Practical Precautions Practitioners Should Consider for Estate Planning: Lessons from Sorensen, Smaldino and Levine

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Agenda

- There have been several recent important decisions out of the United States Tax Court, *Levine Est. v. Comr.*, 158 T.C. No. 2 (February 28, 2022), a taxpayer victory in an intergenerational family split-dollar estate tax case, and *Smaldino v. Comr.,* T.C. Memo. 2021-127 (November 10, 2021), a taxpayer loss in an indirect gift case. Most recently the Sorensen v. Commissioner, Tax Ct. Dkt. Nos. 24797-18, 24798-18, 20284-19, 20285-19 (decision entered Aug. 22, 2022) highlighted the importance of proper documentation and implementation of planning.
- While these cases present a plethora of substantive law issues worthy of discussion, this webinar will focus on the practical lessons for estate planning professionals of all stripes about how to plan considering the lessons of these cases.
- Understanding what was done right or wrong provides valuable guidance on how to better structure and implement estate plans.

Introduction to *Smaldino*

- *Smaldino v. Comr.,* T.C. Memo. 2021-127 (November 10, 2021).
- From a planning perspective, the IRS and the Tax Court recast a gift by husband to wife and then almost immediately by wife to an irrevocable trust for the benefit of the husband's descendants (who weren't also descendants of the donor wife-a blended family) as a gift by the husband/father to a trust for the benefit of his descendants.

Introduction to *Smaldino*

- Implementation and administration failed or was mishandled from several perspectives. That's the case in a nutshell.
- Some have dismissed it as a "bad facts, bad law" case. While the case indeed has many bad facts, dismissing it as nothing more than a "bad facts" case misses a great opportunity to learn about how to do estate planning correctly.
- Provides important lessons for practitioners to consider about how to approach structuring and implementing estate plans for certain clients, especially for clients that practitioners did planning for during the rush in 2012, and throughout 2020 and 2021, and many will repeat in the days leading up to 2026.
- To avoid that problem plan now and plan thoughtfully.

Introduction to *Levine Est.* Case

- A recent Tax Court case decision provided a resounding victory (at least for now) to the taxpayer who had pursued what some might view as an aggressive split-dollar life insurance plan to minimize estate taxes. *Levine Est. v. Comr.*, 158 T.C. No. 2 (February 28, 2022).
- This follows prior cases that indicated problems for held strongly against other taxpayers who had implemented somewhat similar split-dollar arrangements, using somewhat similar arrangements.

Introduction to *Levine Est.* Case

- Understanding what the taxpayer did right in the *Levine Est.* case, and how that contrasts to what taxpayers did wrong in prior cases, *Cahill Est. v. Comr.*, T.C. Memo 2018-84, and the *Morrissette Est.* decisions identified below, may provide guidance to can be used to guide taxpayers contemplating such planning or other planning, including the use of FLPs.
- *Morrissette Est. v. Comr.*, T.C. Memo 2021-60 (May 13, 2021) ("*Morrissette II*"), which follows a case for the same taxpayer, *Morrissette Est. v. Comr.*, 146 T.C. 171 (2016) ("*Morrissette I*").

Introduction to *Levine Est. case*

- But even better guidance may be possible. A careful reading of the *Levine Est.* case to identify steps the *Levine* Court found favorable, might be used to craft a roadmap of how to implement a similar plan.
- Importantly, the points in the roadmap below should be considered by taxpayers undertaking almost any type of estate planning.

Introduction to Sorensen case

i. The donors relinquished dominion and control of all the shares in 2014 so that the gift of the full amount of shares, not the $5 million worth of shares contemplated under the Wandry fixed dollar transfer.

ii. The reporting by the entity did not comport with the purported defined value transfer. The company reported that each trust owned 9,385 shares on its stock ledgers and on income tax returns. The stock ledger and tax returns should have include an "asterisk" referencing an explanation of the intended transaction. Practitioners might provide language to the effect that $5 million of shares were transferred.

iii. In Sorensen, the trusts received pro rata distributions based on the ownership of estimated number of 9,385 shares. Distributions should be based on the initially determined amount of shares, which could be adjusted to be based on finally determined gift tax values, and that the transferors and their trusts would make appropriate adjustments between themselves if the shares were changed.

Introduction to Sorensen case

i. In Sorensen, the IRS argued that the defined value mechanism should not be respected as there was no agreement with the recipient trusts. The trusts have agreed to transfer shares in accordance with the defined value formula and should have countersigned the stock powers, with described the transfers as defined value formula transfers. The trusts should countersign the stock powers to specifically acknowledge the conditions under which they are receiving the stock transfers. A preferable approach might be to not have the equity interests pass to the donee trusts in the case of a gift (or purchasing trusts in the case of a note sale) but rather be held in escrow with an independent escrow agent pending resolution of the contingency of the gift tax value as finally determined.

Lesson 1: Be Cognizant of Your Client’s Level of Knowledge, Sophistication, and Willingness to Follow Professional Advice

- In *Smaldino*, Mr. Smaldino was certified public accountant (CPA) and even had worked as a CPA. Mrs. Smaldino had a master's degree in economics, so she too should have had the sophistication to have some understanding of the planning they pursued for the family’s real estate portfolio was worth about $80 million
- But as risky to the estate planner is the client who is unlikely to seek or follow professional advice on maintenance and tax compliance in potentially fragile situations like S corporations, private foundations, etc. Some clients are best steered away from techniques in which they’ll be their own worst enemies.
- Clients who won’t follow the rules, won’t pay for advice, or won’t come back for regular reviews with their planning team, will have foot faults or worse. Consider offering planning options but document the warnings of complexity and required formalities.

Lesson 2: Stay vigilant about the changing facts and circumstances

- Mr. Smaldino owned and operated numerous rental properties. He established an LLC, as well as a revocable trust called the Smaldino Family Trust. Mr. Smaldino transferred entity interests in 10 different parcels of real estate into the LLC. The LLC's ownership structure was restated so that there was 10 Class A Voting units and 990 Class B Non-Voting units, all of which were initially held under the Smaldino Family Trust.
- Planning conceived or completed under pressure (e.g., 2020-2021) should be followed up upon later to see if any portion of the planning was either missed or not implemented correctly.
- The gift tax return should be an opportunity for a complete second look at the transaction but too many clients view this as a simple formality for a CPA to complete under a pressured budget then as a collaborative effort and review of the entire transaction.

Lesson 3: Must consider the client's asset protection needs and requirements

- In *Smaldino*, it seems that multiple rental properties were held in a single LLC. The structure of having multiple rental properties owned in separate LLCs is a prudent way to endeavor to minimize a client's personal liability so if a tenant or anyone else, for example, sues the client for harm arising from the property owned by the LLC, the tenant (or other creditor) should only be able, as a general matter, to reach the assets held in the LLCs, not the client's other personal assets.
- Having each property held in a separate LLC to prevent a "domino" effect of a judgment against one property being able to reach the assets of the other properties held in the LLC. That way, if there is a lawsuit against one property, the others might remain "untouched."
- A client that won't permit proper planning, e.g., separate LLC for each property, is likely to prove to be a client who won't adhere to other formalities and planning advice. That is a worrisome **red** flag.

Lesson 4: Consider coordinating applicable law for entities and DAPT

- If the plan included establishing a trust in a trust "friendly" state (e.g., Alaska, Nevada, South Dakota), consider establishing the LLC in the state that the trust will be governed under, and then have the LLC authorized to do business in, the state where the real property assets are located. This may help provide additional nexus, to the trust-friendly jurisdiction.
- Many clients won't spend the extra effort and money to properly structure a trust in a trust friendly jurisdiction despite the possible benefits, as recognized by the Levine court. Practitioners might consider documenting the recommendation if it won't be pursued.

Lesson 5: Consistency is the hallmark of excellence

- Mr. Smaldino "purportedly" transferred about 41% of the LLC membership interests to his wife on April 14, 2013. Mrs. Smaldino "purportedly" gifted those same interests to the Dynasty Trust the very next day. The Tax Court had little difficulty recharacterizing the claimed gift Mr. Smaldino made to Mrs. Smaldino, followed by her gift to the Dynasty Trust, as if Mr. Smaldino himself had made the gift directly to the Dynasty Trust. Mrs. Smaldino held the interests possibly only for a day.
- She transferred the same exact interests she received from her husband as a gift to her, as her gift to the Dynasty Trust, and the family and their advisers skipped numerous steps that should have been followed to corroborate that they respected the transaction.
- Avoid circular transactions.

Lesson 6: How long must assets be held?

- Practitioners may need to consider providing different suggestions to clients based on the facts of the case, as the kind of assets being transferred could affect what is a sufficient amount of time between phases.
- In the *Holman* case, the Court accepted six days as sufficient time between phases of a plan. In *Holman*, the IRS also argued that the gift should be viewed as an indirect gift, applying the step transaction doctrine in that instance. *Holman v. Commissioner*, 130 TC 170 (2008), aff'd, 601 F.3d 763 (8th Cir. 2010). This should have already been done.
- Bear in mind the longer the better, but more is advisable, what economically significant events can occur during the ownership period.

Lesson 7: Formalities must be respected

- It is fundamental for much of legal and tax planning that, in order for creditors, the IRS, or others to respect legal structures clients establish as real, the clients themselves should first respect the formalities and maintenance of their separate legal entities.
- The Smaldino's, even with their formal training (CPA; economics), ignored most formalities. Contrast that with the situation in Levine Est., where the taxpayer and the other players respected formalities.
- Respect formalities.

Lesson 7: Formalities must be respected

- Then evaluating the actions taken by the Smaldinos, they did not do well respecting the formalities of their entity, regarding the gift Mr. Smaldino tried to claim he made to Mrs. Smaldino.
- Adhering to the **formalities of the operating agreement restrictions** would not have taken much effort, Mr. Smaldino as trustee of the Revocable Trust and as manager of the LLC could have given written consent for the admission of Mrs. Smaldino as a member, showing adherence to the formalities required by the operating agreement of the entity.
- Observe formalities especially the formalities created in the plan.

Lesson 7: Formalities must be respected

- The Court further notes that *"The LLC's operating agreement was never amended to account for any transfer of units to Mrs. Smaldino. However, exhibit A of the operating agreement was amended 'as of April 15, 2013' to show the Dynasty Trust as holding a 49% ownership interest in the LLC."*
- Practitioners should consider whether the failure to adhere to formalities for the gift to Mrs. Smaldino, and then adherence to the formalities for the transfer to the Dynasty Trust, may have hurt Mr. Smaldino's case.

Lesson 7: Formalities must be respected

- The problem with dates of legal documents in the Smaldino case was significant. The Court felt that the taxpayers were **disingenuous** regarding the dates of the documents. The Court noted that the appraisal report that valued the LLC was dated August 22, 2013. The Court believed that the **documents were signed after the appraisal, months after their effective dates**.
- The legal document used to transfer the LLC interests from Mr. Smaldino to Mrs. Smaldino said that it was "Effective: April 14, 2013" but it did not include a section for each individual signing the document to indicate when that individual actually signed it.

Lesson 7: Formalities must be respected

- In *Smaldino*, the LLC filed its initial partnership income tax return (Form 1065), U.S. Return of Partnership Income.
- On the Schedules K-1, Partner's Share of Income, Deductions, Credits, etc., attached to the Form 1065, the LLC listed Mr. Smaldino as a 51% partner, and the Dynasty Trust as a 49% partner for the entire tax year.
- Mrs. Smaldino was not listed as a partner for any part of the tax year. Thus, the income tax returns did not reflect a partial year ownership (1 day) for Mrs. Smaldino, which was contradictory to the position the taxpayers' tried to argue.
- Have a date documents are actually signed noted on each document even if there is a different effective date.

Lesson 7: Formalities must be respected

- The gift documents for all transfers reflected an intent that the gifts be ***defined value gifts***. But that doesn't appear to have been respected by the Petitioner's business appraiser or by the IRS business appraiser.
- The following footnote from the Tax Court opinion is ***significant***: *"Petitioner concedes that these defined value clauses do not define or limit the amount of his taxable gifts to be determined in this proceeding."*
- How could the Petitioner argue with a straight face that the Tax Court should respect the gift tax position that Mrs. Smaldino was a legitimate holder when ***Mrs. Smaldino never held an ownership position for income tax purposes***, as per the LLC's Form 1065?
- Be sure that all documentation, tax returns, trust records, etc. are consistent with the transaction intended.

Lesson 7: Formalities must be respected

- The gift by Mr. Smaldino to Mrs. Smaldino didn't have to be included on the gift tax return. IRC Sec. 6019(2). But ***should it have been*** notwithstanding IRC Sec. 6019(2)?
- Notwithstanding IRC Sec. 6019(2), we recommend that practitioners consider that ***all spousal gifts be included in all events,*** just in case there was an issue concerning the proper deductibility of a spousal gift because the exception to the general rule that all taxable gifts be scheduled on the Form 709 for spousal **only applies if the gift is properly deductible under IRC Sec. 2523**.

Lesson 8: Make sure that the appraiser(s) are valuing the right properties

- The Tax Court opinion doesn't shed light on why the petitioner's business appraiser issued an opinion of value over a ***stated percentage***-49% of the Class B nonvoting units in Smaldino Investments, LLC that were originally gifted to Mrs. Smaldino on April 14, 2013 and then regifted by Mrs. Smaldino on April 15, 2013 to the Smaldino 2012 Dynasty Trust when the ASSIGNMENT SEPARATE FROM CERTIFICATE "assigns and transfers" to Mrs. Smaldino a "sufficient number" of Class B nonvoting units in Smaldino Investments, LLC "so that the fair market value of such nonvoting units as determined for federal gift tax purposes shall be Five Million Two Hundred Forty Nine Thousand One Hundred Eighteen and 42/100ths Dollars ($5,249,118.42)."
- Consider the Batty case and Dematteo v. Comm'r, Tax Ct. Dkt. No. 3634-21 (July 21, 2022).

Lesson 8: Make sure that the appraiser(s) are valuing the right properties

- The gift instrument was styled as a ***defined value gift.*** In typical defined value gift appraisals, the petitioner's business appraiser ***should have valued one unit*** of Class B nonvoting Smaldino Investments, LLC units, but he clearly didn't do that. According to the Tax Court's opinion, his valuation report stated: "a 49% Class B units nonvoting member's interest in the Company [the LLC] as [of] April 15, 2013 for certain tax reporting requirements on Form 709, US Gift Tax Return." ***Why not?***
- Who instructed the petitioner's business appraiser to value a ***49%*** interest in Class B nonvoting units in Smaldino Investments, LLC, when that percentage of Class B nonvoting units in Smaldino Investments, LLC was ***never transferred***?

Lesson 8: Make sure that the appraiser(s) are valuing the right properties

- Given that there was no transfer of ***49%*** of the Smaldino Investments, LLC Class B nonvoting units, in our opinion, the Petitioner's business appraiser engaged in a ***hypothetical valuation*** in valuing 49% of the Class B nonvoting units in Smaldino Investments, LLC.
- This is an ***assumption***, which is a very important term in the various business valuation standards. On the next few slides, let's examine the business valuation standards that were applicable to the petitioner's business appraiser.

Lesson 8: Make sure that the appraiser(s) are valuing the right properties

- The petitioner's business appraiser was James A. Biedenbender, CPA, whose company website (http://173.201.96.85/) indicates that he holds business valuation credentials from AICPA (the ABV) and NACVA (the CVA). Therefore, Biedenbender is required to adhere to the business valuation standards promulgated by ***both*** AICPA (the SSVS 1) and NACVA (NACVA Professional Standards).
- In the ***NAVCA Professional Standards***, the Development Standards (IVG9), the Reporting Standards (VC1c11 and VC1f for detailed reports) and VC3a9 and VC3b for calculation reports) and the Review Engagement Development Standards (VIIA9) and the Review Engagement Standards (VIIIA3 and VIIIA4a) provide express treatment rules for ***assumptions***.

Lesson 8: Make sure that the appraiser(s) are valuing the right properties

- In the ***AICPA Statements on Standards for Valuation Services (SSVS)***, the term ***assumptions*** appear in .12dii (Professional Competence), .18 (Assumptions and Limiting Conditions), .25 (Analysis of the Subject Interest), .44 (Documentation), .52l (Introduction), .65a (Representation of the Valuation Analyst), .68g and .69 (Conclusion of Value), .70 (Appendixes and Exhibits), .71m and .72 (Summary Report), .74, .75 and .77 (Calculation Report), .78 (Oral Report), .80 (Appendix A-Assumptions and Limiting Conditions), and .82 (Appendix C-Glossary of Additional Terms).
- The Tax Court opinion is silent as to whether the petitioner's business appraiser's valuation report characterized the assignment as an assumption, which it must have been given that the conclusion of value was not responsive to the actual transfers.

Lesson 8: Make sure that the appraiser(s) are valuing the right properties

- Why did the petitioner's business appraiser value a ***49% interest*** instead of either separate ***defined value gifts*** of Class B nonvoting units in Smaldino Investments, LLC, or even an ***8%*** and ***41%*** interest, respectively, which was what was actually gifted?
- Even though the total percentage of Class B nonvoting units in Smaldino Investments, LLC that were transferred was 49%, the two blocks should have been valued separately. It's ***doubtful*** that the sum of the values of separately valued 8.05% and 40.95% interests is equal to the value of the 49% interest. Why? Because the discounts for lack of control and marketability for the 8.05% interest would have been larger.
- It's ***imperative*** that taxpayers who desire to have defined value gifts be respected for tax purposes to themselves honor and respect those clauses. ***This appraisal arguably valued the wrong property and actually supported the IRS position that the Petitioner actually made an indirect 49% gift.*** Unfortunately, the IRS appraiser made the same mistake.

Lesson 8: Make sure that the appraiser(s) are valuing the right properties

- Even though they didn't, couldn't the Smaldinos have accomplished their goals through simple gift-splitting? It appears so. Then why didn't they, especially given that it seemed clear that Mr. Smaldino (or his children, one of whom was trustee) didn't trust Mrs. Smaldino.
- The only possible reason why is if Mr. Smaldino had already used up much of his applicable exclusion amount and would have had to pay gift tax if he'd gift-split.
- But if that was the case then a more prudent approach to the planning goals they pursued should have been used.

Lesson 9: Carefully consider and properly account for interspousal transfers

- The practical effect of the Tax Court's opinion was to negate any taxable gift as having come from Mrs. Smaldino by expressly holding that the taxable gift of units of Class B nonvoting interests in Smaldino Investments, LLC by Mrs. Smaldino roughly equal to her entire applicable exclusion amount to the Smaldino 2012 Dynasty Trust.
- Does Mrs. Smaldino automatically get her entire applicable exclusion amount restored? In our opinion, probably not unless she took some timely independent steps. First, Mrs. Smaldino's gift tax return wasn't at issue in this Tax Court case.
- Even if not required to report or certain formalities may not be necessary, doesn't mean they may not be beneficial to consider.

Lesson 9: Carefully consider and properly account for interspousal transfers

- **Protective Claim**–preserves the taxpayer’s right to amend until a contingency is resolved.
- In this case, Mrs. Smaldino could have used a protective claim to hold-open the statute and retain the right to amend her return.
- This could have prevented the putative result both losing Mrs. Smaldino’s applicable exclusion amount and Mr. Smaldino incurring tax on the same gift.

Lesson 9: Potential perils of joint representation in interspousal transfers

- **Ethics Issue:** Did the same lawyer represent Mr. and Mrs. Smaldino ***jointly?***
- The facts are not clear about whether the same lawyer represented both Mr. Smaldino and Mrs. Smaldino, and if he represented both of them, if he did so jointly or separately.
- If the same lawyer represented both of them, irrespective of the capacity, the lawyer might have a conflict of interest ethics problem if the lawyer either recommended or advised the couple to engage in the transaction without pointing out the obvious risks to Mrs. Smaldino of the indirect gift risk, which I believe should have been readily apparent to any competent estate planning lawyer.
- When spouses are involved practitioners should consider protective steps they might take.

Lesson 10: Remember that related party transactions are closely scrutinized

- The court notes that heightened scrutiny is appropriate for cases, such as in *Smaldino*, where all the parties to the transactions in question are related.
- The courts have viewed family transactions as affording much opportunity for deception and that therefore those transactions should be subject to close scrutiny. Estate planning transactions are invariably between related parties, so communicating to clients that greater caution and care in assuring that the substance of the transaction does not compromise the intended results, specifically through the steps taken (and implemented properly) and the documentation prepared is important.
- Try to understand the actual transactions and don't just rely on a case or ruling. Remember the law is continually evolving.

Lesson 10: Remember that related party transactions are closely scrutinized

- The court quotes several cases for this doctrine: "*See…Kuney v. Frank, 308 F.2d 719, 721 (9th Cir. 1962) ('Transactions between persons in a close family group, whether or not involving partnership interests, afford much opportunity for deception and should be subject to close scrutiny.' (quoting H.R. Rept. No. 82-586, at 33 (1951), 1951-2 C.B. 357, 381)); Estate of Bongard v. Commissioner*, 124 T.C. 95, *119 (2005) ('A transaction between family members is * * * subjected to heightened scrutiny to ensure that it is not a sham or disguised gift.')*"

Lesson 11: Be meticulous in attention to detail

- The *Levine Est.* court recounts in detail the sophistication of the family, the attention to details in all matters not only estate planning, the legitimate and substantial business operations and investments involved (not merely a passive securities portfolio as in some bad fact cases), etc.
- This care and diligence seemed to impress the *Levine Est.* court and appears to have given legitimacy and respect to the overall plan. This was significant and is not what occurs in many plans.

Lesson 11: Be meticulous in attention to detail

- The *Levine Est.* court noted "estate planners as skilled as the ones the family retained." The *Levine* Court seems impressed throughout the opinion with the professionalism of how matters were handled.
- Perhaps this is an indication of how important doing the opposite of what was done in so many bad fact cases is to succeeding in a challenge – be thorough, adhere to formalities, etc.

Lesson 11: Be meticulous in attention to detail

- *“Swanson [the estate planning attorney] spent a good deal of time thinking through all the advantages and disadvantages, conditions and qualifiers. He put together a PowerPoint presentation for the family in late 2007 or early 2008. Then in January 2008 he sent a letter to Larson and the children in which he described the transaction and its legal and tax implications.”*

Lesson 11: Be meticulous in attention to detail

- Deliberate careful planning, well explained to the client. Too often this degree of care does not happen, primarily in many cases because clients do not wish to incur the additional fees to permit their advisers to operate in this manner.
- Perhaps this is all a caution to such clients that being "penny wise and pound foolish" is not the way to handle tax planning. Perhaps advisers should inform clients of the tone and comments in the *Levine Est.* case to support why deliberate, documented, and thoughtful planning is worthwhile. This type of well documented planning assures the client understands the planning and may protect the practitioner from later claims that the plan or its risks were not explained.

Lesson 12: Compile and preserve evidence of financial sustainability

- The *Levine* Court noted: *"From the beginning, Larson [the independent trustee of the ILIT] and Levine's children made it clear to Swanson [the estate planning attorney] that Levine wanted enough money to maintain her lifestyle until her death. This meant that any estate planning needed to be done with Levine's excess capital—i.e., assets that she would not likely need during her lifetime."*
- Preserving adequate resources for the taxpayer engaging in planning is important to deflect a challenge of, for example, an implied agreement with the trustee of a trust, etc. Here, the taxpayers considered this important fact. In too many plans, clients do not have advisers prepare forecasts corroborating their financial comfort after proposed transfers are made.

Lesson 13: Potentially critical help-Independence

- In *Levine Est.*, Larson was the sole member of the investment committee that managed the irrevocable trust.
- Only Larson, the independent insurance trustee (investment committee) had the right to prematurely terminate the life-insurance policies. These arrangements gave the other two attorneys-in-fact for decedent no rights to terminate the policies or the arrangement itself.
- Note: This differs from *Cahill Est*., where decedent/decedent's agents had the right to agree along with an independent trustee of the ILIT to a termination of the split-dollar agreement. This was a critical element of the case that supported the taxpayer victory. But how different in reality was it if Larson was a co-agent and the insurance trustee?
- Consider all the various relationships of the parties, and legal advisers in the particular transaction you are planning and implementing.

Lesson 13: Potentially critical help-fiduciary duty

- Larson was under a fiduciary duty to exercise his power to direct the Insurance Trust's investments prudently, and he faced possible liability to its beneficiaries if he breached that duty.
- Fiduciary duty is an important factor in the Court's analysis in *Levine Est*., as it was to the United States Supreme Court in *Byrum v. U.S.*, 408 U.S. 125 (1972). The Insurance director/trustee (under the title here of Investment Committee) had a fiduciary obligation to the beneficiaries to make reasonable decisions. Is this a *Byrum* type of argument? The Court noted above the independence of the person named (he was not family), and his business and financial acumen.

Lesson 13: Potentially critical help: fiduciary duty

- But in *Cahill Est.*, even though the ILIT trustee was a cousin and business partner of the son, he still had a fiduciary responsibility to act appropriately for the beneficiaries of the trust.
- If that fiduciary responsibility required that he not terminate the split-dollar agreement, then could he be assumed to do so? What quantum of independence might be necessary for that fiduciary responsibility to be relevant?

Lesson 13: Potentially critical help: fiduciary duty

- Would the *Cahill Est.* court opt to disregard the fiduciary responsibility in all situations? Can it? How different is a cousin/business partner in *Cahill Est.* versus a 50-year employee/business partner who was not a relative in *Levine Est.*?
- Would a second cousin be viewed differently?
- How can the facts in the two cases be reconciled to an understandable framework from which to plan?

Lesson 13: Potentially critical help: independent trustee

- South Dakota Trust Company was the general trustee of the trust and was an independent institutional trustee.
- The use of not just an independent trustee but an independent institutional trustee seemed favorable in the Court's view of the case.

Lesson 13: Potentially critical help: independent trustee

- The cost relative to most plans of naming an institutional trustee is quite modest yet many clients resist because of the cost. Again, the *Levine Est.* case provides confirmation that this step may well be worth the cost involved.
- Many clients prefer the use of family trustees because they will not charge and will accommodate any request. But the latter is exactly what using an institutional trustee may infuse more independence, reality and respect for any transaction. Again, another take home lesson from *Levine Est.*

Lesson 13: Potentially critical help: independent trustee and different beneficiaries Under ILIT and estate, etc.

- The *Levine Est.* court noted the: "*…fiduciary obligations Larson owes to the beneficiaries of the Insurance Trust—obligations that would prevent him from surrendering the policies*." Be certain that the facts comport with that requirement.
- Decedent's children and grandchildren were the beneficiaries of the irrevocable trust.
- The court noted: *"The Insurance Trust's beneficiaries were Robert, Nancy, and Levine's grandchildren— the grandchildren that Levine naturally wanted to take care of."*
- The different/distinct beneficiaries should be persons whom the client wants to benefit, and that should be documented.

Lesson 14: Consider Going a Step Further to Avoid the Sorensen Issues

- Use an independent escrow agent to hold documents of title to assure adjustments are made to reflect gift tax value as finally determined.
- Incorporate into the transfer documents an economic adjustment mechanism to assure that if there is a gift tax valuation adjustment the economics of the transaction are properly adjusted as between the parties and charge a CPA with this task.
- Be certain every record of the transaction consistent reports in a manner consistent with the actual valuation adjustment mechanism used.
- Adhering to formalities in all transactions is vital to enhancing the likelihood of success.

Conclusion

- Thank you!!!
- Questions???
- Comments???
- Suggestions???
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