Wealth Management Update

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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.

February 2020 Interest Rates for GRATs, Sales to Defective Grantor Trusts, Intra-Family Loans and Split-Interest Charitable Trusts

The February Section 7520 rate for use with estate planning techniques such as CRTs, CLTs, QPRTs and GRATs is 2.2%, which is slightly higher than the January rate. The February applicable federal rate ("AFR") for use with a sale to a defective grantor trust, self-canceling installment note ("SCIN") or intra-family loan with a note having a duration of 3 to 9 years (the mid-term rate, compounded annually) is 1.75%, which is also slightly higher than the January rate.

The low Section 7520 rate and AFRs continue to present potentially rewarding opportunities to fund GRATs in February with depressed assets that are expected to perform better in the coming years.

The AFRs (based on annual compounding) used in connection with intra-family loans are 1.59% for loans with a term of 3 years or less, 1.75% for loans with a term between 3 and 9 years and 2.15% for loans with a term of longer than 9 years.

Thus, for example, if a 9-year loan is made to a child, and the child can invest the funds and obtain a return in excess of 1.75%, the child will be able to keep any returns over 1.75%. These same rates are used in connection with sales to defective grantor trusts.

Congress Enacts Significant Changes to Retirement Plans under the SECURE Act

On December 20, 2019, Congress enacted significant changes regarding distributions from retirement plans, including 401(k)s and IRAs. These changes allow account holders to continue making contributions to retirement plans after they have attained age 70.5 and push back the required minimum beginning date until an account holder has attained age 72.

Most importantly, the SECURE Act significantly alters the income tax consequences for individuals receiving a retirement plan from a deceased account holder. Under previous law, a retirement plan inherited from a deceased account holder could generally be paid out to a recipient based on the *recipient's* life expectancy. This rule was replaced under the SECURE Act with a new "10-year rule," which requires retirement accounts inherited from an account holder who died on or after January 1, 2020, to be fully paid out within ten years of the account holder's death except when the individual inheriting the account is (a) the account holder's spouse, (b) less than ten years younger than the deceased account holder, (c) a minor under state law, (d) chronically ill or (e) disabled.

The SECURE Act does not, however, make any changes to the statutory scheme for retirement plans inherited by an account holder's surviving spouse.

Please do not hesitate to call us if you would like to discuss existing beneficiary designations or to make sure that beneficiary designations reflect the account holder's current wishes.

Placencia v. Strazicich, 42 Cal. App. 5th 730 (Cal. Ct. App. 2019) – California Court of Appeal Holds that Assets in Joint Account Should be Disposed of as Part of Decedent's Estate

In 1985, Ralph Placencia (the "Decedent") opened a bank account that bore the acronym "JT WROS," which appeared to stand for "joint tenants with rights of survivorship," on which his daughter Lisa was named as a co-owner. In 2009, the Decedent died, leaving a Will and a Revocable Trust that specifically referred to this account and directed that it be divided equally between Lisa and the Decedent's two other children as part of the Decedent's residuary estate. The Decedent's Will and other statements of the Decedent clearly suggested that he did not want the account to pass to Lisa, but rather, to be divided equally between all three of his daughters.

The Court of Appeal reviewed the applicable statutes, and analyzed California Probate Code Sections 5302 and 5303. Ultimately, the Court held that the financial institution properly paid the account to Lisa, as the stated co-owner of the account, but that the Decedent's estate was the beneficial owner of the account, meaning that Lisa would have to pay the account over to the Decedent's estate. The assets from the account would then be distributed equally among the Decedent's three children as part of the Decedent's estate.

This holding was based on a determination that Section 5302's proviso that a joint account will be upheld "unless there is clear and convincing evidence of a different intent" did not require that the Decedent's intent to be proven at the time the account was created. Rather, the Will and other statements of the Decedent were evidence of the Decedent's intent and were ultimately found to be clear and convincing evidence that the account was not intended to be a joint account at the time of the Decedent's death.

Matter of Sochurek, 174 A.D.3d 908 (NY App. Div. 2019) – New York Appellate Division Finds that Beneficiary Can Seek Fiduciary's Removal Without Triggering *In Terrorem* Clause

The decedent left a Will that (a) left a lifetime interest in an operating company to his surviving spouse, with his two daughters as remainder beneficiaries and (b) named his surviving spouse as Executor. The Will granted the decedent's Executor with absolute discretion to manage all property held in the estate. The decedent's Will also included an *in terrorem* clause, which provided that the interest of any beneficiary would be revoked if he or she "institute[s] . . . any proceeding to set aside, interfere with, or make null any provision of this Will, . . . or shall in any manner, directly or indirectly, contest the probate thereof." Decedent's surviving spouse probated the decedent's Will and was appointed Executor without challenge.

Later, the decedent's surviving spouse, as Executor, entered into a contract to sell the operating company to a third party. After the sale was completed, the daughters brought a claim for breach of fiduciary duty against the Executor. In turn, the Executor sought to have the daughters' interests under the decedent's Will revoked pursuant to the *in terrorem* clause.

The Appellate Division ultimately held that the daughters' complaint for breach of fiduciary duty did not trigger the *in terrorem* clause, stating that under New York law, while *in terrorem* clauses are enforceable, "they are not favored and [must be] strictly construed." As a breach of fiduciary duty claim was not a contest to the validity of the will or any provision thereof, it could not be said to implicate the *in terrorem* clause or otherwise revoke the claimants' interests under the decedent's Will.

Sibley v. Sibley, 273 So. 3d 1062 (Fla. Ct. App. 2019) – Florida Court of Appeal Holds that Residuary Disposition to Administratively Dissolved Private Foundation Failed

A decedent's testamentary documents provided that his residuary estate was to be distributed to a specifically named private foundation, but if such foundation "is no longer in existence upon [his] death," then the fiduciary was directed to distribute the residuary estate to a specifically named public charity. Three months prior to the decedent's death, the named private foundation was administratively dissolved under Florida law, and was not reinstated until seven months after the decedent's death.

The Florida Court of Appeal analyzed the meaning of administrative dissolution under Florida law, and determined that no steps were taken to reinstate the foundation at the time of the decedent's death or to otherwise qualify the foundation as a private foundation with the IRS. As the administratively dissolved foundation could not take any actions at the moment of the decedent's death except to complete its dissolution, it was held to not exist for the purposes of the decedent's testamentary disposition.

Accordingly, the Florida Court of Appeal upheld the trial court's finding that the residuary disposition to the specifically named private foundation failed because it was not then administratively dissolved and not in existence. The public charity who succeeded to the private foundation's interest was instead entitled to the decedent's residuary property.

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:

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