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TO OUR CLIENTS AND FRIENDS:

We hope you are enjoying the summer season. We want to bring to your attention some significant recent tax law developments and some thoughts about your confidential digital information.

IRS Attacks Valuation Discounts

The Internal Revenue Service has issued proposed regulations that, if finalized, would appear to increase the value of interests in family investment and business entities for federal estate, gift and generation-skipping transfer tax purposes. This would be accomplished by the elimination of certain common types of valuation discounts, such as those for lack of control and lack of marketability, in the case of transfers of interests in family owned or controlled entities. In addition, the same set of proposed regulations would significantly increase the circumstances under which a lapsing voting power will be treated as a taxable transfer. Essentially, the Service would like to bake in an irrebuttable presumption that family members will act in concert, so that restrictions that limit the ability of owners of interests in family entities to cash out of an investment or business entity lack economic substance. The justification for these changes is a view that under existing rules such restrictions have the effect of reducing ***federal transfer tax value*** but not the ***actual value*** of the interests being transferred within the family.

The American Bar Association, ACTEC, AICPA and other professional organizations are mobilizing to provide comments on these proposed regulations by November 2, 2016 in advance of a public hearing to be held on December 1.

The proposed regulations are stated to be effective with respect to transfers made on or after the date they become final (or in the case of certain changes 30 days after such date). This means that, in all likelihood, new rules will not go into effect before next year. Even if the proposed rules are modified somewhat before being finalized, it is anticipated that the type of "discount planning" that is currently possible may no longer be available, or may be severely limited beginning early next year. Therefore, a word to the wise would be to make any planning that involves transfers of discounted interests in family entities ***a high priority*** during the balance of 2016.

New Basis Reporting

A new and potentially misleading tax form will be making its way to the mailboxes of many individuals. This is a notice called "Schedule A to Form 8971," required as part of the IRS's implementation of the "basis consistency" legislation signed into law on July 31, 2015.

Briefly, executors of any estate large enough to require the filing of a federal estate tax return (Form 706) are now obligated to notify the estate beneficiaries of the values (as reported on Form 706) of estate assets that ***either have been or may be*** distributed to them. Where assets have not been earmarked for distribution or actually distributed, the executor must list all reportable assets which might be distributed to a beneficiary (or a trust for him or her). This will often mean that the same Schedule A, listing multiple pages of securities, business interests, and real estate interests must be mailed to a group of beneficiaries, each of whom eventually will receive an interest in a small subset of those assets. Recipients of Schedule A will have to retain the over-inclusive report for purposes of reporting their own gain or loss on a subsequent sale.

We anticipate that some recipients of a Schedule A may be confused about the distributions they may expect to receive from an estate and unaware of the obligations basis consistency imposes.

Part of the problem arises from the fact that Form 8971 (attaching a Schedule A for each beneficiary) is due a mere 30 days after the filing of the federal estate tax return, which itself is due 9 months after date of death, with a possible 6 month extension. In many estates, for various reasons, distributions will not be finalized by this time, making duplicative reporting on Schedule A a virtual inevitability.

Unfortunately, it gets worse: Further reporting by the executor is required if values are changed on audit of the Form 706. Moreover, if the recipient beneficiary subsequently disposes of an inherited asset by gift or other transaction to certain related parties, he or she will have reporting obligations. Certain assets, including cash, pre-tax or "qualified" retirement plans, some tangible personal property and assets which were sold during the administration of the estate need not be reported. All of this regulatory/reporting nightmare is to combat the perception that some heirs claim a higher cost basis when assets are sold than the value that was reported for estate tax purposes. You should ***retain Schedule A*** with your tax records. If you receive several mailings of Schedule A, do not assume that they are duplicates.

Protection of Client's Digital Information

We all read or hear almost weekly that sophisticated computer experts have hacked into the computer systems of retail store chains, banks, governmental institutions and

most recently the Democratic National Committee. The risk of security breaches for digital records is very real. When clients entrust us with their confidential information, we take our duty to protect that information very seriously. All of our digital client records are securely maintained and managed by a dedicated cloud provider, a company with which we have worked for ten years without any data breaches. To access that client information, every employee of our firm must enter his or her user name and a strong password that is assigned to that individual by the cloud provider (not chosen by the employee) and changed periodically. If a member of our firm is working outside of the office on a personal computer, cell phone or tablet, that device must be protected by a password and in order to access a client document, the user must enter the same user name and password that was assigned to him or her by the cloud provider. We also have an Acceptable Computer Use Policy that outlines the responsibilities of all members of our firm, and it must be signed by each of them.

We do find that email, cell phones and electronic fax services are efficient means of communicating with our clients. Our attorneys and staff use such means unless a client advises in writing that he or she does not wish us to do so. We do not customarily encrypt or password protect electronic communications but will do so whenever that is the client's expressed preference. We do recommend that a client not communicate with us from a work email account as it may be subject to monitoring by an employer. We also encourage our clients to find out whether their internet provider adequately protects the email messages that they are sending or receiving. Some providers are reportedly more secure than others.

Accessing Digital Information

While it is very important to protect your digital information during your lifetime, it is equally important that this information be available to your agent under power of attorney, executor or trustee after your incapacity or death. An increasing number of our clients have stopped receiving paper copies of bank statements and investment account statements. Instead, they prefer to access those account records online. If the client becomes unable to manage those accounts or dies, a fiduciary acting on her or his behalf (such as an agent, executor or trustee) will need access to them. The financial institution that holds the account may be unwilling to release the client's private information unless the client has consented to such a release in a signed written document, such as a power of attorney, will or trust agreement. Legislation has now been introduced in many states to regulate access to digital assets, and client consent is an important element in that legislation. We have started to incorporate a client consent provision in the wills, trusts and similar documents that we are preparing for our clients. If you would like more information about this subject, please contact us.

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The Republican and Democratic National Conventions are behind us and we anticipate hotly-contested elections for the Presidency, the Senate and the House of Representatives. The outcomes of these elections in November may signal the possibility of additional changes in our tax laws. If that happens, we will send you a further report.

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As mentioned in our previous mailings, we would like to keep you informed of new developments by email. If you would like to receive such email updates, please "Join Our Mailing List" at our website www.gswlaw.net.
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