Proskauer

newsletter

Wealth Management Update

June 2017
in this issue

A monthly report for wealth management professionals.

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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.

June Interest Rates for GRATs, Sales to Defective Grantor Trusts, Intra-family Loans and Split Interest Charitable Trusts

The June § 7520 rate for use with estate planning techniques such as CRTs, CLTs, QPRTs and GRATs is 2.4%, which is the same rate as in May. The June applicable federal rate ("AFR") for use with a sale to a defective grantor trust, self-cancelling installment note ("SCIN") or intra-family loan with a promissory note having a term of 3-9 years (the mid-term rate, compounded annually) is 1.96%, down from 2.04% in May.

The relatively low § 7520 rate and AFR continue to present potentially rewarding opportunities to fund GRATs in June with assets that are expected to appreciate significantly.

The AFRs (based on annual compounding) used in connection with intra-family loans are 1.18% for loans with a term of 3 years or less and 2.68% for loans with term of longer than 9 years. For example, if a parent lends funds to his or her child for a 9-year promissory note bearing interest at the 2.68% AFR, any returns generated in excess of 2.68% may be kept by the child free of gift tax.

New York Surrogate's Court Upholds Trust Distribution, Defers to Trustee's Absolute Discretion

New York Surrogate's Court held that the distribution of a life insurance policy to a new trust that eliminated some beneficiaries of the distributing trust was a valid distribution despite not strictly complying with New York's Estates Powers and Trusts Law section 10-6.6 because the terms of distributing trust provided the trustees with absolute discretion to distribute income and principal to one or more beneficiaries to the exclusion of the others, including to another trust. The court also held that the lapse of Crummey powers is not contingent on the beneficiaries being given notice of their withdrawal rights. *In the Matter of Reuben Hoppenstein*, No. 2015-2918/A (N.Y. Sur. Mar. 31, 2017).

Eleventh Circuit Denies Graegin Loan Interest Deduction

The Eleventh Circuit denied an estate's deduction of interest on a loan made by the decedent's closely-held company to the estate because the company had sufficient liquidity to have made a distribution to the estate to pay the estate tax liability. The Eleventh Circuit also agreed with the Tax Court's reduction of a lack of marketability discount to 7.5% from 31.7% where most of the company's assets were liquid. *Estate of John F. Koons, III, v. Commissioner*, No. 16-10646, 2017 WL 1501062, at *1 (11th Cir. Apr. 27, 2017).

District Court Holds That Willful Failure to File FBAR is a Question of Fact

The Eastern District of Pennsylvania denied summary judgment to the IRS and the taxpayer, holding that whether the taxpayer willfully failed to file a FBAR with respect to a Swiss bank account is a question of fact and a genuine issue of fact existed as to the taxpayer's knowledge about the FBAR filing requirements. *Bedrosian v. United States*, No. CV 15-5853, 2017 WL 1361535, at *1 (E.D. Pa. Apr. 13, 2017).

Florida's Fiduciary Lawyer-Client Privilege is on the Books, but is it Good Law?

In 2011, Florida's legislature enacted section 90.5021, Fla. Stat., which provides for application of the lawyer-client privilege – even when the client is a fiduciary.

Specifically, the statute protects communications between a lawyer, on the one hand, and a client who is a trustee, personal representative or executor, or guardian, on the other hand. The privilege applies to the same extent as if the client were not acting as a fiduciary.

Why the need for a specialized statute? Isn't the standard lawyer-client privilege statute good enough to protect communications between a lawyer and a fiduciary?

Well, after years of debate among Florida practitioners, and some ambiguous case law along the way, it was determined that because fiduciaries owe a duty to the beneficiaries, and are really working for the benefit of the beneficiaries, one might conclude that fiduciaries' communications with a lawyer, likewise, are for the benefit of the beneficiaries. If that were true, then a beneficiary should have access to all advice given to fiduciaries by their lawyer – at least, when there is no adversary relationship between beneficiaries and the fiduciary.

To end the debate, the Florida legislature passed section 90.5021, and the privilege became firmly entrenched. At the same time, the Florida Probate Rules Committee – which governs court procedure, and which therefore is subject to approval by the Florida Supreme Court only – petitioned the Court to adopt rule 5.240(b)(2). That rule provides that fiduciaries must give notice to beneficiaries of the fiduciary lawyer-client privilege, to avoid any confusion on the part of the beneficiaries. The rule was adopted by the Florida Supreme Court.

Florida's evidence code, however, is a creature of both substantive law, governed by the legislature, and procedural law, governed by the Florida Supreme Court. Therefore, after

being enacted by the legislature, it is standard practice for the Florida Supreme Court to review evidence statutes, where they are routinely adopted to the extent they are procedural.

In 2014, when the Florida Supreme Court reviewed the fiduciary lawyer-client privilege, it *declined* to adopt it, and it questioned the need for the privilege to the extent it is procedural, without stating more. Suddenly, what was considered a matter of course, became a debatable point. And, with no clear answer as to whether the privilege is substantive or procedural in nature, it is an issue that remains, to this day, murky at best.

Last year, in *Bivins v. Rogers*, the Southern District of Florida dipped its toe in the privilege waters and emerged squarely in favor of the legislature. Sure, the Florida Supreme Court had said that it questioned the need for the privilege to the extent it is procedural, but that did not "vitiate or overturn the statute." The need for the statute was merely questioned, but not because it was unconstitutional or otherwise unlawful, said the federal court.

However, this year, the Florida Supreme Court complicated the matter a bit more. In declining to adopt a different evidence statute, this Court recognized its usual practice of adopting evidence statutes, but stated that "on occasion the Court has declined to adopt legislative changes to the Evidence Code because of significant concerns about the amendments, including concerns about the constitutionality of an amendment." The Court included a footnote and cited its ruling declining to adopt section 90.5021 as support. It seemed that the Florida Supreme Court was implying that its decision not to adopt the privilege was because of some constitutionality problem.

As a result, this year, the Florida Probate Rules Committee and the Code and Rules of Evidence Committee have begun taking steps, in concert, to raise the issue with the Florida Supreme Court. Put simply, the question to be presented is how can the Florida Supreme Court adopt rule 5.240(b)(2), which requires fiduciaries to give notice to beneficiaries of the fiduciary lawyer-client privilege, and then question the propriety of such a privilege in the first place?

It is a question that Florida practitioners may not have an answer to anytime soon.

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.

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