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Estate Tax Closing Letters

By John Bryan

Traditionally, an important event in the life of estates with potential estate tax exposure has been receipt of a closing letter from the IRS. The estate tax return is filed and upon acceptance, the IRS sends a closing letter saying that the estate tax return has been accepted by the IRS and that, absent material or intentional misstatement, no additional estate or gift taxes are due. While the closing letter does not extend to income taxes that may be assessed or due, the closing letter represents a crucial piece in administration process, allowing fiduciaries (typically executors) to distribute an estate without minimal risk of personal liability for unpaid estate taxes.

With establishment of portability of the estate tax exemption – whereby a surviving spouse can elect to claim the unused estate tax exemption available to the deceased spouse - the number of estate tax return filings has increased dramatically, often for the sole purpose of making the portability election (which requires filing of an estate tax return). The IRS apparently felt that the additional burden accompanying these additional returns justified changing the closing letter rules.

Against this backdrop, the IRS has announced that for estate tax returns filed after June 15 2015, the closing letter will only be issued after a formal request. The guidance goes on to provide that for estates below the filing threshold, closing letters generally will not be issued if the portability election was denied due to a late filing.

Further guidance has not been issued but the initial indication is that this request should be delayed until 4 months after the return is filed to allow processing. If the return is not audited and does not contain other errors or other "special circumstances," the IRS says that the closing letter should be issued within 4-6 months after filing.

While the new IRS policy still allows executors to obtain a closing letter for an estate in most circumstances, it will add another item to an executor's checklist to ensure timely administration of an estate.

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Problems with DIY Estate Planning

By Jennifer Schiffer

One of the most common questions asked by someone discussing the need for estate planning is, "why can't I just do it myself?" There are many risks to preparing your own estate plan over the Internet without consulting an expert.

The Potential Costs are High

The online will may be "free," but if there are any problems with it, they likely will not be discovered until it is too late for the problems to be corrected.

Oftentimes, online wills default to a specific state for the applicable law. Thus, the deceased could die a resident of Virginia, yet his will could state that the laws of California apply. This creates high expenses for the deceased's family as well as potential tax and other problems. For example, the family potentially could have to hire two attorneys, two accountants or other professionals to handle probate in one state while applying the laws of another state.

Another major problem with do-it-yourself wills is that they only are as good as the person completing the information. For example, one misdirected click could unintentionally write a user's children out of the will.

Many errors with do-it-yourself wills are at the execution point. Most states have specific requirements about how many witnesses must sign the will, whether it must be notarized and even what color ink is acceptable. Again, without a state-specific expert to consult, a do-it-yourself document may bequeath everything as the deceased intended, yet not meet all the formalities of state law, making the will invalid.

Common Challenges

Another potential problem with the do-it-yourself will is that no two people's situations are the same. An experienced practitioner can ask questions about family circumstances and then draft the will accordingly. For example, is there a family business? While many business owners are focused solely on their business, they need to think about the future and a success plan. Do they intend to have a family member take over? Do they intend to have their partner buy out their interest? These issues typically require an expert to sort through and develop a will that is tailored to the specific situation.

One further issue with do-it-yourself estate planning is that certain assets typically do not pass through a will at all. Usually savings bonds, certain types of bank accounts and certificates of deposits can be designated to automatically pay at death. An experienced practitioner can review your entire asset picture and advise you how to title your assets so they pass most easily to the beneficiary.

Having a will is certainly better than having no will in most circumstances, but having a properly prepared will can help ensure the testator reaches his or her estate planning goals while avoiding the hazards of a do-it-yourself will.

Jennifer Schiffer is a small business and bankruptcy attorney at the firm. She can be reached at jschiffer@beankinney.com or 703.525.4000.

Valuation Discounts

By John Bryan

Based largely on comments made by an IRS representative at a tax conference earlier this year, the IRS has signaled the likelihood of new rules designed to curtail the use of valuation discounts to leverage a taxpayer's gift tax exemption in situations where assets are transferred to or for the benefit of family members. The comments indicated these rules would likely be issued this fall.

The impact of leveraging through discounts can be dramatic. Gifts are valued based on the "fair market value" of the property transferred. A common scenario is the transfer of property by a parent to a limited liability company followed by gifts of interests to children. The value of the ownership interest transferred is discounted, typically because the recipient does not control the LLC (minority interest discount) and cannot freely transfer the interest received (illiquidity/marketability discount). Discounts can range from 30% to 60% in the value of the gifted interest.

The IRS has litigated discount cases for years. Generally the courts have been receptive to reasonable discounts when the other requisites for transfer of the gifted interests (such as credible valuation and bona fide transfer) have been met. In addition to legislative proposals to change the statute, the IRS continues to focus on the issue. The current suggestion is that the IRS would use the rules of Section 2704 of the Internal Revenue Code to reduce or eliminate discounts for purpose of determining the value of certain gifted interests in family-controlled entities. The scope and application of any rules – including effective dates and any limit on the type of assets to which the rules would apply - will not be known until the IRS formally acts but the public mention indicates that the issue remains on the IRS radar. At a minimum, any rules are likely to be subject to a prolonged period before finalization and possible litigation and have a chilling effect on techniques that have become a standard tool in estate planning.

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