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A PARTNERSHIP OF PROFESSIONAL LAW CORPORATIONS

NEWSLETTER

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TRUSTEE DUTIES INCLUDE NOTIFICATIONS TO BENEFICIARIES AND OTHERS

MARY J. PESHEL, ESQ.



Trustees of California trusts have a general duty to keep the trust beneficiaries reasonably informed of the trust and its administration (Probate Code Section 16060). For trusts created after July 1, 1987, trustees are required to provide annual accountings to the beneficiaries (Probate Code Section 16062). Upon the request of a beneficiary, trustees are required to provide information about trust matters, including assets, liabilities, the acts of the trustee and the terms of the trust (Probate Code Section 16061).

For the past decade, California law (Probate Code Section 16061.7) has also required that the trustee provide notification of certain events, notably: (1) when a revocable trust or any portion of it becomes irrevocable because of the death of a trustor and/or (2) upon the change of the trustee of an irrevocable trust.

In both of these circumstances, notification must be provided to the trust

beneficiaries (and to the Attorney General for certain charitable trusts). When the notification is required due to the death of a trustor, the notification must also be given to the heirs at law of that trustor (defined in Probate Code Section 44 as the persons who are entitled to take property of the decedent by intestate succession). This notification apprises the beneficiaries and legal heirs of the existence of the trust and is similar to the notification required in a probate estate.

The notification must be in a prescribed form (described in Probate Code Section 16061.7) which notifies the recipients of the existence of the trust and of his/her right to obtain a copy of the terms of the trust. The notification must be given within 60 days after the death of the trustor or change of trustee.

The statute establishes a 120-day period for persons to contest a trust, but only if the notification is timely and properly sent to all recipients. Should a person entitled to notification request a copy of the trust, the trustee is required to provide a full copy of the trust (and any amendments). The time to contest the trust is then the later of: (1) 60 days following the mailing of the copy of the trust, or (2) the 120-day period.

If the trustee does not make a good faith

effort to comply with the notification statute, he/she can be held liable for any damages caused by failure to give the notification.

New sections of the Probate Code now require *estate attorneys*, beneficiaries, personal representatives and those in possession of property of a decedent to inform the California Victim Compensation and Government Claims Board when a deceased person has an heir who is incarcerated in California (Probate Code Section 216). That notice must be given within 90 days after the death and should provide information as set forth in the statute. Since trustees are persons in possession of property of a decedent, this statute applies to trustees.

A similar statute, Probate Code Section 9202, requires the personal representative of a probate estate to notify the California Victim Compensation and Government Claims Board within 90 days after letters of administration are first issued, if the personal representative or estate attorney *knows or has reason to believe* that an heir is confined in a California prison or similar facility.

The purpose of these laws is to facilitate the collection of restitution orders to crime victims. Because of this special notice, the Victim Compensation and Government Claims Board can pursue satisfaction of a restitution order from the incarcerated beneficiary's share of the estate.

In a probate estate, payment of a restitution order should be straightforward as the incarcerated beneficiary will receive notice of the petition for distribution and can object to having part or all of his/her share distributed pursuant to the restitution order. The personal representative of the estate should obtain a court order which reflects distribution pursuant to the restitution order.

The trustee of a trust may be placed in a difficult position as the trust terms are unlikely to authorize distributions from a beneficiary's share in order to pay a restitution order. Unless the beneficiary approves such payment by the trustee, it may be advisable for the trustee to seek court instruction before making such a

distribution.

Professionals who work with trust clients should be mindful of these California notification laws, as trustees often consult accountants or professionals other than attorneys to assist them in the trust administration process. Attorneys need to be familiar with the laws requiring notification to incarcerated individuals, as estate attorneys are specifically listed among the group required to give the notification.

SEMINAR: BASIC ISSUES IN ESTATE PLANNING

Bradford N. Dewan will be one of the presenters on April 23, 2007 at a seminar in San Francisco sponsored by National Business Institute regarding the federal tax and other issues which should be addressed in an estate plan. For more information, please visit:

<http://www.nbi-sems.com/Enbi/Brochurepdfs/36716.pdf>

**DEFERRING ESTATE TAXES JUST GOT A LITTLE EASIER
(With Proper Planning)**

BRADFORD N. DEWAN, ESQ.



For individuals who own interests in one or more successful family or privately owned businesses, the potential estate tax liability attributable to those interests may be of great concern. These business interests will be included in the owner's gross estate for federal estate tax purposes and, to the extent estate tax is due, the business owner may be concerned that there are insufficient liquid assets in his/her estate to pay the tax and his/her surviving family members will be forced to sell the business in order to pay the tax. In order to mitigate this potential problem of families being forced to sell the business in order to pay an estate tax, Congress has provided a method for opting to pay this tax in installments rather than in a lump sum soon after the death of the business owner. This option is provided in Section 6166 of the Internal Revenue Code.

If an "interest in a closely-held business" is part of an individual's gross estate and the value of such business interest exceeds 35% of the adjusted

gross estate, then the payments of the related estate tax (i.e., the tax attributable to the value of the business interest) can be deferred for five years. Interest on the tax is required to be paid during this five year period, after which the tax (and accrued interest) is required to be paid in installments over the succeeding ten years. The rate of interest required to be paid is significantly less than the rates typically available through commercial borrowing. Although the interest paid is not deductible for income tax purposes, and is not deductible as an administration expense on the decedent's estate tax return, the lower interest rate and deferral of estate tax available under Section 6166 can provide a substantial benefit.

The primary issue in determining eligibility for the estate tax deferral under Section 6166 is whether the business interest constitutes a qualifying "interest in a closely-held business" versus mere management of investment assets. This issue has been particularly relevant to individuals who own interests in real estate (e.g., residential rental properties, commercial properties and entities that own such property).

After thirty years of little guidance in this area, the IRS recently published a revenue ruling (Rev. Rul. 2006-34) that provides needed assistance and, importantly, establishes criteria that will be easier to satisfy for purposes of qualifying as an "interest in a closely-held business." The IRS states in the ruling that it will consider the following nonexclusive factors:

- The amount of time the owner (or agents and employees of the owner, partnership, LLC or corporation) devoted to the trade or business;
- Whether an office was maintained from which the activities of the owner, partnership, LLC, or corporation were conducted and whether regular business hours were maintained;
- The extent to which the owner (or agents and employees of the owner or the partnership, LLC or corporation) was actively involved in finding new tenants and negotiating and executing leases;
- The extent to which the owner (or agents and employees of the owner, partnership, LLC or

corporation) personally made, arranged for, performed or supervised repairs, maintenance to the building (whether or not performed by independent contractors), including painting, carpentry and plumbing; and

- The extent to which the decedent (or agents and employees of the decedent, partnership, LLC or corporation) handled tenant repair requests and complaints.

In addition to listing the above factors, the revenue ruling also discussed five examples. The examples varied based upon (i) the level of activity of the owner, (ii) whether employees or agents of the owner (or the business entity) were involved in the management activities, and (iii) the owner's level of ownership in the business entity that performed the management activities. A summary of the five examples discussed in the ruling can be found by visiting our website: www.mmp-ph.com.

Several positive conclusions can be drawn from this new revenue ruling.

1. The ruling makes it clear that an owner need hold only an interest in a closely-held entity that conducts an active trade or business. Thus, merely owning a significant limited partnership interest in a limited partnership that conducts an active trade or business can now qualify for installment treatment under Section 6166.
2. The ruling underscores the fact that, if the owner controls and supervises the activities of the owner's agents and employees, then the activities of these agents and employees can be attributed to the owner for purposes of Section 6166.
3. Similar to the above, the ruling provides clear support for the position that the activities of a co-owner, like a partner (who might be a family member), can qualify a business interest for Section 6166 treatment when the co-owner, acting on behalf of the jointly owned entity, provides the requisite level activity.

Consequently, many owners of real property and/or entities that own real property may now qualify for Section 6166 installment treatment by simply altering their level of activity, their oversight of employees or agents, and/or their level of ownership in an entity that actively controls and oversees real property. Due to the significant benefits associated with the lower interest rate and

deferral of estate tax available under Section 6166, we look forward to assisting our clients in analyzing and implementing, if necessary, the guidelines set forth in this new revenue ruling.

If you would like to receive further information regarding the topics in this newsletter, or if you would like to let us know any issues or topics you would like to see addressed in future newsletters, please contact us at (619) 239-7777 or newsletter@mmpph.com.

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