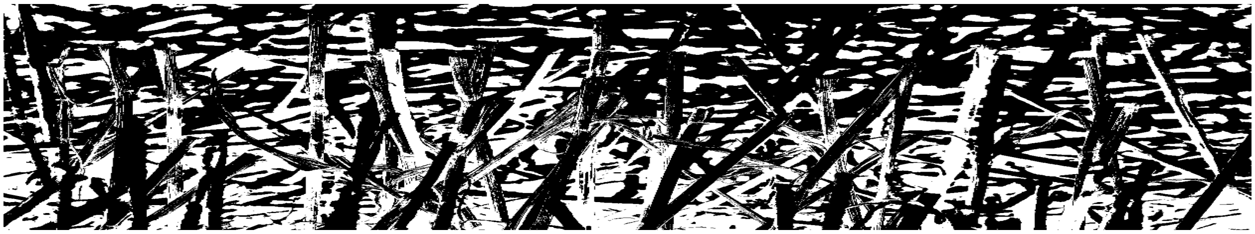

Jack Straw Fortnightly*

mixed signals

Some of you will have seen a brief item Jonathan Tidd posted to Sharpe's blog back in December, in which he suggested that the recently finalized substantiation regs[1] might require a taxpayer creating a charitable remainder trust to secure a "qualified appraisal" of the present value of the remainder interest, even where the trust is funded with cash and/or marketable securities.

When someone posted a link to this item on the discussion boards on the NACGP website, your correspondent rather carelessly responded, "I would have hoped careful planners were already doing this."

What your correspondent was thinking was, if you are claiming a deduction for more than $5k, obviously you need to submit a Form 8283, and this form should attach a statement, maybe from a "practitioner" who is subject to Circular 230, showing the calculation per reg. section 1.170A-6(b)(2), which says the remainder in a split interest trust is valued with reference to the tables, period, simple as that.

Well, it is not a simple as that.

Your correspondent was failing to grasp the point Jon was making, which has to do with what exactly constitutes a "qualified appraisal," and who exactly is a "qualified appraiser."[2]

but first these words

But before getting into the details, I just want to take a moment to say that Jonathan Tidd is a rock star. I have been reading him almost as long as I have been reading Conrad Teitell or Larry Katzenstein. Jon is thoughtful and meticulous, and he has an exceptionally solid grasp of this material, from which he is able to develop fresh and nuanced insights.

Not long ago, Jon moved to southern Arizona, not far from Tucson, which is where your correspondent is based these days, and after close to forty years of reading his commentary I finally had the pleasure of meeting him face to face when he gave a talk last year for the local roundtable on pledges -- enforceable or not, self-dealing issues in satisfying these by distribution from a private foundation, etc.

Rock star, enough said. Thanks, Jon, for all you do.

back to our regular programming

As Jonathan pointed out, what the regs are requiring you to "appraise," at reg. section 1.170A-17(a)(12), is not the property contributed to the trust -- which in the case of marketable securities would not even require an appraisal --, but the "partial interest" itself, *i.e.*, the remainder.

And the newly finalized regs say that only a "qualified appraiser," which the regs define as someone who either has a certification from a recognized professional organization of appraisers within what you might call a specialty, "valuing the type of property" in question, can sign off on a "qualified appraisal," which the regs say must be prepared in accordance with "generally accepted appraisal standards."

Not to mention that the figure the "qualified appraisal" is supposed to substantiate is "fair market value," which is defined by cross-reference to existing reg. section 1.170A-1(c)(2) as

> the price at which the property would change hands between a willing buyer and a willing seller, neither being under any compulsion to buy or sell and both having reasonable knowledge of relevant facts[,]

as though there were a secondary market in unitrust or annuity trust remainders.[3]

None of which on its face seems to make any sense in the context of valuing the remainder interest in a split interest trust funded with cash and/or marketable securities. We have a known value for the contributed property, we have the section 7520 discount rate, we have the life expectancy tables, and we have Publications 1457 and 1458.[4]

And now we are supposed to create a new appraisal specialty with curricula and certification, question mark. This cannot be right.

preambulatory problematics

There is a paragraph in the preamble to the final regs, TD 9836, that says, quote:

> Some commenters suggested that appraisers [sic, fn. 5] be allowed to use certain IRS valuation tables, such as those for charitable remainder trusts, other remainder interests in property, and life insurance policies, instead of a qualified appraisal. These tables may be used to value property in certain other contexts, but they do not necessarily provide a fair market value of the property contributed. Therefore, these tables are not acceptable substitutes for a qualified appraisal to substantiate deductions for charitable contributions under section 170.

What can it mean? When would the tables not "provide a fair market value of the property contributed"? Are they saying they want an appraisal of the price at which a remainder interest in trust would change hands between a willing buyer and willing seller, etc.? With maybe some footnoted commentary on what figures the tables actually yield? And who would be in a position to talk about a secondary market in charitable trust remainders?

What you want to believe is that the key phrase here is "value of the property contributed." If you are putting unmarketable assets into the trust you need an appraisal, but you can go ahead and use the tables for valuing the income and remainder interests.

But that is not what reg. section 1.170A-16(d) and (e) literally say. Those two paragraphs say you need an appraisal per reg. section 1.170A-17, which in turn at (a)(3) defines "fair market value" by cross reference to reg. section 1.170A-1(c)(2), and at (a)(12) requires that a partial interest be separately appraised. In other words, the "property" being contributed here is the remainder interest itself.

At first glance, this paragraph might seem to be a response to comments submitted by Larry Katzenstein, and possibly also to comments submitted by Conrad Teitell, in each case asking the Treasury to make clear that the table rates could be used to value the gift of an unexpired life interest in a remainder trust or a gift annuity, without the necessity of engaging an appraiser certified in a nonexistent specialty.[6]

That should have been a no-brainer, and if this paragraph is meant to expressly reject those comments, we might have a problem -- a somewhat different problem than that described by Jon Tidd, more of a "second tier" problem, you might say, but still a problem.

But maybe that is not what the Treasury is saying.

In fact the paragraph is completely incoherent. In what "certain other contexts" are the table rates appropriate? In what "contexts" is the Treasury saying they are not?

not to worry

But Jack is telling me not to worry. Existing reg. section 1.170A-6(b)(2) says the "fair market value" of the remainder in a split interest trust is determined with reference to the tables, period. None of this willing buyer, willing seller stuff.

And the regulatory project did not revise this section, or even mention it. So apparently the issue was simply not on the Treasury's radar. And why should it be. We have been doing it this way for fifty years.

But as Jon pointed out, there is a mismatch with the literal text of the regs, which does after all require a "qualified" appraisal of the remainder interest, as such. And it would be better if the Treasury would clarify.

In an e-mail message to your correspondent, Larry did say he has a call in to Catherine Hughes at the Office of Tax Policy, so maybe we will get some kind of more or less formal guidance.

bits and pieces

In the end, despite the hesitations expressed in our previous issue, the Greystocke Project did submit a comment on the proposed clawback regs. The comment period closed February 21, and at this writing only fourteen comments had been received.

Nothing yet from the ABA Tax Section or from ACTEC, though sometimes these folks arrive fashionably late. We were not entirely alone in arguing that the legislative text does not authorize the Treasury to forgo clawback.

Several commenters, including the AICPA, the AALU, and the Florida Bar Tax and RPPTL Sections, not only endorsed the proposed regs but asked the Treasury to go yet a step further, allowing a surviving spouse, post-2025, to take advantage of any unused portion of the temporarily increased exemption amount of a spouse who died during the eight-year window.

Jack is biting his tongue.

Interestingly, one of the developers of the NumberCruncher software submitted a rather lengthy comment not only asking that the proposed regs be withdrawn, but also arguing that, in effect, "you're doing it wrong" -- that the computational mechanism set out in the proposed regs would "eliminate any benefit for inflation adjustments" to the underlying $5 million exemption amount for gifts made in excess of that amount during the window, "at least until the inflation adjustments exceed the total of the gifts made that were sheltered" by the increased exemption amount.

Kaestner and *Fielding*

The Supreme Court did not reach *Fielding* in their conference on February 22, and we literally held up publication to see if they would reach it in their conference on March 1. They did not. And there will not be a conference this week. So we are looking at March 18 as the earliest we will see a grant or denial of cert in this case.

Meanwhile *Kaestner* has been set for argument on April 19, the petitioner has already filed its opening merits brief, and the amicus briefs are starting to pour in.

Fascinating stuff, which we will get to in a later issue, after all the briefs are in. For those who want to read ahead, Jack would recommend in particular

- a brief filed by ACTEC ostensibly taking no position on the merits, but laying out an argument why the state should lose on due process grounds, citing *Safe Deposit Trust Company v. Virginia*, 280 U.S. 83 (1929) -- which, Jack will argue, when we get around to it, was wrongly decided --, and

- a brief filed by three constitutional law professors, arguing that the state court decision in *Kaestner*, and by implication the decision in *Fielding*, should be vacated and the cases remanded for briefing and argument of the "dormant commerce clause" question -- which, these professors say, is the more appropriate framework for deciding the question whether a state may tax undistributed trust income where the beneficiary is a resident but the trustee is not.

If we were reading tea leaves, trying to decipher why cert has not yet been granted or denied in *Fielding*, Jack would predict that this is in fact what happens. No decision of either case on the merits, but instead a remand to develop the "dormant commerce clause" arguments.[8]

the Arizona case

The petition for review of the state appeals court decision in *Estate of Evitt*, which was the primary subject our previous issue, was denied this morning, and the respondent co-personal representative has been allowed yet more fees.

Game over, but with this ruling the Arizona supreme court has implicitly endorsed a state appeals court decision adopting a questionable precedent out of Florida. A claim that a decedent breached a contract to provide for the claimant at his death does not "arise before" his death.

To be clear, Jack is not saying the claimant here should have recovered the $150k. But the co-personal representatives should have been called upon to show that a claim that at least one of them almost certainly did know about had already been satisfied -- if it had.

self-promotion

Next Wednesday I will be doing a webinar for Lorman on planning for intergenerational transfer of a vacation home. Folks who sign up through the link provided will get half off the stated rate. Something like an hour and a half of continuing ed credit.

Also, we are continuing to try to build the Patreon subscriber base. For the moment we are not taking anything behind a paywall. The "subscriber" option is functioning as a sort of tip jar. When we eventually get to a place where we can restrict access to "premium" content, we will find a way to get the first five hundred subscribers in, as an expression of thanks.

In the meantime, what we are trying to do is broaden our reach -- in particular, to lawyers who work in estate and gift planning, probate and trust administration, and litigation in matters arising in those contexts.

If you know someone who might be interested in the stuff we talk about here at Jack Straw, please pass along a link or two. Thanks.

afterthoughts

[1]

TD 9836, published July 30, 2018, finalizes regulations proposed almost exactly ten years earlier, implementing very significant amendments enacted in 2004 and 2006 to the substantiation requirements under section 170(f)(11).

Specifically, as concerns our present discussion, those amendments require "qualified" appraisals to substantiate noncash gifts for which the claimed deduction exceeds $5k. There is an exception at paragraph (A)(ii) for marketable securities, but this does not directly address the valuation of a remainder interest in a trust, as such.

Only thirty-five comments were submitted. Most of these focused on what standards should be recognized as "generally accepted" and what "education and experience" should be treated as equivalent to "designation from a recognized professional appraiser organization." Turf wars, in other words.

Exactly two comments were directed even tangentially to the issues we are discussing here, one submitted by Conrad Teitell on behalf of the ACGA and what was then called the NCGP, and the other submitted by Larry Katzenstein. These are discussed more fully in the text.

[2]

More recently Jon has posted a more detailed discussion to the wealthmanagement.com site, which I have not yet read because it is behind a paywall.

[3]

Which, okay, there kinda is. But one potential buyer is a pretty limited "market." Certainly not a "hypothetical" buyer, and pricing is probably not all that transparent.

Also this particular buyer may be setting prices with reference to a portfolio of other purchases that enable it to diversify mortality risk.

[4]

We also have, spoiler alert, existing reg. section 1.170A-6(b)(2), which we will discuss in a moment.

[5]

If in fact this paragraph refers to the comments submitted by Conrad Teitell and Larry Katzenstein, as discussed below, we are already off on the wrong foot. These two were not asking what an "appraiser" would be required to do, they were asking whether an "appraisal" was necessary at all.

[6]

Obviously the Congress in 2004 wanted to tighten up the substantiation requirements for noncash gifts. A lot.

But the legislative history, which is pretty scant, would probably show that the concern here was with difficult to value property like interests in closely held businesses or raw land over which the taxpayer was conveying a conservation easement, etc. -- not with whether someone was correctly applying the tables to the valuation of income and remainder interests in a split interest trust funded with cash or marketable securities.

[7]

Larry was asking specifically whether it should really be necessary to obtain a "qualified appraisal" to substantiate the value of an income beneficiary's gift of her unexpired life or term interest in a remainder trust, where the trust is holding only cash and/or marketable securities.

Conrad made the point that, "as a practical matter" it may not be possible to find anyone who has "verifiable education and experience" in valuing, for example, an expectancy in a life insurance policy.

Perhaps not incidentally, both these comments simply assumed that if the trust were funded with cash and/or marketable securities, establishing the present value of the remainder at inception would not require an appraisal.

[8]

Though how exactly the various Justices might align on these issues is not entirely clear, *see*, *South Dakota v. Wayfair, Inc.*, 138 S.Ct. 2080 (2018).

Jack says,
when the night shows, the signals grow on radios