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ESTATE AND GIFT TAX
FALL 2022
BOGDANSKI

FINAL EXAMINATION
(Three hours)

INSTRUCTIONS

This examination consists of three essay questions, each of which will be given equal weight in determining grades. Three hours will be permitted for this examination. At the end of the three hours, you must return this set of questions to the Registrar's Office in the original envelope in which it came.

You must submit all your answers using Examplify. Copying and pasting from a file outside Examplify is prohibited. Use of the internet or a network is also prohibited, except to view an electronic copy of the course casebook or statute book.

Pay close attention to the final portion, or "call," of each question. Failure to respond to the matters called for will result in a low score for the question. On the other hand, discussion of matters outside the scope of the call of the question will not receive credit.

Be sure to explain as thoroughly as possible your answers to the questions posed. Your reasoning, discussion, and analysis are often as important as any particular conclusion you reach.

The suggested time limit for each question is one hour. Experience has shown that failure to budget one's time according to this limit can result in a drastic lowering of one's overall grade on this examination.

For purposes of this examination, unless otherwise specified, assume that all transactions take place after 2017 and before 2026; and that all persons named in the questions are individuals, U.S. citizens, and U.S. residents. Any references to "the Code" mean the Internal Revenue Code of 1986, as amended.

QUESTION ONE
(One hour)

Betty, a wealthy person, has never been married and has never had children. Betty once had a sister, Ava, who died survived by her child, Nic. Nic is still alive and has an adult daughter named Greta. They are Betty's closest relatives.

Betty and Nic buy some real property, Blackacre, and have title taken in both of their names as joint tenants with right of survivorship. Betty and Nic each furnish one half of the money needed for the purchase price.

Greta needs money to invest in a rental property. Betty lends Greta $1,000,000 to help close the deal. Under the terms of the loan agreement and promissory note, Betty can demand repayment of the loan in full at any time. The loan bears no interest. Although Betty and Greta intend that Greta will eventually repay the entire $1,000,000 of principal to Betty, no repayments are in fact made, and Betty never demands any.

Betty establishes an irrevocable trust for the benefit of Nic. Under the terms of trust, all of the trust's income is to be paid to Nic or Nic's estate annually for 10 years. At the end of the 10 years, if Betty is still alive, the trust is to terminate and the trust corpus is to be distributed back to Betty. If at the end of the 10 years Betty is no longer alive, the trust is to terminate and the trust corpus is to be distributed to Greta.

Betty contributes $500,000 to the trust. The trust instrument provides that within 30 days after any contribution of funds by Betty, Greta may demand to be paid, immediately and in cash, an amount equal to the then-prevailing annual exclusion amount determined for purposes of Section 2503(b) of the Code. Greta is given notice of this withdrawal right, but heeding Nic's advice, Greta never exercises it.

Six years after establishment of the trust, Betty dies, survived by Nic and Greta. By virtue of Betty's death, Nic becomes outright owner of Blackacre. In her will, Betty leaves Greta's promissory note to Greta. The trust continues, with income continuing to be paid to Nic, for the rest of the 10-year term; at the end of the term, the trustee distributes the corpus to Greta.

What are the federal gift, estate, and GST tax consequences to Betty, Betty's estate, Nic, Greta, and the trust of each of the transactions and events just discussed, with and without all available tax elections? Be sure to discuss the amount and timing of each item.

Discuss.

(End of Question 1)

QUESTION TWO
(One hour)

Mai is married to Foster, and the couple has a daughter, Zia. Mai is an accomplished artist – a professional sculptor whose works are displayed in prestigious galleries and museums. Foster is an investment banker. Zia is a graduate student.

On the advice of an estate planning lawyer, Mai and Zia form a limited partnership, FLP. Mai transfers to FLP marketable securities with a fair market value of $4,950,000, and Zia transfers to FLP $50,000 cash that she inherited from an aunt. In exchange for these contributions, Mai receives a 1 percent general partner's interest and a 98 percent limited partner's interest in FLP, and Zia receives a 1 percent limited partner's interest in FLP. On the books of FLP, each partner gets an initial capital account equal to the fair market value of that partner's contribution. Under the partnership agreement and state law, limited partners have no right to control or manage FLP; the general partner has complete control.

Shortly after FLP is formed, Mai gives a 30 percent limited partner's interest to Zia, so that Zia becomes a 31 percent limited partner. Mai remains the 1 percent general partner but is reduced to a 68 percent limited partner as a result of the gift.

At the end of each of the first two years of its existence, FLP makes a distribution of $40,000 cash to Mai, which Mai uses to pay Foster's country club dues and Zia's travel expenses. Each distribution is made out of FLP's bank account, and Mai's capital account is duly debited on FLP's books. FLP makes no distributions to Zia. Mai and Zia hold an informal partnership meeting of FLP every year; the two conduct the meeting over lunch on Mai's birthday.

Two years after FLP is set up, Mai dies suddenly, survived by Foster and Zia. Mai's will leaves to Zia an inventory of finished sculptures that Mai was planning to sell at galleries. Mai's death sparks a renewed interest among art collectors in her work. Mai also bequeaths to Zia all of Mai's interest in FLP.

Mai's will also contains numerous outright bequests and devises to Foster. By the terms of the will, these transfers are void if Foster dies in a common disaster with Mai or dies within six months of Mai's death. If either of those contingencies occur, the assets are to pass to Zia. Foster in fact survives Mai by many years and dies of old age.

The will places Mai's stock portfolio into a trust for the benefit of Foster. The will provides that the income from the portfolio is to be distributed to Foster annually for the rest of Foster's life, but the trustee, Ella, is permitted to distribute some or all of the corpus to Foster as well, if Ella deems it appropriate. At Foster's death, the trust is to terminate and the corpus is to be distributed to Zia or Zia's estate. Mai's will provides that the executor of Mai's estate has the discretion not to fund the trust unless the executor finds it advantageous for minimizing estate taxes. The executor in fact funds the trust.

What are the federal gift, estate, and GST tax consequences to Mai, Mai's estate, and Foster of each of the transactions and events just discussed, with and without all available tax elections? Be sure to discuss the amount and timing of each item.

Explain.

(End of Question 2)

QUESTION THREE
(One hour)

In 2022, Dhani establishes an irrevocable trust, transferring to it some stock in a cellular phone company, Lope. The Lope stock, which is publicly traded, pays ample dividends every year. According to the terms of the trust, all of the income from the trust is to be distributed every year for the rest of Dhani's life to Dhani's son, Som, or Som's estate. Upon Dhani's death, the trust is to terminate and the corpus is to be distributed to Dhani's wife, Wali, or Wali's estate. In the trust instrument, Dhani retains two powers: (1) to require the trustee, a bank, to withhold income from Som or Som's estate and accumulate it, with any undistributed income to be paid to Som or Som's estate when Dhani dies; and (2) with the trustee's consent, to name someone else (other than Dhani) to replace Wali as the remainder beneficiary.

Later in 2022, Som asks for Dhani's financial help in connection with PSP, a partnership in which Som is a one-half partner. The other partner is Som's cousin, Carla. PSP operates an experimental farm that has never been profitable. Dhani transfers $100,000 cash to PSP, and Carla's mother, Ret, does the same. Neither Dhani nor Ret receives any consideration for their cash contributions to PSP.

In 2024, Dhani exercises his power to change the remainder beneficiary of the trust. Dhani names Som to replace Wali as the remainder beneficiary. The trustee consents to this change. As the same time that Dhani substitutes Som as the new remainder beneficiary, Dhani releases both Dhani's power to accumulate income (which he has never exercised) and Dhani's power to change the remainder beneficiary again in the future.

In 2026, Dhani dies unexpectedly, survived by Wali, Som, Ret, and Carla. The trust terminates and the Lope stock is distributed to Som. Dhani's will leaves all of his assets to Wali.

At the time Dhani dies, Dhani owns property with an aggregate fair market value of $40,000,000. However, the estate includes little cash and few readily marketable assets. Anticipating possible liabilities for state taxes, the executor of Dhani's estate sells one of Dhani's assets, a parcel of real estate known as Flatrock, to an unrelated party. The sale price of Flatrock is $8,000,000. The realtor's commission and other selling expenses paid by the estate in connection with the sale total $700,000. Later, the executor pays state taxes of $400,000 out of estate assets.

The fair market value of the Lope stock held by the trust is as follows throughout each year noted:

Year	*Fair market value*
2022	$1,000,000
2024	$1,200,000
2026	$1,500,000

What are the federal gift, estate, and GST tax consequences to Dhani, Dhani's estate, and Wali of each of the transactions and events just discussed, with and without all available tax elections? Be sure to discuss the amount and timing of each item.

Discuss.

(End of examination)