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## **CURRENT EVENTS**

### **November 2005**

1. Final Regulations issued (8/25/05) on Abusive Valuation of Life Insurance Contracts. IRC Section 402(a), 79 and 83.
  - a. Scope. Effective 2/13/04, life insurance transfers from employers or tax qualified plans to an employee – taxed at its FMV.
  - b. Abusive. Premiums large upon employer's payment resulting in greater deduction; cash value small when policy distributed to employee (less income).
  - c. Scope.
    - (1) 412i plans
    - (2) Determining FMV of retirement plans – account balance
2. IRS Releases 8 New Charitable Remainder Unitrust Forms under IRC 664. Rev Proc 2005-52 to 2005-59
3. IRS Releases August 2005 706 showing a deduction for state death taxes
4. Katrina Emergency Tax Relief Act of 2005 (9/23/05)
  - a. Hurricane Katrina Disaster Area Relief Only
    - (1) No 10% penalty for early withdrawal up to \$100,000
      - a) 3 year averaging
      - b) can recontribute amount up to 3 years
    - (2) No income or 10% penalty tax for distribution (2/28/05-8/29/05) for home purchases cancelled

- (3) Loan amount increased from lesser of \$50,000 or 50%, to \$100,000 or 10 for loans outstanding on 8/25/05.

b. Beyond Hurricane Katrina Disaster Area

- (1) \$500 deduction for free use of TP's residence for 60 days
- (2) No 50% ceiling on charitable deductions for cash gifts and 5 year carryover limit not applicable for contributions between 8/28/05 and 12/31/05 election.
  - a) Corporations – 10% deduction limitation waived from 8/28/05 to 12/31/05 but only for Hurricane Katrina relief efforts.
  - b) N/A for gifts to supporting organizations and donor advised funds, private foundations, and gifts of publicly-held stocks.
- (3) No reduction of itemized deductions by 3% of AGI over \$145,950 (2005).
  - a) Applies only to charitable gift. Other itemized deductions subject to 3% phaseout.

5. Proposed Regs clarify aspects of 409A nonqualified deferred compensation rules implementing guidance provided in Notice 2005-1(12/20/04). Prop. Regs. 1.409A-1, 2, 3, and 7. Deadline extended to 12/31/06 for amendment provided plan operated in good faith compliance with IRC 409A.

6. IRS issues temporary and proposed regs to close schemes where annuity values were reduced (cash value lower) at time of Roth conversion in order to avoid taxes, (cash value designed to increase after conversion - escape taxes)Section 1.408A-41 Q&A - 14 (effective 8/19/05)

a. **Significance.** May be considered guidance with traditional IRA distributions with IRA investing in annuities. **Result.** 50% underpayment penalty.

b. Determination of FMV

- (1) Conversion at time annuity contract issued -- premiums
- (2) Conversion -- no future premiums -- comparable products
- (3) Conversion -- future premiums – interpolated terminal reserve -- provided adequate reflection of full value

7. Trust ok'd as see-through Trust (9/23/05 PLR 200538030)
  - a. Trust -- IRA beneficiary
  - b. IRA subdivided f/b/o each beneficiary
  - c. RMD oldest beneficiary
  
8. Separate Accounts Ok'd for Sub-trusts. PLR 200537044 (3/29/05)
  - a. Beneficiary Designation – subtrust vs "Master Trust"
    - (1) Trustee power to accumulate
      - a) Held: no need to consider contingent beneficiaries.  
Reason: Conduit Trust – all retirement distributions distributed to beneficiary.
  - b. Trustee to trustee transfer to 12/31 year after death
    - (1) Held: separate accounts – each beneficiary's life expectancy
  - c. Special power of appointment – lineal descendants
    - (1) Held: does not defeat "beneficiary identifiable requirement".
  
9. Waiver of Rollover Rulings IRC 402(c)(3)(A)
  - a. Not allowed
    - (1) Only spouse can rollover PLR 200540020
    - (2) Despite medical problems, TP was able to keep track of other financial transactions. PLR 200540023
  - b. Allowed
    - (1) Medical problems. PLR 20054001
    - (2) Incorrect advice from employer. PLR 200540021
  
10. Inflation adjusted figures for Estate & Gift Tax Items
  - a. Gift Tax annual exclusion \$11,000 to 12,000
  - b. Special use valuation reduction - \$870,000 to \$900,000 limit

- c. 2% portion for interest on estate tax for farm or closely held business - \$1,170,000 to 1,200,000 plus applicable exclusion amount (\$2,000,000 in 2006)
- d. Increased Annual Exclusion Gift to Noncitizen spouses - \$117,000 to 120,000.

11. Gift to Social Club Qualified for Annual Exclusion. PLR 200533001

- a. Social Club Tax Exempt under IRC 501(c)(7)
- b. Qualified gift present interest (not charitable deduction)
  - (1) Future interest gifts – not exempt. Reg 25.2503-3(a)
  - (2) Transfer to Corporation = transfer to other S/H
    - a) Exception. Transfer to charitable, public, political or similar organizations may be gift to single entity. Reg 25.2511-1(h)(1)
      - (1) Facts here showed gift to single entity – club operated solely for nonprofitable purposes vs members = gift to single entity
- c. **Significance** – good analysis of present interest gift exclusion to an entity.

12. Assignment of Potential Proceeds of Wrongful Death Action to an IT = Completed Gift. PLR 200534015

- a. Donor (Plaintiff) assigned cause of action to IT.
- b. Donor had no rights in IT, but had continual involvement in claim.
- c. Held – complete gift
- d. **Significance** – IRS offered no opinion as to value or present/future interest.

13. New IRS Website – Life Cycle of a Private Foundation. IR 2005-121

- a. Creation
- b. Compliance