Estate and Gift Taxation
Fall 2021
Bogdanski

<u>FINAL EXAMINATION</u>
(Three hours)

QUESTION ONE
(One hour)

Emma, a wealthy, retired widow who has made many large taxable gifts, dies. For several years, and continuously up until the time of Emma's death, Emma was collecting monthly payments from an annuity policy issued by an insurance company. The policy had been purchased as part of a pension plan at Emma's former place of employment. Half of the premiums for the annuity policy had been paid by Emma, and the other half had been paid by Emma's employer. Under the terms of the annuity, after Emma's death, payments continue to Emma's adult child, Finn, for five years.

At the time of Emma's death, Emma was the income beneficiary of a trust established by her late father, Pops. The terms of Pops's trust gave Emma the power, in her complete discretion, to appoint all or any part of the corpus of the trust to any of Pops's many lineal descendants, other than Emma, at any time during Emma's life. When Emma dies, pursuant to Pops's trust's terms, the trust terminates, and the trustee, a trust company, distributes the corpus to Finn.

At the time of Emma's death, Emma was also the beneficiary of a trust established by her late husband. The late husband's trust was required to, and did, pay all its income to Emma quarterly until she died. No one had a power of appointment over the corpus of the late husband's trust. Upon Emma's death, the late husband's trust terminates, and pursuant to the trust's terms, the corpus is distributed to Emma's adult stepdaughter, Stefanie.

Rose is named the personal representative (executor) of Emma's estate. Among the expenses that Rose pays out of estate property are local property taxes, accrued before Emma's death, on real estate owned by Emma; state death taxes; and federal income taxes on income earned by Emma during Emma's lifetime. Some of the income subject to the income taxes was received by Emma before she died, and the rest was received by Rose on Emma's behalf after Emma's death.

At the time Emma dies, Finn is the owner of a life insurance policy on Emma's life. Pursuant to the terms of the policy, the death benefit is paid to Rose, as the executor of Emma's estate. Finn is the sole beneficiary of Emma's estate.

What are the federal gift, estate, and GST tax consequences to Emma and Emma's estate 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.

QUESTION TWO
(One hour)

Dana is a well-to-do individual who has made many substantial taxable gifts during her lifetime. Dana has exhausted all of her unified credit for federal estate and gift tax purposes.

In 2021, Dana establishes an irrevocable trust named the Dana Family Trust. The trust instrument calls for all the income of the trust to be paid to Dana's sister, Ada, for the rest of Ada's life. At Ada's death, the trust is to terminate, and the corpus is to be distributed to Dana's cousin, Bob, or Bob's estate.

Under the terms of the trust, Dana retains the power, during Dana's life, to invade the corpus of the trust "for the happiness and well-being of Bob"; however, the trust provides that in order to exercise this power, Dana must obtain the written consent of the trustee, Taj. Taj is Dana's attorney and unrelated to Dana, Ada, and Bob. Dana never exercises the reserved power.

To provide the initial funding of the Dana Family Trust, Dana transfers to the trust 1,000,000 shares of the stock of Corp, a publicly traded corporation. The 1,000,000 shares represent 30 percent of the outstanding stock of Corp, which is more than is commonly traded in the public markets in a one-year period. On the date of Dana's transfer to the trust, Corp stock is trading on the public markets at $10 per share. Corp pays quarterly cash dividends on its stock.

In 2023, Dana dies, survived by Ada, Bob, and Taj. Dana is also survived by Dana's spouse of many years, Sam. On the date of Dana's death, Corp stock is trading on the public markets at $12 per share.

At the time of her death, Dana owns (along with many other assets) 800 shares, which is 80 percent of the outstanding stock, of XYZ, another corporation. The other 200 shares of XYZ are held by a few XYZ employees, none of whom are related to Dana. In her will, Dana leaves 400 shares of XYZ stock to a new trust, named the Dana Marital Trust, and her other 400 shares of XYZ stock to a university that is an organization described in section 501(c)(3) of the Code.

The terms of the Dana Marital Trust require the trustee (Taj again) to distribute all of the income of the trust annually to Sam for the rest of Sam's life. The trust instrument also gives Sam the power to appoint any or all of the trust corpus to Bob, or to Sam's estate when Sam dies.

What are the federal gift, estate, and GST tax consequences to Dana and Dana's estate 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.

QUESTION THREE
(One hour)

Joy, an elderly unmarried individual with substantial wealth, has a minor grandchild, Gary. One day Joy, meeting with her estate planners, establishes an irrevocable trust for the benefit of Gary.

The terms of the trust provide that the trustee, a financial institution named Bank, is to accumulate the income of the trust until Gary reaches age 24. When Gary reaches age 24, the accumulated income is to be distributed to Gary. Thereafter, until Gary reaches age 35, the trust's income is to be paid to Gary each year. When Gary reaches age 35, the trust is to terminate, and the corpus is to be distributed to Gary. If Gary dies at any time before reaching age 35, the trust is to terminate immediately, and the corpus and any accumulated income distributed to his estate.

The trust grants Bank the discretionary power to distribute any and all of the trust corpus to Gary, or to withhold from him any required distributions of income, at any time before Gary reaches age 35. If Bank resigns or is disqualified as trustee, Joy has the right to name anyone, other than herself, as successor trustee. In fact, Bank remains the trustee and never exercises its discretionary powers.

Maya is Gary's mother and Joy's daughter. Joy and Maya open a joint checking account at Bank. Joy deposits money into the account; Maya does not. Joy withdraws money from the account regularly; Maya does so occasionally.

A few years after opening the account, Joy dies, survived by Maya and Gary. Gary is 15 years old when Joy dies.

Among the assets Joy owns when she dies is a one-half undivided interest as tenant in common in Blackacre, a parcel of real property. The other co-tenant is Joy's nephew, Ned. Joy and Ned's mother, Zia, acquired Blackacre together many years earlier. Joy paid the entire purchase price for the property and had title taken as tenants in common with Zia. Zia subsequently gave her interest in Blackacre to Ned. At the time Joy dies, Blackacre has a fair market value of $3 million.

Joy's will leaves Joy's interest in Blackacre to Maya. However, seven months after Joy's death, Maya delivers a document to the Joy's estate's executor whereby Maya refuses to accept the interest in Blackacre. Under state law and the terms of Joy's will, as a result of this act by Maya, Joy's interest in Blackacre passes to Gary.

What are the federal gift, estate, and GST tax consequences to Joy and Joy's estate 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 examination)