which Porter observed almost always involve bad operational facts and some bad formation facts. He reviewed the "badges of IRC Sec. 2036(a)(1)," all of which deal with whether the parties respected the separate existence of the FLP during the decedent's lifetime, namely (1) commingling of FLP assets with personal assets, (2) non pro rata distributions, (3) delay in funding the FLP, (4) the inclusion of personal use assets in the FLP, (5) the percentage of the decedent's assets that went into the FLP, (6) the discretion of the GP in making distributions from the FLP and (7) post-death operation of the FLP relative to the payment of administrative expenses and death taxes out of the FLP property. Porter stated that he doesn't like distributions from the FLP to pay taxes or administrative expenses, and he also doesn't recommend redemptions of FLP interests to pay those items or collateralizing FLP assets to pay those items. He said that borrowing on commercially reasonable terms is fine.

Porter then discussed the bona fide sale for full and adequate consideration in money or money's worth exception. He noted that satisfaction of the full and adequate consideration prong can be met by meeting the three gift on formation steps discussed above. The "fight" is in the bona fide sale prong. He discussed the Bongard decision, which he tried. Porter suggested having the junior generation be the GP or at least have an interest in the GP. He also suggested "peppering" the file with non-tax reasons for creating the FLP. He observed that since the estate planning attorney likely will be a witness, the client will have to waive the attorney-client privilege.

The final IRS argument that Porter discussed was IRC Sec. 2036(a)(2), which the IRS asserts where the senior generation retains control over distributions. He offered the following tips to assist in avoiding IRC Sec. 2036(a)(2): have the FLP agreement contain affirmative fiduciary duties, prohibit unilateral decisions being made by the senior generation and have the FLP agreement contain ascertainable standards relative to distributions.

He noted that there is no substitute for quality appraisals and that all FLP/IRC Sec. 2036 cases are Appeals coordinated cases, which has had the effect of some cases settling more favorably at the audit level than at Appeals (when it usually is the other way around).

Porter concluded with a discussion of the McCord decision out of the Fifth Circuit. He believes that, contrary to the opinion of many commentators, the Fifth Circuit inferentially took on Procter and Ward in its opinion. Porter also believes that the IRS will continue to push its Procter/Ward argument in circuits other than the Fifth Circuit. He stated that he has a defined value disclaimer case pending in the Tax Court.

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One Size fits all - Tailoring a Form Power of Attorney to Meet Individual Needs Wednesday afternoon, Special Session 1-D, January 10, 2007 Presenters: Prof. Linda Whitton and Prof. William LaPiana

Reporter: Gene Zuspann Esq. of Zuspann & Zuspann in Denver, Colorado

This report summarizes the breakout session. Alan Rothschild reported on the initial session that occurred on Tuesday.

The breakout session included a discussion of the statutory form, followed by numerous questions and comments by the audience and a short discussion of the hypotheticals set out in the materials.

Both Linda Whitton and Bill LaPiana were on the drafting committee for the Act.

The first issue discussed was the inclusion of a proposed form in the Act. The drafters feel that the option is necessary but worry that the lay person will execute a form power of attorney without advice or counsel and include something that may not be appropriate in the circumstances. Linda said “This is a very lay person area.”

The drafters did not want to encourage co-agents. Feedback from a number of attorneys and others was that there are many problems in using co-agents. Linda said that the form omitted this option but that it would be simple for an attorney to add language to authorize co-agents. The important information section at the start of the form indicates that co-agents are possible and the special instructions section should contain these provisions.

Linda reiterated that, by using the statutory form, that the Act is incorporated. If an attorney prepares a custom form, the form must also either incorporate the provisions in the Act or set the desired powers out in the form.

The statutory form and the Act make the POA effective immediately. If the principal wants a springing power, language will have to be added. Linda indicated that she used to prefer springing powers but over the years, has changed her mind.

Some other provisions discussed:

1. If the agent is not an ancestor, spouse or descendant of the principal, then the agent may not benefit other than through compensation.

2. The agent must accept the appointment. This may be done in writing, or by acting under the power of attorney. The principal can execute the power of attorney and hold it for delivery later. In this case, the acceptance of the agent is not necessary until such future time that the appointment is accepted.

Linda reviewed the default provisions in the Act in detail. These are:

1. The POA is durable.

2. It is effective when executed.

3. A spouse-agent’s authority terminates upon filing for divorce, annulment or separation. She said that this is a default rather than a mandatory provision because elder lawyers advised that sometimes divorce is used for purposes other than

the separation of the spouses.

4. Lapse of time does not affect validity.

5. Successor agents have the same authority as the original agent.

6. Successor agent may not act until all predecessors are no longer acting.

7. An agent is not liable for the actions of another agent.
8. An agent is entitled to reimbursement of expenses and reasonable compensation.

9. An agent must accept the appointment in some manner.

10. An agent has default duties - loyalty; not to create a conflict of interest that impairs the ability to act, act with care; competence and diligence and others.

11. Duty to account if a court order or request by the principal.

12. The method of resignation.

She also reviewed some options

1. Acknowledgment of the principal's signature

2. Nomination of conservator or guardian

3. Springing power and authorization of person who will determine that triggering event

4. Appointment of co-agents

5. Exonerations provisions

6. Grants of general authorities

7. Grants of authority for extraordinary acts

8. Special instructions Some of these are recommended, some are not, and some are neutral.

Much of the rest of the presentation involved questions or issues raised by the audience.

There were questions about using springing powers and triggers. Linda pointed out the comments to section 109 and she and Bill discussed the information in the comments. One person suggested the use of an escrow letter.

Linda made it clear that she expects this form to be expanded or modified as necessary.

Several people asked questions about having the attorney serve as the agent. Bill felt that this creates a significant conflict of interest. Linda suggested that the attorney should either act as the attorney or as the agent, but never as both.

One person pointed out that there is no place for a signature for the agent. This was intentional because the principal may not want to deliver the form to the agent at the time of execution.

Bill indicated that NY is working on a form. He indicated that the agent may sign at any time. He also said that the NY form would include a specific lecture to the agent.

Any person may act as the agent, i.e. a corporate fiduciary.

A short discussion of some hypotheticals followed. One duty of the agent is to attempt to preserve the estate plan of the principal. The drafter of the form needs to be careful in allowing gifts by the agent and powers to change or create the estate plan.

Another issue, involved in a domestic partnership, is when does a DP end? In a marriage, it is easy to determine when the marriage ends and when an action is filed to terminate the marriage. This may not be so clear in a domestic partnership and depends on the law of the state.

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When Trusts are Not Enough - Strategic Family Plans Also Require a Strategic Structure: The Private Trust Company
Wednesday afternoon, Special Session 1-E Presenters: John Duncan, Michael Conway, Bryan Dunn and Sarah Hamilton

Reporter: Joanne Hindel Esq. of Fifth Third Bank in Cleveland, Ohio

John Duncan started the presentation by describing the fact that ultra-wealthy families, those with hundreds of millions or billions of dollars of wealth, are setting multi-generational goals and creating strategic plans for achieving them over 50, 100 or more years. The goals include preserving and maximizing not only a family's financial capital but also its "human", "intellectual" and "social" capital down through the generations.

John described "human capital" as the well-being (health, happiness, comfort etc.) of family members together with the human potential each person presents. Intellectual capital is the knowledge necessary or useful to help the family, other people and society as a whole.

Sara Hamilton then discussed the challenges facing multi-generational families and said that when significant family wealth last beyond the founder's life-time, generational planning often spans more than 100-year time periods and requires sophisticated operating and governance structures to implement strategic family goals.

Holding a family enterprise together means addressing the family's unique business heritage; preserving the family's financial success; investing in the development of future generations; working together in a meaningful way and giving back philanthropically.

She reviewed how financial families typically work together to accomplish 5 goals:

* Business Ownership and Control: A continuation of family business leadership and control

* Wealth preservation and enhancement: Growing the purchasing power of wealth as fast as the family grows

* Financial security: Supporting the lifestyle of current owners and ensuring the financial security for future generations

* Family Continuity: Preserving the family history/reputation and building strong personal relationships

* Family Philanthropic Legacy: Reinforcing family values and giving back in meaningful ways. She described the profile of a typical financial family as one with more than $500 million in assets, 2nd to 4th generations in existence; 22 adult households, 46 family members and 101 legal entities, primarily trusts. She also stated that this typical family has 53 family advisors consisting of 12 members of a family office staff, 14 family member trustees, one corporate trustee and 26 other external advisors.

She then described the shared risks that threaten the longevity of the family enterprise and discussed strategies to mitigate the risks as reviewing how the family: * structures the ownership of assets

* manage shared ownership

* organize group decision-making

* engage future owners in the process

* manage family transitions

* invest family capital

She finally discussed the most important financial family goals regarding trusts:

* Institutionalize the beneficiary's voice at the planning table

* Ensure alignment of interests in support of long-term family goals

* Invest in educating younger generations to be responsible owners

* Establish an effective governance/decision –making process

* Bring professionalism to the trustee process

* Eliminate personal trustee liability

* Restructure trust instruments as needed to accommodate branch differences

Byran Dunn then posed a case study for the audience by describing the family situation of the Grimm Brothers and their business Grimm Brothers Fantasies, Inc.

Bryan and John applied some of the principles and issues outlined above to the Grimm Brothers situation.

After describing how many families' strategic structures consist of either a patriarch/matriarch and/or informal family collaboration or a sophisticated family office, John then discussed the advantages of using a Private Trust Company. He described how a PTC is a perpetual entity that is legally qualified to act as trustee of family trusts and is owned, controlled and serves a single family and its trusts, affiliated companies and charitable organizations.

As a regulated trust company, the PTC may act as trustee with full control over family fiduciary assets and exercise comprehensive financial services powers to provide a full range of family investment and other financial services.

He also pointed out that the PTC's powers, family control and inherent risk management assure effective implementation of governance decisions and perform its tasks without exposing the family or assets to undue risk.

John also described how a family charters a PTC with the primary goal of providing a qualified permanent successor to the current trustee of the family trusts. In addition, a PTC may enable a family to a) promote and encourage participation by family members in the family businesses; b) aggregate the management of family wealth in order to find high quality, responsive and flexible financial services at a competitive cost; c) improve fiduciary risk management by using a corporate hierarchical structure with appropriate committees, professional executives and other employees; d) obtain the benefits of regulatory supervision of trustees by a state banking department; e) hire and retain executives and directors without asking them to assume an unreasonable level of personal risk.

The final presentation was made by Michael Conway who discussed the tax challenges and opportunities of PTCs:

Most family-owned PTCs permit and encourage the involvement of family members on their board of directors and committees. In order to avoid adverse tax consequences, firewall procedures should be established so that no grantor or beneficiary should be in a position to control, directly or indirectly, discretionary distribution decisions or the beneficial enjoyment of a related trust while allowing family members to participate as fully as possible in the management of the PTC.

The appointment of a properly structure PTC should not result in the grantor trust treatment of any Family Trust for income tax purposes if the Family Trust was not already taxed as a grantor trust.

The appointment of a properly structured PTC, in and of itself, should not result in the inclusion of the value of any Family Trust in the estate of a grantor for estate tax purposes.

Also, the appointment of a PTC as trustee of a Family Trust is an administrative change and should not be considered a shift of beneficial interest, a modification or a constructive addition under the GST Tax Regulations and should not adversely affect a trust's status as exempt from the GST tax.

All the presenters did an excellent job of laying out the uses and benefits of Private Trust Companies and included very valuable written materials for the audience to use as well.

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Our on-site local reporters who are present in Orlando this year are Gene Zuspann Esq. of Zuspann & Zuspann in Denver, Colorado, Herb Braverman Esq. of Walter & Haverfield, LLP in Cleveland, Ohio, Merry Balson Esq.of Wade, Ash, Woods, Hill & Farley in Denver, Colorado, Paul Hood Esq. of L. Paul Hood Jr. (APLC) in Mandeville, Louisiana, Joanne Hindel Esq. of Fifth Third Bank in Cleveland, Ohio. Jason Havens Esq. of Havens & Miller PLLC in Destin, Florida, Alan Rothschild Esq. of Hatcher, Stubbs, Land, Hollis and Rothschild, LLP in Columbus, Georgia, and Kimon Karas Esq. of McCarthy, Lebit, Crystal and Liffman Co., LPA in Cleveland, Ohio. The editor again this year will be Joseph G. Hodges Jr. Esq, a solo practitioner in Denver, Colorado, who also is the Chief Moderator of the ABA-PTL List.

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GENERAL INFORMATION ABOUT INSTITUTE: Inquiries/Registration: Philip E. Heckerling Institute on Estate Planning University of Miami School of Law Center for Continuing Legal Education P.O. Box 248087 Coral Gables, FL 33124-8087 Telephone: 305-284-4762 / FAX: 305-284-6752 Web site: www.law.miami.edu/heckerling E-mail: heckerling@law.miami.edu

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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 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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**Heckerling Institute 2007**
Reports from the event, as posted to the ABA-PTL List Serve

# Report #4

A complete listing of the proceedings and speakers is available on **the Institute's Web site**

As we have done in January for the last ten 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 41th Annual Philip E. Heckerling Institute on Estate Planning that is being held January 8-12, 2007 at the Orlando World Center Marriott Resort and Convention Center in Orlando, Florida, a new venue for the Institute this year. A complete listing of the proceedings and speakers will be published here later and is also available on the Institute's Web site at http://www.law.miami.edu/heckerling.

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Eratta: Tuesday morning "Free" Life Insurance by Stephan Leimberg - here is a correction from Reporter Kimon Karas: In the 2nd full paragraph above recent developments, in the third sentence, the word "investor" should be "insured."

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This Report contains coverage of the Wednesday morning Question and Answer sessions

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Question and Answer Session Wednesday morning, January 10, 2007 Panelists: Steve R. Akers (SA), Carlyn S. McCaffrey (CM) and Louis A. Mezzullo (LM)

Reporter: Merry H. Balson, Wade Ash Woods Hill & Farley, PC, Denver, Colorado

This session was presented by a panel of Steve Akers ("SA"), Carlyn McCaffrey ("CM") and Lou Mezzullo ("LM"). The questions, comments and answers were as follows.

Q: Given the disparities among the states relating to the repeal of the state death tax credit, it seems that states (governors or state estate tax administrators especially) have not lobbied as heavily as they might. The suggestion in the question (which seemed to be more of a comment) was that the state lobbies should be able to impose on Congress to reinstitute the state death tax credit at the federal level. A: SA thought that might be effective, and that the states have been taken the impact of this repeal and have done little to lobby for reinstatement. The problem is that reinstatement would have a huge impact on federal revenue. None of the panelists have seen this issue in any of the reform discussions.

Q: Does a charity have to be taken into account for purposes of determining whether there is a designated beneficiary for retirement plan purposes where the beneficiary designation states that the charity is the beneficiary only if a child does not reach a certain age? A: Yes. Charity would be taken into account and there would be no designated beneficiary. LM referred to PLR 200228025 in which an IRA was payable to a trust for the benefit of minor children, which terminated when a child reached age 30. If children died before age 30, an uncle, age 67 was to take. The IRS ruled that the uncle was the designated beneficiary because he was the oldest beneficiary. Natalie Choate's special session program may cover this issue in more detail.

Q: What is the preferred method for creating an intentional grantor trust (aka defective grantor trust) that avoids estate tax inclusion? A: LM said that the right to substitute assets is used frequently, although there is no authority on point to authorize this, and there may be an issue with reacquiring assets, so he suggests using another method to make the trust a grantor trust. There are varying preferences on this issue, but LM likes to give an independent person the right to add beneficiaries (e.g., spouses of descendants who are already beneficiaries of the trust, or charitable organizations where the client is already charitably inclined). CM mentioned that some would disagree on LM's conservative approach, and although there is no specific authority on the ability to reacquire assets being a 2036 problem, Jordahl says if the power is held in a fiduciary capacity, there is no problem. Most estate planners agree that so long as the grantor is required to use assets that are equal in value to those exchanged there should be no 2036 problem. SA noted that in Jordahl it was not that the person had the power in an absolute fiduciary capacity, but that they acted in fiduciary capacity and exchanged assets for fair market value. There was a recent PLR along these lines where the IRS refused to rule unless the power was held in a fiduciary capacity. SA agreed that as along as fair value must be given, it would be tough to say there is a 2036 problem. LM disagrees because a grantor could substitute illiquid non-income producing real estate for a liquid income producing CD affecting the character of the property, but CM believes there is only a problem if the trustee is prohibited from selling the real estate and reinvesting it. SA likes to use related persons as trustees, but noted that if a spouse is the third party with power to substitute assets then there is definitely a reacquisition problem because powers held by a spouse are deemed to be held by the grantor, plus if the spouse dies, you need to have a backup provision to retain grantor trust status.

Q: CM was asked to review the example of a sale of a remainder in a GRAT to a grantor trust. A. Grantor establishes a 20 year GRAT funded with asset worth $20M, the annuity payment is $12,100 and is scheduled to increase by 20% each year, with the remainder to pass to a separately funded existing grantor trust. If the assets increased in value by 20% during the GRAT term, at end of the term there would be $2.4M in the GRAT, and the present value of the remainder interest, assuming a 5.6% 7520 rate, would be $1.15M. The grantor could either purchase the remainder interest at its $1.15M present value with the consent of the trustee, or if he had the power, could substitute assets and reacquire the remainder interest, protecting the $1.15M from the mortality risk of the grantor dying before term has ended. To use this technique the GRAT must be drafted without a spendthrift clause and you need a separate beneficiary (here the separately established grantor trust) to deal with. The risk is that the IRS may characterize this as a form of commutation which is prohibited by the regulations. The risk disappears if the transaction occurs after the statute of limitations has run following the reporting on a gift tax return.

Q. Questioner understands that Revenue Ruling 77-454 does not seem to apply to a Walton GRAT, is this correct, and if so what does it mean? A: CM reminded us that Rev. Rul 77-454 establishes a limit on an annuity. The payments are set above the 7520 rate unless the fund is large enough to last up to 107th birthday of the annuitant. The value of the annuity has to be the value of the right to receive the annuity for the lesser of a term or the life of annuitant. The revenue ruling does not apply to a Walton type GRAT because it is payable for fixed term, and you do not need to take life expectancy into account.

Clarifications SA: SA clarified the Focardi (sp?) case, where they used a baseball arbitration approach for valuation. The theory is each party will be more reasonable because a third party will select one of the suggested appraisals. SA had previously said that the Tax Court is the one making the determination here, and when in fact, the field agent and the taxpayer agreed to select 3 appraisers each, and a 3rd party selected one of those appraisers. You may want to use this as a strategy or settlement opportunity in audit.

Update by SA: SA received an update on the Senda argument, relating to the integrated transaction. Theoretically, 1 day between formation and gift should be enough time to prevent the step transaction argument, so long as you make it clear the asset went into entity before the gift. SA had mentioned the Holden case, where the gift was made 8 days later and was rejected, and another case where the gift was made 8 months later and was rejected. The IRS agent in the Holden case argued that no discount applied because there was an undivided interest in the asset. That will be appealed to the Tax Court. The lesson here is that while analytically 1 day should be sufficient, the IRS is making these arguments. LM mentioned that other abusive factors may have been involved, and until we know all the facts he would not be concerned. SA noted that one question in the audit that has not been seen in the past was what attorney set up the transaction and how much the attorney was paid. LM, as the Chair of the business planning committee of ACTEC had appointed a subcommittee to develop an FLP checklist, but after it was created, he decided he did not want that checklist in the client file as it may be viewed as evidence of a purpose to save taxes. He noted that the Church case had a substantial nontax purpose, but the formation mechanics had many problems, yet the Court held 2036(a) did not apply.

Q: If you file a gift tax return when creating a grantor trust doesn't that imply a gift was made? A: LM said it does not, and it is simply notification of the transaction. Incidentally, there may already be a reportable gift of seed money in these transactions.

Q: CM was asked to walk through the steps for a deferred GRAT. A: When the GRAT is created, usually payments start in the first year. If you expect there may be liquidity problems with the assets in the GRAT in early years, one way around this is to create a long term GRAT, with increasing payments at 20% per year so you have small payments up front. A better solution yet is to provide that payments do not begin for a certain period of time (usually short term, e.g., 3 years). Section 2702(b) says you will have a qualified interest if there is a right to receive payments not less frequently than annually, but says nothing about when the payments must start. The GRAT regs require payments be fixed and ascertainable, for life, a period of years, or the shorter of the two, but says nothing about when the payments must start. Regulation section 25.2702-3(d)(2) states that the annuity must be paid to or for the benefit of the holder with the exception of certain contingencies. One exception permits a survival contingency which seems to implicitly sanction deferred GRATs. CM is not aware of these kinds of GRATs coming up on audit as of yet, but suggests it is an appealing strategy.

Q: If a client has a GRAT where the trustee failed to make annuity payments within 105 days, what is problem and what does CM recommend to cure the problem? A: The problem is the IRS may take the position that the failure to make the payment within the required period violates the regulations and may argue this goes to intent to make the payments. There is no authority supporting this position in the GRAT area, but there is some authority in the CRT arena. The IRS has held that a CRT was not a qualified CRT from the outset when payments were not made in time. What can you do if payments are not made timely? The best approach is to have the GRAT pay the client ASAP and memorialize why the payment did not occur so that there is some evidence of an honest mistake. CM suggests considering paying interest on the payment as well.

Q: Is there an adverse effect on the marital deduction if assets in an FLP that are pulled back into the estate at full value under 2036? A: SA stated that the theory here is that 2036 could to include the full value of the FLP in the estate, while the marital deduction is given only for the discounted value, resulting in a potential estate tax due on the 1st death. In the Bongard case, where a gift of a 7% LLC interest to a spouse was brought back into the decedent's estate under 2035, the Trial Court raised the question of whether the IRS could allow a marital deduction for the full value, not just the discounted value. Similarly, in the Korby Estate, the issue was raised when husband and wife, both of whom had contributed to an FLP, died, and prior to litigation, the parties stipulated that if only 32% of assets would be included in the wife's estate then no marital deduction would be allowed. There are other anticdotal cases raising this issue as well. What can be done? One option is to undo the partnership if before the alternate valuation date so that you value the assets of on the alternative valuation date at the full value, removing the argument. LM noted that if you dissolve, you concede the issue up front, before you even know if there will be an audit. He also noted that the marital trust can be disqualified if the value under the buy-sell agreement differs from the fair market value (See the Renaulti (sp?) case).

Q: If a client has a 2036 issue with an FLP or LLC what is the recommended course of action to divest control over the entity? A: LM stated that 2036(a)(2) should not be a problem if Byrum is still good law and you have not negated the fiduciary duty the general partner has, particularly if you have other owners who hold an interest that is more than de minimus (in Strangi third parties owned only a .53% interest). Question is whether controlling interest should be gifted implicating 2035 by the release of power, or should the controlling interest be sold. If there is a sale, the question is what is full and adequate consideration. Cases have held that full and adequate consideration is the actuarial value of the interest in property. However, the property could be more valuable, or could be worth less than that value, so LM would not stake his license on a sale. Another option is to collapse the entity and form a new entity where the grantor does not hold a controlling interest, however, there are income tax consequences on liquidation, the 3 year rule would probably apply because grantor is giving up a right to control enjoyment of income, and the IRS might treat this as a step transaction and exchange of interests. CM noted that Pam Schneider came up with a solution to the problem of determining the what has been given away. Pam suggests that you could amend the partnership agreement to provide that anyone could withdraw at any time, eliminating the valuation discounts. The trustee of a children's trust could then sell the interest to the transferor for the nondiscounted amount. The client's estate is depleted by the nondiscounted amount, and she gives up the discount on the portion transferred to the trust, but she achieves protection for the amount given to the children. SA mentioned that in the December Trusts and Estates Magazine, an article suggests that the spouse could have the unilateral power to cause a liquidation of the partnership, so that the spouse can receive an interest that is undiscounted. CM noted that this not only solves the problem, but also gives the spouse a full step-up in basis of the underlying assets. LM note that in 2006 he was an expert witness in a case where a bank trustee of two QTIP trusts holding marketable securities was sued by adult children remaindermen asserting the bank had a duty to create an FLP to reduce the value of the widow's estate, even though widow did not want an FLP. SA mentioned the Texas Supreme Court held that there was no absolute privity, opening claims against the attorney by beneficiaries, where an FLP was not formed.

Q: Has the IRS taken the position that an original discount should not be available when FLP assets are transferred to a GRAT on a discounted basis, and an independent trustee later redeems the interests in exchange for the capital account such that the GRAT then holds undiscounted marketable securities? A: CM was not sure whether this has occurred and not aware of any specific authority to support this position, but she believes this could be a problem on an audit. This could be viewed as an understanding between the parties if it is too easy to get the assets out of the GRAT, and it is a significant risk.  LM noted that a PLR in the 1990s the IRS required a discount be taken, but he has not seen any rulings on this point since.

Q: Can the IRS use the Fontana case to aggregate a decedent's property with an interest held under a GRAT such that decedent is deemed to own a majority interest, rather than 2 separate minority interests?   A: In Fontana decedent owned an interest in a family entity, and was the beneficiary of a trust owning the same interest.  CM stated the issue was whether the interests should be aggregated, and the Tax Court determined they should be, based on the decedent's actual control over the stock through a power of appointment.  There is no similar control in a GRAT, but some GRATs do give the grantor a power of appointment over assets includible in the estate if the marital deduction does not apply.  In that case, Fontana would be on point and would aggregate interests.  However, if there is no power of appointment there should be no problem.  She noted Revenue Ruling 79-7 dealt with section 2035 and whether an interest in an entity owned by the decedent should be aggregated with an interest in an entity he had given away within 3 years of death.  That ruling held that the interests would be aggregated even hough the decedent had no control because the purpose of 2035 was to treat the asset as if it had not been given away.  It is unclear whether this would apply to 2036, but CM would not be surprised if the IRS took that position.  LM noted that in Bonner, there was no aggregation of a QTIP's interest with a spouse's outright ownership, but one of the reasons was that assets came from different sources.  CM pointed out that Fontana was not looking at voting control but at dispositive control.

Q: Elaborate on why the delay in contributions in the Rosen case was a problem.   A: SA said many of the decisions come down to a smell test with the judges.  This may have been the case in Rosen where the delay in funding was mentioned in several old FLP cases and the Court used that to support its decision.  He mentioned the mechanics in forming this partnership were very bad, and the form was not respected.  The lesson is to follow the mechanics under state law as closely as possible.  LM stated that all of the 2036(a)(1) factors in the outline should be followed, but practically, parties don't always do these things.

Q: Many real estate attorneys use single member LLCs for real estate - does this give you a step up in basis?   A: LM under the check the box regulations, a single member LLC is disregarded for all federal tax purposes, and the member is treated as owning the asset outright so they will get a step up.

Q: If real estate in a state that has state estate tax is placed in an LLC to convert it to intangible personal property can you avoid the state estate tax?   A: LM said it depends on the state law.  In the partnership area, some states look through the partnership.  LM suggested not to place FL real estate in a NY LLC because it will be taxed in NY.  Jonathan Blattmachr noted that if you have a business reason for the formation of the FLP it should be considered intangible property, but if the entity is formed just to avoid estate tax it may not work.

Q:  If FLP is created in year 1, with $10M in underlying assets, after discounting value is $5M for gift tax purposes, but the IRS audits, claiming retained interests, tiered discounts, etc., but during the audit assets depreciate significantly, can you undo the FLP and distribute the assets to make the audit go away?   A: SA says absolutely not.  The asset is valued on the date of gift, and you do not want to create the implication that the FLP can be undone.

Q: Can 2036 be used in gift tax realm?  A: No, it is not a gift tax issue.   Q:  Can a GRAT or entity owned by a GRAT lend money to the transferors spouse, with a note to be repaid prior to the end of the GRAT, if other assets are available to make the payments, and then the borrowed funds are used to buy an apartment with the grantor or the trust?   A: CM first noted that the use of the funds is not important.  So long as the spouse and the trustee can show a genuine loan, and it is not a distribution to the spouse which would be a problem under the regulations there should be no problem with this.  The GRAT can purchase an interest in the apartment like any other investment decision.  CM does not believe this would be a commutation problem so long as it is a commercially viable transaction.  SA asked what interest rate should be used and CM responded that the AFR should be sufficient under 7872.  SA noted that if the GRAT purchases an undivided interest in the real estate the spouse's estate will get an undivided interest discount for the asset.

Q: When forming an LLC, how do you avoid the Senda issues?   A:  LM tries to have all family members or trusts contribute consideration when forming the LLC, so that it is protected from creditors at the outset, rather than starting with a single member LLC which is not protected from creditors and then converting to multi-member.  This also avoids the gift on formation argument that might be made under the tax rules that provide the entity is formed when it becomes a multi-member entity.  SA notes that several years ago the IRS argued gift on formation, but the IRS lost on this point and the argument has not been made for some time.

Q: GRAT is for 6 year term, with 2 years remaining, and is funded with illiquid rapidly appreciating assets. The trustee wants to borrow money to make the GRAT payment, but the bank refuses unless the grantor guarantees the debt. Can the grantor make this guarantee for a fee without being in violation of section 2702? A: CM is not sure. The IRS has taken the position that when 1 person guarantees a loan the transaction is treated as if the guarantor borrowed the money and then reloaned it to the lender. The IRS may try to make the same argument in this context.

Q: If you wait up to 105 days to make the GRAT annuity payment and you pay in kind, what is the valuation date of assets used to pay the annuity? CM said that reasonable people disagree on this. As a matter of state law, if the trustee has the obligation to pay a fixed amount to a beneficiary, then the trustee must satisfy that obligation with assets worth the amount owed to the beneficiary, so you would have to use the date of distribution value.

Q: Will submitting to a required physical exam be treated as notice and consent to purchase insurance under the new requirements? A: LM would use that as a backup argument but would not rely on this as a planning tool.

Q: Client who intends to sell LLP interest to a grantor trust has used his gift tax exemption. Can he fund the trust with $1M but retain the right to determine who will receive that money so that the gift is incomplete, and then later distribute the $1M to the grantor's spouse that qualifies for the marital deduction so that none of the assets in the trust are included? A: LM stated that this would require very careful drafting and it is probably not a good idea. CM agreed and noted that if the seed money is an incomplete gift, then there is no basis for arguing the entire trust is not an incomplete gift. LM disagreed, saying the sale of the assets cannot be a gift. SA noted that this was a novel approach, but he would be skeptical, because if we could make a specific dollar value incomplete, we wouldn't need GRATs.

Q: Why do people think you can allocate GST exemption to a 2 year GRAT? If you can allocate, how much do you allocate, the gift amount or the funding amount? If you allocate the full amount, do you need to elect out of the automatic GST allocation rules when the remainder is a GST trust? A: CM began by explaining that the ETIP rules prevent allocation of GST exemption to a GRAT until the termination of grantor's interest. This seems to apply to GRATs because if the grantor dies immediately after the GRAT is created, at least a portion of the property will be included in the grantor's gross estate under 2033, 2036 or 2039. However, an exception to the general rule under Treas. Regs. 26.2632-1(c)(ii) says the value of transferred property is not subject to inclusion in the gross estate of the transferor if the possibility of of inclusion is so remote as to be negligible. Under the regulations, this means that there must be less than 5% probability of inclusion, and a transferor would have to be over age 68. Taken literally, the regulation says that GST can be allocated to many GRATs. While some believe that GST need only be allocated to the value of the gift portion of the interest, CM disagrees and notes that the regulations require the determination of the applicable fraction, where the numerator is the amount of GST allocated to the trust, and the denominator is the value of property transferred reduced by the value of charitable transfers. The regulations do not say to reduce the denominator by the value of any retained interest. Thus, CM believes there is no basis for taking the position that the denominator is anything less than the full value of assets held by the GRAT. Usually, allocating GST is not a good idea, unless the GRAT has highly appreciating assets that will at least double in value by the end of the term. Assuming you do not want to allocate GST exemption, you should elect out of the automatic allocation rules which will apply when assets pass to nonskip persons or to a trust that is a GST trust.

Q: Please repeat the patent number relating to the CRT. A: SA repeated that the patent number is 7149712 issued 12/12/06. Although this was a specialized annuity, it is worth looking reviewing.

Q: Husband wants to create a QTIP for a second spouse, with minimum mandatory payout and corpus distributions of 5%, is this a problem? A: SA said it was not.

Q: Will a trust providing for mandatory income to spouse, discretionary power to pay principal to spouse for health, support, maintenance and education, and a 5 x 5 power qualify for QTIP treatment? A: SA says yes, but in the year of death, if the spouse dies owning the right to withdraw, the spouse will have a general power of appointment (with no impact on the tax). CM noted that there could be problems if you wanted to make a reverse QTIP election.

Q: Client's GST exemption has been exhausted and does not want to give a child/beneficiary a general power of appointment - what does the panel recommend? A: CM pointed out that a general power of appointment does not have to give the holder any real powers. For example, the power could be exercised only with the consent of an independent trustee under 2041.

Q:  If a private trust company is a trustee and pays an investment advisory fee the panel mentioned that the 2% floor does not apply.  Is the result the same if a commercial bank serves?     A: CM said this is a section 67 issue.  Trustee fees are not caught by the 2% rule.  If investment fees are not separately charged and instead are part of the overall trust services provided as part of the trustee fee, the trustee commissions would be fully deductible under section 212 without incurring section 67 limitations.  The problem is that trust companies unbundle their fees now.  If an institution is wiling to rebundle their services and that bundle includes investment advice they can avoid the section 67 limitations.  This concept should work with a commercial trustee, but they may not be able to incorporate the investment fees into their overall trustee fee given the external pressures on fees.  Where the trustee pays an outsider for investment advice, there is a greater chance the IRS may require unbundling of fees and subject that fee to the section 67 limitations.  SA noted that the Rudkin case brief cited authority that Treasury could require unbundling, so the regulations may incorporate this.

Comment by SA:  SA addressed the impact of a powerholder to exercise a lifetime power of appointment over a trust where there is a mandatory income beneficiary.  If the person holding the power is not a beneficiary there are no implications of exercising the power during life.  If the powerholder is a beneficiary, then appointment is a gift under the 2514 regulations of the mandatory income portion.  The discretionary principal authority is unclear.  No cases suggest that this would be a gift, but a few mid-80s PLRs say it could be a gift.  One solution is to give a limited power of appointment to someone other than a beneficiary.

Q: How is a life insurance trust used in a buy-sell agreement and if multiple shareholders use trusts is there a reciprocal trust problem?      A: SA noted that if a buy sell agreement is funded with life insurance and the arrangement is an entity purchase arrangement, there is a cascading value problem as each shareholder dies.  With each death, the insurance needed increases, and the proceeds may be included in all shareholders' estates.  This can be avoided by using a cross purchase agreement, and by acquiring life insurance in a manner that is not subject to estate tax.  Each shareholder can create a life insurance trust for the benefit of his/her family and that trust can hold policies on other shareholders' lives.  At the death of a shareholder, the trust will then purchase the stock under the buy-sell agreement and the proceeds are not in anyone's estate.  SA does not believe there is a reciprocal trust issue here. LM mentioned that Monroe v. Patterson case should be reviewed on the potential transfer for value issue.  SA pointed out that partners of a partnership are excluded from rule.

Q: What are the transfer tax and income tax consequences of domestic partnership?       A: LM addressed CCM 200608038 where the IRS said that an individual who is a domestic partner must report income for the performance of services.  Domestic partners in CA have all rights and benefits, and are subject to all duties and responsibilities of a spouse.  Other states have similar laws and even same sex marriages.  For gift tax purposes, as a domestic partner acquires property treated as community property, there should be no gift of one-half of the value because the rights accrue under state law.  However, the IRS could say that becoming a domestic partner was voluntary and treat this as a gift.  The federal "Defense of Marriage Act" states that marriage means only 1 woman and 1 man, and a spouse can only be a person of the opposite sex, so if this argument is made by the IRS, there would probably be no marital deduction.  If a person attempts to transmute property into community property, there probably would be a gift.  For estate tax purposes, state community property law may be a problem because 100% is included in the decedent's estate, but under CA law, all property would be treated as community property, but they may not get a step up in basis under section 1014 because the Defense of Marriage Act would prevent the partner from being a "spouse" under 1014.

SA referred folks to Pennell's book (specifically page 15) to answer questions regarding the effect a joint brokerage account has on basis.

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Our on-site local reporters who are present in Orlando this year are Gene Zuspann Esq. of Zuspann & Zuspann in Denver, Colorado, Herb Braverman Esq. of Walter & Haverfield, LLP in Cleveland, Ohio, Merry Balson Esq.of Wade, Ash, Woods, Hill & Farley in Denver, Colorado, Paul Hood Esq. of L. Paul Hood Jr. (APLC)  in Mandeville, Louisiana, Joanne Hindel Esq. of Fifth Third Bank in Cleveland, Ohio. Jason Havens Esq. of Havens & Miller PLLC in Destin, Florida, Alan Rothschild Esq. of Hatcher, Stubbs, Land, Hollis and Rothschild, LLP in Columbus, Georgia, and Kimon Karas Esq. of McCarthy, Lebit, Crystal and Liffman Co., LPA in Cleveland, Ohio. The editor again this year will be Joseph G. Hodges Jr. Esq, a solo practitioner in Denver, Colorado, who also is the Chief Moderator of the ABA-PTL List.

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**Heckerling Institute 2007**
Reports from the event, as posted to the ABA-PTL List Serve

# Report #5

A complete listing of the proceedings and speakers is available on **the Institute's Web site**

As we have done in January for the last ten 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 41th Annual Philip E. Heckerling Institute on Estate Planning that is being held January 8-12, 2007 at the Orlando World Center Marriott Resort and Convention Center in Orlando, Florida, a new venue for the Institute this year. A complete listing of the proceedings and speakers will be published here later and is also available on the Institute's Web site at http://www.law.miami.edu/heckerling.

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This Report contains coverage of the Wednesday sessions on Malpractice Claims Against Estate Planning Counsel, What Yesterday's FLP Calls For, and Emerging Issues Under the Twin UPIAs

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Defense Strategies, Risk Management and Evolving Theories and Trends in Malpractice Claims Against Estate Planning Counsel Wednesday afternoon, Special Session 2-A, January 10, 2007 Presenters: Kevin Rosen, Mary Beth Robinson and Pamela Bresnahan

Reporter: Alan Rothschild Esq. of Hatcher, Stubbs, Land, Hollis and Rothschild, LLP in Columbus, Georgia

This breakout session panel included Kevin S. Rosen, who presented the main lecture on this subject, Mary Beth Robinson, in house counsel with a large malpractice insurance company, and Pam Bresnahan, chair of Vorys Sater's Washington D.C.'s litigation group.

The first thing a lawyer should do is identify the client – for example, husband, wife or both? Mary Beth suggested representing jointly is the safest approach. Similarly, must clarify who attorney represents in estate administration. Whatever the arrangement, it should be documented in writing and attorney must follow terms of the relationship once established.

A large percentage of malpractice claims derive from poor intake system. Should do basic due diligence on client – do they have history of suing counsel or not paying fees; are there conflicts of interest to consider/resolve.

Not only are engagement letters necessary, also a good idea to inform client in writing when relationship ends or in areas where there may be uncertainty, such as who attorney does – and does not - represent in an estate administration.

In litigation, if prospective client alleges they believed attorney represented them, if belief is reasonable, enough to get past summary judgment. Who attorney thinks they represent rarely matters. Absent written communication defining relationship or lack thereof, courts will generally favor individual and allow case to go forward.

From the standing perspective, privity rules are being expanded, again, courts generally give the benefit of the doubt to the individual.

If client contact is different from the client, panel urged lawyer to be careful. For example, if one child acts as spokesperson for elderly parent, they may be representing their own interest, not their parent's interest.

Attorney serving as fiduciary – good idea? If client asks, clearly document it was their request, not the attorney's suggestion. Be prepared to accept the additional risk of serving. If attorney represents estate, duty generally to the estate, but if they are also executor, they own duties to the beneficiaries in their fiduciary capacity. Can you reconcile these differences? There may also be malpractice coverage issues. Mary Beth suggests having the management committee approve the firm's attorneys serving in a fiduciary capacity. Questions to ask include experience of person, type of assets that will be managed, history of conflict between beneficiaries.

In Georgia, the Supreme Court has issued a form letter required for a lawyer to be appointed fiduciary in the state that serves a good guide on the issue. Was it client's idea? Did attorney suggest other possible fiduciaries? Discuss conflicts and payment of fees.

However, panel suggested that attorney as fiduciary is an easy target because, in retrospect (i.e. in litigation), it is always easy to argue that there was a better fiduciary alternative.

Another area of high malpractice risk arises when attorney works through client's other advisors and rarely has direct access to client. Attorney must make sure their recommendations are getting to client – safest way is through written communications sent directly to client. Communicating through other advisors also raises privilege issues.

If attorney has financial relationship with other advisors – proceed with extreme caution. Attorney must exercise informed, independent judgment, existence of relationship with advisor can create picture that attorney not independent in their counsel.

The panel then discussed their thoughts on opinion letters and legal memos. Make sure you clearly identify the topic/issue – i.e. define the question. State what the facts are, whether you independently investigated or relied on client. Identify risks associated with transaction.

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What Yesterday's FLP Calls For: Rejoicing or Repairing Wednesday afternoon, Special Session, January 10, 2007
Presenters: Ronald Aucutt and Daniel Markstein

Reporter: Paul Hood Esq. of L. Paul Hood Jr. (APLC) in Mandeville, Louisiana

Their materials for this afternoon session consisted of a brief discussion of applicable provisions of Subchapter K that apply to distributions from partnerships and four "fact patterns," which really were the facts of four of the "dirty dozen" IRC Sec. 2036/FLP cases.

Aucutt took up the first fact pattern, which contained the facts of Strangi. He urged the attendees to assume that these facts occurred during lifetime of the client, who still has time to "fix" the problems or to do something about it. He and Markstein then began to take up different variables.

The first such variable was the amount of a client's property in an FLP as a percentage of the client's net worth, which is an FLP organization issue. The panel suggested either collapsing the FLP or getting assets out of the FLP in order to reduce the percentage of the client's estate. They called particular attention to personal use assets, which they advised should not be a part of the FLP asset base.

The second variable was the small or unnecessary FLP, which can occur either at the outset (an FLP organization issue) or due to post-formation issues such as changes in the law or net worth. In these cases, they recommended collapsing the FLP.

The third variable was the FLP formed on behalf of the incompetent client, particularly where the agent is "standing on all sides of the transaction." While Aucutt indicated that, in his opinion, he was unsure that this variable, standing alone, would be enough for a court to apply IRC Sec. 2036 to the FLP, it was still something that should be addressed by looking at checks and balances on the power holder.

The fourth variable, another organization issue, was sloppy formation facts, e.g., failing to file certificate of limited partnership, failing to timely fund, etc. The panel recommended doing an FLP audit and to fix the problems found. They also suggested the potential for adding partners, etc.

The fifth variable, an operational issue, was consistency with the FLP agreement. Examples of inconsistency included non pro rata distributions, commingling, etc. The panel strongly recommended fixing that problem by repaying the excess with interest. Markstein strongly advised all to exchange checks in this regard and not to do the fix through bookkeeping changes to the capital account.

The sixth variable, another operational issue, was facts that could give rise to the existence of an implied agreement. The panel recommended tightening of the checks and balances on the controlling/violating party and even transferring control to the younger generation.

At this point, the panel was interrupted by a stream of questions and comments, unfortunately too many of which were far afield from the subject.

Markstein went through the outline material on Subchapter K, which he described as a "cheat sheet."

The panel concluded with a very brief discussion of the applicability of IRC Sec. 2035 on FLP's, the materials for which were set forth in Aucutt's main session outline.

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Emerging Issues Under the Twin UPIAs Wednesday afternoon, Special Session 2-C. January 10, 2007 Presenters: Susan Porter and Alan Acker

Reporter: Gene Zuspann Esq. of Zuspann & Zuspann in Denver, Colorado

The purpose of this session was to review the Uniform Prudent Investor Act and the Uniform Principal and Income Act.

Porter started with a discussion of the duty to diversify in the Prudent Investor Act. She said that the only particular action mandated by this Act is the duty to diversify trust investments, but that the Act gives the trustee latitude in exercising that power.

She first discussed the history and the prudent man standard that required the trustee to review the prudence of each investment. The Bank of New York (Spitzer), 1974, held that this was true even though the performance of the trust fund as a whole was excellent.

She then reviewed several cases illustrating practical aspects of imposing a duty of diversification.

Some cases hold that the concentration of trust investments is not a breach of duty. Each of the cases cited included language that the trustee hold the stock position. Susan said that this language overrides the duty of loyalty.

Some cases also hold that lack of diversification, even with the above language, subjected the trustee to liability. One case held the trustee liable because the instrument did not have a specific power to hold bank stock.

Another case, Estate of Charles G. Dumont, had held that the corporate trustee was liable for holding Kodak stock, even though the instrument provided "neither my Executors nor my said trustee shall dispose of such stock for the purpose of diversification of investment and neither they [n]or it shall be held liable for any diminution in the value of such stock." When the case was decided in 2004, the court awarded substantial damages to the beneficiaries. This case has been discussed at the Institute in the past two years.

In 2006, the appellate Division reversed that holding, although the grounds for reversal were narrow and the decision was not an approval of the corporate trustee's actions regarding diversification. The Court of Appeals denied the objectants leave to appeal in September, 2006.

She then reviewed the changes in the Restatement (Third), Trusts - the Prudent Investor Rule. The Restatement and the Uniform Prudent Investor Act made five fundamental changes to the criteria for prudent investing:

- The standard of prudence applies to the trust as a whole;
- The overall investment strategy should incorporate risk and return objectives reasonably suited to the trust;
- The duty to diversify is in general a part of the investment strategy;
- No investment is imprudent, per se; and
- The delegation of investment authority is permitted subject to safeguards.

The law has been changed regarding assets in the trust at inception and the holding of inception assets is now not much protection. Also, Susan discussed language to negate the duty to diversify.

Acker pointed out an Article in the most recent issue of the ACTEC Journal that indicates there is a duty to diversify, even in an irrevocable insurance trust. He does not know if this is correct.

There was also discussion of a Nebraska Case and a law review article that special assets such as a family farm, should not be diversified.

The discussion then turned to the Uniform Income and Principal Act. The trustee owes a duty of impartiality to all beneficiaries and cannot act to favor one beneficiary over another unless directed or permitted to do so under the governing instrument.

With this caveat in mind, Acker discussed the power to adjust under UPIA §104. There are conditions that must be met to exercise the power to adjust:

1. The trust must be invested as a prudent investor;
2. The trust must describe the amount that may or must be distributed by referring to the trust's income; and
3. The trustee must determine that to administer the trust impartially, an adjustment is necessary.

There are limitations on adjustments. Most of these are tax driven - no adjustment may be made if the adjustment would cause the trust to fail its intended purpose, e.g. in a marital trust if the adjustment would cause the trust to fail to qualify for the marital deduction. He questioned whether a downward adjustment would ever be made in a marital trust.

An adjustment may not be made if all of the trustees are beneficiaries or if the adjustment would benefit the trustee. However, if one of the trustees is not in either of these classes, then that trustee may make the adjustment.

Another factor to consider is the intent of the settlor. However, he does not know how a trustee would determine the intent. He feels that this is a challenge. Ackers also noted that the adjustment in not a needs based test - the object is to be impartial.

Ackers briefly discussed the unitrust concept and indicated that he is not a supporter of a unitrust. He pointed out that the unitrust was considered by the drafters of the Act and rejected in favor of the power to adjust. He also discussed the various unitrust percentages (3 - 5%), the 643 regs and the problems determining which is appropriate.

Issues continue to emerge. One is the determination of income accrued before death. In the prior act, this would be prorated. In the current act, this is income when paid. The rule applies to payments such as rents, dividends and interest. Both agreed that the trustee does have the power to adjust.

Section 401 provides that the general rule is that cash from entities is income and property is principal. An exception is when the entity designates the payment as a liquidation payment, or if the payment is greater than 20% of the entity's gross assets, in which case the payment is principal.

Porter discussed section 105 of the Act. This was a separate section regarding notice that was added to the Principal and Income Act after it was initially approved. She stated that the 105 does not give the court the power to second guess the judgment of a fiduciary.

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More News From The Vendor Hall

All of the vendors seem plenty busy, especially the software vendors. Two vendors seemed to be not very busy were Lawgic and Inheritance plus West's Cowles and Fastax, but that may just be our timing.

Don Kelly is working hard on the interstate stuff where the different states have different taxes. He said there are now 20 states that have a different tax structure. Vince Lackner is also coming out with a program for this.

Someone at the Miami alumni lunch said that the number of attendees was 2,600+ but they do not have the final numbers on the walk-ins. Regardless, this is probably the second best audience that they have ever had.

Finally, the questionnaire in the materials has a question about the facilities. It asks whether to come back and how people feel. It also states that rates in South Florida have gone sky high and that the rooms cost about $350 now. It will be interesting to see what people think about this new venue.

We anticipate a full report on the vendors from Jason Havens in the next day or so.

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Our on-site local reporters who are present in Orlando this year are Gene Zuspann Esq. of Zuspann & Zuspann in Denver, Colorado, Herb Braverman Esq. of Walter & Haverfield, LLP in Cleveland, Ohio, Merry Balson Esq.of Wade, Ash, Woods, Hill & Farley in Denver, Colorado, Paul Hood Esq. of L. Paul Hood Jr. (APLC) in Mandeville, Louisiana, Joanne Hindel Esq. of Fifth Third Bank in Cleveland, Ohio. Jason Havens Esq. of Havens & Miller PLLC in Destin, Florida, Alan Rothschild Esq. of Hatcher, Stubbs, Land, Hollis and Rothschild, LLP in Columbus, Georgia, and Kimon Karas Esq. of McCarthy, Lebit, Crystal and Liffman Co., LPA in Cleveland, Ohio. The editor again this year will be Joseph G. Hodges Jr. Esq, a solo practitioner in Denver, Colorado, who also is the Chief Moderator of the ABA-PTL List.

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GENERAL INFORMATION ABOUT INSTITUTE: Inquiries/Registration: Philip E. Heckerling Institute on Estate Planning University of Miami School of Law Center for Continuing Legal Education P.O. Box 248087 Coral Gables, FL 33124-8087 Telephone: 305-284-4762 / FAX: 305-284-6752 Web site: www.law.miami.edu/heckerling E-mail: heckerling@law.miami.edu

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Brought to you by the ABA-PTL Discussion List Moderators.

# Report #6

A complete listing of the proceedings and speakers is available on **the Institute's Web site**

As we have done in January for the last ten 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 41th Annual Philip E. Heckerling Institute on Estate Planning that is being held January 8-12, 2007 at the Orlando World Center Marriott Resort and Convention Center in Orlando, Florida, a new venue for the Institute this year. A complete listing of the proceedings and speakers will be published here later and is also available on the Institute's Web site at http://www.law.miami.edu/heckerling.

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EDITOR'S COMMENT: For those of you who are counting, it is currently anticipated that there will be one more Report #12 that will be posted either later today or sometime tomorrow pending my receipt of the required reports.

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Eratta: At the end of this Report is an Eratta regarding the Thursday afternoon Special Session 4-B Report by Joanne Hindel that has just been submitted to us for publication by Gideon Rothschild, one of the Presenters.

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This Report contains coverage of Fundamentals Programs No. 2 and 3. No. 2 held on Wednesday afternoon dealt with the tax and non-tax considerations in drafting buy-sell agreements. No. 3 held Thursday afternoon dealt with making "friends" with Subchapter K. These Fundamentals Programs run all afternoon are concurrently with the Special Sessions that are held in the afternoons. This Report also contains coverage of the Wednesday afternoon Special Session 1-C Navigation without a Compass - Charitable Planning in 2007 presented by Kathryn Miree and Jerry McCoy Since that is a charitable session, we will be sending a copy of this Report to the GIFT-PL and PG lists too.

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Fundamentals Program #2 - The Blount Trust About the Family Business: The Tax and Non-Tax Considerations in Drafting Buy-Sell Agreements Wednesday afternoon, January10, 2007
Presenters: Howard Zaritsky and Farhad Aghdami

Reporter: Herb Braverman Esq. of Walter & Haverfield, LLP in Cleveland

Presented by Howard M. Zaritsky and Farhad Aghdami, Esqs. Reported by Herbert L. Braverman, Esq.

This was a fundamentals presentation at the Institute. It reflected that different presenters take on a task differently. There were 3 fundamentals programs at the Institute this year. Professor Pennell presented on the wealth transfer tax using a 49 page outline; Richard Robinson introduced Subchapter K, partnership taxation, in 36 pages; while Zaritsky and Aghdami produced a 261 page outline, which was substantially excerpted from prior publications by the presenters (with others). The materials are thorough, including some "sample" forms, and I recommend them to your attention, perhaps more so than the tape of the presentation itself.

Mr. Zaritsky explained that buy-sell agreements are used to (1) maintain closely-held status; (2) guarantee a market for the stock of a decedent; (3) freeze asset value for estate tax purposes; (4) consolidate control in a family; (5) protect S corp. status; (6) prevent deadlocks; and (7) restrict competition from former stockholders or family members. Although the buy-sell agreement was never defined per se, it was pointed out that it is a contract, should be in writing and should include a purchase price for corporate shares. Furthermore, the agreement should be reflected in other corporate documents, such as minutes, stock certificates, by-laws, etc.

The 3 basic forms of buy-sells were reviewed: (1) the redemption agreement between the corporation and the stockholders, in which the corporation agrees buy offered stock at specified terms; (2) the cross-purchase agreement between or among stockholders, in which the stockholders agree to purchase offered stock at specified terms; and (3) the hybrid agreement which contains elements of both (1) and (2) in various combinations and forms.

The estate planning advantages of buy-sells include (1) the estate tax value freeze; (2) simplicity to create and to maintain; (3) ease of elimination, if desired; and (4) liquidity through market creation. But, there are some disadvantages, (1) Chapter 14 issues that prevent freezing values; (2) older stockholders get the values included first, others may not benefit from the values sought; (3) funding costs and complications; and (4) difficulty obtaining favorable income tax treatment on redemption of decedent's interest.

Focusing on the estate value freeze objectives, the presenters covered the 6 requirements that must be met in order for a buy-sell agreement to set estate tax values. The first 4 requirements come from a variety of sources: (1) the estate must be obligated to offer the interest for sale at the decedent's death; (2) there must be a reasonable and ascertainable price for the interest; (3) there must be lifetime restrictions that preclude a transfer of the interest at a price higher than the agreement price at death; and (4) the so-called device test, to demonstrate that the agreement is not merely a device to transfer the interest to the natural objects of the decedent's bounty for less than full and adequate consideration. These requirements are discussed at length, with considerable citations throughout. Similarly, the 2 requirements added in 1990 by Section 2703 of Chapter 14 are covered in great detail--both (1) the bona fide business purpose requirement and (2) the comparability requirement, the terms of the agreement must be comparable to similar agreements entered into among unrelated persons. The important cases establishing the interpretation of these requirements are cited and fully discussed in the outline, including the cases whose names are used in the title of the presentation to whet the intellectual appetite. The cases include both taxpayer wins and losses, so a review of the outline and these cases is certainly recommended. For example, in the True case (Estate of True -v- Comm., T.C.Memo 2001-167), the Tax Court and subsequently the 10th Circuit, the agreement is discussed at length and found to be a "device" failing the test, whereas, in Estate of Amlie -v- Comm., T.C.Memo 2006-76, the agreement as found not to be a device. The requirement of arm's length comparability, added by Section 2703, is examined carefully in Estate of Blount -v- Comm., T.C.Memo 2004-116. The first taxpayer victory in a case decided under Section 2703 came in Estate of Amlie -v- Comm., T.C.Memo 2006-76.

The presenters touched on topics that are covered in depth in their lengthy outline. These topics include income tax planning with buy-sells, taking into consideration the form of corporation and the form of buy-sell agreement; funding a buy-sell, including a discussion of life insurance planning; the importance of certain non-tax buy-sell provisions; ethical considerations for attorneys representing parties in buy-sell negotiations; Circular 230 issues; and sample agreements for your consideration.

The subject was covered well in the materials; unfortunately these materials are only available to Institute Registrants. However, the Presenter's books on this subject are available for purchase though various legal publishers.

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Fundamentals Program #3 Making "Friends" with Subchapter K Thursday afternoon, January 11, 2007 Presenter: Richard Robinson

Reporter: Herb Braverman Esq. of Walter & Haverfield, LLP in Cleveland, Ohio

Mr. Robinson conceded that he could not teach the group Subchapter K in 3 hours and the group conceded that it could not learn Subchapter K in 3 hours either. However, he indicated that he would touch on a survey of issues, not really in depth, but to give the group some familiarity with Subchapter K, its intricacies and its importance to the estate planner.

He began with entity classification. A partnership includes a syndicate, a group, a pool, a joint venture or any other unincorporated organization in which any business, financial operation or venture is carried on...that is not a trust, an estate or a corporation. State law is not determinative for federal income tax purposes. Sections 761 and 7701.

An unincorporated entity with 2 or more owners may elect to be classified as an association (and thus a corporation) or a partnership; and an unincorporated entity with one owner may elect to be classified as an association or to be disregarded as an entity separate from its owner. Unless the entity elects otherwise, a domestic eligible entity is a partnership if it has 2 or more owners or is disregarded as an entity separate from its owner if it has a single owner. An eligible entity may elect to be classified as other than its default classification or to change its classification by filing Form 8832, "Entity Classification Election," or "check the box" with the service center. The Form may be filed any time during the year and may be made effective on the date of filing, one year after the filing or 75 days before the filing. This filing is automatic if the entity files Form 2553, electing a Sub S election for the entity. If a Sub S filing is made erroneously because of "substantial economic effects" issues, use the procedures of Rev. Proc. 2003-43 which allows for a 2 year extension for filing the correction; beyond that, you have to seek a ruling to correct.

Robinson used schematic drawings and tables to set forth problems and scenarios illustrating his points and it is recommended that his outline be reviewed in connection with the study of Subchapter K. Some portions of this summary may not be as clear as we would like without these items.

See Rev. Rul. 99-5 and 99-6, discussing income tax characterization for distributions from a single member to a multiple member entity or from a disregarded entity to a partnership; and vice-versa (99-6)

For example, Robinson distinguished between a partnership and a tenancy-in-common and suggested that Rev. Proc. 2002-22 is the guideline in this arena. Mere expense sharing, joint repairing, maintaining and leasing real property is not a partnership; he used a condominium rental pool arrangement to illustrate this point. If you have partnership status, there is a penalty for failure to file a partnership tax return of $50 per partner per month for up to 5 months. See Section 6698 of the Code. Similarly, a partnership interest cannot qualify for a tax-free exchange under Section 1031 of the Code--this possibility must be examined closely before attempting such a tax-free exchange.

No gain or loss is recognized when property is contributed to a partnership in exchange for a partnership interest, unless the partnership would be taxed as an investment company within the meaning of Section 351. See Section 721. A transferee entity is an investment company if more than 80% of the value of its assets are stock or securities and the transfer results in a diversification of stock or securities. Money, futures, contracts, precious metals, etc., are stock or securities for this purpose. However, diversification does not occur if no more than 25% of the assets are in one issuer and not more than 50% of the assets are in 5 or fewer issuers. This is why a large commercial hedge fund may have no problem avoiding the investment company issues, but a husband and wife may not do so when forming an FLP. Robinson suggested that the spouses make asset exchanges between themselves prior to contributing to an FLP to avoid the "diversification" complications.

Robinson then discussed contributions of property that is subject to liability to an entity and how this complicates gain recognition under Section 731. He reviewed the issues surrounding recourse and non-recourse liabilities and how they differ for partners who contribute or who assume such liabilities. See Section 752 and its proposed regs. Each year, partners have to look at their own personal liability at the beginning of the year versus at the end of the year to determine his/her gain from changes during the year from partnership contributions. Robinson made it quite clear that complexities abound in these areas that he was not covering in his presentation.

Also discussed were contributions and distributions treated as disguised sales under Subchapter K. If the distributions resulted from business operations, a disguised sale problem may not exist, but if the distribution is from borrowed monies, then a determination of whether or not a disguised sale has occurred is warranted. This analysis is impacted by the 2 year rule--transfers between a partnership and a partner more than 2 years apart are presumed not to be a sale unless circumstances clearly establish otherwise. See Section 707 and regs.

Robinson spent considerable time discussing partnership interests in exchange for services. The analysis varies depending on whether the persons involved in the transaction are related or not. The receipt of a vested capital interest in exchange for services is a taxable event. Compare receipt of a non-vested profits interest for services, which may not be a taxable event. See Rev. Procs. 93-27 and 2001-43. As a part of this analysis, Robinson suggested that a key employee wishing to avoid tax complications resulting from a liquidation within 2 years should file a Section 83 protective election using a "zero" value for the interest received.

Also, Robinson discussed the self-employment taxes issues in an LLC, since it is not clear whether a member of an LLC should be treated as a general partner or as a limited partner for purposes of self-employment taxes. He told the story of the proposed regs. That IRS prepared in this area in the '90's and noted that they were so controversial that Congress actually passed a bill prohibiting their publication. Nevertheless, he felt that the essence of these proposed regs that will never be finalized are still worthy of giving us proper direction. So, a limited partner is someone who has no personal liability for entity debts, who has no authority to bind the partnership and who does not do more than 500 hours of service per year. Of course, one could always go the limited partnership format or to the S corp format to deal with these issues. See PLR's 9432018 and 9452024 for LLC cases where self-employment taxes were enforced.

Robinson also had chapters in his outline for allocations of profits and losses, special allocations for LLC's, partnership sales and distributions, disguised sales of partnership interests, Section 752(b) relief of liabilities, distributions of property that was previously contributed (or not ) and Section 754 elections.

The tape of this presentation is very helpful and recommended, as is the printed materials for the schematics and tables used by the presenter. Unfortunately these are only available to Institute attendees.

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Special Session 1-C Navigation without a Compass - Charitable Planning in 2007 Wednesday afternoon, January 10, 2007 Presenters: Kathryn Miree and Jerry McCoy

Reporter: Jason E. Havens, Esq. of Havens & Miller, P.L.L.C. in Destin, Florida

Kathryn W. Miree, Esq. and Jerry J. McCoy, Esq. continued Kathryn's discussion during her general session on charitable gift planning. They presented charitable gift planning options from the donor's perspective from less to more complicated.

First, Kathryn described her "kitchen table philanthropy" concept in the context of a family's outright/direct charitable giving. She recommended gathering children and/or grandchildren at the table and telling them that they could each give $1,000 or whatever amount to their favorite charitable causes. I have also seen this described in terms of giving younger family members a number of pennies (e.g., ten each) each year and allowing them to give as many as they desire to whatever organization(s). The family could donate a much greater amount (e.g., $100K per "representative penny"), but the concept still works well as a teaching tool.

Second, Jerry and Kathryn focused on the next level of giving in using gift agreements to provide conditions on an outright charitable gift. Gift agreements can define how a particular gift can be used and also a "gift over," which is a contingency that if triggered causes the gift to "migrate" from one exempt organization to another, e.g., to Harvard but if Harvard fails to abide by the express conditions of the gift, then to Yale. Jerry and Kathryn affirmed the usefulness of a "watchdog" to ensure that the gift is used as intended. Jerry recommended the excellent 2006 Probate & Property article of Alan Rothschild, Jr., Esq. (who was in attendance), "Planning and Documenting Charitable Gifts," which addresses the use of gift agreements; this article can be accessed freely online even by non-members (in HTML format -- with the PDF version only available to ABA RPPT members): http://www.abanet.org/rppt/publications/magazine/2006/ja/rothschild.shtml.

Third, Jerry highlighted the use of a charitable lead trust (CLT) to provide income to a charity for a specified period of time, with the remainder ultimately distributed to family members or other beneficiaries. He generally noted the income and estate tax benefits of using a CLT.

Fourth, Kathryn and Jerry noted the continuing use of donor advised funds (DAFs). However, they cautioned that the Pension Protection Act (PPA) has created a new regime of regulating DAFs that did not previously exist under the Internal Revenue Code or the Treasury Regulations. Kathryn had already covered much of the substance of the PPA's changes in the DAF context. She referred the attendees to her materials, which in the special session consist of Jerry's detailed summary of the PPA's charitable gift planning provisions.

Fifth, Kathryn and Jerry discussed the use of supporting organizations (SOs) and also the limitations created by the PPA. Both agreed that SOs might now be on par with private foundations (PFs) for many (if not most) donors who desire to be much more involved in terms of continuing control of their charitable gifts. Jerry discussed with one of the attendees the provisions of Notice 2006-109, which gives guidance to private foundations in determining the type of SO to which the PF is making grants. (The same rules of that notice apply to DAFs making grants to SOs.)

Jerry and Kathryn anticipate more changes from Congress to address perceived abuses in the charitable gift planning arena. Both highlighted a few of the other provisions contained in the PPA, such as changes impacting conservation easements and fractional interests in tangible personal property, which are covered extensively in the general and special session materials. Jerry noted the outcry of museums and other charitable organizations regarding the latter change, which could dramatically impact a gift of art (especially for estate tax inclusion purposes). They concluded that this has been quite an active year in charitable gift planning developments!

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Eratta for Special Session 4-B The Ethics of Asset Protection Planning Held Thursday afternoon, January 11, 2007 Presenters: Alexander Bove, Jay Adkisson, Mathew Mtiasevich and Gideon Rothschild. Eratta submitted by Gideon Rothschild - it is published here in full.

I believe that Joanne Hindel's reporting of our panel was not entirely accurate. Firstly, it was Matt Matiasevich who followed Alexander and discussed the ethics rules and it was Jay who followed Matt. I tried to note the corrections below in CAPS, including some of the substantive comments.

Alexander introduced the session by saying that the concept and the sub-specialty of asset protection planning in the law are generating more and more controversy and criticism, even angry criticism, most of it directed at asset protection trusts, and most of that directed against offshore asset protection trusts.

He said that it is puzzling that articles criticizing asset protection planning don't make an equally emotional attack on such things as limited liability companies, bankruptcy-remote entities, acquisition of exempt assets, and pre-bankruptcy planning in general.

He poses a typical scenario of a radiologist, who, as a result of a flawed X-Ray machine, has a rash of malpractice claims filed that are then all settled. Six months later, when no actions are pending, he is considering the establishment of a self-settled asset protection trust.

Alexander then turns over the discussion to Jay Adkisson (NOT JAY - IT IS MATT DISCUSSING THE FOLLOWING). Jay approaches the discussion from the perspective of a litigator and says that asset protection planning really boils down to two issues:

1. Is asset protection planning (APP) per se fraudulent?

2. Are attorneys who do this kind of work committing an ethical breach?

He points out that facing discipline in this area will involve questions of moral turpitude that will justify a lengthy review and stiff penalties if found liable. He also states that most malpractice insurance will not cover the lawyer if found liable in this area.

He says that some states, such as California, put this area under the category of interference with justice.

He says that a disciplinary tribunal will apply ethical principles but the law of fraudulent transfers may also be applied.

He differentiates between the states that follow the Model Rules and those that follow the Model Code and indicates that in the Model Rules states, practicing in the area of APP will not be found to be a violation of the ethical rules but in the states following the Model Code, APP will be considered a per se violation.(I DO NOT BELIEVE HE SAID APP WILL BE A PER SE VIOLATION. WHAT HE SAID WAS THAT ENGAGING IN A FRAUDULENT TRANSFER WILL BE A VIOLATION - A HUGE DISTINCTION)

He says that it is important to understand what a fraudulent transfer is and which ethical rules of your jurisdiction apply. He suggests that maintaining a disciplined case review and intake system can help in actions involving this area. He also suggests that the lawyer pay attention to the possibility that you are acting in a capacity other than just planner for your client, for instance when you are dealing directly with creditors of the client.

Matthew (THIS IS NOT JAY'S PRESENTATION) starts off by pointing out that many early Americans came to the U.S. in order to flee onerous creditor laws in other countries and were themselves debtors. He also mentions that Thomas Jefferson might have drafted the first Asset Protection trust when he set up a spendthrift trust for his daughter.

He points out that contrary to general belief, APP is meant to avoid fraudulent transfers and keep clients on the right side of the law.

He warns that the financial services industry has engaged in the creation of products to provide for asset protection and that APP is being productized with clients expecting standardized pricing for the service.

He analogizes APP to a swimming pool with the shallow end consisting of the safe methods of APP and the deep end having no bottom and containing mutant sharks otherwise known as litigators.

He continues this analogy by suggesting that the shallow end has statutes that are intended to let people protect and plan. His examples include state and federal exemption planning and corporate planning. He also says that spendthrift trusts are an example of traditional APP and that insurance products also represent a transfer of risk from the individual to the insurance company with the client having the ability to keep assets.

He does point out that laws have developed to limit the planning one can do in the shallow end of the pool such as the Bankruptcy Act and spendthrift protection limitations.

He then suggests that in the middle of the pool are the laws that are not intended to protect against creditors but have the effect of APP. His example is that of a charging order protection allowing the protection of partnership assets so that for instance, a partner can't force his other partners into an agreement that involves his own creditors. He also points to tax shelters as good examples of legislation in this area.

He warns that if the lawyer plans to practice in this area, you have to have an understanding of the laws so as not to inadvertently place your client or their assets in jeopardy.

He then describes the deepest end as the area where the legislation has prohibited APP. He says that all questions in this area will be resolved against you and it is fraught with high client risks such as losing their business and being subject to criminal sanctions.

He says this is where the fraudulent transfer laws exist and suggests that one should never even use the term: asset protection but instead refer to this area as the creation of self-settled spendthrift trusts.

Having said that he points out that most states do not allow these kinds of trusts to escape creditor access and that since there have been so few cases in this area, you don't know how courts might rule if a matter is litigated and it is best to not draft domestic asset protection trusts.

He says that if a foreign asset protection trust is challenged the court might order repatriation of the assets or throw the settler in jail.

He also mentions that most of the bad cases seem to deal with trusts created in the Cook Islands.

Gideon then agrees (AGREES WITH WHAT?) and suggests that the bad case law decisions in this area are similar to the FLP arena with bad facts making bad law. He also suggests that we all engage in APP when we draft LLCs. Gideon also suggests that you may actually be held liable for malpractice if you don't advise your clients about APP options and uses a tenancy by the entireties situation as an example.

He suggests that this area can be handled ethically if you conduct proper due diligence including the review of a client's financial records and the preparation and completion of an APP audit checklist. He also suggests that the lawyer should keep a record of the clients that have been rejected to show a court if necessary to substantiate the review and due diligence aspect.

He recommends conducting a solvency analysis: what will the client retain after the transfer of assets to an asset protection trust?

He reviews a few cases and points out that if legitimate reasons can be found, the courts will uphold self-settled trusts. He mentions some legitimate reasons for foreign asset protection trusts might be to engage in asset diversification, benefit foreign heirs or avoid forced heirship laws. He also points out that some laws, notably the bankruptcy laws, do allow self-settled trust that are older than 10 years.(ACTUALLY WHAT I SAID WAS THE UNDER THE NEW BANKRUPTCY CODE, IF A TRANSFER TO AN APT IS MADE MORE THAN 10 YEARS PRIOR TO FILING, IT WILL NOT BE DEEMED A FRAUDULENT TRANSFER, THUS SHOUDL NOT BE SUBJECT TO ETHICAL BREACH. BUT IT MAY STILL HAVE TO SATISFY THE REQUIREMENT THAT THE TRUST IS A VALID TRUST UNDER APPLICABLE LAW)

All the panelists did a great job of providing another perspective on asset protection planning and on dispelling the commonly held belief that this is done to defraud creditors.

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Our on-site local reporters who are present in Orlando this year are Gene Zuspann Esq. of Zuspann & Zuspann in Denver, Colorado, Herb Braverman Esq. of Walter & Haverfield, LLP in Cleveland, Ohio, Merry Balson Esq.of Wade, Ash, Woods, Hill & Farley in Denver, Colorado, Paul Hood Esq. of L. Paul Hood Jr. (APLC) in Mandeville, Louisiana, Joanne Hindel Esq. of Fifth Third Bank in Cleveland, Ohio. Jason Havens Esq. of Havens & Miller PLLC in Destin, Florida, Alan Rothschild Esq. of Hatcher, Stubbs, Land, Hollis and Rothschild, LLP in Columbus, Georgia, and Kimon Karas Esq. of McCarthy, Lebit, Crystal and Liffman Co., LPA in Cleveland, Ohio. The editor again this year will be Joseph G. Hodges Jr. Esq, a solo practitioner in Denver, Colorado, who also is the Chief Moderator of the ABA-PTL List.

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Brought to you by the ABA-PTL Discussion List Moderators.

# Report #7

A complete listing of the proceedings and speakers is available on **the Institute's Web site**

As we have done in January for the last ten 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 41th Annual Philip E. Heckerling Institute on Estate Planning that is being held January 8-12, 2007 at the Orlando World Center Marriott Resort and Convention Center in Orlando, Florida, a new venue for the Institute this year. A complete listing of the proceedings and speakers will be published here later and is also available on the Institute's Web site at http://www.law.miami.edu/heckerling.

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EDITOR'S COMMENT: This will be our final Report for 2007. We hope you have enjoyed these Reports and found them to be both timely and informative. Please feel free to send us any suggestions or comments you may have for better Institute reporting in future years. We will see you again at the 42nd Institute in Orlando, Florida, January 14-18, 2008.

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This Report contains coverage of the various Vendors who exhibited during the Institute, a Report on the status of Special Session 2-E, and another Eratta regarding Special Session 4-B in Report 11.

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Special Session 2-E GRATs vs. Installment Sales to Grantor trusts vs. Direct Gifts: What Do the Numbers and Theory Say? Wednesday afternoon, January 10, 2007 Presenters: Jonathan Blattmachr, Robert Weiss and Diana Zeydel

Reporter: Jason Havens Esq. of Havens & Miller PLLC in Destin, Florida

The Report for this Special Session was not turned in time to be published. However, this Session built on the regular Session on the same topic that was presented by Jonathan Blattmachr on Tuesday morning, January 9, 2007. We refer you to the report for that Session, which was done by Reporter Paul Hood, as the same was published in Report #3.

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Eratta #2: At the end of Report #11 there was an Eratta regarding the Thursday afternoon Special Session 4-B Report by Joanne Hindel that was submitted to us for publication by Gideon Rothschild, one of the Presenters. Gideon has now submitted his own Eratta for part of his earlier Eratta submission, as follows:

Sorry for the confusion. I have made a typo myself. See below where I have noted in brackets. This should have said that it is Jay's presentation (not Matt's)

Matthew (THIS IS [NOT] JAY'S PRESENTATION) starts off by pointing out that many early Americans came to the U.S. in order to flee onerous creditor laws in other countries and were themselves debtors. He also mentions that Thomas Jefferson might have drafted the first Asset Protection trust when he set up a spendthrift trust for his daughter.

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Report on the Vendors

Reporter: Jason Havens Esq. of Havens & Miller PLLC in Destin, Florida

This report covers the software and some other vendors who are exhibiting at the Institute.

The number of software and other vendors at the 2007 Institute has expanded further. A complete list of those vendors was posted previously in the Preliminary Report.

Following are the highlights among the software and other vendors. These highlights are generally classified in categories that will hopefully prove helpful to list members.

A. CALCULATION SOFTWARE:

There were not many developments to note in the calculation arena this year. However, one (Item #1 below) created quite a buzz:

1. DecoupleCruncher: Vince Lackner and Steve Leimberg, both well-known experts in the estate planning technology field, have created a new tool known as DecoupleCruncher. DecoupleCruncher will handle a wide range of calculations in order to determine estate or inheritance taxes due in a single state or in multiple states. The program handles deductions, including an optimized marital deduction (or the option to elect to pay estate taxes if desired), and allows you to reallocate assets among two or more states as well as to "Show or Refine Calculations." Vince and Steve have also included all relevant federal and state tables to assist you in understanding some of these rather odd results under various state regimes.

Vince and Steve held a lunch session to illustrate their new tool, which is based on the solid FileMaker Pro database platform that Vince uses for his 6-in-1 Estate Administration System. For more information, please contact The Lackner Group, Inc. (http://www.lacknergroup.com) or Leimberg & LeClair, Inc. (http://www.leimberg.com). This program was just released at the Institute, so there is not even a direct website or link available right now.

2. Brentmark Software, Inc. (http://www.brentmark.com): Brentmark is adding state-specific inheritance and/or estate tax calculations to their product lines. The first release will be their Estate Planning QuickView, followed by Estate Planning Tools and others throughout 2007. This is a major project that Brentmark expects to be well-received by their customers. They are also renaming their Pension & Roth IRA Analyzer (to remove the obsolete term "pension").

B. DRAFTING SOFTWARE:

There are a few new developments to share regarding drafting systems:

1. InterActive Legal Systems (http://www.ilsdocs.com): Wealth Transfer Planning (WTP) has been running on the HotDocs platform/engine for about two years. There have been several updates during the past year. I highlighted most of those updates in my Law Office Computing review (April 2006) of WTP (http://www.ilsdocs.com/news/news_display.php?id=1037) and the more recent Leimberg Information Services, Inc. (LISI) podcast.

There are several other items to highlight, however, regarding WTP. First, their "JumpStart Coaching" program, which is a free additional coaching session in addition to your basic training session (WTP 101: The Basics), is a very popular addition for current and potential WTP users. This program walks you through the actual preparation of your first set of client documents. Second, ILS offered a successful continuing education program last year. They intend to offer the next program in or about May 2007. Details will be forthcoming. Third, in conjunction with the National Association of Estate Planners and Councils (NAEPC), Jonathan Blattmachr will be speaking to various local estate planning councils across the country, which will include highlights of WTP.

The last (but not least) item is Jonathan's "Supercharged Credit Shelter Trust," which he has added to WTP. He highlighted this technique on Tuesday afternoon at the ILS booth. Jonathan's and Mitchell Gans' article on this technique is available on the ILS website: http://www.ilsdocs.com/docs/alerts/SuperCharged_Credit_Shelter_Trust.pdf. The companion to this technique, which involves the creation of a lifetime QTIP marital trust, resulted in an updated lifetime QTIP template, which is now available to current subscribers on the ILS website.

2. Lawgic (http://www.lawgic.com): Lawgic announced the future release of new Wills & Trusts products for New Jersey (Andy DeMaio's firm as editors) and Tennessee (Steve McDaniel's firm as editors). Lawgic representatives are also discussing a new, nationally-known editor for their California Wills & Trusts product. They hope to release the official news on the California ACTEC fellow's addition to the Lawgic team in the near future.

In addition to Lawgic's estate planning and drafting system, they are working on a Florida probate system. The system will prepare probate pleadings/documents in the same logical manner as the drafting system. Lawgic's Florida probate system is scheduled for release in 2007.

3. WealthCounsel (http://www.wealthcounsel.com): WealthCounsel is an ever-popular booth. The WealthDocs drafting system, which also runs on the HotDocs platform, saw several changes in 2006, as well as some developments in the WealthCounsel membership in terms of ancillary services to subscribers/members.

WealthCounsel implemented the transition of conduit trusts to accumulation trusts in the WealthDocs "Retirement Trust" library (consistent with Priv. Ltr. Rul. 200537044, obtained by WealthCounsel member Phil Kavish as represented by Robert Keebler of Virchow Krause, CPAs). For joint revocable trust plans, the same interview now includes ancillary documents for both spouses. There are also newly-expanded "Irrevocable Trust" options, including an ILIT designed to hold a second_to_die life insurance policy, either as a joint trust or an individual "spousal access" trust" (as supported by Priv. Ltr. Rul. 9748029). Finally, the WealthCounsel system implemented "Business Succession" documents in the library bearing the same name (including a buy-sell agreement and a deferred compensation agreement).

There are also new built_in scenarios (or plan designs) throughout the WealthCounsel system, allowing for streamlined data entry and document generation. This is an important update that should allow users to increase their efficiency and productivity.

In 2006, WealthCounsel began their online WealthDocs training program using Microsoft Live Meeting, as well as monthly WealthDocs webcasts (available to members in the Knowledge Base).

In addition, I would like to note that Tom Ray, co_founder of WealthCounsel, authored CHARITABLE GIFT PLANNING, which in my estimate is an excellent ABA RPPT Section treatise. (Tom is currently working on the second edition.)

C. TRUST ACCOUNTING & RELATED ADMINISTRATION SOFTWARE:

1. Gillett Estate Management Suite (GEMS) (http://www.gillettpublishing.com): In addition to my full review referenced in the first technology report this year, following are some updates regarding GEMS. Gillett Publishing has added five new state modules to GEM706 during 2006. They now currently support Illinois, Indiana, New Jersey, New York, Ohio, and Wisconsin. According to representatives of Gillett Publishing, more states are on the way.

Also, they added a Quicken interface to GEMAcct which permits the user to import asset and transaction information from brokerage accounts directly into the accounting module. This can save a considerable amount of time.

For more information, please visit the Gillett Publishing website, where you can download a free, fully-functional demonstration version of GEMS -- only limited in its printing capability.

2. FASTER Systems, LLC (http://www.fastersystems.com): New FASTER Systems products for 2007 are the addition of the New York and Connecticut Estate Tax modules. Both include state-level estate tax returns and applications for an extension to file and/or pay state-level estate tax. New York also includes an estate tax power of attorney and a tentative payment form. In addition, FASTER Systems maintains that their FASTER ASP is the only fiduciary accounting and estate/gift tax software offered in a secure, online, hosted environment.

D. RESEARCH SOFTWARE & SERVICES:

1. LexisNexis (http://www.lexis.com): Lexis introduced its new Tax Center, which streamlines research for those in estate planning and related areas. The "dashboard" separates the functionality of the new service into tabbed components, including "Research," "Get a Document," "Shepard's," "Tax News," and "Tax Forms." The research area is divided into primary and secondary/analytical sources. Under the "Estate, Gift & Trust" analytical sources, you can subscribe to the BNA Tax Management Portfolios and numerous other resources from CCH, Tax Analysts, Matthew Bender, and Kleinrock.

2. LexisNexis (http://www.lexis.com): Lexis also introduced its new Total Practice Solution for estate planning lawyers. This service is just being rolled out, so there is very limited information on this right now. However, based on their similar solutions in other areas of law, everything from calculations to drafting to practice/case management to research should be integrated. Please contact your Lexis representative for more details.

3. Lawyers USA (http://www.lawyersweekly.com): Lawyers USA offers client newsletters, which are personalized newsletters that also include an online component that law firms can add to their website or send via e_mail. They have produced these newsletters for estate planning lawyers in the past, but recently have added two new practice_specialty categories: real estate and elder law.

E. MISCELLANEOUS VENDORS:

1. Lucion Technologies (http://www.lucion.com): Lucion Technologies, which was founded by zCalc creator Jeff Pickard, featured a new addition to their FileCenter and FileBackup capabilities. FileConvert provides batch or bulk conversion of files currently in portable document format (PDF). You can set up a scheduled conversion, e.g., perform optical character recognition (OCR) during the middle of the night. This process converts image files, such as pictures (in TIF, JPG, or similar formats) and also image-only PDF files (that you have created using a scanner, which literally takes a "picture" of a document), into searchable PDF files.

2. Academy of Special Needs Planners (http://www.specialneedsplanners.com): The Academy of Special Needs Planners is a new national organization of attorneys dedicated to the practice of planning for people

with special needs. They are focused on providing members and the public with useful tools to assist them in the legal aspects of caring for themselves or their family members with special needs. There is also a public site: http://www.specialneedsanswers.com.

3. ElderLawAnswers (http://www.elderlawanswers.com): This site was founded by NAELA fellow Harry S. Margolis. It provides information to elder law attorneys and their clients.

4. Equity Trust Company (ETC) (http://www.trustetc.com): ETC is a leading custodial provider of self-directed IRAs and small business retirement plans. Due to recent legislative changes, ETC is offering a Roth 401(k) plan, which is available to anyone with a 401(k) or Solo(k) plan (without the income limitations of a Roth IRA).

5. Fort Pitt Capital Group (http://www.fortpittcapital.com): As a new vendor at the Heckerling Institute, Fort Pitt Capital Group, with offices in Pittsburgh and Naples, is a registered investment advisor with over $1 billion in assets under management. They offer customized individual securities accounts, mutual fund portfolio management, and the Fort Pitt Capital Total Return Fund. Fort Pitt Capital Group does not offer trust services.

6. The Insurance Design Center, LLC (http://www.insurancedesigncenter.com): The Insurance Design Center's goal is to disseminate truth and accuracy to the advisor community regarding the life insurance industry. They seem to offer an abundance of information on premium financing (the good, the bad, and the scary!). The Insurance Design Center only acts in an advisory capacity and apparently does not sell life insurance products (e.g., "we simply offer advice").

10. Lincoln Financial Group/Lincoln Financial Advisors (http://www.lfg.com): As yet another new vendor at the 2007 Heckerling Institute, Lincoln Financial Group has received numerous honors in the financial planning industry. The Financial Planning Association recognized Lincoln as the first FPA Alliance firm. Lincoln acquired Jefferson Pilot last year to expand its insurance and financial planning platform.

11. National Philanthropic Trust (NPT) (http://www.nptrust.org): NPT provides "effective philanthropic solutions for individual donors, families, advisors, and financial institutions." NPT has extensive experience with supporting organizations and donor advised funds, both of which were discussed during the general and special sessions by Kathryn Miree and Jerry McCoy (in connection with the Pension Protection Act). NPT has lowered its fees on its donor advised fund, and is celebrating its tenth anniversary this year.

12. Northern Trust (http://www.northerntrust.com): New and noteworthy items at Northern Trust include: (a) a dedicated website, Wealth Advisor, offering around-the-clock access to information and Northern Trust resources to help advisors meet their clients' needs; (b) Delaware capabilities, providing full asset protection and administrative trust capabilities; (c) expanded access to Northern Trust Will & Trust Forms; and (d) enhanced investment solutions, including third-party manager solutions.

13. Private Family Trust Company (PFTC) Service by South Dakota Trust Company, LLC (SDTC) (http://www.privatefamilytrustcompany.com): South Dakota Trust Company, LLC highlighted their new website, which has been improved to address the common questions and concerns that families and their advisors face in pursing a PFTC. SDTC serves as corporate agent and/or trustee agent for several PFTCs established in South Dakota.

14. Wachovia Trust (http://www.wachovia.com): Wachovia Trust introduced their new investment management platform. The Advantage investment advisory process is one of just a few offerings combining sophisticated investment products with the advice of a corporate fiduciary. Wachovia was selected as the 2006 Platform Provider of Year by Private Asset Management magazine as a result of this

innovative new option.

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Our on-site local reporters who are present in Orlando this year are Gene Zuspann Esq. of Zuspann & Zuspann in Denver, Colorado, Herb Braverman Esq. of Walter & Haverfield, LLP in Cleveland, Ohio, Merry Balson Esq.of Wade, Ash, Woods, Hill & Farley in Denver, Colorado, Paul Hood Esq. of L. Paul Hood Jr. (APLC) in Mandeville, Louisiana, Joanne Hindel Esq. of Fifth Third Bank in Cleveland, Ohio. Jason Havens Esq. of Havens & Miller PLLC in Destin, Florida, Alan Rothschild Esq. of Hatcher, Stubbs, Land, Hollis and Rothschild, LLP in Columbus, Georgia, and Kimon Karas Esq. of McCarthy, Lebit, Crystal and Liffman Co., LPA in Cleveland, Ohio. The editor again this year will be Joseph G. Hodges Jr. Esq, a solo practitioner in Denver, Colorado, who also is the Chief Moderator of the ABA-PTL List.

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A complete listing of the proceedings and speakers is available on **the Institute's Web site**

# Report #8

As we have done in January for the last ten 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 41th Annual Philip E. Heckerling Institute on Estate Planning that is being held January 8-12, 2007 at the Orlando World Center Marriott Resort and Convention Center in Orlando, Florida, a new venue for the Institute this year. A complete listing of the proceedings and speakers will be published here later and is also available on the Institute's Web site at http://www.law.miami.edu/heckerling.

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This Report contains coverage of the Thursday afternoon Special Sessions on The Ethics of Asset Protection, IRS Analysis of Gifts, Estate Planning for Real Estate Transfers, and a Holistic Approach to Analysis of Private Annuity Trusts to Defer Capital Gains

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Special Session 4-A - Simplified Trail Resolution from an Estate Planner's Point of View. Thursday afternoon, January 11, 2007 Presenters: Robert Goldman, John Rogers, Bridget Logstrom and Bruce Stone

The substance of this Special Session is covered by the similar Special Session 3-A that was presented on Thursday afternoon and the main Session that was presented on Thursday morning.

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Special Session 4-B The Ethics of Asset Protection Planning - An Oxymoron Thursday afternoon, January 11, 2007 Presenters: Alexander Bove, Jay Adkisson, Matthew Matiasevich and Gideon Rothschild

Reporter: Joanne Hindel Esq. of Fifth Third Bank in Cleveland, Ohio

Alexander introduced the session by saying that the concept and the sub-specialty of asset protection planning in the law are generating more and more controversy and criticism, even angry criticism, most of it directed at asset protection trusts, and most of that directed against offshore asset protection trusts.

He said that it is puzzling that articles criticizing asset protection planning don't make an equally emotional attack on such things as limited liability companies, bankruptcy-remote entities, acquisition of exempt assets, and pre-bankruptcy planning in general.

He poses a typical scenario of a radiologist, who, as a result of a flawed X-Ray machine, has a rash of malpractice claims filed that are then all settled. Six months later, when no actions are pending, he is considering the establishment of a self-settled asset protection trust.

Alexander then turns over the discussion to Jay Adkisson. Jay approaches the discussion from the perspective of a litigator and says that asset protection planning really boils down to two issues:

1. Is asset protection planning (APP) per se fraudulent?

2. Are attorneys who do this kind of work committing an ethical breach?

He points out that facing discipline in this area will involve questions of moral turpitude that will justify a lengthy review and stiff penalties if found liable. He also states that most malpractice insurance will not cover the lawyer if found liable in this area.

He says that some states, such as California, put this area under the category of interference with justice.

He says that a disciplinary tribunal will apply ethical principles but the law of fraudulent transfers may also be applied.

He differentiates between the states that follow the Model Rules and those that follow the Model Code and indicates that in the Model Rules states, practicing in the area of APP will not be found to be a violation of the ethical rules but in the states following the Model Code, APP will be considered a per se violation.

He says that it is important to understand what a fraudulent transfer is and which ethical rules of your jurisdiction apply. He suggests that maintaining a disciplined case review and intake system can help in actions involving this area. He also suggests that the lawyer pay attention to the possibility that you are acting in a capacity other than just planner for your client, for instance when you are dealing directly with creditors of the client.

Matthew starts off by pointing out that many early Americans came to the U.S. in order to flee onerous creditor laws in other countries and were themselves debtors. He also mentions that Thomas Jefferson might have drafted the first Asset Protection trust when he set up a spendthrift trust for his daughter.

He points out that contrary to general belief, APP is meant to avoid fraudulent transfers and keep clients on the right side of the law.

He warns that the financial services industry has engaged in the creation of products to provide for asset protection and that APP is being productized with clients expecting standardized pricing for the service.

He analogizes APP to a swimming pool with the shallow end consisting of the safe methods of APP and the deep end having no bottom and containing mutant sharks otherwise known as litigators.

He continues this analogy by suggesting that the shallow end has statutes that are intended to let people protect and plan. His examples include state and federal exemption planning and corporate planning. He also says that spendthrift trusts are an example of traditional APP and that insurance products also represent a transfer of risk from the individual to the insurance company with the client having the ability to keep assets.

He does point out that laws have developed to limit the planning one can do in the shallow end of the pool such as the Bankruptcy Act and spendthrift protection limitations.

He then suggests that in the middle of the pool are the laws that are not intended to protect against creditors but have the effect of APP. His example is that of a charging order protection allowing the protection of partnership assets so that for instance, a partner can't force his other partners into an agreement that involves his own creditors. He also points to tax shelters as good examples of legislation in this area.

He warns that if the lawyer plans to practice in this area, you have to have an understanding of the laws so as not to inadvertently place your client or their assets in jeopardy.

He then describes the deepest end as the area where the legislation has prohibited APP. He says that all questions in this area will be resolved against you and it is fraught with high client risks such as losing their business and being subject to criminal sanctions.

He says this is where the fraudulent transfer laws exist and suggests that one should never even use the term: asset protection but instead refer to this area as the creation of self-settled spendthrift trusts.

Having said that he points out that most states do not allow these kinds of trusts to escape creditor access and that since there have been so few cases in this area, you don't know how courts might rule if a matter is litigated and it is best to not draft domestic asset protection trusts.

He says that if a foreign asset protection trust is challenged the court might order repatriation of the assets or throw the settler in jail.

He also mentions that most of the bad cases seem to deal with trusts created in the Cook Islands.

Gideon then agrees and suggests that the bad case law decisions in this area are similar to the FLP arena with bad facts making bad law. He also suggests that we all engage in APP when we draft LLCs. Gideon also suggests that you may actually be held liable for malpractice if you don't advise your clients about APP options and uses a tenancy by the entireties situation as an example.

He suggests that this area can be handled ethically if you conduct proper due diligence including the review of a client's financial records and the preparation and completion of an APP audit checklist. He also suggests that the lawyer should keep a record of the clients that have been rejected to show a court if necessary to substantiate the review and due diligence aspect.

He recommends conducting a solvency analysis: what will the client retain after the transfer of assets to an asset protection trust?

He reviews a few cases and points out that if legitimate reasons can be found, the courts will uphold self-settled trusts. He mentions some legitimate reasons for foreign asset protection trusts might be to engage in asset diversification, benefit foreign heirs or avoid forced heirship laws. He also points out that some laws, notably the bankruptcy laws, do allow self-settled trust that are older than 10 years.

All the panelists did a great job of providing another perspective on asset protection planning and on dispelling the commonly held belief that this is done to defraud creditors.

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Special Session 4-C It is Better to Give and then Receive - is the IRS's Favorable Analysis Correct?
Thursday afternoon, January 11, 2007 Presenters: John Bergner and Mitchell Gans

Reporter: Kimon Karas Esq. of McCarthy, Lebit, Crystal and Liffman Co., LPA in Cleveland, Ohio

This was a special session following up on the earlier presentation by Mr. Bergner of "Waste Not Want Not---Creative Use of General Powers of Appointment To Fund Tax-Advantaged Trusts."

Basic fact pattern to the presentation. What is attempting to be solved is the situation between spouses of unequal wealth and the potential wasting of the poorer spouse's unified credit.

Example: Assume richer spouse has $4M in assets, poorer spouse has assets of $200,000. First spouse dies when credit amount is $2M, and second spouse dies when credit is still $2M. If richer spouse dies first, typical A/B trust arrangement works well by funding the bypass trust and the balance to the marital trust. The bypass trust passes to heirs after surviving spouse's death at no tax and surviving spouse's estate pays tax on the amount in marital trust of $2M plus her own assets of $200,000, or $90,000. Family receives $4.1M after death of second spouse. Alternatively if poor spouse dies first only $200,000 of $2M of credit shelter trust is funded "wasting" $1.8M of credit. When surviving spouse dies with a taxable estate of $4M with an estate tax of $900,000, only $3.3M passes for the family.

Traditional solutions are:

* Rich spouse makes a lifetime outright gift to poorer spouse; or

* Lifetime QTIP.

Problem is oftentimes (or sometimes) the richer spouse is concerned with "control."

Solution based on PLRs 200101021,200210051,200403094, and 200604028. Generally they are the same with some variations with the exception the 2006 ruling the spouse had the right to disclaim.

Rulings.

* Richer spouse creates and funds a revocable trust;

* Richer spouse grants poorer spouse a general power of appointment by formula (so as to use poorer spouse's unused unified credit) exercisable during life or at death, creating a bypass trust for the surviving spouse or if the spouse does exercise the power of appointment that the assets pass to the bypass trust on the lapse of the power; Note-Richer spouse retains right of revocation over general power of appointment that lapses at the moment of death.

* Surviving, richer spouse, is granted rights in the bypass trust but does not have powers that would cause inclusion in richer spouse's estate.

IRS Holds:

* No taxable event occurs while both spouses are living so long as the general power of appointment is not an intervivos power that is exercised.

* Upon poorer spouse's death, richer spouse makes a completed gift to poorer spouse that is the subject to poorer spouse's general power of appointment.

* Gift from richer spouse to poorer spouse qualifies for the gift tax marital deduction.

* Property that is subject to the general power of appointment is includible in poorer spouse's estate.

* Poorer spouse is treated as transferor of all property that funds bypass trust, including property that passes through the e exercise or non-exercise of the general power of appointment.

* Richer spouse can be both beneficiary and trustee of bypass trust so long as the power to make distributions is limited by ascertainable standards and can have an intervivos and testamentary limited power of appointment over the trust property.

* Richer spouse's property probably does not receive a new income tax basis at poorer spouse's death, at least to the extent of richer spouse's interest in the property.

Mr. Gans addressed possible attacks with the strategy.

* The gift to the spouse must qualify for the marital deduction. IRS concludes it qualifies but there is no analysis associated with its conclusion. Mr. Gans cited Johnstone, 76 F2d 55 (9th Cir.) for the proposition that a general power of appointment that can be revoked at any time but that is extinguished if the donee dies causes Section 2041 inclusion for the donee. The gift is made at moment before death. An alternative argument is that the spouse is granted a limited power of appointment and because of that power the gift is incomplete.

* Is there is terminable interest?

Mr. Gans believes there is some risk but that can be addressed as follows:

* Spouse exerecises the power of appointment citing RR 82-184;

* The spouse's power if it lapses passes to spouse's estate;

* Create a QTIP. .

3. Sections 2038 (Skifter analysis) or Section 2036. Mr. Gans states Reg. Section 25.2523(f)-1(f), Ex.11, which provides a lifetime QTIP cannot be challenged by IRS under either Section 2036 or 2038.

4.Creditor argument under Section 2041. The limited power of appointment should foreclose that argument.

The presenters discussed other possible applications of this strategy between spouses and others where control is not an issue. For example special assets or even between non-spouses (same sex partners). For example in a married couple situation assume in husband and wife situation husband owns $2M of assets and wife has a $2M IRA. If wife dies first and has a general power of appointment she can direct the husband's other assets of $2M fully funds a credit shelter trust and her IRA is left directly to the husband qualifying for the marital deduction and also allowing the husband to rollover wife's IRA.

The presenters also suggested that in estates of less than $2M that spouses create a joint trust each having a general power of appointment. In the case posited the parties do not care about the marital deduction and leave everything to a credit shelter trust. This strategy is possible only if there is no separate state estate tax because the parties have intentionally not structured a marital disposition.

Mr. Gans discussed another alternative based on the fact pattern. Richer spouse creates a revocable QTIP for spouse, or just places assets in QTIP for spouse. Trust provides income to life for spouse, the revocation power terminates at spouse's death, at spouse's death the assets are split into a credit shelter/marital allocation with the bypass trust for the spouse who is granted a limited power of appointment and also has a veto power over distributions. Spouse has an invasion power subject to ascertainable standards. The QTIP election is made following spouse's death. The potential issue is filing a gift QTIP in the year of death. Mr. Gans posits that should be acceptable but if not the spouse has retained a special power of appointment making the transfer an incomplete gift.

Mr. Gans then reviewed a concept that he called "Supercharged Credit Shelter Trust" that will be the subject of an article that he and Jonathan Blattmachr have written. Comparing a conventional credit shelter trust with this concept assuming the trust earns 8@ and an effective tax rate of 25%. Assuming $2M in trust, after five years a conventional trust has $2.68M vs. $2.94M; after 20 years the spread is $6.41 vs. $9.32.

What is the concept.  Husband creates QTIP for spouse.  At spouse's death Section 2044 inclusion in spouse's estate.  Husband is a permissible income beneficiary of by pass trust.  Under Ex. 11 Sections 2036/2038 do not apply at husband's death.  The credit shelter trust for income tax purposes is treated as a grantor trust under Reg. Section 671-2 because husband funded the trust.  For estate tax purposes a trust that is included in the spouse's estate but for income tax purposes a trust deemed created by the husband. The income tax paid by the husband for the trust allows the trust to grow without income tax consequences.  There is no gift under RR 2004-64 when a grantor pays tax for his grantor trust there is no gift.  There is a possibility of basis step up also in this trust.  Husband can swap assets income tax free or alternatively under Reg. Section 1001, Ex 5, when grantor trust status ends it is deemed as if grantor transferred assets at that time (again for income tax purposes).

The presenters also discussed the concept has merit even if portability of unified credit becomes the law.

The presenters' outline included a number of various forms that may be of interest.  Included in the forms is an "Inheritance Trust" form--designed to create a trust for a person that can receive property inherited from others as well as a series of 12 other forms dealing with grants of testamentary and inter vivos general powers of appointment,  commentary regarding the non-exercise of  general powers of appointment, and exercises of testamentary general powers of appointment.

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Special Session 4-D Death, Dirt and Duties: Estate Planning for Real Estate Transfers Thursday afternoon, January 11, 2007 Presenters: Wendy Goffe and Scott Osborne

Reporter:  Merry Balson Esq.of Wade, Ash, Woods, Hill & Farley in Denver, Colorado

This session reviewed selected real estate issues, including §1031 exchanges.

Title Insurance and Deeds.  Mr. Osborne, a real estate attorney, began by addressing the preferred type of deed to use.  While this will inherently be a state law issue, the issues to be considered are the same regardless of the jurisdiction.  The first question is what kind of warranties do you want to convey with the property, and whether you want to convey the same warranties you received when you took title.  If the passage of warranties is important, generally you should not use a quitclaim deed, because in many states, that will destroy the ability to claim under prior warranties (e.g., the warranties possessed by the grantor). Many people use trustee deeds, which are essentially limited warranty or special warranty deeds, which tend to limit the warranties conveyed to those things created or suffered by the grantor during the grantor's ownership only, and not to acts occurring prior to ownership.  His position was that generally speaking you do want those warranties to pass to the donee.  He suggests obtaining a copy of the deed the grantor received originally (i.e., the vesting deed) from either a title insurance company or from the courthouse.

In the West, no one relies on warranties contained in the deed because most rely on protections contained in the title insurance policy purchased at the time the grantor acquired the property.  Note that if you convey title to an entity (including an LLC, or trust) the title insurance may not cover the entity as an insured in many inter vivos transactions.  The ATLA policy contained a rather limited definition of insured for many years, and did not include many entities even when they are used in estate planning transactions.  Owners policies are not assignable, and claims can be made only by the covered "insured" while they own the policy.  The definition of "insured" in most homeowners policies since 1998 has been expanded to contemplate transfers to trusts with continuation of coverage, but that definition remains limited and does not include all entities used in the estate planning context.  If you are aware of a potential transfer to an entity at the time of purchase, Mr. Osborne suggests obtaining a "Fairway" endorsement (based on Fairway Development Co. v. Title Insurance Co. of MN, 621 f. supp 120 (ND Ohio 1985)) an example of which is contained in the materials, to ensure that the policy coverage will continue even if there is a change in the members of an entity.    See also, Gebhardt Family Restaurant LLC v. Nation's Title Ins Co. of NY, 132 Md. App. 457 (2000) for example of attempt by grantors to obtain coverage when property was transferred to an LLC.  A deed conveying warranties may create rights in the grantee to claim through the grantor, but many states limit the damages/claim to the amount the grantee paid for the property, which may be a problem where family members contribute to the LLC and no payment is actually made.  See e.g., Point of Rocks Ranch, LLC v. Sun Valley Title Ins. Co., 146 P.3d 377 (Idaho 2006) where LLC claimed title company had an obligation to defend title under warranties by grantor.  The claim was denied there because the deed contained language that the transfer was subject to all easements of record, and the claim related to an easement not covered in the title policy, but that was of record, therefore, there was no breach of warranty.

Options to preserve title policy coverage include:

(1) obtaining a "Fairway" endorsement on the front end;

(2) purchase an additional or successor insured endorsement for the policy; or

(3) obtain a new owners policy, which is less expensive if done in connection with a refinance of the property.

Note that the new 2006 ALTA policy adopted in most states has a significantly broader definition of the named insured, and includes transfers to other entities, even if no consideration is actually paid if the entity is wholly owned by insured/grantor.  The policy is reproduced in the materials.

If residential real property is transferred with a mortgage it is not subject to the due on sale or due on transfer provisions of the mortgage under federal law.  However, commercial properties are not protected in the same manner, and if a right to transfer is not contained in the mortgage, you must obtain permission from the lender to make the transfer or the note may be accelerated.

Ms. Goffe addressed IRC §121 which permits an exclusion of gain up to $250,000 per person, or $500,000 for a married couple, when the residence is used as a principal residence for a period of 2 out of 5 years, and the ownership and use tests are satisfied.  So long as one spouse meets the ownership requirement and both meet the use requirement, the full $500,000 exclusion is available.  The $250,000 per person exclusion can also be applied to separately owned residences if the ownership and use tests are met.  Section 121 contains some exceptions for shortened use and fractional reductions, including

(1) a change of employment where the new place of employment is at least 50 miles from the old place of employment,

(2) certain health issues;

(3) unforseen circumstances regarding involuntary conversion, disasters, unemployment, divorce or separation, multiple births from the same pregnancy and other facts and circumstances (such as an adoption requiring an additional bedroom in the house, spouse moving to hospice, and need to parent/in-law); or

(4) a sale due to a move to the nursing home.

The safe harbor applies if a qualifying individual (i.e., taxpayer, spouse, co-owner or person who lives in the same house, or persons related to these individuals) applies to the IRS.  The reduction is based on a fraction stated in the Code.  Tacking of ownership and use periods is available in some limited circumstances, including for certain military personnel and overseas spies.  The gain exclusion is available once every two years, and the taxpayer can opt not to apply it to a transaction.  The gain exclusion is not available where the residence is owned by an irrevocable trust, but does apply to any grantor trust, life estate, coop and sale of a remainder interest in the residence if the sale is to an unrelated party. If a taxpayer has multiple residences a facts and circumstances test applies, where the IRS looks at which home is used the majority of the year, where the taxpayer is employed, the address used for tax returns, automobile and voter registration, where the taxpayer has a driver's licence and where he/she banks.

Mr. Osborne then addressed §1031 exchanges. The materials discuss the mechanics and requirements so he did not review those in detail. With the increased personal residence gain exclusion, the §1031 exchanges have become less common. Traditionally these are used for rental property, where the taxpayer trades property throughout his/her life without gain recognition, then dies owning the property and receives a step up in basis. Usually the taxpayers who use the §1031 exchange are "pathological tax avoiders." The personal residence gain exclusion provides some additional flexibility when using the 1031 exchange because a taxpayer can exchange a property, then live in it for the required time, sell it and exclude much of the gain.

Mr. Osborne then addressed reverse exchanges which is not in the materials and is a misnomer. It is not actually a reverse. Instead, it is a method of parking property you want to acquire prior to the time you sell property you want to exchange. You should analyze the transaction, and the potential tax benefits and the expenses involved to ensure it makes sense before automatically entering into §1031 exchanges. 1031s have been available since 1979, but in 2000 Revenue Procedure 2000-37 (effective September 15, 2000) set out safe harbors for these transactions. The safe harbor contains strict time limits to identify the relinquished property (45 days) and to complete the transaction (180 days), so the client needs to have the property in mind at the outset. If the safe harbor time limits are not followed there are general rules that may still protect you, but keeping within the safe harbor is certainly better.

Exchanges of mature property for property under construction presents unique problems. Identification of the property can be difficult if it has not yet been built, but you can reference plans and specs or provide a general description of the project. The easiest way to deal with construction problems is to wait to exchange property until the property under construction is far enough along to have sufficient value to soak up all proceeds from the relinquished property, and then do a simultaneous transaction (i.e., delay the closing until the construction is complete). If this is not possible, then close within 180 days after the trade. There can be difficult issues surrounding the use of sales proceeds by the intermediary. Sales proceeds (from exchange property) cannot be used to pay for the construction. Monitoring and participating generally in construction is permitted, but be mindful of the constructive receipt issues.

Common §1031 problems/issues include: compliance with the strict safe harbor timing rules; ensuring that the new investment is at least as expensive as what is being sold; creation of unintended tax when cash is taken out of the sales proceeds (e.g., refunds of security or other deposits) or when sales proceeds are used to fund non-property related acquisition costs (these can usually be funded separately); using a §1031 exchange where there is personal property involved (e.g., these exchanges do not usually work for hotels and apartments for this reason); using an entity to sell and individual to purchase or vice versa (the same entity that acquires the property must do the exchange); ensuring you have a good intermediary/qualified facilitator sot that the transaction works properly (most states have these available); and attempting to use §1031s on second homes/vacation rentals.

Ms. Goffe reviewed the many charitable giving issues that can arise with real estate. The materials on this topic are in her main outline on estate planning for the second home. Valuation and substantiation rules must be followed when donating real estate to charity. The general rule is that the asset must be valued at fair market value. A qualified appraisal by a qualified appraisal is required to obtain the charitable deduction if the asset is valued at more than more than $5,000. Additionally, if the value is in excess of $500,000 an appraisal summary must be filed so the IRS can determine whether the value is inflated. If the charity disposes of the property within 3 years (formerly 2 years), the charity must file a Form 8282 showing the amount they received on the sale of the property. The Pension Protection Act ("PPA") also increased the penalties for overvaluation. Note that if the value of a CRT remainder is less than $5,000 there is no appraisal requirement.

Prearranged sales are not permitted. If the donor enters into a binding contract to sell prior to the transfer to the charity, no deduction will be allowed.

Ms. Goffe then discussed the unrelated business taxable income (UBTI) issues. Generally, if income from a trade or business is not substantially related to the exempt purpose, it will be UBTI and subject to income tax. However, most passive income is subject to UBTI only to the extent that it is derived from debt financed property. The Tax Relief and Health Care Act of 2006 (enacted in December 2006) changed the UBTI rules with respect to CRTs. Rather than disqualifying the CRT for the entire year if it had any UBTI, under §424 only the UBTI is taxed and the CRT is not tainted.

Transferring mortgaged property to a charity creates UBTI to the recipient because it will be considered debt financed income. However, if the transfer occurs through a devise on the death of a donor, the first 10 years of ownership are not treated as debt financed. Additionally, the charity can own property for 10 years if the donor had the debt for at least 5 years before the transfer to the charity.

Close attention must be paid to the self dealing rules when transferring real property to a private foundation, CRT or CLT. For example, if a mortgage was placed on the property within 10 years prior to the transfer. If the donor is personally liable on the mortgage, the CRT can be treated as a grantor trust and will lose its benefits and the donor will be liable for the capital gains tax. With few exceptions, the self-dealing rules prohibit any transaction between a “disqualified person” and a foundation, CLT or CRT. The disqualified person cannot continue to reside in a residence (even if rent is paid) where a home is transferred to a charity.

Fewer traps exist with outright gifts of real estate to charities. The deduction value will be the fair market value only if the donor is not a dealer in the property. A dealer’s deduction is limited to basis. When a donor makes a gift of real property to her foundation the deduction is also limited. However, the donor may not receive any benefit in exchange for the transfer (e.g., if donor obtains favorable zoning on property for development of adjacent property).

A charity can purchase property for a bargain sale. In that case, there must be an allocation between a gift and a sale, and the donor will recognize gain only on the sale portion.

The self-dealing rules present problems for CLTs funded with commercial real estate. The lease of real estate to the grantor or persons related to the grantor will give rise to self-dealing tax, but you can plan around this, usually with a $0 rent. Foundations, CLTs, and CRTs are subject to the excess business holdings rule, and must dispose of those holdings within 5 years to avoid the excise tax. Ms. Goffe noted that a disposition back to the grantor or a related party is prohibited. The Code authorizes 5 year extensions under certain circumstances.

Ms. Goffe mentioned that you need to be mindful of the self-dealing rules with disclaimers of real estate that pass to a private foundation. The disclaimant who is also a disqualified person should not be in control of the real estate in the private foundation for management or distribution purposes to avoid the self-dealing rules.

If real estate owned by an S corporation is contributed to a CLT, the CLT would be a permitted shareholder as an S corporation, and a nongrantor trust could elect ESBT treatment, but the CLT will be taxed on income at the highest rate and under §642(c) it is denied the charitable deduction, so it loses its tax benefit.

Ms. Goffe noted that fractional gifts of real estate are addressed in the material so she would not discuss this today.

Charitable gift annuities can be funded with unmortgaged real estate but are a type of bargain sale. Note that under the new private annuity proposed regulations the amount realized is going to be taxed at the fair market value of the contract and immediately subject to capital gain tax. Charitable annuities are not currently subject to that rule, but Senator Carl Levin suggested this might be coming in future legislation.

Mr. Osborne reviewed conservation easement issues. A conservation easement is a permanent restriction on privately owned land that creates a charitable deduction for the value passing to the holder of the easement (a charity). The value of the easement is the difference between the fair market value before the transaction, and the value after the easement is imposed. Conservation easements can be made at death in a will or by election in the estate. The concept is that this will preserve open space and limit development. Conservation easements have become increasingly popular, with approximately 1700 private land trusts in the U.S., and 37 million acres of land subject to conservation easements. The PPA contained a number of provisions affecting conservation easements mostly as a result of abuses with the charitable deductions. The new provisions included: (1) the amount of the available deduction was increased; (2) the carryforward was stretched to 15 years; and (3) the penalties were increased on appraisers. Under Notice 2006-96, the IRS issued some transitional guidance including new appraiser guidelines. Generally the appraiser now needs a designation of some kind.

When a client wants a conservation easement, you need to consider several principal issues. Form documentation for a conservation easement is included in the materials. Consider the rights retained (which should not be so expansive as to destroy the conservation purpose) and the sufficiency of enforcement mechanisms in place for the land trust (which should include a cash gift for monitoring and enforcement). Keep in mind this is a permanent arrangement whether or not it turns out as the taxpayer might have hoped. The client's primary motive should be to conserve property, and the easement needs to further some conservation purpose. The appraiser needs to be reliable and believable. Finally, the statutory requirements must be fulfilled (e.g., any debt must be subordinated by the easement, and a land trust must accept the easement). Mr. Osborne commends to our reading the following cases in this area: Turner v. Comm'r, 126 T.C. No. 16 (May 16, 2006); and Glass v. Comm'r, 2006 U.S. APP Lexis 31387, 2006 Fed App 0464P (6th cir, Dec. 21, 2006).

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Special Session 4-E A Holistic Approach to Analysis of Private Annuity Trusts to Defer Capital Gains, Including Exit Strategies Thursday afternoon, January 11, 2007 Presenters: Jerome Hesch and Kevin McGrath

Reporter: Paul Hood Esq. of L. Paul Hood Jr. (APLC) in Mandeville, Louisiana

Hesch led off with a description of the benefits of private annuities over installment sales, at least prior to the promulgation of the proposed regulations that pertain to private annuities. He then described the new proposed regulations, which now cause recognition of all of the gain immediately (rather than over the life expectancy of the annuitant). He reminded everyone that pre-October 18, 2006 private annuities are grandfathered.

He then went over an example that was in his materials in which a private annuity could do for clients something that a GRAT could not do. Hesch underscored the importance of remembering to include a "switch" in a trust document to "turn off" grantor trust status since that status can be a bad thing if the trust property and income significantly grows in value.

McGrath then described the exhaustion test under the IRC Sec. 7520 regulations (and formerly under Rev.

Rul. 77-454). He reminded everyone that failure to meet the exhaustion test out to age 110 will cause an inadvertent gift. McGrath gave some potential solutions to the gift problem, which ranged from making a larger gift, beneficiary guarantees to spousal guarantees to funding the trust with a seed gift to using a self-cancelling installment note instead of a private annuity.

Hesch then discussed the advantages and disadvantages of the private annuity as far as the income tax consequences go. He reminded all that the income tax disadvantages of private annuities have always outweighed their advantages. Hesch suggested buying back the private annuity as an exit strategy.

The panel concluded with a guest, who discussed the ABA comment process relative to the proposed private annuity regulations. The ABA is likely to recommend application of the installment sales rules and the OID rules to private annuities in lieu of the draconian rule contained in the proposed regulations.

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Our on-site local reporters who are present in Orlando this year are Gene Zuspann Esq. of Zuspann & Zuspann in Denver, Colorado, Herb Braverman Esq. of Walter & Haverfield, LLP in Cleveland, Ohio, Merry Balson Esq.of Wade, Ash, Woods, Hill & Farley in Denver, Colorado, Paul Hood Esq. of L. Paul Hood Jr. (APLC) in Mandeville, Louisiana, Joanne Hindel Esq. of Fifth Third Bank in Cleveland, Ohio. Jason Havens Esq. of Havens & Miller PLLC in Destin, Florida, Alan Rothschild Esq. of Hatcher, Stubbs, Land, Hollis and Rothschild, LLP in Columbus, Georgia, and Kimon Karas Esq. of McCarthy, Lebit, Crystal and Liffman Co., LPA in Cleveland, Ohio. The editor again this year will be Joseph G. Hodges Jr. Esq, a solo practitioner in Denver, Colorado, who also is the Chief Moderator of the ABA-PTL List.

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Brought to you by the ABA-PTL Discussion List Moderators.

# Report #9

A complete listing of the proceedings and speakers is available on **the Institute's Web site**

As we have done in January for the last ten 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 41th Annual Philip E. Heckerling Institute on Estate Planning that is being held January 8-12, 2007 at the Orlando World Center Marriott Resort and Convention Center in Orlando, Florida, a new venue for the Institute this year. A complete listing of the proceedings and speakers will be published here later and is also available on the Institute's Web site at http://www.law.miami.edu/heckerling.

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Errata: The Report for The Perfect Storm Ethics Rules session on Thursday morning in Report No.7 was actually for the Special Session 3-E on the subject that was held Thursday afternoon. Thus, we will start below with the Report from the main morning session. We apologize for the mixup and any confusion.

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This Report contains coverage of the Thursday afternoon Special Sessions on Post-Mortem Planning for Retirement Benefits, Directed Trustees and Ethics Rules of Circular 230

Fundamentals Program #3 - Making Friends with Subchapter K Thursday afternoon, January 11, 2007 Presenter: Richard Robinson

The Report for this Program will be published later

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Special Session 3-A - Simplified Trail Resolution from an Estate Planner's Point of View. Thursday afternoon, January 11, 2007 Presenters: Robert Goldman, John Rogers, Bridget Logstrom and Bruce Stone

The substance of this Special Session is covered by the similar Session that was presented on Tuesday morning.

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Special Session 3-D - Coordinating Business and Succession Plans Thursday afternoon, January 11, 2007 Presenter: Jonathan Lurie

The Report for this Special Session will be published later

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Special Session 3-F - Planning with Derivatives and Structured Products Thursday afternoon, January 11, 2007 Presenters: Stacy Eastland and George Albright

The substance of this Special Session is covered by the Session by the same title that was presented on Tuesday morning.

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The Perfect Storm: How the Confluence of Tax Planning and Ethics Rules Can Sink the estate Planner, the Fiduciary and the Estate Plan Thursday morning, January 11, 2007

(Note: the report for Special Session 3-E for this topic was mistakenly included as part of Report 7 as if it was the report for the main session, so we are including the text of the main session report here. The reporter for both sessions is the same) Presenter: Mary Ann Mancini

Reporter: Paul Hood Esq. of L. Paul Hood Jr. (APLC) in Mandeville, Louisiana

Mary Ann Mancini presented the topic “The Perfect Storm: How the Confluence of Tax Planning and the Ethics Rules Can Sink the Estate Planner, the Fiduciary and the Estate Plan.”

Mancini highlighted the various ethics rules that apply to estate planners, and she noted that estate planners owe a duty to the system, which has increased substantially over the past few years due in large part to the so-called “tax gap.”

She pointed out a tension between the conflicting positions of the ABA and the ABA Section on Taxation relative to whether the position between the IRS and a taxpayer is adversarial.

She reviewed Circular 230. In particular, in reviewing Section 10.21, Mancini noted that practitioners must inform a client of a material omission or other noncompliance with the tax laws, even though the client has no duty to file an amended return. She also reviewed in detail Section 10.34, which applies to both written and oral advice. Mancini alerted all to the realistic possibility of success (one in three).

Mancini gave four central tenets for tax planning: the planner must represent the client diligently, you must keep client confidences, you can only accept information from the client if you have a reasonable belief that the information is correct and you can not mislead the IRS or allow the client to use you to mislead the IRS.

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Special Session 3-B It All Starts When the Participant Dies: The Executor's Guide to Post-Mortem Compliance and Planning for Retirement Benefits Thursday afternoon, January 11, 2007 Presenter: Natalie Choate

Reporter: Merry Balson Esq.of Wade, Ash, Woods, Hill & Farley in Denver, Colorado

This special session covered retirement benefit issues after the plan owner dies, the executor’s and trustee's duties, advising beneficiaries who have inherited a retirement plan. The materials are in Volume Two of the Special Session Materials, outline number III-B [available only to registrants - not sold after Institute].

There are at least three difficult issues that arise for the executor/trustee when the estate/trust consists substantially of retirement benefits.

1. Whether to recharacterize a Roth IRA conversion. A Roth IRA can be recharacterized and essentially returned to a traditional IRA during a certain period of time after conversion from a traditional IRA to a Roth IRA. The regulations permit the executor to essentially undo the initial conversion. The executor would have a duty to undo the conversion to avoid penalties to the estate. The problem arises where the Roth IRA beneficiary and the estate beneficiary are different persons for the following reasons. Upon conversion, income tax is generated and would be a debt owed by the estate if the tax is unpaid at the time of death. The executor would seemingly have a duty to undo the conversion to maximize the estate and avoid the tax. However, the Roth IRA beneficiary would receive the Roth IRA income tax free if it passes to him as a Roth IRA, and would have to pay income tax on the IRA if it is converted back to a traditional IRA. There is no guidance on how to handle this issue from the IRS or the courts.

2. Whether to complete a rollover of a distribution where the decedent took the distribution during life intending to rollover the distribution into another plan, but died before completing the rollover. As of 2001, the normal 60 day time frame to rollover assets could be extended by the IRS in cases of hardship, where not to extend it would violate equity or good conscience. The legislative history and regulations provide examples of hardship, which include institutional error, illness, famine, flood, and death. After years of resistance, the IRS has finally started to allow extensions for death based on hardship. Now the executor must put this on the checklist of things to do in an estate. The executor must not only look for distributions within 60 days of death, but because a hardship exception might be granted, older distributions might also qualify and the executor's responsibilities here are now unclear. Ms. Choate raised the additional problematic question of how the executor determines what IRA to contribute the funds to, or who to designate as beneficiary if a new IRA is created for this purpose. There is no clear guidance on this point.

3. Decedent's failure to take the minimum required distributions ("MRDs"). There is a penalty on the failure to take MRDs of 50% of the amount of the missed distribution. The executor is personally liable for the decedent's personal taxes, including the penalty. Note that when the executor requests a liability for income and other taxes be sure to include this on the list. If the executor notices that a decedent over age 70 1/2 reported no MRDs on prior income tax returns, the executor should file an amended income tax return for the year of the missed distribution attaching a Form 5329 (describing the amount of the missed distribution and calculating the penalty), and request a waiver of the penalty. The reporting is to be made on the return for year the distribution was missed. Filing the return is required not to report the income from the missed distribution, but to report that the decedent missed the distribution and therefore a penalty applies. The IRS will waive the penalty if the taxpayer shows good cause for missing the distribution, and that an effort was made to remedy the shortfall. The remedy is difficult when the decedent/owner has died because the beneficiaries, not the executor, have no control over the IRA. If the beneficiaries of the IRA and the estate beneficiaries are different persons, the IRA beneficiaries will not want to make a distribution from the IRA to satisfy the missed MRDs. Ms. Choate noted that the good news is that it now appears that the requirement to pay the penalty when the waiver is requested has been dropped from the instructions to Form 5329, and publication 590 (it never appeared in the Code or

regulations).  A related question is whether the statute of limitation period for missed distributions starts to run at the filing of the decedent's Form 1040 or upon the filing of the Form 5329.  The cautious approach (and the one recommended by Ms. Choate) is to recommend that everyone over 70 1/2, and everyone with an inherited IRA, file a Form 5329 with an explanation of how you calculated the distribution every year with every return showing there is no penalty owed just to get the statute of limitations started.

Next, Ms. Choate addressed issues relating to how retirement benefits are treated on the estate tax return.

1.  Retirement benefits are reported as annuities on the estate tax return.  The value of the assets in the IRA is the reported value, however, the application of the alternate valuation date rules on IRAs are unclear.  If poorly performing stock in the IRA is sold shortly after death and is reinvested in a stock that appreciates while the other estate assets are depreciating, the executor may want to make the alternate valuation date election.  The unresolved question is, for alternate valuation date purposes, is the IRA is the asset that is valued (in which case the higher value on the date that is 6 months after date of death is used), or do you look inside the IRA and determine value on a stock by stock basis (in which case the lower value on the date of sale is used).  The IRS has not issued any guidance on this issue, and as long as you are consistent on the return, you can probably value it either way.

2.  Several cases have now held that a valuation discount on the estate tax return is not available on an ira for the income tax liability built in to the account.

Ms. Choate reviewed cleanup strategies when things go wrong in an estate with retirement benefits.

1.   Payment of estate expenses, taxes, etc.  The IRS has hinted that if an IRA is payable to a trust that contains what is often boilerplate provisions authorizing the trustee to use assets of the trust as necessary to pay the estate's debts, expenses and taxes, that this may result in a nonindividual beneficiary (the estate) and the see-through rules will not apply.  Despite this hint, the IRS has never disqualified a trust for containing that clause in any published ruling, regulation or other authority. Approximately 50 rulings have allowed see through treatment, and these rulings are outlined at page 26 of the materials.

2.  Strategies where the decedent's estate is the beneficiary.  The primary advantage of an IRA is tax deferral, which can be achieved only by leaving the benefits to an individual human beneficiary or a qualifying see through trust.  The qualified beneficiary can stretch out distributions over the beneficiary's life expectancy deferring the tax.   If the plan is payable to an estate, the life expectancy payout is not available, and the payout period is generally much shorter resulting in less deferral.  If the owner dies before age 70 1/2, payout is 5 years for an estate; if death is after age 70 1/2, the payout is whatever was left of the decedent's life expectancy, which is better than 5 years usually, but not as good as the beneficiary's life expectancy.  In cleanup mode, there are several ways to deal with an IRA payable to an estate.

a.  Do not assume the default beneficiary is the estate just because there is no named beneficiary.  In many cases this is true, but you must read the plan document to be sure.  Qualified plans are required by law to be payable to the surviving spouse unless the spouse consents to another designation.  Some IRAs default beneficiary is the spouse or issue.

b. If the decedent intentionally named the estate as the beneficiary, look for way to invalidate that designation through failed requirement (such as spousal consent or missing notarization).

c. Consider reforming the beneficiary designation through a court proceeding if some evidence exists that the reformation would carry out decedent's intent. A recent PLR approved reformation of a beneficiary designation.

d. Use the spousal rollover through the estate or a trust by using the elective share. This is particularly useful where the spouse can select the assets to fund the elective share. The spouse could select the IRA as her elective share asset and then roll it over into her own IRA. The IRS seems to have no trouble approving a rollover of this nature where the spouse has the right to take the IRA out of estate or trust and she's the only one with the right to pay to herself.

e. Use the spousal rollover in a will contest, where a legitimate and reasonable settlement provides that the spouse can take the IRA as her share outright. The rollover will only work if litigation is bona fide.

f. Pages 38-40 of the materials set out a series of rulings going back into the 1980s where the IRS has allowed a rollover through an estate or trust where the spouse has the right to take the money out of the estate. Ms. Choate noted that one of her biggest gripes with the IRS is that despite the consistent PLRs on this issue, they refuse to issue a regulation or Revenue Ruling. As a result, IRA providers often require a letter ruling to allow this kind of rollover because the beneficiary designation is payable to the estate.

If the decedent dies before taking his MRD, the beneficiary must take it.

An estate or trust can distribute an IRA out to the beneficiary in tact and the fiduciary need not terminate the IRA to make the distribution. The trustee simply distributes the IRA to the beneficiary, who will take over as the successor beneficiary of the IRA and will receive distributions personally. The fiduciary should use the sample letter provided in the materials at page 47 to instruct the IRA provider to change title of the account to be payable to the individual as beneficiary. The plan administrator may say they cannot do that, and if they refuse, the fiduciary can transfer the IRA in the name of the estate or trust to an IRA provider that is more enlightened. Ms. Choate provides a lists of those providers who will allow this kind of transfer at her website: www.ataxplan.com.

Ms. Choate took a series of questions and answers as follows:

Q: Taxpayer is over 70 1/2, owns an IRA and realizes he hasn't taken the MRDs for several years. To calculate the MRDs, do you reduce the account balance by the MRDs that should have been taken? A: There is no authority for doing that and you should use the actual account balance, or get a ruling approving the reduction.

Q: Where the IRA names the estate as beneficiary, and a power of attorney gives the agent powers in estate and trust matters and the power to make gifts, can the agent change the beneficiary designation? A: The answer depends on the document and will be based on state law.

Q: A trust is the beneficiary of an IRA and is taking distributions over the life of the oldest beneficiary. The trust will be terminating and has multiple beneficiaries. Can separate accounts be set up for each beneficiary, using the oldest life expectancy for MRD purposes, so that each beneficiary is responsible for his or her own MRD? A: The law here is nonexistent. The IRS has allowed similar account set ups in PLRs, but the concepts are not easy to reconcile because technically they have a single account for MRD purposes.

Q: IRA beneficiary is a conduit trust with multiple beneficiaries and discretion to spray income and principal, where the oldest beneficiary's life expectancy is being used for MRDs. Must the trustee make distributions pro rata? A: There is no requirement that the MRD is distributed pro rata if the trust gives the trustee the power to spray distributions among a group. So long as the trustee takes the required distribution and pays it out to someone in the group, the MRD is satisfied, and there is no requirement that the payments be made equally.

Q: Can you designate subtrusts within a revocable trust (e.g., trust a, trust b, and trust c) and use the life expectancy of the oldest beneficiary of each trust for MRD purposes? A: Yes, if the beneficiary designation specifies x% to trust a, x% to trust b, etc., the division is created in the beneficiary designation, and the MRD for each subtrust will be the oldest beneficiary of that trust. However, if the beneficiary designation names the funding trust, then you must use the oldest beneficiary of all trusts. See Chapter 6 of Ms. Choate's book for more on this.

Q: 401(k) owner dies prior to the PPA naming a nonspouse beneficiary and the beneficiary is still within the 5 year deferral period with no distributions having been made since death. Can the beneficiary use the new provision under the PPA to turn this into an inherited IRA? A: It is unclear. Under PPA, a 401(k) beneficiary can now transfer the fund to an inherited IRA. The plan here required a lump sum distribution to be taken within 5 years, and the beneficiary chose to defer payment as long as possible. PPA creates a completely new right so we are in limbo where the existing regulations appear to say that the beneficiary must make an irrevocable election between the 5 year rule and the life expect payout no later than end of the year of the year of death. However, at the time of death there was no election to make, so the IRS will have to fill in this gap. A ruling may be needed here. Ms. Choate was hopeful the IRS would allow this conversion so long as you took a catchup distribution for the missed years.

Q: Does the new law apply to distributions from profit sharing plans? A: Yes, the ability to convert to an inherited IRA applies to any plan, including 403(b)s, defined benefit, pension, and profit sharing plans, not just 401(k)s.

Q: Does Ms. Choate still believe that if a trust that is not a conduit trust is payable outright to a beneficiary at some time that there is no need to look to the contingent beneficiaries for purposes of determining the oldest beneficiary? A: No, the regulations now say that this does not work, and you must consider the contingent beneficiary.

Q: Is there a solution for an IRA left to 1 of 5 children who was to divide it up among the siblings? A: Consider reformation or disclaimer.

Q: If the IRA funds are transferred to nonspouse beneficiaries, and the spouse later files for the elective share asking to satisfy the share with the IRA, is that eligible for a spousal rollover? A: If the funds are held in the IRA (not distributed to the nonspouse beneficiaries) and the spouse is successful, she can get the IRA as part of the election and may be able to make a late rollover, but if the other beneficiaries already received the IRA assets and paid the tax, this will not work and there are other problems.

Ms. Choate mentioned that disclaimers are often the Cadillac of post mortem planning. The chapter on disclaimers from her book is reproduced at page 51 of the outline. Keep in mind that when the default beneficiary is children, and the owner designated the estate as beneficiary, the IRS has said that the estate cannot disclaim because of the acceptance of benefits issues. Ms. Choate also noted that in Revenue Ruling 2005-36, the IRS held that when a surviving spouse takes a year of death MRD from the decedent's IRA, that would not constitute an acceptance of benefits for disclaimer purposes, and the spouse could later disclaim all or part of the plan benefits. Additionally, the IRS said that a year of death distribution does not have to be taken proportionately if there are multiple beneficiaries, as long as some beneficiary receives the money. If the spouse took out the MRD and an extra amount, she may still be able to disclaim, but she would note fall within the safe harbor of the revenue ruling so she would have the burden of proof to show she accepted the distribution but not the rest of the plan. Ms. Choate recommended that the spouse file something saying she is taking a portion of the plan now, but not deciding whether to accept the rest of the plan, so that she might have partial disclaimer. Note however that if the spouse directs the sale and reinvestment of IRA assets she cannot later disclaim because she exercised control over the assets.

Page 69 of the materials includes a chart outlining the differences between an inherited IRA and a person's own IRA. These differences need to be explained to the beneficiary of the inherited IRA, and include: the beneficiary owns the inherited IRA tax purposes, but it is the original owner's IRA, not his IRA for all other purposes; the beneficiary can take money out of the inherited IRA whenever he wants even if he is under age 59 1/2; the beneficiary cannot contribute to the inherited IRA, only to his own; the beneficiary does not have to take distributions from his own IRA until age 70 1/2 using the uniform lifetime table, but distributions from the inherited IRA must be taken out right away over the beneficiary's life expectancy based on the single life table; the beneficiary can convert his own IRA to a Roth IRA, but cannot convert an inherited IRA; and the IRAs cannot be commingled.

Plan administrators sometimes refuse to cooperate with an executor's request for information about the retirement plan and say they will only deal with the beneficiaries of the plan. In planning mode, the best solution to this problem is to include in the beneficiary designation form that the plan administrator must provide information to the executor. In cleanup mode, use the letter on page 49 of the outline which essentially notifies the plan administrator that because they have refused to provide the executor the necessary information, under §6018(b) the obligation to file the estate tax return for the retirement plan has shifted to the plan administrator as the person in possession of the asset.

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Special Session 3-C Directed Trustees, Co-Trustees, and Successor Trustees - Fiduciary and Regulatory Issues Thursday afternoon, January 11, 2007 Presenters: Dennis Belcher, David Pankey and Ann Hart Wernz

Reporter: Joanne Hindel Esq. of Fifth Third Bank in Cleveland, Ohio.

Dennis Belcher started off by reviewing the trustee's duties when delegating investment responsibility.

Assuming delegation is authorized by the governing instrument and applicable law, a trustee has these duties in delegating investment responsibility:

- determining whether the trustee should delegate all or a portion of the investment responsibility

- exercising reasonable care in the selection of the investment manager

- determining the scope and terms of the delegation, and

- reviewing and monitoring the delegation.

A trustee must be process oriented and should document the process followed in each of the steps mentioned. The first step should be the development of a written investment policy and should have a written agreement with the party to whom the delegation is made. If possible, the beneficiaries should also acknowledge the delegation.

He then discussed the duty of a directed trustee to supervise actions of a trust advisor.

In reviewing the trust instrument, the trustee should pay particular attention to the role of the trust advisor under the document; the terms of the grant of authority to the trust advisor; the duty of the trustee to supervise and monitor the directions given the trustee by the trust advisor; the procedure, if any, for the directed trustee to question the directions given the trustee by the trust advisor and whether there is any limitation on the liability of the directed trustee for following the trust advisor’s directions.

The panel then discussed five discussion problems contained in the materials.

In the first problem, a small community bank trust department, with little investment expertise, assumes trusteeship of a trust established by an individual who was a member of the Bank’s board. The trustee proposes to invest 50% in equities and 50% in bonds and the panel is asked whether the trustee should consider delegating the investment management to a third party and if so, what steps the trustee should take in this regard.

The panelists agree that the trustee should consider the delegation of investment management to a third party and then discuss what type of record of the delegation will be required and whether the trust beneficiaries should be consulted in the delegation.

In discussing the involvement of the beneficiaries, a distinction is made whether the beneficiaries want the trustee to use a particular third party investment manager, in which case the trustee should attempt to obtain some type of acknowledgement and perhaps exculpation for the use of that third party. If, however, the trustee chooses the outside money manager, then the input of the beneficiaries is not required.

The panelists discuss the terms of the delegation to the third party.

The trustee and the investment managers should agree on the investment objectives, the asset allocation, the appropriate measuring benchmarks and the trust’s cash needs.

The agreement should also address fees and the trustee should consider the total cost of the services and their tax deductibility.

If the investment manager to whom the trustee will be delegating the investment authority is an affiliate of the trustee, it will be necessary to add additional language covering the self-dealing aspects of using an affiliate.

A trustee who delegates the investment management function to a third party should consider whether the trustee can have the benefit of an exculpation clause for the acts of a third party investment manager. In some states, exculpation clauses are not enforceable. Even in those states that recognize exculpation clauses, the clauses are not generally enforceable in all instances.

The panelists discuss the appropriateness of providing the third party money manager with a complete copy of the underlying trust agreement. Dennis indicates that this should be done so that the money manager knows the trust terms and does not have to rely upon paraphrasing by the trustee, whereas Ann suggests that the entire document should not be given to the money manager and the terms of the delegation should be spelled out in the Investment Policy Statement (IPS) thereby protecting the confidential nature of the trust.

David addresses the question of ongoing monitoring by the trustee of the actions of the money manager and suggests that it should be done at least once a year or preferably more frequently. In conjunction with questions from the audience, the panel agrees that the monitoring should be a combination of review of the IPS and assurance that the money manager continues to follow the IPS terms and an investment performance review against stated benchmarks.

The panelists also suggest that if a lawyer is counseling an individual trustee, that the counsel include the retention of a consultant to help in picking an outside money manager.

David also suggests that the IPS include that the assignment to the money manager is not further delegable or assignable and should include an arbitration or dispute resolution provision.

In Problem #2, the corporate trustee is larger and is considering delegating investment management to an affiliated investment adviser.

Ann suggests that most states have laws that allow delegation to an affiliate but a trustee can obtain authorization to so delegate if no state law exists if the agreement provides for the delegation; the conflict for the trustee is waived by all the beneficiaries or a court orders the delegation to an affiliate.

She also indicates that in delegating to an affiliate with proprietary mutual funds fees and performance are factors that should be considered by the trustee.

She also points out that if the bank charges its full fee at the account level and then pays the money manager its fee out of the bank’s fee then no conflict exists.

In Problem #3 a small bank with little investment expertise is trustee of a grantor trust over which the grantor has retained all investment authority. When he dies, the stock plummets in value and the beneficiaries ask to meet with the trustee.

The questions posed to the panel are whether the trustee has any liability exposure and if so, on what basis?

Ann outlines the general state of the law in this area.

The UTC , in a significant departure from the Restatement (Second) and the common law, sets out two standards for a directed trustee, one applicable to direction of a settler of a revocable trust and the second to persons other than a settler of a revocable trust.

Section 808 provides that while a trust is revocable, the trustee may follow a direction of the settler that is contrary to the terms of the trust. With respect to a third party's power to direct, the UTC sets a significantly different standard than the common law in requiring the trustee to act in accordance with the direction unless it is manifestly contrary to the terms of the trust or the trustee knows the attempted exercise would constitute a serious breach of trust.

She suggests that the trustee should look for additional language in the document beyond the settlor's ability to direct the trustee and that is specific language giving the trustee the ability to retain the directed stock. She also suggests that the trustee meet regularly with the settler and his family, if he allows, and document the ongoing recommendation to diversify along with the family/settlor's decision not to do so.

In Problem #4, the bank serves as co-trustee with the son of the settler, who is also the president of the settlor's company. The trust assets consist primarily of company stock. The trust beneficiaries are the son and the daughter who also hold veto approval over the co-trustees in their ability to change any of the assets of the trust, including sale of the company stock. When the daughter asks the bank to sell the stock, the son, co-trustee objects.

The panel is asked what liability exposure the bank has and what it can do to protect it from liability.

All panelists agreed that this scenario is ripe for litigation since the daughter and son do not agree and the son has a self-interest in retaining the company stock. They all suggest that the trustee should soon seek court instruction on how to handle the situation.

Dennis further points out that the same lawyer should not represent both co-trustees however Ann suggests that both co-trustees can use the same expert witness to advocate diversification of the stock.

In Problem #5, a bank is asked to assume successor trusteeship of a trust that has purportedly been mismanaged by the prior trustee. The questions for the panel are what should the bank do before assuming trusteeship (what due diligence) and does the successor trustee have an obligation to review the actions of the predecessor and then bring an action against him if necessary.

The panelists agree that the bank should discuss the situation with the beneficiaries in advance of assuming the trusteeship and then, if warranted, pursue a claim against the prior trustee.

Dennis points out, however, that anyone should consider walking away from a bad piece of business and this one might be just that kind of situation.

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Our on-site local reporters who are present in Orlando this year are Gene Zuspann Esq. of Zuspann & Zuspann in Denver, Colorado, Herb Braverman Esq. of Walter & Haverfield, LLP in Cleveland, Ohio, Merry Balson Esq.of Wade, Ash, Woods, Hill & Farley in Denver, Colorado, Paul Hood Esq. of L. Paul Hood Jr. (APLC) in Mandeville, Louisiana, Joanne Hindel Esq. of Fifth Third Bank in Cleveland, Ohio. Jason Havens Esq. of Havens & Miller PLLC in Destin, Florida, Alan Rothschild Esq. of Hatcher, Stubbs, Land, Hollis and Rothschild, LLP in Columbus, Georgia, and Kimon Karas Esq. of McCarthy, Lebit, Crystal and Liffman Co., LPA in Cleveland, Ohio. The editor again this year will be Joseph G. Hodges Jr. Esq, a solo practitioner in Denver, Colorado, who also is the Chief Moderator of the ABA-PTL List.

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**Heckerling Institute 2007**
Reports from the event, as posted to the ABA-PTL List Serve

A complete listing of the proceedings and speakers is available on **[the Institute's Web site]**

# Report #10

As we have done in January for the last ten 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 41th Annual Philip E. Heckerling Institute on Estate Planning that is being held January 8-12, 2007 at the Orlando World Center Marriott Resort and Convention Center in Orlando, Florida, a new venue for the Institute this year. A complete listing of the proceedings and speakers will be published here later and is also available on the Institute's Web site at http://www.law.miami.edu/heckerling.

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Eratta #2 Thursday afternoon Special Session 4-C on Tax-Advantaged Trusts by Bergner and Gans.

Because PLRs can only be relied upon by the taxpayer to whom the ruling is issued to, both ACTEC and the ABA Tax Section have requested the IRS to issue a revenue ruling endorsing the estate and gift tax positions taken in the PLRs regarding the general power of appointment trust. The specific ruling requested deals with the following issues: "(1) that property belonging to the surviving spouse but over which the first spouse to die holds a general power of appointment exercisable at death will be included in the gross estate of the first spouse to die under Section 2041 and against which any unused exclusion amount of that spouse may be applied, and (2) that the gift made by the surviving spouse to the first spouse to die by granting that spouse the general power of appointment qualifies for the marital deduction under Section 2523. Both organizations requested that rulings be issued with respect to both a revocable trust funded solely by the surviving spouse and a "joint revocable trust" created and funded with property from both spouses. Neither organization requested the IRS to address the income tax basis of the property over which the first spouse to die has been granted the general power of appoint

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This Report contains coverage of the Friday morning regular sessions on Financing the Cost of Long-Term care, Keeping the Vacation Home in the Family and What We Have Learned (at Heckerling) and What to Do with it as well as the Thursday Afternoon Special Session on Coordinating Business and Succession Plans

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The Inheritance Threat That Dares Not Speak Its Name: Financing the Cost of Long-Term Care Friday morning, January 12, 2007 Presenter: Prof. Richard Kaplan

Reporter: Kimon Karas Esq. of McCarthy, Lebit, Crystal and Liffman Co., LPA in Cleveland, Ohio

Professor Kaplan discussed the various methods of financing one's long-term care from public and private sources. At the outset he stated the topic is very broad based and hours could be spent covering just one of the aspects of long-term care and thus this topic/session was a broad brush overview. For those wanting more detailed analysis Professor Kaplan referred to his book, Elder Law in a Nutshell, by Thompson/West (4th ed. 2007). In that text there are separate chapters dedicated to the issues of Medicare, Medicaid, Long-Term Care Insurance and Nursing Homes.

Professor Kaplan started with an overview of the area. The statistics he cited were that about 43% of persons age 65 and over will spend some time in a nursing facility; the average stay is 408 days, with 31% being less than one month and 11% extending beyond three years; and average costs of a nursing home being $71,000, and in many areas even greater.

He stated this will become a bigger issue as the population ages. In traditional estate planning this has been an area that has not been addressed or often overlooked. The majority of the people do not plan for it and then when it strikes it is too late.

Sources of financing long-term care.

- Medicare
- Supplemental "Medigap" Insurance
- Accelerated Life Insurance Benefits
- Medicaid
- Long-Term Care Insurance

Medicare. Charges in a "skilled nursing facility" are covered but if only the following conditions are satisfied:

- Hospital stay must precede the SNF admission by no greater than 30 days
- Hospital stay must have been at least 3 days (excluding the discharge day)
- SNF must be Medicare-approved
- Recipient is receiving "skilled nursing care"---services ordered by a physician requiring professional administration ( i.e. insulin, shots)on a DAILY basis.

Even if one satisfies these tests (which are becoming harder because of advances in medicine as well as cost containment issues which results in persons being discharged sooner from facilities) complete coverage is limited to the first 20 days, with costs for the next 80 days covered except for a daily deductible of $119 (in 2006). After 100 days nothing covered.

Services of a home health agency are covered pursuant to a plan reviewed by a physician. The recipient must be under a physician's care and medical necessity must be re-certified every two months. If one qualifies it is limited to 28 hours per week.

Supplemental "Medigap" Insurance. Fills in the gaps where Medicare does not cover. There are 14 various types of policies. All of these policies provide "core benefits"Part A hospitalization co-insurance amounts, Part B co-insurance, hospital coverage for 365 days beyond Medicare's coverage. Optional benefits include Part A deductible, Part B deductible, SNF co-insurance, excess "balance billing" expenses for "non-participating providers, foreign travel emergency. In certain of the policies, C –L will cover the deductible for SNF not covered by Medicare for days 21-100, provided all of the other requirements to qualify for Medicare coverage in the first instance are met.

Accelerated Benefits on Life Insurance. A rider to an insurance policy that will pay a designated portion of a policy's face amount prior to the insured's death as "accelerated" or "living" benefits. Eligibility varies with policies but generally restricted to person who are likely to die within one year.  The proceeds may be used for any purpose.  The proceeds received are tax-free if the insured is "terminally ill" or "chronically ill."  The benefits are limited to $250 per day in 2006 or the actual costs of long-term care, if higher, for chronically ill persons but this limitation does not apply to terminally ill persons.

Medicaid. Combination of a federal and state program.  One does not automatically qualify for this program but must apply.  Programs are administered by the state and many of the definitions and rules are governed by the state and can even vary within each state. A nursing home to qualify for Medicaid patients must accept the state maximum which is generally less than the costs to the facility to provide these services.  Nursing homes thus monitor very closely their private pay versus Medicaid census.

Medicaid has asset qualifications.  A Medicaid recipient may retain generally $2,000.  Also a recipient can retain personal effects and household goods, without limit, as long as they do no have investment value and equity in a residence of up to $500,000 as long as the person "intends to return" to live there.  The state will lien the personal property and residence to secure any payments made on behalf of recipient.

Other non-countable assets include, a motor vehicle (as long as used to transport applicant or member of applicant's household); life insurance as long as face value does not exceed $1,500; burial spaces(without limit); and certain testamentary trusts.

No penalty applies to transfers of assets made by the applicant more than 60 months prior to applying for Medicaid.  Exchanges made for full consideration.  All other transfers cause the period of ineligibility during which benefits will not be paid.  The penalty is calculated by divided the value of the transfer by the monthly cost of care. The penalty period begins with the month in which the transferor would otherwise be eligible for Medicaid.

Income Eligibility. A recipient's countable income for Medicaid includes all investment income, profits from dispositions of stocks, bonds, gifts/bequests, social security receipts.  Small amounts such as $30-$50 can be retained. "Medically Needy" states provide that if monthly income does not cover the nursing home costs, Medicaid will pay the difference.  Other states "Income Cap" states provide that if monthly income exceeds a specified limit ($1809 in 2006) the person is ineligible for Medicaid even if that income is less than the person's nursing home expenses.  In Income Cap states a person with excess income can transfer all of their income to "qualified income trusts" and after the patient's death, any remaining assets go to the state to the extent of Medicaid outlays made on the patient's behalf.

Long-Term Care Insurance.  It is private insurance that one must apply and qualify for.  Does not help the person who is in crisis mode.  It is very selective and applicant must go through medical underwriting.

Premiums are deductible as medical expenses up to specified limits that depend upon the insured's age. Because of the adjusted gross income limitations for deducting medical expenses these premiums will probably not be deductible.

Evaluating policies one should consider the following:

- Inflation protection.
- Financial strength of insurer.
- No prior hospitalization required.  Should not be a condition for receiving benefits.
- Custodial care covered. Note, Medicare does not cover.
- Waiting period of less than 90 days.
- Exclusions due to pre-existing conditions.
- Length of benefit payout period.
- Cost.
- Covers home care assistance.

Professor Kaplan concluded with an example of self funding the costs of a policy.  The goal was to replicate the John Hancock policy of four years at $100 per day, with a 5% compounded inflation protector.  Annual premiums are $1,740.  The prospective insurer is single and 65 years old.  Insurance is not needed until person reaches age 80.  Premiums are unable to be deducted.  Person's effective federal/state income tax rate is 26%.  The insurer does not raise the premium rates after policy's issuance.

The cost of this goal.  A $100 per day after 15 years of 5% annually compounded increases to a daily benefit of $208, or $6,240 per 30-day month.

The amount needed at 6% to generate four years of benefits of $6,240 per month is $265,699.  To obtain this amount, annual $265,699.  To obtain this amount, annual investments of $1,740 for 15 years must earn 28.9% compounded annually AFTER-tax or pretax of 39.1%.

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From NASCAR Condominiums to Private Mausoleums: Keeping the Vacation Home in the Family
Friday morning, January 12, 2007 Presenter: Wendy Goffe

Reporter: Gene Zuspann Esq. of Zuspann & Zuspann in Denver, Colorado

This presentation focused on the family vacation home and planning to keep the home in the family for generations to come.

Throughout the materials and the presentation, the property is referred to as the cabin, regardless of value or size or how ornate the property.

Cabins have different meanings and goals in different families.  Some uses of the cabin:

To relax

An ongoing, never finished project to improve or maintain the property

To enjoy a common interest; an example is the condominiums being built that overlook NASCAR racetracks.  The owners can sit in their hot tubs and watch the race.

An opportunity to teach descendants to appreciate the benefits of nature

Many times the cabin represents a large portion of the family wealth because the vacation property has increased in value much faster than the other assets.

It is helpful if the family creates a master plan. The best plans are negotiated between family members, sometimes with the help of a mediator or facilitator. As part of the planning, the family sometimes creates a mission statement. The mission statement often addresses questions such as

what is most important to the family about the cabin?;

what does the family value most about how it uses the cabin?; and

how would the family like to see the ownership affect the ways the various members interact?

If the family will not accept the use of a facilitator, a survey can be sent by the attorney. Sometimes, the senior generation finds that the younger generations have no interest in retaining the cabin. The results may also reveal worries of the family members that need to be addressed in the master plan.

She discussed conservation easements and the benefits that they may have in preserving the property in its current condition. Also, many parts of the country have local land trusts or land banks that preserve or protect the property.

There are issues when conveying an interest in the property to one of these organizations. It is important that there is an agreement to define who pays what and allows the donor some control. She indicated that the result is not a reduction in the cost of owning the property.

Some qualified organizations for a conservation easement are a private operating foundation and a supporting organization. A private foundation is not an eligible donee.

A QPRT is another possibility but donors must pay rent after the term. She likes this alternative as it gets rent out of the donor’s estate. However, many donors do not like this part at all. Some problems arise with the use of a QPRT. It may be necessary to carve out the residence from the rest of the property.

An outright gift of the cabin is the best alternative to get the property out of the donor’s estate. If the gift of an undivided interest in the cabin is given, a discount in the value may also be obtained for the gift. The downside to intervivos gifts in the lack of a step-up in basis.

Irrevocable trusts can also be used. However, the lack of ability to adapt to changes in the future may make these poor choices. It may be hard to add members in the future and to maintain an adequate reserve to cover future costs.

An LLC can be a good alternative The members will have limited liability, the management is flexible and can be changed in the future, it can exist perpetually and it is easy to amend if the requisite number of members or membership interests agree.

She used to like sales to family members using a private annuity, but the issuance of the new regulations can cause a problem with the use of this method.

The senior generation may also want to use a revocable trust for an initial period. She referred to this method as "a trust with training wheels." If things do not work out among the family members, the senior generation can revoke the trust.

The ongoing management of the cabin should be set out in a written management agreement. The agreement needs to put into place the mechanisms to manage the property, resolve conflicts and provide for the maintenance of the property. There are also numerous issues that should be considered in the management agreement. Her materials include a large laundry list of these issues. A number that she mentioned were pets, smoking, perfume, assessments and the manager.

She feels the best arrangement is for one member to be elected manager and authorized to maintain the property in its current condition. Any improvements must be voted on. The hardest problem - spouses of the family members. Among other problems, you may want to provide a buyout provision if a spouse receives an interest in the cabin in a divorce.

Another tough issue is how to handle a buyout in the event that a member withdraws. One issue in this case is whether the buyout is at a discounted rate to avoid a hardship on the remaining owners.

If the property is large enough that there are or can be several homes, the family should consider a homeowners' association. This type of arrangement is good when there are common facilities such as a swimming pool or a dock.

She also suggested that a cabin is a great opportunity for an irrevocable life insurance trust to fund the property when the senior generation is no longer available to provide additional funds as needed. This would require the senior generation to be insurable.

She concluded that it is important to recognize the cabin often is a symbol of the history, emotions and value of the family. It can embody a whole range of emotions for the family. Understanding these attributes and building on these is critical in developing a master plan to continue to happily own the cabin.

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There's got to be a Morning After: What We Have Learned and What to Do With it. Friday morning, January 12, 2007 Presenter: Mark Edwards

Reporter: Herb Braverman Esq. of Walter & Haverfield, LLP in Cleveland, Ohio

In prior years, the presenter assigned to close the Institute with a case study synthesis that brings together all the information presented by others during the prior week has had a daunting task that sometimes proved to be quite difficult. This year, Mr. Edwards simply took a different approach. He had his own message ready to be delivered to the attendees and, during the course of the week, he attempted to work into his message some of the ideas presented by others who had presented at the Institute.

Referring to himself as a storyteller and opening with a reference to the 1972 movie, The Poseidon

Adventure, and its best known lyric, "There's Got to be a Morning After", he suggested that we were experiencing the perfect storm in our professional lives and have been reading in this direction ever in 2001 when Congress created an environment of pervasive uncertainty in our professional area. Congress was going to phase in the estate tax repeal that, with the recent elections, will now never happen. We are looking forward to a substantial credit shelter amount with spousal portability, perhaps lower rate(s), reunification within the transfer tax and other unknown changes in the tax law.

Mr. Edwards expressed concern about the financial markets and their future--no more high flying '90's and how will we ever replace the 6 lost years of compounding he has calculated in his materials. Along with the financial uncertainty, he cites the affects of aging in a society dominated by "the Boomers", those born between 1945 and 1965. By 2020, someone will be turning 65 years old every 5 seconds every day; 44% of us will be 65+ and only 13% will be under 19. He presented other similar "facts" and pointed out that our clients will have a different profile.

They will be anxious, increasingly so, as they age. They will be risk adverse and have a much longer life expectancy. They will need "life planning" not estate planning. Their focus will be on the longer conservation period of their lives and not on transferring money and wealth to children or grandchildren. Their real estate and 401(K)'s will not be appreciating like they did in the 90's. They will do targeted giving to benefit their natural bounty, but probably for educational and medical purposes, but only after they feel secure.

Mr. Edwards turned to issues of capacity and noted that we will be dealing with these issues increasingly. He spoke of the "fog" of incapacity that comes on slowly and does not result from trauma or other acute events. We must be cautious and sensitive to these changes in our clients. He provided in his materials some basic capacity testing materials and urged us to obtain the available ABA materials and handbook on the subject.

Mr. Edwards spoke of better prepared powers of attorney--not rote or statutory forms, but carefully tailored documents. He included an example in his materials, but cautioned against it except as a guide. Nevertheless, he emphasized the importance of certain provisions--those dealing with gifting, retirement accounts, insurance transactions, acceptance by 3rd parties.

He spent some time on qualified retirement accounts and related items, indicating they are and would be increasingly important assets. He suggested that attorneys should not hide behind their limited licenses, but should be prepared to give advice regarding the mechanic of the financial world around us (and our clients).

Mr. Edwards suggested that we and our clients "embrace the risk of longevity". We should increase our involvement in the management of our clients financial lives.

Mr. Edwards gave a provocative presentation--one that few were expecting (although his outline did suggest something different). I hope that all who attended the conference will take a moment to reflect upon his ideas. I think he is asking us to be aware of the changes that are constantly occurring around us and affecting our clients (as well as ourselves) and he is encouraging us to be "current" in a more fundamental way.

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Special Session 3-D Coordinating Business and Succession Plans Thursday afternoon, January 11, 2007 Presenters: Jonathan C. Lurie and Read Moore

Reporter:Gene Zuspann Esq. of Zuspann & Zuspann in Denver, Colorado,

This report summarizes that breakout session following up on Jonathan Lurie's presentation on Tuesday. Read Moore assisted with this presentation.

The materials contained five hypotheticals. The discussion covered four of these. This session was Socratic and involved the audience to a large degree. The audience made suggestions, recommendations and asked numerous questions.

The first hypothetical involved an LLC. The operating agreement allowed transfers by the member to a permitted transferee, and upon such transfer, the transferee becomes a member. The agreement also contained a call right in the LLC. The issue discussed was whether the operating agreement should include a provision to allow the LLC to buyout the permitted transferees of the deceased member upon the triggering event (death).

Point 1: When drafting your estate planning documents always ascertain ownership in entities and whether buy-sell provisions exist.

Point 2: You need to ascertain the intent of the client when of these situations exist. The drafter of the documents needs to make sure the documents prepared properly account for various situations, even though not contemplated by the parties.

Point 3: To try to determine problems, the attorney(ies) need to run through a variety of different scenarios with the client(s) and make sure the results under the agreement are those that are expected.

In most of the scenarios, the materials contained suggested language for addition to the various documents. However, often there is no correct answer - the clients need to determine how they want the documents drafted.

Scenario 2 involved a corporation. The bylaws provide that, upon the vacancy of a director, that the vacancy may or may not be filled until the next election. There was also a buy-sell agreement containing a call right for the corporation to purchase a deceased stockholder's stock based upon a formula. Due to some mistrust between the three stockholders, they required that the call right be exercised by a unanimous vote of the directors. Each of them are appointed as directors. Election of the directors occurs at the annual meeting. One stockholder dies about a month before the annual meeting.

Problem: Upon the death, the remaining two stockholder/directors reviewed the formula clause and determined that the price was favorable to them. They then exercised the call right by the unanimous exercise (by the two of them, because the third director would not be elected until the annual meeting) of the call right. The deceased stockholder's family is bound by the agreement.

There was substantial discussion of this issue. There were proposed solutions but no one really agreed on the most appropriate one. All agreed that the problem existed because the documents did not really reflect what the stockholders understood would happen - that all three families would be voting on exercise of the buy-sell provisions.

Other things all agreed on: the corporation bylaws and the buy-sell agreement did not work together, the decedent's estate planning documents need to appropriately handle these other agreements, and the formula pricing needs to be up-to-date.

The exercise issue could have been solved had the agreements contained provisions that the two surviving directors could not act before the spouse of the deceased stockholder was appointed as a director.

Other issues discussed:

1. Should the formula contain a discount for a minority interest. Jeff Weiler pointed out that this was negotiable.

2. Both one comment by the audience and Lurie agreed that insurance could have solved both problems - the discount and the price.

3. The materials also pointed out that the estate planning documents must complement the corporate documents - the two surviving directors should not be the trustees or executors of the deceased stockholders estate, and therefore, voting on whether to exercise the call right.

The problem that often exists is the lack of coordination between the estate planning documents and the corporation documents. The drafter(s) of the documents must have all of the relevant information. This is an example of a situation where working through the different scenarios could have eliminated the problem.

Scenario #3

The problem: coordinating the trust agreement and the stockholders' agreement.

Trust law requires that the assets in the trust must be diversified. In most cases, this needs to be overriden in the trust document for special assets.

The drafter must be careful when drafting language to override the duty to diversify. The language must be clear and effective. There are cases both ways on this issue. See report #6 containing the discussion of the twin UPIAs on diversification.

The attorney must document the files. The transmittal letter needs to explain these provisions. It must be clear that the provision overriding the duty to diversify was intended in the trust document and that it is not just boilerplate. Several courts have indicated that when the language is boilerplate, the duty to diversify a specific asset was not overridden.

Scenario #5: Where the property is community property, must the spouse be involved in the stockholder agreement? Further, must the spouse sign the document. This seemed to depend on the state and the practice of the various attorneys. John said that having the spouse sign in California is common. Read felt that the stockholder agreement need not be signed by the spouse. All agree that this is a thorny issue. Also, this issue is state specific. If there is a question between the states, local counsel needs to advise.

Other issues:

1. Some community property states allow a spouse to deal it his or her sole and separate property.

2. If the spouse entering the agreement is the manager and the other spouse is not involved in the business, the answer may be different.

3. Lurie said that if the agreement is negotiated in an arms-length transaction, that the agreement is binding on the spouse.

4. It may not do any good to have the spouse sign. The material included a Washington case that said that, where the spouse was not active in the negotiation, it was not binding on that spouse - should they have separate counsel?

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**Heckerling Institute 2007**
Reports from the event, as posted to the ABA-PTL List Serve

# Report #11

A complete listing of the proceedings and speakers is available on **the Institute's Web site**

As we have done in January for the last ten 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 41th Annual Philip E. Heckerling Institute on Estate Planning that is being held January 8-12, 2007 at the Orlando World Center Marriott Resort and Convention Center in Orlando, Florida, a new venue for the Institute this year. A complete listing of the proceedings and speakers will be published here later and is also available on the Institute's Web site at http://www.law.miami.edu/heckerling.

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EDITOR'S COMMENT: This is a supplement to our final Report #12, as the Special Session Report that was missing then has finally arrived and is being published here. There also is a technical note from EstateWorks at the end.

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This Report contains coverage of Special Session 2-E on GRATs vs.

Installment Sales to Grantor Trusts vs. Direct Gifts and a note from EstateWorks

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Special Session 2-E GRATs vs. Installment Sales to Grantor Trusts vs.

Direct Gifts: What Do the Numbers and Theory Say?

Wednesday afternoon, January 10, 2007

Presenters: Jonathan Blattmachr, Robert Weiss and Diana Zeydel

Reporter: Jason Havens Esq. of Havens & Miller PLLC in Destin, Florida

Diane S.C. Zeydel discussed certain legal aspects of grantor-retained annuity trusts (GRATs) and installment sales. Robert then discussed the financial impact of doing a GRAT and an installment sale, using various modeling techniques. Jonathan stayed in the background and offered his insight as each person proceeded with their presentation.

There were no additional special session materials beyond those found in the general session materials prepared by Jonathan and Diana. However, mention was made in the special session that if anyone wanted the extensive slide show prepared by Robert, he could be contacted at robert.weiss@alliancebernstein.com. Some of these slides are very compelling in illustrating the benefits of these techniques to your clients.

Diana started the presentation by pointing out that although attorneys can identify the legal risks attendant to GRATS, she cannot identify the potential economic risks in a way that the financial world can. On the other hand, the financial world sometimes has difficulty understanding the strategies being proposed by attorneys. As a result, there is a disconnect between the legal and financial worlds. Her goal was to try to bring the two disciplines together and get them to start talking to each other.

They used as their model a nearly zeroed-out, two-year GRAT. They thought that you could zero out but maybe you had better not. Although they think that there is no minimal term, it is better not to do something out of the ordinary. Diana then proceeded to finesse the legal issues.

First issue: Qualifying for the marital deduction (pages 12-14 of main

materials): You do your GRAT, and grantor dies during term. The IRS thinks that the entire GRAT is includible in the estate. You want the GRAT to qualify for the marital deduction to delay the tax event. Query: How many interests do you have? The IRS might say that you have more than one interest and not just one GRAT. In other words, they might say you have an annuity interest and a remainder in a GRAT. If that is the case, then you cannot solve the marital deduction issue because you cannot get the remainder in the GRAT to become a QTIP because the remainder interest in the GRAT does not mature until the GRAT term ends. Thus, the remainder interest cannot be paid to the surviving spouse or the QTIP.

In a Walton GRAT, you have to have the annuity interest paid to the estate if the grantor dies prior to the term so that the GRAT does not collapse. To qualify the annuity payment for the marital deduction, all the income of the GRAT must be paid to the spouse. Therefore, to the extent the annuity payments consist of income, the income must be paid to the spouse. If the annuity payment falls short of the GRAT's income, the shortfall must be distributed to the surviving spouse from the GRAT -- but through the grantor's estate. Finally, the GRAT remainder must be paid to the surviving spouse.

Second issue: Zeroing out the remainder: TAM 200245053, issued after Walton but before the IRS announced its acquiescence, indicated that a zeroed-out formula for a gift could violate Proctor if you set the annuity payment so you always zero out the GRAT. To avoid this risk, always have a minimal gift of the remainder interest. In structuring a minimal remainder, the IRS will not rule unless you use a five-year term and a ten percent remainder interest, which comes from the charitable remainder trust area; however, the analogy does not fit in the GRAT area.

Diana stated her formula in the main materials, which provides a minimal remainder interest and avoids an unanticipated technical disqualification by providing formula language that would adjust the retained annuity to produce whatever remainder value may be legally required, and likewise to adjust the fixed term to whatever duration is necessary in order to have a tax-qualified GRAT. The following provision may accomplish those two goals:

(A) The “Annuity Amount” shall be determined as provided below, and shall be paid to the Grantor [specify payment terms, such as annually during the Fixed Term on the date immediately preceding the anniversary of the Funding

Date]:

(1) In the first year of the Trust, the Annuity Amount shall be a Fixed Percentage of the Gift Tax Value of the assets contributed to the Trust on the Funding Date; and

(2) In each subsequent year of the Trust during the Fixed Term, the Annuity Amount shall be one hundred twenty percent (120%) of the Annuity Amount payable in the preceding year.

(B) The “Fixed Percentage” shall be that percentage that will cause the Gift Tax Value of the taxable gift to the Trust (taking into account the determination of the Fixed Term as provided in Paragraph (D)) to equal the greater of:

(1) [specify the percentage of the fair market value of the assets contributed to the GRAT that the value of the remainder will represent, such as one one-hundredth of one percent (.01%)] of the Gift Tax Value of the assets contributed to the Trust on the Funding Date rounded up to the nearest whole dollar; and

(2) The smallest amount such that Annuity Amount will constitute a qualified annuity interest within the meaning of Internal Revenue Code

§2702(b)(1) and Treas. Reg. §25.2702-3(b)(1).

(C) The “Funding Date” shall be the date of the initial assignment, conveyance transfer or delivery of property to the Trustee.

(D) The “Fixed Term” shall commence on the Funding Date and end on:

(1) [specify the date upon which the annuity payments to the Grantor will end as an anniversary of the Funding Date, such as the second anniversary of the Funding Date]; or

(2) such later anniversary of the Funding Date as shall be necessary in order that the Annuity Amount shall constitute a qualified annuity interest within the meaning of Internal Revenue Code §2702(b)(1) and Treas. Reg.

§25.2702-3(b)(1).

(E) The “Gift Tax Value” of any property shall be the fair market value of such property as finally determined for Federal gift tax purposes.

She stated that there should not be a Proctor problem with this formula because an actuary can determine the value of the remainder on day one using the formula.

The Adkinson case was discussed in which a CRAT was not administered properly and determined to be void ab initio and the importance of making the annuity payments as required.

Third issue: The situation where the annuity payments have not been paid:

Jonathan resolves this problem by saying that payments vest in the grantor-beneficiary even if not paid and trustee acting as agent for grantor. This might not work, but at least you have something to say. In another case which Jonathan has where annuity payments were not made, he is arguing if the grantor is the trustee, then under Delaware law there might be constructive receipt of the payment even if not made. However, Jonathan mentioned there is a trend where the IRS is looking to see if the payments are made.

Fourth issue: How do you deal with GST exemption? As a general rule, if you have an ETIP (and that is the IRS position at least with a GRAT), you cannot allocate GST exemption until the ETIP expires. Remember if the possibility of the payments reverting to the grantor's estate is so remote to be negligible and that percentage is five percent, then you do not have an ETIP and in a two-year GRAT, this might be possible and you might have possible automatic allocation -- but then how much? Is it for the entire amount in the GRAT? This would be a disaster. Nevertheless, you have to elect out and then try allocating GST exemption. How? Use a formula with a ceiling: "so much as necessary but not more than the value of the remainder."

Jonathan mentioned the concept of "deference" in the Supreme Court case of Auer v. Robbins, which held that the federal courts must follow the proposed construction of the IRS as in the regulations unless the proposed construction is unreasonable. The chance of allocating GST exemption in light of the Auer doctrine is extremely remote.

Fifth issue: Funding of the GRAT: You cannot make additions to the GRAT. The presenters mentioned the idea of the revocable GRAT proposed by Manigault and Hatcher in a recent Probate & Property article. The idea is to make it revocable until all the funds are retitled in the name of the GRAT to avoid an argument that you made an addition. Once you have them all titled, at that point you revoke your revocation right.

Sixth issue: Do you have one asset for each GRAT? This could be administratively impossible because hedge fund managers might not want to do it. One solution is to use a single-member LLC for 50 different LLCs, which is disregarded for tax purposes. In the LLC, you specifically provide that the owner can assign interests in the LLC attributable to specific assets in the LLC. To GRAT one, you assign hedge fund A. To GRAT two, you assign hedge fund B. As far as hedge fund managers are concerned, there is only one LLC and no change of ownership.

Diana next discussed legal issues with installment sale to Grantor trusts. Jonathan said that there is no gain recognition at death. What about 2701, 2702, and 2703? The issue is whether you have equity or debt? If you have debt, you do not come under these sections. If payments are not tied to income in the assets, then you do not have a tie in and thus avoid 2036. You are looking for true debt and not something that looks like an income interest. The Dallas and Rosen cases, as mentioned in the general materials, were discussed as indicia of whether you have debt or a retained interest characterized as equity. Jonathan said practically speaking if you pay off the debt, you do not even have to face the IRS questioning whether you have equity and not debt.

The duration of the note should require payment within the grantor's life

expectancy. Use of discounting is easier with sale vs. the GRAT.

An informal survey was conducted in Florida on a marketable securities vs.

primarily marketable securities FLP, and the survey revealed 2/3 of cases indicated a discount of at least 30% on audit.

Diana said that Robert will say that discounting is not the most important factor in determining the success of GRAT and sale strategies. The most important component in the success of a strategy is grantor trust status, second most important is asset performance, and third is discounting.

Robert was next. He has slides which were inexplicably excluded from the materials, but see the e-mail address above (where they can be obtained). These slides are critically important in understanding his presentation.

He stated the legal and financial world should work together to "turbo-charge" the strategies.

Without discussing the means in which he came to the following conclusions, these were his conclusions.

GRAT conclusions: You should do a rolling GRAT with each annuity payment coming out creating a new GRAT, and you should do asset-splitting GRATs in which you put different stocks based upon asset allocation into separate GRATs. You do rolling asset-splitting GRATs by having the international GRAT annuity payments go back into the same instrument which created the original international GRAT, but have separate internal bookkeeping with each GRAT and thus in reality have any number of GRATs. In other words, if you start out with four GRATS, you only have four documents but are administering any number of rolling GRATs. The accountants are happy even if the legal draftsman is not. When looking at GRAT success, it is important to look at the estate taxes saved.

The beauty of the math of GRATs is that the children never get hurt -- only benefitted. The shorter the GRAT, the more you capture the dynamics of a volatile market.

Jonathan stated that when he does a GRAT or a sale, he will often have the spouse named as a beneficiary when the GRAT ends. The spouse can also make a guarantee if it is necessary. He will also define the spouse as the person "to whom you are married at any given time."

The risk for short-term rolling GRATs is that you stop the strategy and do not fully account for the volatility of the market.

Installment sale conclusions: Discounting is important. If interest rates go down, you can reset the AFR and increase the chances of it being successful. Also, if you have a profit, you can capture the profit by prepaying the note and then start another installment sale. Mortality risk is better managed with GRATs. Long-term structure with sales will not

capture market volatility as well as GRATs. Also, the seed money is at

risk in sales when there is a falling market.

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