The Mortmain

A Publication of the Atlanta Bar Association, Estate Planning & Probate Section - Winter 2008

Jonathan Blattmachr Speaks on Estate Tax Reform, Middle-Class Clients, and the Income Taxation of Estates & Trusts

Shari Harvey, Diversified Trust, and Jacquelyn H. Saylor, The Saylor Law Firm, LLP

On November 8, 2007, over 120 attorneys and CPAs gathered at the Ritz-Carlton, Buckhead, for the fourth joint program of the Estate Planning and Probate Section of the Atlanta Bar and the Estate and Financial Planning Section of the Georgia Society of CPAs. With the help of Diversified Trust Company, the two sections presented nationally known estate planning expert, Jonathan G. Blattmachr, of Milbank, Tweed, Hadley & McCloy LLP.

Following a welcome by Hal Daughdrill, Chairman of Diversified Trust Company, Julie Childs of McLain & Merritt, PC, the current Chair of the Estate Planning and Probate (EP & P) Section, introduced Blattmachr. Blattmachr is a regular speaker at the Heckerling Institute on Estate Planning and was already well known to many. Blattmachr's presentation was entitled "Estate Planning Mysteries: Planning for the Middle Class Client and Income Taxation of Estates, Trusts, and Other Entities." While the subjects generally do not prompt overwhelming excitement, the speaker's charismatic style and active engagement of his audience easily held the attention of his listeners.

In addition to the two main topics, Blattmachr also addressed the politics behind potential reform or repeal of the estate tax. Blattmachr met Senator Max Baucus (D – Montana) about six weeks before the November seminar. According to Blattmachr, the Senator initially said that nothing on estate tax reform will happen before 2009, for two reasons: First, because the current deficit is $9 trillion (up from $4 trillion in 2001), and second, because repeal or reduction of the estate tax would be a big revenue loser. Blattmachr also said that Senator Baucus also believed that the Republican Party would push to allow the repeal of the estate tax to come into effect in 2010, hoping that political pressure will force repeal to be made permanent once

Blattmachr Continued on Page 2

Robert Morgan Presents on Florida Law

David L. Watson, Gomel & Davis, LLP

On November 14, 2007, the Section was treated to a presentation from Robert M. Morgan of the firm of Ford Bowlus Duss Morgan Kenney Safer & Hampton, PA, a law firm in Jacksonville, Florida. (How would you like to be their receptionist?) Robert is the brother of Richard Morgan who is an active member and former Chair of our Section. The full title of Robert's presentation was "Putting Florida Real Property in Trust: Be Careful What You Wish For".

It seems that almost every estate planning practitioner in Georgia will at some point or another be confronted with a question regarding Florida law. This may result from a client who has moved residency to Florida, or who has simply purchased real estate in Florida. Robert was kind enough to answer many of our common questions that arise in these situations, as well as giving us much additional information about

Pictured are guest speaker **Robert M. Morgan**, *Ford Bowlus Duss Morgan Kenney Safer & Hampton, PA* and Section Chair **Julie Childs**, *McLain & Merritt, PC.*

Morgan Continued on Page 3

Disclaimer Note: The case notes and other information in The Mortmain *are provided as a service to the members of the Section, and are written and edited on a volunteer basis. They are general in nature, and are not intended to be a comprehensive or detailed statement of applicable law. Therefore, the reader may not rely on any materials in* The Mortmain *in providing specific advice to clients in his or her practice. The views and conclusions expressed in the articles herein are those of the authors and not necessarily those of the Editorial Board of* The Mortmain*, nor of the Directors and Officers of the Section.*

Blattmachr Continued from Page 1

it happens. Moreover, Blattmachr noted that exemption increases are much more expensive than rate changes; he thinks that the chance of a $3.5 million exemption is zero since that would require heavier taxes elsewhere and create too much political uproar. The "sleeping giant" of the Alternative Minimum Tax (AMT) will create even greater political pressure for reform or repeal than the estate tax will. Blattmachr thinks there may be a 5% chance that carryover basis will exist in at least 2010.

According to Blattmachr, the main concerns of middle-class clients are protecting their wealth from creditors and taxes. The problem is that lifetime transfers are the most tax effective and provide most creditor protection benefits, but those at the $5 million level or so do not want to give up their assets or affect their lifestyles. The "King Lear" effect also worries people; if they give assets to their children during their life, the children may turn against them. A person can minimize the pain of lifetime gifts through gifts of assets in trust, which can be a particularly favorable technique when used with life insurance policies. Trusts offer one benefit by allowing the giver to maintain some control over the gifted property and when and how it may be enjoyed by the gift beneficiaries. Additionally, trusts tend to create very good creditor protection, as Section 541 of the Bankruptcy Code provides that spendthrift rules created by state law apply in federal bankruptcy.

Another way to make lifetime gifts less painful is a Qualified Personal Residence Trust (QPRT). A QPRT can be especially efficient for the middle class, because retained interests can equal 60-75% or more of the transferred property's value. The main downsides to a QPRT are that the grantor must survive the term of the trust and the grantor must pay rent if he wishes to use the house after the term of the QPRT expires. Blattmachr suggests that after the initial term, the QPRT property should remain in a grantor trust for the benefit of the grantor's spouse.

Blattmachr also suggested giving away tangible personal property as another way to reduce the pain of making lifetime gifts. Annual exclusion gifting can be very powerful for middle-class clients but not so powerful for the very wealthy because of the relative significance of the gift amount limitations. Blattmachr advocated the use of trusts with Crummey powers for lifetime gifts. Non-gift transfers, such as medical or educational payments made directly to the service providers, are another way for middle-class clients to effectively pass money to the next generation. Blattmachr suggested setting up a special bank account with the children as authorized signers that can be used by the children to pay medical and educational expenses as agents for the parents.

The second main topic of Blattmachr's presentation was fiduciary income taxes, paid by trusts and estates. Knowing fiduciary income tax rules can be critical to allowing a fiduciary to properly carry out his fiduciary duties. These rules can also help the client minimize state and local income taxes. Blattmachr also reported that IRS's estate and gift tax attorneys are increasingly being directed towards auditing fiduciary income tax returns, as the number of estate and gift tax returns filed has decreased, so a good knowledge of these rules may be increasingly important in the future.

Blattmachr defined two broad categories of trusts for income tax purposes: "ordinary" trusts and "grantor" trusts. Grantor trusts are effectively treated as if they are invisible for income tax purposes, with the grantor of the trust being considered to receive the trust's income. Grantor trust status can be important, as it can allow a significant amount of planning to take place. The two most important revenue rulings for estate planners, according to Blattmachr, concern grantor trusts. He first cited Revenue Ruling 85-13, which indicates that a grantor trust is disregarded for income tax purposes, including purposes of engaging in sale or loan transactions with the grantor. Next he cited Revenue Ruling 2004-64, which provides that paying income tax on a grantor trust is not a gift by the grantor to the trust.

Ordinary trusts are separate entities from their grantor and their beneficiaries for income tax purposes, although the application of the Distributable Net Income (DNI) rules can cause a significant portion of the trust's income to end up effectively taxed to the beneficiaries. Ordinary trusts are either simple or complex. "A 'simple trust' is a trust for which all income is to be distributed currently and no other amounts (e.g., capital gains) are actually distributed." (Tax and Accounting Center BNA.) Complex trusts do not have that requirement. All estates are treated as complex trusts.

Blattmachr began a discussion of the DNI rules by joking that "DNI is just slightly more complicated than DNA." DNI relates to a special rule which allows a trust or estate to make distributions to a

Blattmachr Continued on Page 4

Estate Planning and Probate Section Upcoming Events

Section Breakfast • March 12, 2008 • 7:30 am

"Planning for the Care of our Furry Friends: Pet Trusts and Other Alternatives"

Speaker: Shelley E. Nixon, Esq., Morris, Manning & Martin, LLP

Pro Bono March Madness: Wills and Advance Directives Project • March 5, 2008

8:30 am - 11:45 am, Registration starts at 8:00 am

3 CLE hours, including 1 Professionalism

** See our ad on page 7*

Morgan Continued from Page 1

homestead and other issues unfamiliar to us.

Robert first reviewed the unique characteristics and benefits that relate to homestead real property, including creditor protection and restrictions on transfer. In general, a homestead is the real property owned by a Florida resident which is used as his/her primary residence. However, note that the definition of a "homestead" can vary for different purposes, depending on which provision in the Florida constitution or statutes applies to the particular issue.

One area in particular that may be unfamiliar to Georgia practitioners is the restrictions on the transfer of a homestead. In general, these restrictions on transfer apply even when the homestead property is owned through a revocable trust.

In the event of the death of the owner of the homestead, under the Florida constitution, the homestead cannot be devised if the owner is survived by a spouse or a minor child, except the homestead may be devised to the owner's spouse if there is no minor child. (The Florida statutes define a "devise" to include a disposition by trust.) However, if the homestead was owned by the decedent and his/her surviving spouse as tenants by the entirety, such homestead will not be subject to the constitutional or statutory restrictions on devise, but shall vest in the surviving spouse by operation of law. The determination of whether real property is a homestead for purposes of devise and inheritance is generally determined when an interested party files a petition in the court having jurisdiction over the probate proceeding to determine the homestead status of the property.

In addition to the restrictions on transfer at death, a married individual cannot alienate the homestead by mortgage, sale, gift or other conveyance without the joinder of his/her spouse.

Homestead property in Florida also provides certain exemptions from the assessed value for the purposes of determining ad valorem taxes. There is a general exemption for the first $25,000 of homestead value.

Robert then reviewed the near legendary creditor protection that Florida law provides for a homestead. In general, Florida law exempts all of the homestead from forced sale under process of any court, except for payment of taxes and assessments and contractual obligations relating to the purchase, improvement or repair of the property. Robert then went over several cases which dealt with the apparent conflict between the generous Florida homestead protection versus the limits imposed by the federal Bankruptcy Act of 2005. Robert then reviewed the current state of the law with respect to homestead property transferred to a revocable trust. Although several recent cases in both U.S. Bankruptcy Court as well as the Florida Court of Appeals have extended homestead protection to real estate owned through a revocable trust, Robert was still not totally confident that a residence in a revocable trust will always qualify for homestead protection. He urged continued caution.

Robert then fielded several questions from the attendees. He mentioned that under a special clause, if real estate qualifies as a primary residence, then title can pass pursuant to a summary probate proceeding, thereby avoiding expense and delay.

Robert also said that if real estate is not homestead property, and was transferred to a limited liability company, then it would probably avoid probate in Florida. He did mention that documentary stamp tax may be imposed on the transfer to the LLC.

We appreciate Robert traveling to Atlanta to share his knowledge and experience in this very relevant area of law.

Wills of the Rich and Famous

Beverly B. Bates, Bates & Baum

On October 10, 2007, Section attendees at the monthly breakfast relaxed with an entertaining program, the presentation of Jeremiah W. Doyle IV, Esq., Senior Vice President, Bank of New York Mellon, Private Wealth Management, Boston, MA. Doyle introduced us to his coterie of the rich and famous:

John F. Kennedy
Jacqueline Kennedy Onassis
Linda Louise McCartney
Jerome John Garcia
Anna Nicole Smith
James Marshall Hendrix

Though the listeners were still glassy eyed from the names of the decedents, Doyle proceeded to chart the beneficiaries of those decedents by Power Point as a Who's Who in the Will. Bequests to each offered us a personal insight which may have escaped public notice. For instance, Jackie Onassis bequeathed to Alexander D. Forger, attorney and friend, a copy of JFK's inaugural address signed by Robert Frost.

Doyle's subtitle (and now we were "back in the saddle" of estate and probate) was "What We Can Learn from Their Estate Planning". Jackie Onassis set up several Charitable Lead Annuity Trusts. Doyle noted with respect to one, the result was that 98% of the value of the CLAT qualified for the estate tax charitable deduction. For another, a potential GST Problem: If $1 million GST exemption was assigned to the CLAT in May 1994, the adjusted GST exemption in 2018 would be $6,065,272. [Citing IRC Section 2642(e) and Reg. 26.2642-3].

Doyle closed by emphasizing the consideration of inheritance and guardianship for after-born children, the importance of determining domicile, inclusion of an "ultimate disaster" clause in estate planning documents, and the drafting of documents by a competent attorney.

A lasting impression was Doyle's offhand reference to visiting courthouses that have custody of the Wills of the famous. Let's trust that some of these Wills remain extant as long as those of Shakespeare and other famous figures in Great Britain now available on electronic sites.

Pictured are guest speaker **Jeremiah W. Doyle IV**, *Senior Vice President, Bank of New York Mellon*, and Section Chair **Julie Childs**, *McLain & Merritt, PC*

Blattmachr Continued from Page 2

beneficiary and take an income tax deduction for those distributions. DNI is generally based on the trust's income for the tax year, with certain adjustments ("six special rules," as Blattmachr called them). Certain types of distributions carry out DNI to the beneficiary of the distribution, while other types of distributions do not. Also, certain items which could be generally viewed as income are not always counted when determining DNI. DNI limits how much a beneficiary can be taxed on trust distributions. If it is not DNI, it is not deducted by the trust and it is not taxable to the beneficiary. DNI also preserves the character of income as it passes from trust to beneficiary.

Trust taxation and the calculation of DNI depend largely on state fiduciary and accounting income rules, which differ for each state. The provisions of the Will or trust can also affect the calculation of DNI and the determination of whether a given item is "income" or something which is considered corpus. However, IRC Section 643 and the regulations thereunder provide that provisions of state law or the will or trust can be ignored for federal income tax purposes if they differ too much from traditional fiduciary accounting definitions and rules.

Nontaxable distributions of corpus from an ordinary trust or estate do not carry out taxable income. Nontaxable distributions of corpus include amounts distributed in satisfaction of a specific bequest of an item of property or a specific amount. In addition, distributions which are made in excess of the trust's DNI are considered nontaxable distributions of corpus.

Blattmachr advised that IRC Section 642(c), not Section 170, controls when charitable contributions are made by trusts and estates. There are two main requirements: 1. The contribution must be made out of gross income (that is, no conservation easement deduction, no tangible personal property contribution, etc…) 2. Gross income must have been paid "pursuant to the terms of the governing instrument."

Following the presentation, the attendees took advantage of the networking opportunities available, while they enjoyed a sumptuous cocktail reception. Olen Earl, member of the Board of Directors for our Estate Planning & Probate Section and also Director of Planned Giving of The Community Foundation for Greater Atlanta, particularly enjoyed the evening, as he won an iPhone which Diversified Trust gave away as an added enticement for seminar attendees to enjoy the post-seminar festivities. While the reception began promptly at 4:45 p.m., it continued until 7:30 p.m., certainly suggesting that a good time was had by all.

The now annual event began in 2005 when Ben Pruett, former Atlanta Bar Estate Planning & Probate Section Chair, currently with Bessemer Trust, suggested to his board that their section join forces with their peer section at the Georgia Society of CPAs to present an upscale event which would combine high quality continuing education with a relaxed atmosphere for networking following the event. Lou Mezzullo was engaged to speak at the first such event, followed by Bob Keebler, then Natalie Choate who drew a crowd of over 180 in 2006.

While the venue may change in 2008, the format will likely be the same: a half-day CLE featuring a nationally known speaker presenting to over a hundred attorneys and CPAs whose practices include estate planning. To submit suggestions for speakers or topics, please contact the Section Chair, Julie Childs, or other board members.

Thanks to Loraine M. DiSalvo of Morgan & DiSalvo, P.C., who provided notes for the political and substantive portions of the article. A portion of this article was earlier printed in The Atlanta Lawyer. – JHS

Case Notes

Francis M. Bird, Jr.

Land v. Burkhalter, ___ Ga. ___, ___ SE2d ___ (decided 1/28/2008) S07A1878 FCDR 2/4/2008 p. 2B

Practice Note: This case is another example of why it is not a good idea to let clients handle the signing of their wills without an attorney present.

A caveat was sustained (on motion for summary judgment) in the trial court on the ground that the requisite two witnesses did not sign the will in the presence of the testatrix. The Supreme Court added a wrinkle, holding that since the will was not self-proving, the signature of a notary who admittedly signed in the presence of the testatrix counted toward the legal requirement of two signatures. There was conflicting evidence whether either of the other two witnesses signed in the presence of the testatrix, resulting in reversal of the grant of summary judgment.

Biggers v. Crook, ___ Ga.___, ___ SE2d ___ (decided 1/28/2008) S07A1786 FCDR 2/4/2008 p.1B

Practice Note: Be careful in dealing with how much leeway a client has in rearranging his or her interest in jointly held assets without the participation of the other joint tenant. Watch for the reaction of the real estate, creditor and bankruptcy bars to this case.

This is a case of first impression in Georgia. Joint Tenants A (brother) and B (sister) inherited property as joint tenants with right of survivorship from their parent. Joint Tenant A executed a deed to secure debt in the jointly held property to Creditor C, his wife's sister. Joint Tenant A died. Joint Tenant B sued for a declaratory judgment that the deed to secure debt did not sever the joint tenancy, was extinguished by A's death and was void, and that Creditor C had no interest in the property. Joint Tenant B wins in the trial court and on appeal to a full bench. Despite the fact that a Georgia deed to secure debt grants legal title to the creditor, the Supreme Court, following a California decision involving a deed of trust, observed that a deed to secure debt is for security, likened the effect to the "highest order" of lien, and refused to find any interest in the property in the creditor. The Court noted that whether or not a prenuptial agreement between the deceased joint tenant and his wife was valid had no bearing on the outcome.

Estate of Christiansen, 130 T.C. No.1; No. 15190-05 (decided 1/24/2008)

Bird Continued on Page 5

Bird Continued from Page 4

Practice Note: As the use of marital deduction or credit shelter trust formulae based on the "Applicable Exclusion Amount" becomes less favored in wills, and as the use of disclaimers becomes more favored, it will pay to review the basics (as well as some nuances, such as appear in this case) of what constitutes a "qualified disclaimer" within the meaning of Section 2518 and applicable regulations.

In the **Christiansen** case, the Tax Court agreed with the government on most of its case. The decedent had left an estate worth $9,578,896 to her daughter outright, with a provision that to the extent the daughter disclaimed, the property disclaimed would be divided in specified percentages between a private foundation and a charitable lead trust. According to the formula, the amount going to the foundation worked out to $807,224, and the amount going to the charitable lead trust was $2,421,672. The trust was to last for a term of 20 years; if the daughter outlived the 20 year term, the property then in the trust would go to the daughter. If she failed to outlive the trust, the remainder would fail and all the property would go to the foundation.

In a 10-2 decision, the Tax Court upheld the government's full disallowance of the amount of the charitable deduction claimed for the amount going to the trust, but upheld the deduction of the full amount going to the foundation.

The daughter had not disclaimed her contingent remainder interest in the property going to the trust, which resulted in a "partial disclaimer". This could be resolved in the estate's favor if the disclaimer was a "qualified" disclaimer. The government contended, and the Tax Court agreed, that the daughter's disclaimer was not a "qualified" disclaimer within the meaning of Section 2518. This turned on whether the remainder interest was either (a) severable property, or (b) an undivided portion of the property. The majority held, and the dissent disagreed, that the remainder was neither severable property nor an undivided portion of the property.

Incidentally, the disclaimer itself did contain a provision purporting to be a savings clause to the effect that if the disclaimer was deficient in any way, then the daughter really did do whatever was necessary to meet the requirements for a qualified disclaimer. This did not help the taxpayer.

Tuttle v. Ryan, ___ Ga.___, ___ SE2d ___ (decided 11/05/2007). S07A835 FCDR Nov. 16, 2007 p 3375

The Supreme Court, applying the "any evidence" standard of proof, upheld the Probate Court's order admitting a will to probate based on the testimony of the attorney who prepared the will, an associate of the attorney who witnessed the execution, and the legal secretary who notarized the signatures at the execution.

In re Estate of Ehlers, ___ Ga.App.___, ___ SE2d ___ (decided 12/14/2007) A07A1632 FCDR Dec. 28, 2007 p. 3850

Practice Note: How long can a year's support case last?

Albert T. Ehlers died in 1993. His widow, Dora W. Ehlers, filed a year's support petition in 1994. Several family deaths, several courts, and several legal actions later, the year's support petition was almost finally resolved by an order of the Fulton County Probate Court on February 6, 2007. However, there was a default of timely answer to an amendment (to the petition), and the Probate Court declined to open the default. On appeal, the Court of Appeals held that the Civil Practice Act provision for opening a default as a matter of right within 15 days of default applied, and reversed the Probate Court.

Davis v. Walker, ___ Ga.App.___, ___ SE2d ___ (decided Nov. 21, 2007) A07A0908 FCDR Dec. 28, 2007 p. 3866

Practice Note: Watch for potential legal consequences where a testamentary trustee (who has an interest in the trust) holds land and a residence, but no financial resources in the trust for taking care of the property. The trustee in this case did not report to other beneficiaries (at least to the extent that they filed a complaint alleging his lack of communication), used his own funds to preserve the property, and did not attempt to rent or sell the property.

The Court of Appeals affirmed the trial court on these rulings:

The trustee was removed for conflict of interest and waste of trust assets. He had held a non-income producing home and land in trust. Instead of selling or renting the property, for 11 years he had made personal loans to pay taxes, upkeep and the like. He had also failed to make periodic accountings to the beneficiaries. On the other hand, there was no evidence to sustain the beneficiaries' contention that a joint account with right of survivorship was not the property of the surviving joint tenant (the same person as the trustee). No legal fees were awarded to either side.

Dan Munster Provides Timely Update on Medicaid Rules

David L. Watson, Gomel & Davis, LLP

Daniel D. Munster, of Daniel D. Munster & Associates, provided the Section with another timely update on recent changes to the Medicaid rules. Dan spoke to a full room on September 12, 2007. Dan also furnished attendees with his usual excellent outline.

The full title of Dan's presentation was "What You Need to Know about Nursing Home Medicaid and Estate Recovery". Dan has spoken to our Section several times before, and is recognized in our area as a leading expert on Medicaid planning. This particular presentation was designed to give attendees a basic understanding of the various ways long-term care could be financed, with special emphasis on the Georgia Nursing Home Medicaid program.

Dan first noted the significant increase in the average annual cost per Medicaid recipient. Consequently, states such as Georgia have further restricted the criteria for eligibility in an effort to force individuals and their families to pay for care longer before entering the Medicaid system. Dan then described the four most common ways to pay for nursing home care: Medicare (which generally only covers a very short time period), long-term care insurance, private payment, and Medicaid. Because the first three options often are not sufficient to fully fund adequate care for an individual, Medicaid has become an essential component of many families' long-term care plans. Consequently, Dan devoted the remainder of the presentation to Medicaid planning.

In general, Medicaid planning is a means of preserving funds for the benefit of those who would otherwise be economically devastated by the exorbitant cost of private nursing home care. Proper Medicaid planning allows a resident continued access to many things not otherwise covered by nursing home Medicaid. It also can prove vital to the long-term financial picture of a community spouse.

To qualify for Medicaid, a recipient must pass two financial tests.

Munster Continued on Page 6

Munster Continued from Page 5

The first is an income limit. Currently under Georgia law, to the extent that a nursing home resident's includable income is $1,869 or less per month, the resident passes the income test. For those with income above that amount, it may still be possible to pass the income test using a Medicaid Qualifying Income Trust (a/k/a a "Miller Trust"). Such a trust serves as a shell entity with its single asset being a non-interest bearing checking account. Because Medicaid policy requires that the Miller Trust be established by the recipient or an agent under a power of attorney that expressly authorizes settling of a trust, Dan strongly advised that all financial powers of attorney drafted for candidates for nursing home placement include the authority to settle a Miller Trust. Dan then described how the Miller Trust checking account should be opened and the trust funded.

Dan then explained that even when the recipient has income less than the income limit or has successfully utilized a Miller Trust, he or she must still pay a fair share of the bill of the nursing home. This is known as "patient liability" or "cost share".

The second financial test governing nursing home Medicaid eligibility is the resource test, which looks at the assets the resident owns on an ongoing basis. Medicaid policy divides all assets into two categories: exempt property and non-exempt property. Although in the past applicants have sometimes made gifts of their property to their family members prior to applying for Medicaid assistance, Dan noted that since February 8, 2006, the "look back" period has been extended from three years to five years. Dan then went over specific types of assets for purposes of qualification, especially the home place.

After covering several of the other technical rules related to planning for resource eligibility, Dan's final topic related to new estate recovery rules implemented by Georgia in February 2007. In general, estate recovery is the process whereby a state may seek reimbursement from the estate of a deceased person who was receiving Medicaid assistance. This recovery is usually sought against the probate assets of the decedent. The applicable Georgia law authorizes the Georgia Department of Community Health to make claim against the "estate" of the Medicaid recipient, without use of the narrower term "probate estate". The final regulations promulgated by the DCH stated that for purposes of these rules, the "estate" includes all real and personal property under the probate code as well as real property passing by reason of joint tenancy, survivorship, trust, etc. Dan seemed to think that DCH exceeded the scope of its authority in attempting to recover from such real estate that was not included in the decedent's probate estate. The DCH has even taken a position that life insurance and tax-qualified retirement accounts, which pass directly to a beneficiary outside of probate, are also subject to recovery. Again, Dan thought that this approach went beyond the authority granted to the DCH by its enabling statute.

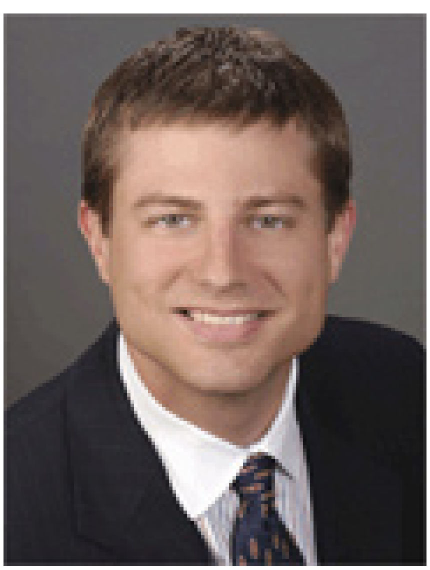
Obviously, the applicable rules are much more complex and

Munster Continued on Page 7

Edward M. Manigault Speaks to Our Section on GRATs

Loraine M. DiSalvo, Morgan & DiSalvo, PC

On August 8, 2007, our fellow Section member Edward M. Manigault, who is also an ACTEC fellow, the Chair of the Tax Section of the State Bar of Georgia, and a partner at Jones Day, spoke on "GRATs - Unresolved Issues, Potential Pitfalls and Random Observations." Mr. Manigault's presentation provided our breakfast meeting attendees with a detailed and fascinating look at a number of issues which should be considered when dealing with GRATs. He began with the observation that there have actually been some Department of Justice investigations into GRAT gifts, indicating that creating and funding these trusts is not as simple as some may think. In fact, Mr. Manigault warned, drafting and administering a GRAT requires very careful attention to detail.



Pictured **Edward M. Manigault**, *Jones Day*

One aspect of GRAT drafting that Mr. Manigault mentioned was how to determine and define the annuity payments to be made to the grantor. He recommended always using an annuity amount which is based on a fixed fraction or percentage of the initial fair market value of the contributed assets, rather than a fixed dollar amount, since the fraction or percentage approach helps protect the grantor against the effects of an IRS revaluation of the contributed assets by automatically causing a corresponding increase in the annuity payments. Mr. Manigault also suggested that the fixed fraction or percentage might best be determined using a mathematical formula (which he derived in his own practice and kindly shared in the materials) to arrive at a fraction which is then stated in the GRAT instrument, rather than using an express percentage or a defined-value type formula.

Two other aspects of GRAT drafting which Mr. Manigault explored in some detail were (1) whether it is possible to have a GRAT which produces a gift value of zero (a "zeroed-out GRAT"), and (2) the minimum length for a GRAT term. He stated that his personal conclusion has been that both a zeroed-out GRAT and a GRAT with a term as short as two years are permissible under the current rules, and indicated that he tends to prefer very short GRAT terms in his practice. However, he also stated that he prefers not to fully zero out GRATs in his practice, even though he believes it permissible to do so, since having some taxable gift amount means that a gift tax return is required. If the gift tax return showing the taxable gift is properly prepared , you should be able to trigger the running of the three

Manigault Continued on Page 7

Manigault Continued from Page 6

year statute of limitations. In his materials, Mr. Manigault also pointed out that the adequate disclosure standard under Treas. Reg. Section 301.6501(c)-1(f) does not apply to GRATs. Instead, the GRAT must be "adequately shown" under Treas. Reg. Section 301.6501(c)-1(e) if the statute of limitations is to run, and the requirements have some differences.

In discussing how to determine whether to use graduated payments or level payments during the GRAT term, Mr. Manigault points out that, in most situations, a graduated payment will produce a better result than a level payment. In general, he said, as long as the GRAT's performance in its second year beats the Section 7520 rate which applies to the GRAT, the graduated payment GRAT will always beat the level term GRAT, all else being equal. Only when the GRAT fails to beat the Section 7520 rate and the payments to the grantor are always deferred for the longest possible period do level payments normally produce a better result than graduated payments in a GRAT, but in that case, "better" is more properly understood as producing a less negative result.

Mr. Manigault also provided a number of warnings regarding the choice of assets used to fund a GRAT, and reminded us that we must be aware of all transfer restrictions which apply to the property and ensure that all such restrictions are complied with and can be complied with in a timely manner to allow proper GRAT administration. He pointed out that hedge funds are generally not good assets for GRAT funding, since they tend to carry a lot of fees and restrictions on transfers, in addition to being very difficult to value and requiring appraisals to be obtained for each transfer. With regard to more typical marketable securities, he mentioned that, while the method for valuing such securities is fixed for purposes of determining the annuity amount, the method for valuing such securities is not so fixed for purposes of valuing securities that are being distributed in kind as part of an annuity payment to the grantor, which complicates the process of determining what to distribute. He also recommended that stocks be held in street name, rather than in certificate form, since the many steps required to effectively transfer stocks held in certificate form can end up delaying the actual transfer date and causing problems. Finally, he warned us to be aware of the potential for insider trading issues where the grantor is an insider with regard to a publicly traded company whose stock will be used to fund the GRAT, and to be careful of potential patent violation issues when considering funding a GRAT with stock options.

We are grateful to Mr. Manigault for his excellent presentation.

Munster Continued from Page 6

technical than described in this summary. Many estate planning attorneys, such as this author, will refer those clients seeking Medicaid assistance to an expert such as Dan. Dan can be reached at (404) 920-0521 or danmunster@georgiaelderlaw.net. We again thank Dan for his time and hard work in putting together this timely presentation.

Atlanta Bar Association
400 International Tower
229 Peachtree Street NE
Atlanta, GA 30303-1601

Return Service Requested