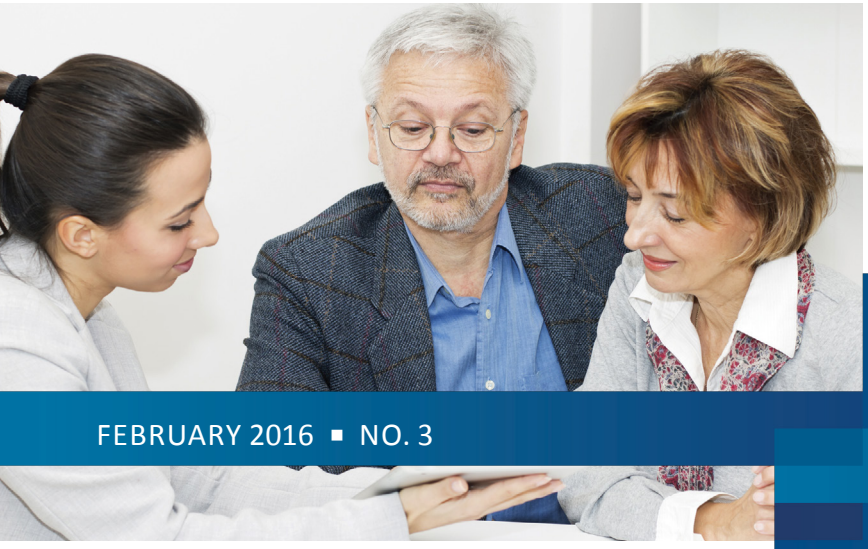

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BLANK ROME LLP
COUNSELORS AT LAW

Private Client

Annual Estate Planning Newsletter: Part Three

Action Item: This is the third installment of our Annual Estate Planning Letter, and covers some topics of interest not discussed in our previous installments. We urge you to review this installment to ensure that your 2016 estate and tax planning is in order.

1. **Life Insurance.** Life insurance proceeds are generally exempt from income tax. In addition, all estate tax on life insurance proceeds may be avoided on the death of the insured through proper planning: Insurance proceeds can be available free of estate tax to the surviving spouse, but by designating other family members or a trust for their benefit as owners and beneficiaries, estate taxes can be avoided in both spouses' estates. "Joint life" (or "survivorship" or "second to die") policies make life insurance planning affordable for many more people. You should consider the ownership and beneficiary designations for any newly acquired life insurance carefully before the policy is purchased. You also should review the ownership and beneficiary designations of your existing policies; your revocable living trust or Will does not generally control distribution of life insurance proceeds. "Split-dollar" life insurance plans now are subject to much more stringent rules; we suggest that you review with an insurance professional or with us any "split-dollar" life insurance programs in which you currently participate or in which you contemplate participating. Finally, recent economic activity may have caused your life insurance policies to experience financial problems; you may wish to contact your insurance professional to discuss the current status of your policies.

2. **Charitable Tax Planning.** There are several techniques available to transfer significant wealth to intended beneficiaries in a tax-favored manner and at the same time benefit charity. This is particularly true in connection with a sale of highly appreciated assets; a charitable remainder trust can be used to advantage in these circumstances. You also may be able to arrange to receive a lifetime annuity in exchange for cash or appreciated property, or even for agreeing to transfer your residence to a charity at your death (or at the death of the surviving spouse). You also may be able to transfer property to your descendants without (or with reduced) transfer taxes by establishing a

charitable lead trust (these are particularly advantageous in a low interest rate environment as currently exists as discussed in our second installment). The income tax benefits of donating partial interests in tangible personal property items (such as works of art) are currently restricted. The popular "Charitable IRA Rollover" rules that expired on December 31, 2014, were extended retroactively and made permanent on December 18, 2015; these rules are discussed in paragraph 3 below. Wealthier taxpayers may be interested in a private foundation or a donor-advised fund established at a public charity, such as a community foundation. The IRS has developed two web pages that may be of interest to these taxpayers: *Life Cycle of a Private Foundation* deals with private foundations (www.irs/gov/charities/charitable/article/0,,id=127912,00.html); and *Life Cycle of a Public Charity* deals with public charities www.irs.gov/charities/charitable/article/0,,id=122670,00.html).

3. **Employee Benefit Plans and IRAs.** Assets in pension and profit-sharing plans, IRAs, and other retirement plans (other than Roth plans) can be subject to severe taxes at death. You should ***review your plan benefits to determine whether you can avoid or postpone these taxes*** and whether your plan benefits are coordinated with your estate plan; your revocable living trust or Will generally does not control disposition of these benefits. Plan proceeds still can be the most advantageous to use for charitable gifts at death, including transfers to charitable remainder trusts and to establish charitable gift annuities. The "Charitable IRA Rollover" provisions expired on December 31, 2014, but were extended retroactively and made permanent on December 18, 2015, so in 2015 taxpayers who had attained age 70½ were able to and in future years will be able to direct a maximum of $100,000 to charity from an IRA (only); the payment will not be included in the taxpayer's income for the year, but it nevertheless will count against the taxpayer's "minimum required distribution" for the year. No charitable contribution deduction will be allowed, but most taxpayers nevertheless would benefit by using this technique as opposed to withdrawing funds from an IRA (taxable) and contributing those funds to charity (deductible, but subject to certain limitations).

4. **Subchapter "S" Corporations.** The use of Subchapter "S" corporations has become somewhat less popular because of the increased use of limited liability companies ("LLCs"). Care must be taken, however, with respect to existing Subchapter "S" corporations. For example, upon the death of a Subchapter "S" corporation shareholder, Subchapter "S" corporation status can be lost unless the decedent's shares pass to a qualified shareholder in a timely manner. All Subchapter "S" corporation shareholders therefore should ***assure that their estate plans allow for the continuation of Subchapter "S" corporation status.*** Subchapter S corporations also might be used to reduce payroll taxes imposed on their owner-employees.

5. **Family Limited Partnerships and Limited Liability Companies.** A "family limited partnership" ("flp") or "family limited liability company" ("fllc") can be an excellent estate planning vehicle for clients who own valuable assets. A flp or fllc can be advantageous if a family member encounters creditor problems in the future. Gifts of flp or fllc membership interests to your beneficiaries or to trusts for their benefit can qualify for the gift tax "annual exclusion" (as also discussed in our second installment) if properly drafted, and the value of those gifts can reflect the "discounts" available for minority and nonmarketable interests. "Discounted" values also can be used in connection with sales to desired limited partners or LLC members, including family members or trusts for their benefit. Some recent IRS challenges to these entities have been successful, however, so all administrative and operational details must be respected; some recent court decisions have focused on the actual organizational and operational aspects of the family entities. The tax benefits anticipated at the time of the formation of the entity should be available at the donor's death if the entity is organized for a significant non-tax business purpose and

operated strictly in accordance with the provisions of the governing instrument and applicable state law, the donor has retained enough assets outside the entity to satisfy the donor's personal financial needs, and the donor is not a general partner or LLC manager. **We continue to urge all clients who have implemented flps or fllcs to review those entities now.**

6. **"Buy-Sell" Agreements/Options.** A "Buy-Sell" or option agreement (whereby a family member or business associate has the obligation or option to acquire assets at an established price) can be used to advantage to restrict ownership of a business, to establish the value of an asset for estate tax purposes, and to provide a market for the asset to allow owners to plan for liquidity. This estate planning device is subject to restrictions, but some of these restrictions do not apply to agreements made before October 9, 1990. You therefore should be very careful if you wish to modify "Buy-Sell" or option agreements made prior to October 9, 1990. Employer-owned life insurance generally now is subjected to income taxation, **although insurance used to fund a Buy-Sell Agreement is exempt from income taxation, provided that certain written notice and consent requirements are met *in advance.***

7. **Regulatory Notice.** We are providing this letter and the enclosure as a commentary on current legal issues as a service to our clients and friends; neither should be considered legal advice, which depends on the unique facts of each situation. Receipt of this letter and the enclosure does not establish an attorney-client relationship.

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The attorneys in Blank Rome's Private Client group have extensive experience in implementing cutting-edge estate planning techniques to take advantage of these unique opportunities and challenges. Please contact us to assist you in reviewing and updating your estate plan.

For additional information, please contact a member of Blank Rome's private client group:

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