Wealth Management Update

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Edited by Henry J. Leibowitz
Contributor: Nathalie Stenmark

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

November 2021 Interest Rates for GRATs, Sales to Defective Grantor Trusts, Intra-Family Loans and Split Interest Charitable Trusts

Federal interest rates increased slightly for November of 2021. The November applicable federal rate ("AFR") for use with a sale to a defective grantor trust, self-canceling installment note ("SCIN") or intra-family loan with a note having a duration of three-nine years (the mid-term rate, compounded annually) is 1.08%, up from 0.91% in October and up from 0.39% in November of 2020.

The November 2021 Section 7520 rate for use with estate planning techniques such as CRTs, CLTs, QPRTs and GRATs is 1.40%, up from 1.0% in October.

The AFRs (based on annual compounding) used in connection with intra-family loans are 0.22% for loans with a term of 3 years or less, 1.08% for loans with a term between 3 and 9 years, and 1.86% for loans with a term of longer than 9 years.

Thus, for example, if a 10-year loan is made to a child, and the child can invest the funds and obtain a return in excess of 1.86% the child will be able to keep any returns over 1.86%. These same rates are used in connection with sales to defective grantor trusts.

Buck v. U.S. (DC CT, 128 AFTR 2d) — Discounts for Fractional Interests

In a gift tax refund case involving a taxpayer's disputed use of discounts in valuing two 48% interests in timberland that he simultaneously gifted to two sons, the government was denied summary judgment on its claim that discounts based on separate values of interests which each son received could not apply when the taxpayer did not hold those interests in factional form pre-gift. The government argued that such discounts would "endorse a circumvention of one of the primary purposes of the gift tax, which is to assure that estate tax is not avoided". The government further argued that the valuation should reflect the "economic reality" that, to the taxpayer, the gifts equaled a 96% interest and should be aggregated for gift tax purposes. However, the court held that those theories were not supported by relevant case law and violated established gift tax principles that gifts were to be valued at the time of the gift, not before or after, and that separate gifts were to be valued separately.

Interestingly, the government's motion to compel discovery of the taxpayer's will and testimony of his financial manager was granted. The court held that the information was relevant to the government's defense that fractional discounts did not apply. The taxpayer's objections, including that the financial manager's testimony was protected by attorney-client privilege, were rejected.

Arlene Williams-Paris v. April Nelle Joseph, Priscilla Paris-Austin, Theodore Paris, and Samuel Paris — Morning of the Marriage Premarital Agreement Held Enforceable

This case involved the enforceability of a prenuptial agreement that was executed hours before the wedding by two Florida residents in Massachusetts. On the day of the wedding, the husband woke his wife in the morning demanding her to find a prenuptial agreement online and sign it. Feeling pressured by the significant potential embarrassment of canceling the wedding, the wife reluctantly worked with the husband to draft an online prenuptial agreement and then they both signed the document hours before the wedding.

After the husband died four years later, intestate, while still married to the wife, the wife filed an action in court challenging the validity of the prenuptial agreement. The petition argued that the prenuptial agreement was invalid based on fraud, deceit, duress, coercion, misrepresentation, and overreaching since the husband never explained that it would apply in the event of death, and because it contained unfair or unreasonable provisions. Additionally, she petitioned for rescission of the agreement based on her unilateral mistake.

The husband's children moved for summary judgment, arguing that the prenuptial agreement had a specific provision pertaining to a spouse's death and therefore discounted the wife's argument that it was only effective in the event of divorce. Additionally, in response to the wife's contention that the husband did not fully disclose his assets prior to the agreement being signed or in the exhibits attached to the agreement, the children argued that full disclosure was not required under Florida law when the agreement's validity is contested in a probate proceeding.

The probate court granted the children summary judgment on the wife's coercion and duress arguments. However, the probate court denied the children summary judgment on the wife's unilateral mistake argument, ruling material disputed facts remained as to whether the husband had represented that the agreement was to apply only in the event of divorce and not death. After a nonjury trial on the disputed issue of misrepresentation and unilateral mistake, the probate court denied the wife's petition to invalidate the prenuptial agreement on those issues. The wife then appealed.

The appellate court affirmed the trial court's summary judgment as to the validity of the agreement, dismissing the wife's claims that the prenuptial agreement should not be enforced based on duress, coercion, over-reaching or undue influence. With respect to the choice of law issue, a lot was at stake because Massachusetts law requires financial disclosure for a prenuptial agreement's validity and for a postnuptial agreement's validity, whereas Florida law only requires financial disclosure for a postnuptial agreement's validity and does not require financial disclosure for a premarital agreement waiving post-death rights. The appellate court opinion discussed the doctrine of *lex loci contractus* and its exceptions, ultimately concluding that the public policy exception applied in this case, as the parties never lived together as a married couple in Massachusetts and the wife had no connection to Massachusetts other than the fact that she signed the agreement and married the husband there.

The case was remanded to the probate court to determine the wife's interest in a particular asset that was exempted from the prenuptial agreement so this case is not yet final. This case can be contrasted with *Bates v. Bates*, 46 Fla. L. Weekly D287c (3rd DCA, February 3, 2021) from earlier this year in which a prenuptial agreement that was signed the day before the wedding was voided based on arguments of coercion.

PLR 202139005 — Inadvertent Termination of S Corporation

A corporation will continue to be treated as an S corporation, where termination of its S corporation election was inadvertent due to the beneficiaries' failure to file timely QSST elections for certain trusts and the trustees' failure to file ESBT elections for other trusts. The corporation represented that the circumstances resulting in the failure to file the necessary QSST and ESBT elections were inadvertent and not motivated by tax avoidance or retroactive tax planning.

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

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

BOCA RATON

Albert W. Gortz
+1.561.995.4700 — agortz@proskauer.com

David Pratt
+1.561.995.4777 — dpratt@proskauer.com

Lindsay A. Rehns
+1.561.995.4707 — lrehns@proskauer.com

LOS ANGELES

Mitchell M. Gaswirth
+1.310.284.5693 — mgaswirth@proskauer.com

Andrew M. Katzenstein
+1.310.284.4553 — akatzenstein@proskauer.com

NEW YORK

Nathaniel W. Birdsall
+1.212.969.3616 — nbirdsall@proskauer.com

Stephanie E. Heilborn
+1.212.969.3679 — sheilborn@proskauer.com

Henry J. Leibowitz
+1.212.969.3602 — hleibowitz@proskauer.com

Jay D. Waxenberg
+1.212.969.3606 — jwaxenberg@proskauer.com