

NEW YORK COUNTY
NYCLA
 LAWYERS' ASSOCIATION

ESTATE PLANNING FOR BUILDING OWNERS

Prepared in connection with a Continuing Legal Education course presented at New York County Lawyers' Association, 14 Vesey Street, NY, NY scheduled for October 6, 2010

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NYCLA'S ESTATES AND TRUSTS SECTION
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Estate Planning for Building Owners

Wednesday, October 6, 2010

9:00 AM ~ 12:00 PM

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Estate Planning for Building Owners
Wednesday, October 6, 2010
9:00 AM – 12:30 PM

AGENDA

- | | |
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| 9:00 AM - 9:05 AM | Welcome and Announcements
<i>Bari Chase, Director, NYCLA CLE Institute</i> |
| 9:05 AM - 9:20 AM | Overview / Fiduciary Responsibilities
<i>Susan Lipp, Editor in Chief, Trusts & Estates Magazine</i>
<i>Robin A. Bernstein, Deputy Counsel, RSA</i>
<i>Sylvia Di Pietro, Chair NYCLA Estates and Trusts Section</i> |
| 9:20 AM-10:10 AM | Forms of Building Ownership: Protecting Your Asset Today
<i>Matthew S. Brett, Esq.</i>
<i>Belkin Burden Wenig & Goldman, LLP</i> |
| 10:10 AM-11:00 AM | Estate Planning Options: Protecting Your Asset in the Future
<i>Jeremiah W. Doyle IV, Senior Vice President,</i>
<i>BNY Mellon Wealth Management</i> |
| 11:00 AM – 11:10 AM | BREAK |
| 11:10 AM-11:35 AM | Succession Plan for Family-Owned Real Estate Business
<i>Jeremiah W. Doyle IV, Senior Vice President</i>
<i>BNY Mellon Wealth Management</i> |
| 11:35 AM -12:05 PM | Estate Planning Devices
<i>Douglas Moore, Managing Director, U.S. Trust Family Office Group</i> |
| 12:05 PM – 12:30 PM | Questions & Answers |



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Presented by Sylvia Di Pietro, Chair NYCLA Estates and Trusts Section

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LEXSEE 60 AD3RD 892

[*1] Estate of Saul Schneider, appellant, v Victor M. Finmann, et al., respondents,
et al., defendant. (Index No. 10847/07)

2008-05738

SUPREME COURT OF NEW YORK, APPELLATE DIVISION, SECOND DE-
PARTMENT

2009 NY Slip Op 2319; 60 A.D.3d 892; 876 N.Y.S.2d 121; 2009 N.Y. App. Div. LEXIS
2346

March 24, 2009, Decided

NOTICE:

THE LEXIS PAGINATION OF THIS DOCUMENT IS SUBJECT TO CHANGE PENDING RELEASE OF THE FINAL PUBLISHED VERSION. THIS OPINION IS UNCORRECTED AND SUBJECT TO REVISION BEFORE PUBLICATION IN THE OFFICIAL REPORTS.

SUBSEQUENT HISTORY: Leave to appeal granted by *Estate of Schneider v. Finmann*, 12 N.Y.3d 715, 912 N.E.2d 1072, 2009 N.Y. LEXIS 2587, 884 N.Y.S.2d 691 (2009)

Reversed by, Motion denied by *Estate of Saul Schneider v. Finmann*, 2010 N.Y. LEXIS 1169 (N.Y., June 17, 2010)

COUNSEL: Nicholas J. Damadeo, P.C., Huntington, N.Y., for appellant.

Cullen and Dykman, LLP, Garden City, N.Y. (Justin F. Capuano and Peter J. Mastaglio of counsel), for respondents.

JUDGES: PETER B. SKELOS, J.P., STEVEN W. FISHER, FRED T. SANTUCCI, RUTH C. BALKIN, JJ. SKELOS, J.P., FISHER, SANTUCCI and BALKIN, JJ., concur.

OPINION

[**892] [***122] DECISION & ORDER

In an action to recover damages for legal malpractice, the plaintiff, Estate of Saul Schneider, appeals from an order of the Supreme Court, Nassau County

(Woodard, J.), entered May 14, [**893] 2008, which granted that branch of the motion of the defendants Victor M. Finmann and Victor M. Finmann, P.C., which was to dismiss the complaint insofar as asserted against them for failure to state a cause of action pursuant to CPLR 3211(a)(7).

ORDERED that the order is affirmed, with costs.

In 2005 the decedent, Saul Schneider, transferred ownership of a life insurance policy on his own life from a limited liability partnership that he controlled to himself. He allegedly was acting on the advice of the defendant Victor M. Finmann, through Finmann's professional corporation, the defendant Victor M. Finmann, P.C. (hereinafter collectively Finmann). Schneider died in October 2006. The transfer of ownership of the policy allegedly resulted in an increased estate tax liability. Schneider's estate commenced this action against, inter alia, Finmann seeking damages for legal malpractice. The Supreme Court granted that branch of Finmann's motion which was to dismiss the complaint pursuant to CPLR 3211(a)(7) for failure to state a cause of action. We affirm.

"The well-established rule in New York with respect to attorney malpractice is that absent fraud, collusion, malicious acts or other special circumstances, an attorney is not liable to third [*2] parties, not in privity, for harm caused by professional negligence" (*Estate of Spivey v Pulley*, 138 AD2d 563, 564, 526 N.Y.S.2d 145). Inasmuch as the estate was not in privity with Finmann, and there is no allegation that one of the exceptions to the privity requirement is applicable here, the estate may not maintain an action for legal malpractice against Finmann

2009 NY Slip Op 2319, *; 60 A.D.3d 892, **;
876 N.Y.S.2d 121, ***; 2009 N.Y. App. Div. LEXIS 2346

in its own right (see *Deeb v Johnson*, 170 AD2d 865, 566 N.Y.S.2d 688; cf. *Estate of Nevelson v Carro, Spanbock, Kaster & Cuiffo*, 259 AD2d 282, 285, 686 N.Y.S.2d 404). Moreover, Schneider himself did not have a claim during his lifetime against Finmann for legal malpractice, since the only alleged [***123] damage suffered from the malpractice was the increase in estate tax liability, which could not have been incurred while Schneider was alive. Consequently, the estate may not maintain this action

under EPTL 11-3.2(b) (see EPTL 11-3.2[b]; *Deeb v Johnson*, 170 AD2d at 866; *Rutter v Jones, Blechman, Woltz & Kelly, P.C.*, 264 Va 310, 314, 568 S.E.2d 693; cf. *Nembach v Giaimo & Vreeburg*, 209 AD2d 222, 222-223, 618 N.Y.S.2d 307).

SKELOS, J.P., FISHER, SANTUCCI and BALKIN, JJ., concur.

[*1] Estate of Saul Schneider, Appellant, v Victor M. Finmann, et al., Respondents, et al., Defendant.

No. 104

COURT OF APPEALS OF NEW YORK

2010 NY Slip Op 5281; 2010 N.Y. LEXIS 1169

June 17, 2010, Decided

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PRIOR HISTORY: Estate of Schneider v. Finmann, 60 A.D.3d 892, 876 N.Y.S.2d 121, 2009 N.Y. App. Div. LEXIS 2346 (N.Y. App. Div. 2d Dep't, 2009)

DISPOSITION: [**1] Order reversed, with costs, and defendants' motion to dismiss the complaint denied.

CASE SUMMARY

PROCEDURAL POSTURE: Plaintiff decedent's estate appealed from an order of the Appellate Division (New York) holding that, in the absence of privity, the estate could not maintain an action for legal malpractice against defendant estate planning attorneys and affirming a decision by a lower court that granted defendants' motion to dismiss the complaint for failure to state a cause of action.

OVERVIEW: Defendants represented the decedent from April 2000 to his death in October 2006. In April 2000, the decedent purchased a \$ 1 million life insurance policy. Over several years, the decedent transferred ownership of the policy several times. At his death, the proceeds of the policy were included as part of his gross taxable estate. The estate commenced a malpractice action in 2007, alleging that defendants negligently advised the decedent to transfer, or failed to advise the decedent not to transfer, the policy which resulted in an increased estate tax liability. Privity, or a relationship sufficiently approaching privity, existed between the estate and defendants. The estate essentially stood in the shoes of the decedent and, therefore, had the capacity to maintain the malpractice claim on the estate's behalf. The estate was entitled to raise an estate planning malpractice claim against defendants because they caused harm to the estate. Moreover, that type of claim comported with EPTL 11-3.2(b), which generally permitted a personal representative of a decedent to maintain an action for "injury to person or property" after

2009 NY Slip Op 2319, *, 60 A.D.3d 892, **;
876 N.Y.S.2d 121, ***; 2009 N.Y. App. Div. LEXIS 2346

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**[*1] Estate of Saul Schneider, appellant, v Victor M. Finmann, et al, respondents,
et al, defendant. (Index No. 10847/07)**

2008-05738

**SUPREME COURT OF NEW YORK, APPELLATE DIVISION, SECOND DE-
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JUDGES: PETER B. SKELOS, J.P., STEVEN W. FISHER, FRED T. SANTUCCI, RUTH C. BALKIN, JJ. SKELOS, J.P., FISHER, SANTUCCI and BALKIN, JJ., concur.

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ORDERED that the order is affirmed, with costs.

In 2005 the decedent, Saul Schneider, transferred ownership of a life insurance policy on his own life from a limited liability partnership that he controlled to himself. He allegedly was acting on the advice of the defendant Victor M. Finmann, through Finmann's professional corporation, the defendant Victor M. Finmann, P.C. (hereinafter collectively Finmann). Schneider died in October 2006. The transfer of ownership of the policy allegedly resulted in an increased estate tax liability. Schneider's estate commenced this action against, inter alia, Finmann seeking damages for legal malpractice. The Supreme Court granted that branch of Finmann's motion which was to dismiss the complaint pursuant to CPLR 3211(a)(7) for failure to state a cause of action. We affirm.

"The well-established rule in New York with respect to attorney malpractice is that absent fraud, collusion, malicious acts or other special circumstances, an attorney is not liable to third [*2] parties, not in privity, for harm caused by professional negligence" (*Estate of Spivey v Pulley*, 138 AD2d 563, 564, 526 N.Y.S.2d 145). Inasmuch as the estate was not in privity with Finmann, and there is no allegation that one of the exceptions to the privity requirement is applicable here, the estate may not maintain an action for legal malpractice against Finmann in its own right (*see Deeb v Johnson*, 170 AD2d 865, 566 N.Y.S.2d 688; *cf. Estate of Nevelson v Carro, Spanbock, Kaster & Cuiffo*, 259 AD2d 282, 285, 686 N.Y.S.2d 404). Moreover, Schneider himself did not have a claim during his lifetime against Finmann for legal malpractice, since the only alleged [***123] damage suffered from the malpractice was the increase in estate tax liability, which could not have been incurred while Schneider was alive. Consequently, the estate may not maintain this action under EPTL 11-3.2(b) (*see EPTL 11-3.2[b]*; *Deeb v Johnson*, 170 AD2d at 866; *Rutter v Jones, Blechman, Woltz & Kelly, P.C.*, 264 Va 310, 314, 568 S.E.2d 693; *cf. Nembach v Giaimo & Vreeburg*, 209 AD2d 222, 222-223, 618 N.Y.S.2d 307).

SKELOS, J.P., FISHER, SANTUCCI and BALKIN,
JJ., concur.

Tax Law Update*

By David A. Handler, partner in the Chicago office of Kirkland & Ellis LLP, and Alison E. Lothes, associate in the Boston office of Sullivan & Worcester LLP

• **Strict privity requirement relaxed in New York: Personal representative of estate may sue estate-planning attorney for negligence**—In *Estate of Schneider v. Finmann*, 2010 NY Slip Op. 05281 (June 17, 2010), the Court of Appeals of New York relaxed its doctrine of strict privity, which holds that neither an estate nor its beneficiaries may maintain an action for malpractice against an attorney who advised a decedent regarding his estate plan.

In 2000, Saul Schneider purchased a \$1 million life insurance policy on his life. Over several years, he transferred the policy to entities of which he was the principal owner. In 2005, he transferred the policy back to himself, individually. When Saul died in 2006, the insurance policy proceeds were included in his taxable estate. The personal representative of Saul's estate sued Saul's estate-planning attorney for malpractice, alleging that the attorney hadn't properly advised Saul of the estate-tax ramifications of both transferring and owning the policy. Both lower courts granted the attorney's motion to dismiss, holding that sufficient privity didn't exist to allow the estate to maintain its action against the attorney. In New York, an attorney generally isn't liable to third parties who aren't in privity with an attorney for harm caused by professional negligence.

However, the Court of Appeals held that there was sufficient privity between the personal representative of an estate and the deceased person's estate-planning attorney to maintain a malpractice action. The court noted that most states no longer adhere to the doctrine of strict privity and commented on the unfairness of a doctrine that left an estate without recourse against a negligent estate-planning attorney. It didn't relax the privity requirement to the extent necessary to allow beneficiaries or other third-party individuals to sue for malpractice without evidence of fraud or collusion or other special circumstances. To do so, the court explained, would produce uncertainty and limitless liability.

*This article appeared in the August 2010 issue of *Trusts & Estates*.

Forms of Building Ownership, Protecting Your Asset Today

▪ Article

By Matthew S. Brett, Esq., Belkin Burden Wenig & Goldman, LLP

Forms of Building Ownership:
Protecting Your Asset Today

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**Forms of Building Ownership:
Protecting Your Asset Today**

Matthew S. Brett, Esq.
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Introduction

The right to own and hold title to real property is one of the most enduring and fundamental arrangements of humankind.

In fact, the laws and concepts surrounding "ownership" have in part emerged from an ongoing struggle between governments (that aim to tax) and individuals (who desire to own property with the least amount of government interference as possible).

However, as we sit here today contemplating the appropriate type of ownership for our own personal needs, we are less concerned about the history of property law and how we got here and more concerned about our current rights and liabilities.

What follows is a brief introduction to the types of ownership that exist for New York City residential property owners. In particular, we will examine the various forms of ownership that are available to residential building owners and the relative advantages or disadvantages of each form.

Specifically, we will examine Sole-Proprietorship, Partnership, corporate ownership (both C-Corps and S-Corps) and Limited Liability Companies in a broad attempt to understand why one would choose to take title to a property in a particular manner as opposed to another available form.

Obviously, the mere fact that there exist several forms of ownership demonstrates that there is simply no "one size fits all" arrangement for property ownership. Thus, there is no such thing as a perfect form of ownership.

Accordingly, the most important thing to take away from this discussion is also its disclaimer: every transaction should be thoroughly examined with an eye to not only the legal consequences of the creation of a particular form of ownership but also the financial implications.

However, before we get into the specifics of each form of ownership, we need to take a look at a few basic underlying principals of property law.

What is Property?

In the most basic legal sense, the term "**property**" is an aggregate of rights which are guaranteed and protected by the government.ⁱ Property has been defined as anything that may be the subject of "**ownership**".ⁱⁱ In essence, it is a thing that person may have "**title**" to.

Title is essentially ownership. When title changes, ownership passes to another. Ownership to a certain extent is an exclusive right of possession or a legal or just claim to title, or proprietorship.ⁱⁱⁱ

How is property owned?

As mentioned previously, "**property**" is anything that can be owned. The *degree* to which property is owned, the *quantity* of ownership or *interest* in ownership is often referred to the "**estate**" in property.^{iv} There are several types of estates of ownership, but the most common estate in property for the purposes of our discussion of building ownership is the "**fee simple**" estate.

The fee simple estate in its most basic sense is outright ownership. There is no greater ownership of property than fee simple ownership.

There are several other types of estates, such as "**life estates**" and "**term for years**", that go well beyond the scope of our discussion.

When title is passed to more than one "**individual**", the law must deal with their respective rights. As a result, there is a considerable body of law that deals with "**co-tenancies**".

In terms of co-tenancies, there are essentially three relevant arrangements: the "tenancy in common", the "joint tenancy" and the "tenancy by the entirety".

At the outset, for the purpose of our discussion, except in the case of a joint tenancy or tenancy by the entirety (which is exclusive to human beings) the term "**individual**" will not be limited to a natural person, but also may include business entities such as LLCs.

A "**tenancy in common**" is the most basic of all three co-tenancies. It is in essence the default arrangement for ownership by more than one individual and if it is not declared when title passes, title shall pass to the individuals as tenants in common.

In a tenancy in common, each owner is regarded as owning separate and distinct shares of the same property. Each tenant in common has an equal right to enjoy all or any portion of the property as if he or she is the sole owner". There is a presumption that shares to a property held by tenants in common are equal.

However, that presumption is rebuttable by proof of ownership in differing amounts.^{vi}

Tenants in common have no right of survivorship. This means that that if one tenant in common dies, that tenant's

interest in the property will be part of his or her personal estate.

Finally, in the absence of any restriction agreed to between all the tenants in common, any tenant in common may sell, alienate or otherwise deal with his or her own interest in the property.

A "**joint tenancy**" is similar to that of the tenancy in common. However, unlike the tenancy in common, in a joint tenancy there is a right of survivorship. This means that upon the death of one joint tenant, that tenant's interest does not pass to his or her estate, but rather to the joint tenant.

As in a tenancy in common, in the absence of any restriction agreed to between all the joint tenants, each of the joint tenants may sell, alienate or otherwise deal with their own interest in the property.

A joint tenancy is not a default co-tenancy like a tenancy in common. Thus, there must be clear and convincing evidence of an intention to create a joint tenancy.^{vii}

Additionally, unlike a tenancy in common, a business entity (aside from certain religious institutions) may not be a joint tenant.^{viii}

Finally, it is critical to note that where two or more individuals acquire title to a property at different times or by different conveyances, a joint tenancy is not created.^{ix}

A "**tenancy by the entirety**" is created when property is conveyed to a husband and wife. The tenancy by the entirety is similar to a joint tenancy in that there is a right of survivorship.

It differs from the joint tenancy in that neither spouse may devise or alienate the property while the other spouse is living without the assent of the other spouse.

Forms of Property Ownership

Thus far we have examined what property is and how it is owned by certain "individuals". It is time now to take a deeper look at these "individuals" and what form they may come in. We will now examine the various types of *forms* of property ownership and the relative advantages and disadvantages of each form.

The Sole-Proprietorship

The Sole-Proprietorship is the most basic forms of property ownership in New York City. While most sophisticated business owners may dismiss outright the notion of owning a property as a natural personal (without the perceived shield of corporate ownership and the threat of personal liability) there are some surprising advantages.

First the advantages:

- In its most basic sense there are no substantive start-up costs to a sole proprietorship (aside from the cost of the property to be acquired).
- Single taxation: all taxes are paid by the individual (maybe be a disadvantage)
- There are no substantive formation costs or procedures. No applications to fill out (unless you are operating under an assumed name). It is just you!
- There are very few administrative costs procedures.
- The sole proprietor has complete control over the management and operation of the property unless delegated to another.

- Easy to operate.
- Ability to recover rent stabilized units for "personal use".

This last advantage is perhaps less so an advantage and more so a legal requirement. However, it is a critically important consideration when acquiring a residential property with rent regulated units.

Specifically, pursuant to Rent Stabilization Code ("RSC") § 2524.4, an *individual* owner may refuse to renew a Rent Stabilized tenancy if the *individual* owner seeks *in good faith* to recover that unit for his or her own personal use and occupancy as his or her primary residence in the City of New York and/or for the use of a member of his or hers immediate family as their primary residence in the City of New York.^x These provisions do not apply to cooperative and condominium ownership.^{xi}

A non-individual business entity such as a corporation, partnership or LLC may not avail themselves of this provision of law. Thus, before an owner can even refuse to renew a rent regulated lease upon these grounds, title to the property must be in a person's individual capacity.

However, (and this is where its gets a little confusing) where there are multiple owners as in the case of tenants in common, joint tenants or tenants by the entirety, only one of the individual owners may recover possession of one or more dwelling units for personal use.^{xii} Lest it be unclear, there is a distinction between property owned as *co-tenants* (personal use recovery permitted) and property owned by a business entity, including a partnership (personal use recovery prohibited).

Accordingly, inasmuch as personal use proceedings are complicated, it is imperative to speak with a qualified attorney

about such a proceeding if you are purchasing or currently own a property and desire to recover a unit for personal use.

Now, the disadvantages of Sole-Proprietorship:

- Unlimited personal liability.
- Interest in ownership is not easily transferable. To transfer the interest stocks cannot be assigned to another. The entire property must be conveyed.
- Capital must be provided for by the sole proprietor.
- Ownership lasts only as long as the person lives or until the person retires.
- An Assumed Name Certificate must be filed with the clerk of the county in which the property is located (and the business is operated) is the business is being operated under a name other than the proprietor's name.

Obviously, the most critical disadvantage is the prospect of bearing full personal liability. This factor alone leads many to opt for another form of ownership.

Partnership

For the purposes of our discussion there are essentially two types of partnerships: the "**General Partnership**" and the "**Limited Partnership**".

A partnership is an association of two or more persons to carry on as co-owners of a business for profit.^{xiii} Unlike a corporation, a partnership is not a legal entity distinct from the individuals who own it.

In a General Partnership all partners are exposed to liability. In a Limited Partnership, only the general partner is exposed to liability.

In general the overall advantages of a General Partnership are:

- General Partnerships are relatively easy to establish. There are limited start-up costs (aside from the cost of the property to be acquired).
- There are no substantive formation costs or procedures. No applications to fill out (unless you are operating under an assumed name). **However, it is wise to spend the time preparing a General Partnership Agreement to set out t**
- Single taxation: all taxes are paid by the individual partners (may be a disadvantage). The profits from the business flow directly through to the partners' personal tax returns.
- With more than one owner, the ability to raise funds may be increased.

In general, the disadvantages of a General Partnership are:

- Liability. Partners are jointly and individually liable for the actions of the other partners.
- Decision making and management is often conducted amongst the partners which can lead to irreconcilable issues.
- The partnership may be limited in duration and could terminate upon death or withdrawal of a partner.

With respect to Limited Partnership, the advantages are the same as a General Partnership with the added bonus that the limited partners of the Limited Partnership have limited personal liability for business debts as long as they don't participate in management (as opposed to the general partner,

who will manage the Limited Partnership and bear full personal liability).

The C-Corp

The polar opposite of Sole-Proprietorship is the "C-Corporation". The C-Corp is a type of corporate entity formed pursuant to both state and federal laws and is often limited to situations where there are a multitude of investors and a large amount of capital. In other words the C-Corp may not be appropriate for the smaller NYC Property owner.

The advantages:

- Limited liability protection. Owners are not typically responsible for business debts and liabilities.
- C-Corps can have an unlimited number of shareholders.
- Ownership is easily transferable through the sale of stock.
- A C-Corp will theoretically exist in perpetuity. The C-Corp does not cease to exist upon the death of an owner.
- Capital can be raised by selling stock.
- A perception of reliability.

Now, the disadvantages:

- Formation is more complicated than sole-proprietorship. A certificate of incorporation must be drafted and filed with the State.
- The set up is costly.
- Administration is costly and difficult. Annual meetings must be held. Elections for the board of directors

and officer must be held. Records must be kept as to operation.

- **Double taxation:** this means that the corporate profits are taxed a corporate rate and shareholders dividends are taxed separately at the individual level.

Thus, for the purposes of the small property owner, a C-Corp is probably not the best option.

The S-Corp

Much like the C-Corp, the "**S-Corporation**" is a corporate entity that is formed pursuant to both state and federal laws that makes a valid election to be taxed under Subchapter S of Chapter 1 of the Internal Revenue Code. Among various other state and federal requirements, in order to qualify as an S-Corp, the corporation must have less than 100 shareholders.^{xiv}

The advantages of the S-Corp:

- Limited liability protection. Owners are not typically responsible for business debts and liabilities.
- **Single taxation:** In general, S- Corps do not pay any federal income taxes. Instead, the corporation's income or losses are divided among and passed through to its shareholders. The shareholders must then report the income or loss on their own individual income tax returns.
- Ownership is transferable through the sale of stock (with certain restrictions promulgated by the IRS).
- A S-Corp will theoretically exist in perpetuity. The S-Corp does not cease to exist upon the death of an owner.
- Capital can be raised by selling stock.

Now, the disadvantages:

- Limited amount of shareholders.
- Shareholders must be natural persons (aside from certain estates and trusts).
- An S-Corp cannot own 80 percent or more of the stock of another corporation
- Formation is more complicated than sole-proprietorship. A certificate of incorporation must be drafted and filed with the State.
- The set up is costly.
- Administration is costly and difficult. Annual meetings must be held. Elections for the board of directors and officer must be held. Records must be kept as to operation.

The LLC

Perhaps the newest kid on the block is the "**Limited Liability Company**". The LLC is in effect a legal hybrid of the Partnership and the S-Corp, taking the best attributes of both forms.

The advantages of the LLC:

- Limited liability protection: Owners (referred to as "Members") are not typically responsible for business debts and liabilities.
- Flexible in the structure of management. Members can devise their own management structures in an Operating Agreement.
- Members need not be natural persons:
- Few administrative requirements. Much less formal than corporations.

- Single taxation: Unlike C-Corps (and like S-Corps) there is no tax at the entity level (unless corporate taxation is elected by members). Taxes are passed through to members.
- Interests can be transferred (but only pursuant to the terms of the Operating Agreement and/or Article of Organization).
- Easy to Operate.
- Can be owned by single individual Member.
- Can exist forever but only pursuant to the terms of the Operating Agreement and/or Article of Organization to avoid corporate taxation.
- Has the option of taxation like a corporation if Members find that beneficial.

The disadvantages of the LLC are:

- More expensive and complicated to set up than Sole-Proprietorships or Partnerships.
- Articles of Organization must be drafted and filed with the State.
- Publication of organization must occur and a Certificate of Publication must be filed with the State.
- Unlike an S-Corp, reorganization may not be tax free and merger and reorganization benefits are much less beneficial than the provisions for Corporations.
- The entity is relatively new and there is a less developed body of law governing it.

Conclusion

As indicated earlier, there is no one size fits all approach to selecting the appropriate form of ownership for New York City residential property owners. Thus, it is crucial to examine each transaction and consider the issues of costs, personal liability, taxation and the ability to convey the property to another at the appropriate time with an attorney, a financial advisor and/or an estate planner.

Notes:

ⁱ 87 NEW YORK JURISPRUDENCE 2D, *Property* § 1, citing *Fulton Light Heat & Power Co. v. State*, 65 Misc. 263, 121 N.Y.S, 536 (Ct. Cl. 1909).

ⁱⁱ 87 NEW YORK JURISPRUDENCE 2D, *Property* § 1, citing *In re Delaney*, 256 N.Y. 315, 176 N.E. 407 (1931).

ⁱⁱⁱ 7 NEW YORK JURISPRUDENCE 2D, *Property* § 9.

^{iv} AM. JUR. 2D, *Estates* § 1.

^v 24 NEW YORK JURISPRUDENCE 2D, *Cotenancy and Partition* § 3.

^{vi} 24 NEW YORK JURISPRUDENCE 2D, *Cotenancy and Partition* § 7.

^{vii} *Matter of Estate of Bonanni*, 250 A.D.2d.1022, 673 N.Y.S.2d 269 (3rd Dep't 1998).

^{viii} 24 NEW YORK JURISPRUDENCE 2D, *Cotenancy and Partition* § 18.

^{ix} 24 NEW YORK JURISPRUDENCE 2D, *Cotenancy and Partition* § 17

^x RSC § 2424.4(a)(1)

^{xi} *Id.*

^{xii} RSC § 2424.4(a)(3)

^{xiii} New York Partnership Law § 1

^{xiv} 26 U.S.C. § 1361(b)(1)(A)

Estate Planning Options: Protecting Your Asset in the Future

▪ **PowerPoint Handout: Real Estate—Choice of Entity**

By Jeremiah W. Doyle IV, Senior Vice President, BNY Mellon Wealth Management

Real Estate: Choice of Entity

Jeremiah W. Doyle IV
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October, 2010

BNY Mellon Wealth Management

The Choices

- Sole Proprietorship
- General Partnership
- Limited Partnership
- C Corporation
- S Corporation
- Limited Liability Company

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Issues When Selecting Entity

- Operation of the business
- Cost
- Simplicity
- Holding assets
- Accessing capital
- Liability protection
- Tax advantages
- Ease of transfer

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Sole Proprietorship

- Advantages
 - Simple and inexpensive to form
 - No separate tax filing
 - No state filings
 - Income and losses pass through to owner
 - Use Schedule C

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Sole Proprietorship

- Disadvantages
 - Unlimited personal liability
 - Limited access to capital
 - Self-employment tax – 15.3%
 - Business ceases to exist on death of owner

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General Partnership

- Advantages
 - Easy and relatively inexpensive to form
 - One level of taxation
 - Losses pass thru to partners
 - Simple administration

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General Partnership

- Disadvantages
 - Requires two or more partners
 - Unlimited personal liability
 - Liability for partner's actions
 - Limited access to capital
 - Can't attract outside investors
 - Won't want to become general partners due to unlimited liability
 - Tax return required (Form 1065)

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Limited Partnership

- Advantages
 - Two types of partners: general and limited
 - Limited personal liability for limited partners
 - Facilitates outside investors
 - Investors can become limited partners
 - Pass through tax treatment

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Limited Partnership

- Disadvantages
 - Unlimited personal liability for general partners
 - Creature of statute
 - Certificate of limited partnership must be filed with secretary of state
 - Limited partners may not participate in management
 - Tax return required (Form 1065)
 - State filings

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C Corporation

- Advantages
 - Limited liability
 - Access to capital
 - Best entity to attract venture capital
 - VC funds generally invest only in C corporations (esp. those formed in Delaware and generally avoid pass-through entities such as S corporations or limited liability companies)
 - Flexible capital structure
 - Can have different classes of stock, may issue preferred stock, bonds, convertible notes and subordinated debt
 - Centralized management
 - Easy to transfer interest
 - May be established in favorable jurisdiction e.g. Delaware

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C Corporation

- Disadvantages
 - Double taxation
 - More difficult to administer
 - Onerous formalities and recordkeeping
 - Costly set up and maintenance
 - Separate tax return (Form 1120)
 - State filings

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S Corporation

- Advantages
 - One level of tax
 - Limited liability
 - Easy to convert to C corporation
 - Pass through tax treatment
 - Losses pass through to shareholders (limited to "basis")

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S Corporation

- Disadvantages
 - Must file election with IRS
 - Complicated tax rules
 - Inflexible capital structure
 - Only one class of stock allowed
 - Limited number of shareholders (100)
 - Must be U.S citizens or residents, estate, or certain trusts
 - Distributions subject to ordering rule for tax purposes
 - Flow through of losses limited to "basis"
 - Limited access to capital
 - Tax return required (Form 1120S)
 - State filings required

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Limited Liability Company

- Advantages
 - Single level of taxation
 - Cash and property distributions generally tax-free (to extent of basis)
 - Pass-through tax treatment
 - Limited liability
 - Exception in some states: single member LLC
 - Flexible capital structure
 - No limit on number or eligibility of owners
 - "Series" LLC allowed in some states e.g. Delaware
 - Flexibility in administration
 - Controls distribution of cash, allocation of income and losses
 - Broader ownership allowed

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Limited Liability Company

- Disadvantages
 - New type of entity – case law limited
 - Poses tax and administrative complexities
 - Generally taxed as partnership
 - Operating agreement requires extensive tax provisions
 - Costly tax compliance
 - Unattractive to outside investors
 - VC and other investors shy away
 - Converting LLC to C corporation is difficult and expensive
 - State filing requirements

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Which One to Use?

Issues Affecting Choice of Entity

Tax Issues	Non-tax issues
Sale of Business/liquidation	Limited liability protection
Tax rate exposure	Capital structure
Use of losses	Stockholder and buy-sell agreements
Compensation issues	Type of business/investment activity
Complexity	State law issue
State tax issues	Ease of transfer

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Which One to Use?

- Sole proprietorship or general partnership ideal if:
 - Small business with one or two owners
 - Little capital required
 - No outside capital required
 - No liability protection required
 - Limited assets at risk
 - No sale of business anticipated

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Which One to Use?

- Limited partnership ideal if:
 - Focus is on single or limited-term project e.g. real estate project
 - For labor-capital partnerships
 - General partners do the work and limited partners supply the capital e.g. private equity or hedge fund

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Which One to Use?

- C corporation ideal if:
 - Limited liability desired
 - Pass through of income not important
 - Growth of business anticipated
 - Broad ownership needed
 - Access to capital important
 - Future sale of business anticipated

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Which One to Use?

- S corporation ideal if:
 - Business will remain relatively small
 - Capital retained for growth
 - No significant investment in appreciable assets
 - Limited liability desired
 - No special ownership requirement
 - Single level of taxation

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Which One to Use?

- Limited Liability Company ideal if:
 - Limited liability desired
 - Pass-through tax treatment is desired
 - Flexibility with respect to distributions, allocations and/or management is desired
 - Ideal for real estate investors

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Conclusion - The Choices

- Sole Proprietorship
- General Partnership
- Limited Partnership
- C Corporation
- S Corporation
- Limited Liability Company

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Thank You!!

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Succession Plan for Family-Owned Real Estate Business

▪ PowerPoint Handout

By Jeremiah W. Doyle IV, Senior Vice President, BNY Mellon Wealth Management

Succession Planning: Real Estate

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Boston, MA
October, 2010

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Issues

- Preserve the business
 - 30% of businesses make it to 2nd generation, 10% to 3rd generation
- Continued support of business owner upon cessation of control
 - Consulting agreement
 - Retain control thru voting stock
- Liquidity needs
- Valuation – See revenue Ruling 59-60 which lists 8 factors
 - In case of sale or other disposition
 - In case of death for estate taxes

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Issues for Owner

- Determine successor
- Establish plan to transfer control of ownership
 - Appoint family member as successor
 - Hire outside manager
 - Sell the business
- Implement the plan

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Two Types of Planning

- Lifetime
 - Outright sale for cash
 - Installment sale
 - Tax-free merger
 - Transfer on discounted basis
 - Private annuity (not discussed)
 - Sell to ESOP (not discussed)
- Death
 - Buy-sell agreements
 - §2032A valuation
 - §303 redemption
 - §6166 deferral of estate tax
 - Preserving the S election

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Lifetime Planning

- Outright sale for cash
 - Buyer may not have sufficient cash
 - Opportunity for loan to buyer at low interest rate – rates* for October, 2010
 - Short-term (3 yr or less) .41%
 - Mid-term (>3 yr ≤ 9 yr) 1.73%
 - Long term (>9 yr) 3.32%
 - Triggers immediate income taxation on gain

* Based on annual compounding

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Lifetime Planning

- Installment sale
 - Down payment plus promissory note
 - Opportunity for loan to buyer at low interest rate – rates* for October, 2010
 - Short-term (3 yr or less) .41%
 - Mid-term (>3 yr ≤ 9 yr) 1.73%
 - Long term (>9 yr) 3.32%
 - Gain recognized on installment basis as payments made
 - If face amount of note is over \$5 million, interest on deferred tax is payable annually to IRS
 - Seller may forgive portions of installment note each year to the extent of the annual exclusion (\$13,000 for 2010)
 - Note may be a self-canceling installment note (SCIN)

* Based on annual compounding

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Lifetime Planning

- Tax-free merger
 - Stock for stock
 - Assets for stock

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Lifetime Planning

- Transfer on discounted basis
 - Gifts of minority interests
 - Value of transfer discounted for lack of marketability and lack of control
 - Gift fractional interest in underlying interest in real estate
 - Transfer business interest to GRAT
 - Payments must be made to grantor
 - Sell sufficient assets to meet payments
 - If business interest is flow-through entity (S corporation, p/ship/ LLC), the entity may distribute earnings to cover GRAT payment
 - Distribute assets in-kind
 - Sale to IDGT
 - Transfer business interest to FLP
 - Transfer LP interests at discount
 - Transfer LP interest to GRAT for double discount

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Death Planning

- Buy-sell agreement – applies both to death and lifetime planning
 - Triggering events: death, disability or retirement
 - Purposes
 - Continuation of the business
 - Liquidity for seller
 - May establish valuation
 - Two types
 - Entity agreement – entity buys business
 - Cross purchase agreement – other owners buy business
 - How to determine price
 - Predetermine price subject to periodic review
 - Appraisal or arbitration
 - Formula
 - Paying the purchase price
 - Life insurance
 - Long-term payout i.e. secured promissory note

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Death Planning

- Buy-sell agreement (continued)
 - Disadvantages
 - Owner's lifetime rights are restricted
 - Price may become unrealistic
 - Removes alternative of liquidating the business
 - Removes alternative of retaining business for family member

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Death Planning

- For valuation to be binding for Federal estate tax purposes:
- Elements:
 - Agreement must be bona fide business arrangement
 - Agreement must not be a device to pass property at less than FMV
 - Terms must be comparable to similar arrangements entered into by persons in an arms-length transaction
- If persons who are not members of transferor's family own more than 50% of the business, the tests are deemed to be satisfied
- Other requirements:
 - Agreement must restrict the owner's interest during lifetime
 - Owner's estate must be required to sell
 - The purchase price be determinable from the agreement

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Death Planning

- §303 redemption for stock
 - Stock must have value of more than 35% of adjusted gross estate
 - Stock of two corporation may be combined to reach 35% threshold if decedent owns more than 20% of stock of each corporation
 - Redemption proceeds cannot exceed Federal and state death taxes, funeral and administration expenses
 - Proceeds entitled to capital gain treatment

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Death Planning

- §2032A special use valuation
 - Real estate used in a closely held business may be valued at "actual" rather than "highest and best" use
 - Complicated requirements
 - Valuation reduction limited to \$1,000,000 for 2009
 - Tax savings subject to "recapture" of property if use ceases or property disposed of within 10 years of death

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Death Planning

- §6166 estate tax deferral
 - Estate tax attributable to interest in closely held business may be deferred and paid over as long as 14 years 9 months
 - Pay 5 annual installments of interest only
 - First principal payment due five years after due date of estate tax return with balance of tax plus accrued interest payable in 9 installments
 - Interest of 2% payable on first \$1 million in excess of estate tax exemption
 - Interest on balance of tax is 45% of the interest rate otherwise charged
 - Allows estate tax to be paid with business cash flow
 - Complicated qualification requirements
 - Business interest must be at least 35% of adjusted gross estate
 - Among other things, must be an active business
 - See Rev. Rul. 2006-34 to determine if real estate is an active business

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Death Planning

- Preserving the S corporation election
 - S corporation stock may only be held by certain individuals, estates and certain trusts
 - If S corporation stock transferred to ineligible shareholder, S corporation status is lost and the corporation becomes taxable as a C corporation i.e. potential double taxation
 - Biggest problem: make sure S corporation stock is transferred to an eligible S corporation shareholder
 - Provisions in will or revocable trust may ensure continued eligibility

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Conclusion

- Lifetime
 - Outright sale for cash
 - Installment sale
 - Tax-free merger
 - Transfer on discounted basis
 - Private annuity (not discussed)
 - Sell to ESOP (not discussed)
- Death
 - Buy-sell agreements
 - §2032A valuation
 - §303 redemption
 - §6166 deferral of estate tax
 - Preserving the S election

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Thank You!!

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Estate Planning Devices

- **PowerPoint Slides: Sale to Directed Grantor Trust**
- **Estate Planning & Taxation: The Right Time for Real Estate?**, *reprinted from Trusts & Estates Magazine*

Douglas Moore, Managing Director, U.S. Trust Family Office Group

Sale To Directed Grantor Trust

Douglas Moore, Managing Director
U.S. Trust Family Office

October, 2010



Bank of America Private Wealth Management

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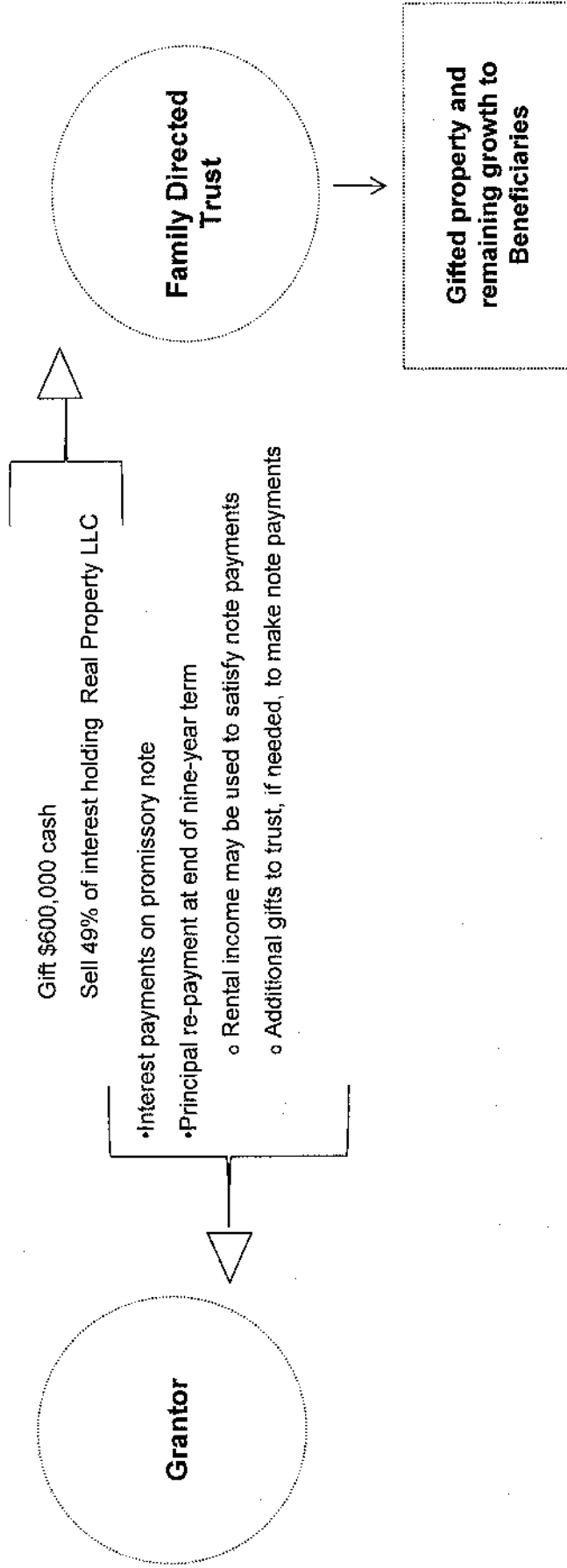
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Sale to Grantor Trust



Gift and Sale of Property to a Grantor Trust

Objective

- Transfer property by gift and/or sale at discounted values
- Exclude a significant portion of the transferred property's potential appreciation from the grantor's assets/estate

How does the plan work?

- Grantor creates a grantor trust
- Grantor gifts property to the trust
- Grantor sells property at a discounted value to the trust (no more than 10 times the value of the existing trust property)
- Grantor receives a promissory note from the trustee for the full purchase price (discounted value) as payment
- Note typically has interest only payments for 9 years with a balloon payment at the end of 9 years
- Interest rate is based on the IRS discount rate (e.g. mid-term applicable federal rate) published for the month in which the sale occurs
- No income tax event when the grantor sells the property or receives interest payments (on the note) because the trust is a grantor trust
- All trust income is taxable to the grantor, not to the trust or its beneficiaries

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Gift and Sale of Property to a Grantor Trust cont.

antages

Remove assets at discounted values

- Exclude significant amount of potential appreciation from grantor's assets/estate
- Can create a dynastic trust (multiple generations) by allocating generation-skipping transfer (GST) tax exemption to the trust
- Trust assets can avoid estate, gift and GST tax while held in trust for future generations
- Income taxable to grantor during his life so trust assets grow income tax-free and income distributions are not taxable to the beneficiaries
- Promissory note can contain a no prepayment penalty provision
- Trust can contain substitution of assets provision for flexible plan

advantages

- Gift tax on gifted property may be wasted if gift tax exemption increased
- Gift tax paid is wasted if trust property value decreases substantially
- Need updated appraisal value for property to be sold
- Possible IRS gift tax audit
- Possible reduction in income tax basis

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Gift and Sale Summary 2009

1. Estimated fair market value of property	\$42,165,118
Less: debt	<u>(22,513,825)</u>
Equity in property	<u>\$19,651,293</u>
Value of 49% of property to be sold	<u>9,629,134</u>
44% discount of property to be paid with a 9 year note	<u>5,400,000¹</u>
2. Cash Gift (10% of FMV of property to be sold to Trust)	<u>600,000</u>
3. Estimated federal gift tax	<u>270,000²</u>
4. Amount removed from estate assuming 6% annual return	<u>\$9,458,700</u>

For illustrative purposes only.

¹ The note has an IRS mid-term rate (e.g. 2.8% for 8/09). Interest paid annually and principal at end of 9 years.

² Assumes \$1 million lifetime gift tax exemption used. No federal gift tax if gift tax exemption is available.

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Delaware Administrative (Directed) Trusts

Key Characteristics

- An investment advisor directs a Delaware administrative trustee to enter into specific transactions, make investments, retain concentrated holdings and to enter into loan transactions.
- Delaware law allows trustees to take investment directions from investment advisors, without responsibility for their performance.
- Administrative trusts are a bifurcation of duties of the fiduciaries, not a delegation under the Uniform Prudent Investor Act.
- The investment advisor serves as a point of contact for the family, while a Delaware Trustee performs the administrative functions and exercises non-investment discretion.

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Trusts & Estates®

The Journal Of Wealth Management For Estate Planning Professionals

ESTATE PLANNING & TAXATION

The Right Time for Real Estate?

By Douglas Moore, national director, Estate and Charitable Planning,

Citigroup Trust and The Citigroup Private Bank, New York, N.Y.

Trusts and estates professionals representing high-net-worth clients have become more adept at maximizing planning techniques for specific asset classes as their awareness of the assets' economic factors and the effect of current markets on the assets has grown. For instance, professionals are paying significant attention to assets other than marketable securities despite the continually low "Section 7520 rate" during the past year and the devaluation of equities, with the expectation that they may reverse course in the not-too-distant future.

Consequently, high-net-worth clients are considering gifting and planning opportunities with asset classes that they have greater confidence will appreciate in value and be less likely to depreciate. This includes alternative investments, with their intended low correlation to the public market (for example, private equities and hedge funds). And recently, in many parts of the country, both commercial and residential real estate values have increased significantly. As a result, real estate or real estate-related investments may be viewed as sound. Here are some planning ideas and opportunities related to real estate holdings for the high-net-worth client.

Commercial real estate is attractive because it's conducive to discounting techniques.

COMMERCIAL REAL ESTATE

Estate planning with commercial real estate can be effective because of its potential to appreciate in value and produce significant income and its conduciveness to various discounting techniques for gift tax-planning purposes, especially under current conditions: a low-interest-rate environment and volatile markets. Typically, property owners transfer commercial real estate to a business entity that is well suited for asset protection, property management and transferability. The entities can be established as limited liability companies (LLCs), S corporations or family limited partnerships (FLPs). The general partner of the FLP should be either an LLC or S corporation to avoid personal liability for an individual acting as general partner.

Depending on state law, LLCs are becoming the entity of choice because they protect against personal liability for managing and non-managing members, and provide partnership income-tax treatment and flexibility within the partnership rules regarding allocation of profits and losses for

their members. For asset-protection purposes, the client should consider having a separate LLC for each piece of real property.

The flexibility of voting/nonvoting membership units is conducive to family planning and gifting issues. Not only can the transfer of the nonvoting membership units support lack of marketability and minority discounts for valuation-discount purposes, but the transfer of nonvoting interests also allows the senior family member (presumably the donor) to maintain control of the enterprise. Depending on the restrictions imposed by state law on transferability and liquidation of the entity, discounts on the value of nonvoting interests can be significant.

Another effective way of discounting the value of the nonmanaging units is to have the senior family member (or junior family member) enter into an arm's length agreement for management services rendered on behalf of the entity. This reduces the profitability of the entity and thereby supports a reduction in the value of the nonmanaging units. The arrangement may also offer flexibility to provide funds to the donor or other family member (provided the arrangement is not a disguised gift).

OPPORTUNITIES

Effective gifting (or selling) of nonvoting or nonmanaging interests lends itself to numerous planning opportunities, such as:

- a grantor retained annuity trust (GRAT);
- a grantor trust;
- a sale to a grantor trust;
- a grantor trust combined with life insurance.

GRATs have certain advantages as well as disadvantages when used in connection with entities that own commercial real estate. Gifting nonvoting membership units (with minority and lack of marketability discounts) into a GRAT (with an additional discount based on the retained annuity interest) may allow for significant discounts, especially in a low interest rate environment. Also, if a final determination for gift-tax purposes increases the value of the property transferred to the GRAT, the grantor's annuity payments are increased.³ Consequently, there would be no increase in the taxable gift. The grantor receives annuity payments, an economic consideration for some grantors. Because the trust is a grantor trust for income tax purposes, the grantor would be responsible for the tax on the income earned and gains realized from the trust (not for the amount of the annuity payments). The property should generate sufficient income to satisfy the annuity payments; if not, the grantor would receive partially discounted business units. This situation would

require updated valuations of trust property and reduce the benefit of discounting.

But there are some disadvantages to using a GRAT. If the grantor dies during the term of the GRAT, the assets, including post-gift appreciation, are included in his estate for estate-tax purposes (Internal Revenue Code sections 2036(a), 2039). The amount of used gift-tax credit would be restored. But this situation represents a lost opportunity, albeit one that's hard to quantify, that could have been avoided by choosing another strategy.

Another technique that may be suitable is gifting non-managing units into a dynastic or nondynastic grantor trust, for income tax purposes.⁴ Besides the nontax benefit (for example, spendthrift provisions and distribution control)

of gifting the property into a trust, the grantor would be responsible for the tax on the income earned and gains realized from the property. The trust's assets are undiminished by income taxes. This is particularly effective since commercial real estate business entities typically generate significant income.

Private equities invested in commercial real estate can provide such benefits as anticipated high appreciation, long-term holding periods resulting in favorable capital gains treatment, no secondary market that lends itself to lack of marketability discounts for gift-tax purposes and, as stated earlier, a low correlation to the public market. The trust can own the private equity either directly or indirectly through LLC units. The liquidation events typically cause realized gains paid by the grantor, not by the trust or its beneficiaries. This technique can be particularly effective because it uses a combination of benefits, such as discounts, spousal gift-splitting (Section 2513), imposition of income tax liability on the grantor and post-gift appreciation not included in the grantor's estate.

Another variation on the theme: a sale of additional non-managing units to the grantor trust. Because the grantor sold the assets to a grantor trust, the sale does not cause income taxation. Commentators typically suggest there be additional assets in the trust valued at a minimum of 10 percent of the value of the assets sold to the trust to avoid a retained-income interest in the grantor's estate under Section 2036(a). The grantor receives a promissory note with interest at the applicable federal rate (AFR) in effect under Section 1274(d).⁵ The AFR will avoid gift-tax implications on the note's interest-payment portion because this rate is considered fair market value. A grantor's sale of discounted high income-producing assets using a note with a low AFR can create significant estate- and gift-tax savings.

For instance, the April 2003 mid-term AFR was 2.96 per-

LLCs are becoming popular because they protect against liability and offer flexibility.

cent for annualized payments for a note (a term of more than three years through nine years). If the note's terms provide for a balloon principal payment at the end of nine years, the actual return on trust property (undiminished by income taxes because the grantor is liable for the taxes) will probably be greater. In addition, because the nonmanaging membership units are discounted, a greater amount of property is transferred to the trust, enhancing its return. For example, if the prediscouted value of the gifted property is \$1.5 million, and its value is discounted by 35 percent (for lack of marketability and minority interest), the property's value for gift-tax purposes is \$975,000.

However, it is the prediscouted property value of \$1.5 million, not the discounted value of \$975,000, that generates income for the trust. To the extent that the actual investment return on the property exceeds the 2.96 percent rate, the excess passing to the heirs is not subject to gift or estate tax. That difference and the amount discounted can be significant. If the grantor/holder of the note dies during the note's nine-year term, the estate may be entitled to a discount on the note's principal amount for estate-tax purposes.

There are certain benefits of this technique over a GRAT. If the grantor dies during the trust term, the trust property is not included in the grantor's estate. Also, the mid-term AFR is less than the Section 7520 rate (for example, in April 2003, compare the mid-term AFR of 2.96 percent to the Section 7520 rate of 3.6 percent). The grantor can also allocate generation-skipping transfer (GST) tax exemption on making a gift to the trust before the property appreciates in value. The grantor cannot allocate GST tax exemption at the time of the contribution to the GRAT.⁶

With the grantor-trust approach, the income from the business entity owned by the trust (in other words, the trust provisions provide for accumulation of income) can be used to purchase a life-insurance policy on

the life or lives of the grantor and/or the grantor's spouse. Because the trust is a grantor trust for income tax purposes, the accumulated income, not reduced by income tax liability, is available, for premium payments after the interest payments on the note are made. This scenario provides additional liquidity for the family to use to pay estate taxes for what may be a fairly illiquid estate.

CHARITABLE PLANNING

Opportunities exist for charitable planning. However, these opportunities are more limited and complex than with noncharitable planning, primarily because the business entity may be considered an active trade or business in a pass-through entity (for example, an LLC). For instance, if a charitable remainder trust (CRT) receives income from real estate or from an LLC with acquisition indebtedness, the income may be treated as unrelated business taxable income (UBTI).⁷ UBTI causes a CRT to lose its tax-exempt status for that tax year, nullifying the benefit of avoiding immediate capital gains tax on the sale of trust assets or possible deferral of trust income. There may be other situations where there is no UBTI because there is no acquisition indebtedness, or because an exception to the rule applies, which may provide greater opportunities to make contributions to the trust. If properly structured and timed, transferring this type of property into a CRT can provide significant savings or deferral on capital gains taxes if the trust property is eventually sold.

Charitable lead trusts (CLTs) are not tax-exempt entities, like CRTs, and are generally created as nongrantor trusts for income tax purposes. Consequently, the UBTI generated from trust property will not threaten tax-exempt status, but will reduce allowable income tax deductions for the trust. In all likelihood, this will cause the CLT to incur more taxable income than if the trust had not generated UBTI.⁸ Therefore, careful consideration must be given to

the overall income tax effect and to what extent it reduces the CLT property's total return. Also, there are private foundation rules,⁹ such as those governing self-dealing and excess-business holdings, that must be considered before transferring business entities of this type into either CRTs or CLTs.

However, charitable lead annuity trusts can be effective in a low interest rate environment, that is, when there is a low Section 7520 rate. The present value of the non-charitable remainder beneficiaries' interest is reduced for transfer-tax purposes. The actual investment performance, which exceeds the Section 7520 rate, passes free of estate or gift taxes.

LIQUIDITY

Commercial real estate business entities can create significant liquidity needs for the owner's estate in the form of estate taxes, debts and administration expenses. The three approaches that follow can help satisfy liquidity needs:

First, life insurance owned either in an irrevocable life insurance trust or used in conjunction with a buy-sell agreement can provide liquidity. Clauses concerning purchase price formula—which satisfy the requirements of Section 2703, if applicable—can be incorporated into the agreement to mandate a sale of the property on the owner's death, and establish a purchase price and value for estate-tax purposes as well as a payment schedule to the estate by the purchasing parties.

Second, if the value of the closely held business entity represents more than 35 percent of the deceased owner's adjusted gross estate, tax payment deferral may be allowed on an installment arrangement.¹⁰

Third, the business entity or third-party lender enters into a bona fide lending arrangement with the owner's estate. Fixed interest payments (no prepayment of interest is permitted)

are expenses necessarily and actually incurred for the purposes of using the loan proceeds to pay estate taxes. If the arrangement is properly structured, the aggregate amount of interest payments to be made by the estate to the lender may be treated as an administration expense and an allowable deduction for estate-tax purposes."

RESIDENTIAL REAL ESTATE

The primary planning technique with primary or secondary residences is the qualified personal residence trust (QPRT).¹ However, there are reasons very high-net-worth clients do not use this technique on a regular basis:

First, QPRTs are more effective when the Section 7520 rate is high. A low interest rate environment reduces the grantor's income interest and increases the value of the taxable gift of the remainder beneficiary's interest. Second, if the residence has a mortgage, the monthly mortgage payments attributable to principal are taxable gifts, and do not qualify for the annual exclusion gift because they are not present interests.²

Third, many of these residences have significant values. To adequately reduce the value of the gift for tax purposes, the trust term would typically be for an extended period. This increases the likelihood the grantor would not survive the trust term and the trust property would be included in the grantor's estate for estate-tax purposes. The grantor may make a gift of a partial undivided interest in the residence while retaining the balance of ownership in the house, but

this tends to be impractical. Also, there is a natural reluctance on the part of high-net-worth clients to relinquish ownership of substantial residences. Vacation residences may be placed in QPRTs, but for the very wealthy, this technique may reduce transfer taxes insignificantly.

CHANCE FOR CREATIVITY...

Many opportunities exist when planning for commercial real estate or for business entities with commercial real estate as an underlying asset. Planning with this asset class allows the client

Life insurance owned in an irrevocable life insurance trust can provide liquidity,

and tax practitioner to be creative and proactive in structuring techniques to complement the client's objectives while maximizing the particular attributes of the property.

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Endnotes

1. IRC Section 7520, Treas. Reg. Section 20.7520-1, et seq. The rate used for determining the present value of an annuity, an interest for life or a term of years, or a remainder or reversionary interest. This rate is adjusted each month.
2. IRC Section 2704(b)(2), Treas. Reg. Section 25.2704-2.
3. Treas. Reg. Section 25.2702-3(b)(2).
4. IRC Sections 671-679.
5. Also see IRC Section 7872.
6. Treas. Reg. Sections 2032-1(c)(1) & (2). The estate-tax inclusion period (ETIP) precludes allocation of GST tax exemption during the period in which the property will be in the grantor's or spouse of the grantor's estate.
7. IRC Section 512, IRC Section 681(a), Treas. Reg. Section 1.664-1(c), see exception to debt acquisition rule IRC sections 514(c)(2)(A) and 514(c)(2)(B). Practitioners should consider the bargain-sale rules under IRC Section 101(b).
8. IRC Section 642(c).
9. IRC Sections 4941-4945.
10. IRC Section 6166.
11. Estate of Graegin v. Commissioner of Internal Revenue, T.C. Memo 1988-477 (U.S. Tax Court, 1988).
12. IRC Section 2702, Treas. Reg. Section 25.2702-5.
13. IRC Section 2503(b)(1).

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Robin A. Bernstein is Deputy General Counsel to the Rent Stabilization Association of NYC, Inc., New York City's largest real estate trade association whose 25,000 members own or manage over 900,000 housing units. Prior to her current position Ms. Bernstein served as in-house General Counsel to a major New York City property owner, and was in private practice in the areas of landlord/tenant and real estate litigation and transactions.

Ms. Bernstein is responsible for revamping RSA's summary nonpayment proceeding workshop and seminar series to reflect the changes in the New York City Housing Court procedures in recent years. Ms. Bernstein has coordinated and co-authored materials for numerous RSA seminars including: *Understanding the New Rent Stabilization Code*, *Managing Rent Regulated Property in New York City*, *Navigating the Section 8 Maze*, and *Bed Bugs: a Property Owner's Liability Nightmare*.

Ms. Bernstein has lectured at Real Estate Industry Seminars, Continuing Real Estate Education Courses and HPD Small Property Owner Courses. She regularly contributes articles to the RSA's monthly newsletter, the RSA Reporter.

Ms. Bernstein is a member of the New York City Bar Association, The New York State Bar Association, the New York County Lawyers' Association and the Association of Corporate Counsel. She has served on the Housing Court, Housing Court Public Projects, and the Judiciary Committees of the New York Bar Association. She is a current member of the Civil Court Practice Section of the New York County Lawyers' Association.

Prior to the implementation of the Housing Court Resource Centers, Ms. Bernstein supervised RSA staff located in the court houses who assisted unrepresented small property owners. The written owners' materials now distributed in the Resource Centers were modeled on documents drafted by RSA. She is a certified member of the Volunteer Lawyers Program of the Housing Part of the Civil Court of the City of New York. She served on the New York City Hoarding Task Force, and is a member of the New York City DRIE Board.

Matthew S. Brett joined Belkin Burden Wenig & Goldman, LLP in 2000 and became a Partner in 2007. He specializes in real estate litigation and has worked on notable cases including *Lenox Hill Hospital v. Spitz* and *HF Associates v. Sullivan*.

Mr. Brett earned his Juris Doctor from Brooklyn Law School where he was a Moot Court Honor Society Quarter Finalist in the National Environmental Law Moot Court Competition. He earned a Bachelor of Arts degree in Political Science and Human and Natural Ecology from Emory University. He is the Chairman of the New Jersey Emory University Alumni Association.

Mr. Brett is an Owner's Representative on the Advisory Council of the Housing Part of the New York City Civil Court. He was also a member of the Housing and Urban Development Committee of the New York City Bar Association. Mr. Brett was a member of the Housing Court Committee of the New York City Bar Association and has served as Co-Chair of Continuing Legal Education (CLE) courses hosted by the New York Bar Association including How to Successfully Navigate, Litigate & Resolve Mold Issues, Housing in Cyberspace and Future Perspectives on Affordable Housing and Economic Development in New York City.

Mr. Brett has lectured on the Internet and Evidence for the Rent Stabilization Association and Rent Regulation for the New York City Bar Association.

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Sylvia E. Di Pietro is a native New Yorker, admitted to practice law before the courts of the State of New York, the Eastern and Southern Districts of New York. Sylvia is a graduate of the Honors Program from Long Island University, receiving a BA and MA in English. As a graduate of Brooklyn Law School, she received distinction and high honors in Real Estate Law and Moot Court Trial Advocacy. Upon graduation, she was the recipient of the Distinguished Achievement Award in the Art and Science of Trial Advocacy from the International Academy of Trial Lawyers.

Sylvia is member of New York County Lawyers Association's Board of Directors, its Foundation, a member of the Communications, CLE and Membership Committees, and a NYCLA Delegate to the New York State Bar Association House of Delegates. She is the Chair to the Estates Trusts Section, and former Chair of the Real Property Section, and Co-Chair of the Committee on Coops and Condos. She is a frequent speaker at NYCLA Continuing: Legal Education classes, more recently covering the new NYS Power of Attorney, Detecting Forgery in Trusts and Estate and Will Contests, Ethics, Probate, Will Contests, Not for Profit Boards, Estate Planning for Non-Traditional Families, Bridging the Gap programs, and topics relating to Trust and the Fiduciary Duty. She is a member of NYCLA's Mentoring Program.

As a member of the New York State Bar Association, Sylvia is a Vice-Chair of the Continuing Legal Education Section for Trusts and Estates. She also participates as a member of the Elder Law Section and Committees on the Elderly and Disabled, Estate Litigation and Pre-Mortem Probate. She is also a member of the Commercial and Federal Litigation Section, and a former member of the Special Committee on Cyberspace Law. Her dedication to the legal profession includes membership in the Jewish Lawyers Guild as well as the Columbian Lawyers Association, First Department, which she represents as a Board Member to the Network of Bar Leaders. Her contribution to the Bar also encompasses membership at New York City Bar, where she sits as a member of the Council on Judicial Administration, Chair of the Subcommittee on Guardianship Law, and various other subcommittees. She is a former member of the State Courts of Superior Jurisdiction.

As a Vice President, Recording Secretary and former Board Member of the New York Women's Bar Association, Sylvia served as a Delegate to the Network of Bar Leaders and a Delegate to the Women's Bar Association of the State of New York. She created CLE programs and also participated as Chair and Co-Chair of numerous events. She is dedicated to the advancement of women in all professions.

Prior to entering law, Sylvia enjoyed a rich career as an official court reporter in the Supreme Courts of Queens and Kings County reporting major civil and criminal trials. Thereafter, she was the Managing Director of Forsythe International Limited located in New York, a premium incentive marketing company, specializing in promoting creative ideas to Fortune 500 Companies. As the owner of her own consulting company, her work concentrated in the research and marketing of intellectual properties, creating advertising and sales promotional campaigns and handling all aspects of public relations and media placement for a celebrity clientele.

As an accomplished public speaker, Sylvia has appeared on national radio shows on topic covering issues related to retirement and estate planning, relationship conflicts over money, the need for prenuptial agreements, the Boston Catholic Church, cyber adultery, father's rights and custody issues.

Pro bono activities include mentoring attorneys and law students and counseling individuals in matrimonial matters. She has also been a participant as a Pro Bono Employer/Mentor with CUNY's Associate Degree Program at New York City College of Technology, Legal Assistant Studies Department, where she mentored paralegal students prior to seeking employment. As Chair of the Estates Trusts Section at NYCLA, Sylvia also mentors law students who are interested in pursuing a career in probate and administration.

Biographies

WEALTH PLANNING PROFESSIONALS

Jeremiah W. Doyle, IV, Esq. Senior Vice President

Jere Doyle is an estate planning strategist for BNY Mellon Wealth Management and a senior vice president of BNY Mellon. He has been with the firm since 1981. Jere provides wealthy individuals and families throughout the country with integrated wealth management advice on how to hold, manage and transfer their wealth in a tax efficient manner.

Jere is admitted to practice law in the Commonwealth of Massachusetts and before the United States District Court, United States Court of Appeals (First Circuit) and the United States Tax Court. He formerly served as a member of the Massachusetts Joint Bar Committee on Judicial Appointments. He is the editor and co-author of Preparing Fiduciary Income Tax Returns, a contributing author of Preparing Estate Tax Returns, a contributing author of Understanding and Using Trusts and a contributing author of Drafting Irrevocable Trusts in Massachusetts, all published by Massachusetts Continuing Legal Education. Jere is also a reviewing editor of the 1041 Deskbook published by Practitioner's Publishing Company.

Jere received a L.L.M. in banking law from Boston University Law School, a L.L.M in taxation from Boston University Law School, a juris doctor from Hamline University Law School and a bachelor's degree from Providence College. He is a member of the American Bar Association, Massachusetts Bar Association, Boston Estate Planning Council and the Essex County Bar Association. He served as president of the Boston Estate Planning Council and a member of its Executive Committee and was a 20-year member of the Executive Committee of the Essex County Bar Association. He was named as the 2009 Estate Planner of the Year by the Boston Estate Planning Council. Jere has spoken at numerous professional education programs throughout the country on various topics, been quoted in numerous business publications and has appeared on CNBC, MSNBC and CNN.

Susan Lipp

Susan Lipp, attorney and 20 year veteran editor and contributor of several respected legal, real estate, and business publications, is Editor-in-Chief of Trusts & Estates Magazine. For 17 years, Lipp served in leadership positions at Brownstone Publishers, Inc. of Vendome Group, LLC. with editorial responsibility for such publications as Landlord Vs. Tenant, Apartment Law Insider, and over a dozen newsletters addressing the legal, regulatory, and policy issues of owning and managing housing and commercial real-estate. Following her tenure at Brownstone Publishers, Susan joined Community Housing Improvement Program (CHIP) as General Counsel where she implemented initiatives to educate members on the legal requirements involved in owning and managing apartment buildings in New York City. In addition to her most recent position at CHIP, Susan served as a freelance editor and writer for McKinsey and Company and Kaplan Test Prep, where she wrote and edited review materials for the New York and Florida Bar Exams. Susan began her career as an attorney at Rosenberg and Estis, a real estate law firm in New York City.


Susan holds a Bachelor of Arts in Sociology from Brandeis University, Massachusetts, and a Juris Doctor Law degree from Hofstra University School of Law, New York, where she graduated with distinction and served as Associate Editor of the Law Review. Lipp is a member of the New York State and New York City Bar Associations and served on the Housing Court Committee.

Douglas Moore

Douglas Moore has been a managing director and the senior planner in the U.S. Trust Family Office Group (specializing in estate and charitable planning) since 2008. He regularly meets with families and their advisors to design and implement estate, charitable and trust plans.

Doug has been a trusts and estates attorney for more than 30 years. Before joining U.S. Trust, he was the head of estate and charitable planning at The Citigroup Private Bank for five years and Citi Trust for over one year. He was Senior Counsel of the Estate and Trust Services Group at Smith Barney for over five years. Before joining Smith Barney in 1996, Doug practiced law in Manhattan for over 16 years as a trusts and estates attorney and was involved in all aspects of estate planning and estate and trust administration.

Doug has written numerous articles on estate and charitable planning, including articles on investments for trusts and private foundations, fiduciary responsibility, real estate and life insurance. His work has been published in *Trusts & Estates*, *Estate Planning*, *Taxation of Exempts*, *Practical Tax Strategies* and *BNA Tax Management*. Doug also serves as a co-chair person of the Estate Planning and Taxation Committee on the advisory editorial board of *Trusts & Estates* magazine. He has lectured before various professional groups on estate and charitable planning.

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