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In the Spotlight:

Moses & Singer was named to the 2017 "Best Law Firms" List according to *U.S. News & World Report* and *Best Lawyers*.

Arlene G. Dubin was quoted on CNBC Personal Finance Section on Millennials and Prenups.

Gideon Rothschild was listed as a leading lawyer in this year's Best of the Best USA Edition of Expert Guides.

Upcoming Events:

Lori Ann Douglass will be speaking at Cornerstone Baptist Church in Brooklyn NY on "Year-End Estate Planning." on December 11, 2016.

Gideon Rothschild will present on strategies to provide greater divorce/creditor protection on January 10, 2017 at the 51st Annual Heckerling Institute in Orlando.

Daniel Rubin will be speaking on "Protecting Your Assets from Your Future Former Spouse" on January 17, 2017 at the New York State Society of CPAs Financial Planner Conference.

Gideon Rothschild joins a distinguished international panel assembled to exchange ideas and discuss developments in international estate planning at the STEP and New York State Bar Association's 13th Annual International Estate Planning Institute on March 23-24.

Tax Law Updates That Affect Estate Planning

By: Ira Zlotnick

Federal:

The recent election of Donald Trump as the 45th President of the United States of America combined with the Republican sweep of both the House of Representatives and the Senate has added a degree of uncertainty to the future of both the U.S. gift and estate tax. Candidate Trump had proposed a full repeal of the U.S. gift and estate tax but there are both political and non-political considerations which may make the repeal of both of these taxes less than a certainty. Even if the repeal of the gift and estate tax were to happen, Candidate Trump also proposed a capital gains tax at death for those transfers at death in excess of $10,000,000 (with certain exemptions for family businesses and farms) which would significantly alter the "stepped-up" basis landscape to which we have grown accustomed.

If these proposals were to be enacted, it is quite possible that trust planning might become more important than ever to avoid the triggering of the capital gains tax at death. In addition, many of our clients will continue to want to create trusts for many other reasons including for asset protection purposes or for succession planning purposes or simply as a hedge against reinstatement of the gift, estate and generation-skipping transfer tax under a future administration. Moreover, trusts will continue to be extremely useful in planning for divorce and in second marriage situations.

Although there is a great deal of uncertainty with respect to the future of the gift and estate tax we believe that clients should continue with their typical year-end planning, including making annual exclusion gifts, paying tuition and medical care costs gift tax free, and possibly using their remaining lifetime exemptions and/or zeroed out GRATs. We will, of course, continue to update our readers as developments occur but you should feel free to reach out to us in the interim.

New Jersey:

New Jersey recently passed legislation to repeal the New Jersey estate tax effective January 1, 2018. In addition, for decedent's dying after January 1, 2017 but prior to January 1, 2018, the New Jersey state estate tax exemption is increased from its current level of $675,000 per person to $2,000,000 per person. This legislation dramatically overhauls the state estate tax landscape for New Jersey residents and makes New Jersey one of the most taxpayer friendly states from an estate tax perspective.

While New Jersey repealed its estate tax, it remains one of a handful of states in the U.S. with a separate inheritance tax. The inheritance tax is levied on the transfer of assets to heirs, based on the relationship of the inheritor to the deceased. While the New Jersey inheritance tax does not apply to bequests to spouses and children, it does, for example, apply to bequests to siblings, nieces and nephews and thus should not be overlooked by a New Jersey resident when doing his or her planning especially since the inheritance tax exemption is nominal.

Given the repeal of the New Jersey state estate tax and the continuing application of the New Jersey inheritance tax, we recommend that clients living in New Jersey review their Wills to determine whether the legislation requires any changes thereto.

Connecticut:

Effective October 1, 2016, Connecticut enacted the Connecticut Uniform Power of Attorney Act (the "Act") updating the law governing powers of attorney. The Act provides two optional statutory forms (a new statutory short form and a revised statutory long form) each of which includes an updated list of basic powers that are being given to the agent. In addition, the long form includes additional gift giving powers that one can opt to give to his or her agent which could prove extremely useful in certain instances.

In addition, the Act (i) requires that a third party accept powers of attorney in most circumstances and limits when a third party can refuse to accept powers of attorney, (ii) provides that a filing of divorce or a separation action automatically revokes the spouse's agency, and (iii) presumes that the power of attorney remains effective during the principal's incapacity even if the form is silent on this issue.

Although the Act expressly provides that existing powers of attorney remain valid, it may be advisable for Connecticut residents to update their powers of attorney to benefit from the various additional provisions that are spelled out in the Act.

Reflections On Leadership And Family Business Conflicts

(Why It Matters for Family Attorneys)

By: Roy P. Kozupsky

"*Within every family, every community, and every organization, there are trials, tests, and tribulations. Do these lead to arguments, blame, and recrimination? Or does the group see them providentially, as a route to some future good (a "descent that leads to an ascent" as the Lubavitcher Rebbe always used to say)? Does it work together to meet the challenge? Much, perhaps all, will depend on how the group defines its reality. This, in turn, will depend on the leadership or absence of leadership that it has had until now. Strong families and communities have a clear sense of what their ideals are, and they are not blown off course by the winds of change.*"

Rabbi Jonathan Sacks, Lessons in Leadership

Attorneys advising wealthy families and their family owned enterprises are frequently asked by these clients what are the characteristics to help them navigate the inevitable tumultuous family conflicts and stay true to their purpose and mission?

One might think that the logical solution to avoiding these conflicts, or at least substantially mitigating them, lies in the process of more structural business planning. That is too narrow a conclusion.

One thoughtful family advisor perceptively (& humorously) articulated the problem:

> "*There is an old estate planning joke (of sorts) where an attorney is being arrested standing over the dead body of a client with a smoking gun on his desk. When questioned as to his motive, the lawyer says -"That plan he just signed was so complex and elegant, with so many moving pieces, I just had to see if it would actually work.*" [1]

There is no shortage of real-life cases where the courts have commented on the brilliance of some type of estate planning strategy which resulted in significant estate tax savings for the family but that very same plan seemed to have provided the petrol for the fire for the ensuing acrimonious litigation resulting in the near destruction of the family enterprise.

Families with diverse business interests are like ships at sea. When the weather is fair and the sea calm, the structural integrity of the ship is not under stress. Vulnerabilities, such as deeply rooted family issues or even leadership succession issues, are either not recognized or ignored under the guise of not being imperative. Unfortunately, human nature being what it is, all things change-including the values and perspectives of different family members which in many cases frequently diverge from tax centric "estate planning" strategies ingrained in the operating business. And when these forces collide the family enters a tempest.

The events could be unexpected and internal, such as the untimely death of a family patriarch or matriarch that provided the "glue" of keeping the family bound together, or external business pressures that materially degrade the ability of the family business to generate sufficient cash flows to satiate the needs of diverse stakeholders in the family enterprise. Today, changes come rapidly, sometimes unexpectedly to all industries, the immunities are none. But, when these changes happen to family enterprises, highly technical tax driven family planning

that ignores conflicts of interests between different family members can quickly digress into a perfect storm, endangering the fabric of the family and stress to the entire business enterprise.

Causes

The relatively new multidisciplinary world of advisory services focusing on family owned enterprises, has populated significant research into the area of the root causes of conflicts and the triggering events that are all too often seen by those attorneys and other professionals focused on this area of work.

It certainly should be noted that even the word "conflict" in family owned enterprises can be a misleading term. Some practitioners have noted the positive outcomes of family conflict. "Conflict provides an opportunity to obtain greater understanding of the opposing parties and how they think, act and feel. It gives individuals a chance to demonstrate an acceptance and respect for the unique ways in which others think, act and feel." [2]

But conflict left unchecked without help from professionals deeply schooled in understanding this area of work is likely to spiral out of control. And as many professionals have noted, families in business have a hard time openly talking about and analyzing these divisive issues-even when they can negatively impact an operating business. But this aversion to deal early on with these issues is depriving the family (and the business) of its needed oxygen.

In a valuable new book entitled *Deconstructing Conflicts – Understanding Family Business, Shared Wealth and Power* [3], the authors frame three core reasons for all conflict in business families. While seemingly self-evident to many practitioners, these reasons are: Opposing goals, Incompatible values and Historical Impasse.

Examples are indeed abundant of opposing goals and have no complete inventory, but for many families who share business enterprises some examples include:

> Paying dividends to help lifestyles of non-working family members vs. reinvesting free cash flow for growth,

> Sell the company to monetize all the years of hard earned work vs. retaining ownership of the enterprise as a means of perpetuating the legacy of those family member(s) who still work in and control the enterprise.

But all of this begs the question of what triggers these conflicts. As noted earlier, many of these "estate plans" seem fine when conceived. My (non-scientific) observations are that hibernating over long periods of time there is a subtle noxious interplay between leadership that can become compromised and highly structured business planning that has the potential to alienate different family members by creating subtle conflicts of interest.

"Conflict is triggered by the exertion of power by one individual or group over another, in a manner that is perceived as without legitimate authority or moral authority, arbitrarily, undeservedly… or humiliating to the target of the power." [4] Conflicts of interest can certainly devalue legitimate authority.

And when conflicts erupt the differences in the attributes of a leader and a trustee's fiduciary duties become apparent. Compromised fiduciaries, once camouflaged by indifference, are now targets of anger.

Examples usually involve family values that collide, deep conflicts of interest in one key family member having different roles in overseeing the enterprise, preferred and non-transparent compensation systems and deeply rooted family behavior that predates most advisory services.

So, how does this relate to the practice of law and the delivery of services to these business families? How can attorneys be of value to these families when all too often clients either want quick answers or are too impatient to pay for services that are indeed hard to conceptualize arising in the future?

Thoughts About Leadership

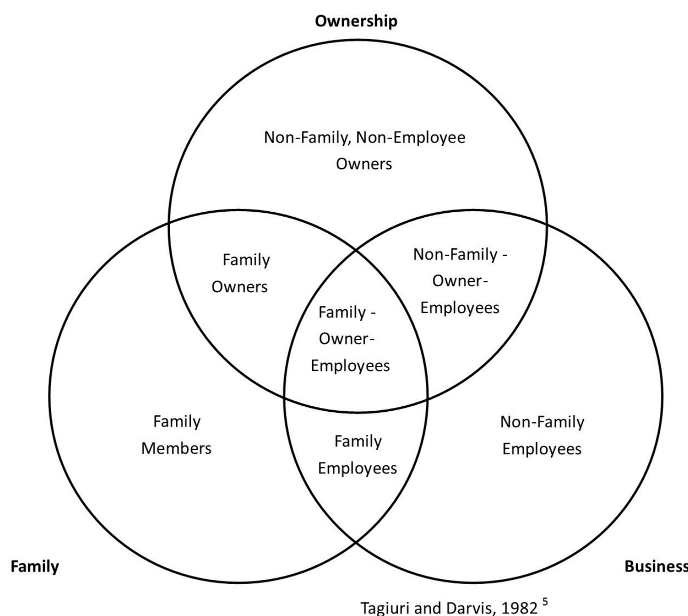
A few short comments about family business leaders. Being a leader is not (or should not) be something anyone inherits-it needs to be earned and not just by hard work-a leader needs to exercise a high level of moral authority, be a keen listener and have humility for their office. Today, leadership based upon primogeniture is rarely of long term benefit to a family.

As Rabbi Sacks has noted: "It is the vision that matters, not the office, the power, the status, or the authority. Leaders are led by their vision of the future, and this is what inspires others." Like a sieve, compromising this office, this moral human compass with conflicted duties, only dilutes one's authority and vision no matter how well intended.

Being a trustee and being a leader of a family enterprise should never be confused as simultaneous duties. There is indeed a fundamental difference between a family choosing the right leader (which is certainly hard enough and which can fill a library with literature) and a non-conflicted fiduciary acting as Trustee for other family members who are stakeholders in the family's

enterprise. A family member assuming the twin duties of these two offices (leader & trustee), even under the best of intentions, will likely not work.

Even a quick glance at the famous three circle model below [5] details the complexity of most family enterprises – making it clear to any casual viewer the complexities of managing family enterprises. So, why complicate matters?



Tagiuri and Darvis, 1982 [5]

In The Context Of Planning

It is not unusual for the parents of a family enterprise to leave their discounted and non-voting business interests in trusts centrally managed by trustees who all too often lack a deep understanding of the family, business and fiduciary duties. This type of legal planning only exacerbates deeply rooted family behaviors. Unfortunately, all too often this planning fails to account for the fact that some family members are getting disenfranchised and have no voice in the vision of the company, and have few, if any, clearly defined exit strategies to monetize the value of a gift or inheritance.

But in this author's opinion not carefully thinking this through, not building into the family business a set of checks and balances is like walking on thin ice in an April thaw-go too far out in time and there will likely be severe fractures in values and expectations of different family members ultimately culminating in the family falling into the great morass of frigid water. One just never knows when these fractures occur, but poor governance systems deeply rooted concentric only tax planning are one of these fracture points.

Without a system of checks and balances, the appointment of a director or other key officer as trustee of a trust that owns a family business can easily compromise the general fiduciary duties of loyalty and impartiality that any trustee owes to its beneficiaries. Officers and directors often have very different viewpoints about what is best for the family enterprise. Thus, it is not hard to imagine a situation arising where some family members might feel alienated and estranged when they are disenfranchised from the decision-making process. They inherited their status due to, in this example, estate planning ideas that were good for tax mitigation- i.e. creating business interests that have no voice or control in the business. While it is often noted that not all conflicts are conflicts of interests in the legal sense, preventing the interested family member or board member from serving as a trustee, diligence must remain high to carefully plan with key professional advisors the structures of governance that remain transparent and elastic over extended periods of time. These are systems where values are aligned in the family and where the checks and balances of governance are ingrained in the family's ethos.

Navigation through family conflict usually requires a leader with a keen and sincere sense of listening to other family members and who has no ingrained conflicts of interest.

Some might say that there is even a simple example to emulate- our three branches of government, executive, judiciary and legislative, are there for a reason.

<u>*Endnotes*</u>

1. *The Problem with Planning*, Matthew Wesley, The Wesley Group.

2. *The Legacy Family*, Lee Hausner & Douglas Freeman, 2009, Pg. 140

3. *Deconstructing Conflict*, *Understanding Family Business, Shared Wealth and Power*, By Doug Baumoel and Blair Tripp, 2016

4. Id, page 57

5. The Three-Circle Model of the Family Business System was developed at Harvard Business School by Renato Tagiuri and John Davis in the 1970s. It continues to be, the central organizing framework for understanding family business systems, used by families, consultants and academics worldwide. This framework clarifies, in simple graphic terms, the three interdependent and overlapping groups that comprise the family business system: family, business and ownership. As a result of this overlap, there are seven interest groups present, each with its own legitimate perspectives, goals and dynamics. The long-term success of family business systems depends on the functioning and mutual support of each of these groups.

Administering an Irrevocable Life Insurance Trust – Trustee Responsibilities

By: Kerrie C. Horrocks

Irrevocable life insurance trusts ("ILITs") are commonly used in estate planning to remove life insurance proceeds from the insured's taxable estate, allowing the life insurance proceeds to pass free of estate tax. The ILIT will also receive the life insurance proceeds free of income tax, providing significant liquidity at the insured's death.

Although commonly used in estate planning, the technical aspects of administering an ILIT are often misunderstood and mistakes can easily be made. Failure to properly administer an ILIT can result in adverse tax consequences to the grantor and to the beneficiaries, with consequent liability to the trustee, so it is important to be mindful of the following issues in administering an ILIT.

Opening a Bank Account and Paying Insurance Premiums

The trustee should open a bank account for the trust. The account should be used for the annual gifts made to the ILIT (generally in the amount of the insurance premiums). These gifts should be deposited from the grantor's individual bank account into the ILIT's bank account at least thirty days before the premium due date in order to allow the trust beneficiaries the ability to exercise their "Crummey" rights of withdrawal under the trust agreement (as discussed further below). As soon as the withdrawal period lapses, and assuming the beneficiaries have not exercised their withdrawal rights, the trustee should promptly pay the insurance premiums from the trust account, as the failure to make timely payments could result in a lapse of the policy.

In most cases, funds will only be held in the account for short periods of time, so a non-interest bearing account may simplify tax matters, as there will then be no interest income requiring the filing of an income tax return for the trust.

During the grantor's lifetime, it is not necessary for the trustee to obtain an Employer Identification Number (EIN) and the ILIT may use the grantor's social security number. However, in some instances a bank or insurance company may insist upon the ILIT obtaining a separate EIN, in which case the trustee can complete and submit IRS Form SS-4 to obtain a separate EIN.

Notice to Beneficiary Concerning "Crummey" Withdrawal Rights

Generally, the amounts gifted to a trust are taxable gifts. To qualify gifts to an ILIT for the annual exclusion (currently $14,000 per donee), the trust agreement will commonly grant some or all of the beneficiaries the right to withdraw certain amounts each year (commonly referred to as "Crummey" rights of withdrawal). The trustee should notify any beneficiaries (or, in the case of a minor beneficiary, the non-insured parent or guardian of the minor) who have Crummey withdrawal rights whenever the grantor makes any gifts to the ILIT. Importantly, a gift to the ILIT may include, for example, the contribution of a life insurance policy to the ILIT, the contribution of funds necessary to pay the insurance premiums or the direct payment of insurance premiums to the insurance company. The notice should be in writing, given immediately after the gift is made, contain a description of the gifted property, describe the respective rights of withdrawal in the beneficiary resulting from the gift and advise regarding the period of time in which the beneficiary has a right to exercise his or her power of withdrawal. Failing to provide such notice contemporaneously could result in adverse gift tax consequences.

Recordkeeping

The trustee should establish and maintain a permanent file to preserve important trust documents, including the trust agreement, insurance policies, assignments of insurance policies and valuations (if any), EIN (if required), and copies of all notice letters sent to Crummey beneficiaries. The trustee should also keep records of all trust activity, including receipts of deposits and payments of insurance premiums.

Monitor and Review Insurance Policy and Company

Trustees have a fiduciary obligation to make prudent investment decisions regarding trust assets, including life insurance policies. As such, the trustee should monitor and review the performance of the policy (or policies) as well as the financial health of the insurance carrier, and should be prepared to take action if necessary. The trustee should maintain a copy of the original illustration for each policy and should also obtain "in force" illustrations periodically to monitor whether such policy is performing in line with the projections and determine if any adjustments, including, if warranted, exchanging or surrendering the policy, are necessary to better satisfy the ILIT's objectives. This is particularly important with universal or variable policies.

Given today's low interest rate and low return environment, longer life expectancies and higher expenses being charged by some carriers, the trustee may find that policies are underperforming and expected cash values are being depleted, requiring the payment of premiums for a longer period or of a higher amount than anticipated and/or resulting in potentially reduced death benefits or worse, the ultimate lapse of the policy.

Collection of Insurance Proceeds

On the death of the insured, the trustee has the obligation to collect the proceeds of the life insurance policy held by the ILIT and to distribute the proceeds in accordance with the trust agreement.

ILITs can be great estate planning tools. However, mistakes in maintaining them, even honest mistakes, may prompt the IRS to challenge the trust and tax the insurance proceeds.

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