



PROBATE & ESTATE PLANNING SECTION

Supplemental Attachments for

Friday, April 14, 2023

Meeting of Committee on Special Projects (CSP),

and

Meeting of the Council of the Probate and Estate Planning Section

at the University Club of Michigan State University
3435 Forest Rd, Lansing, MI 48910

Or *via* Zoom

**Probate & Estate Planning Section of the
State Bar of Michigan**

You are invited to the April meetings of the Committee on Special Projects (CSP) and
the Council of the Probate & Estate Planning Section:

Friday, April 14, beginning at 9 AM
at the University Club of Michigan State University
3435 Forest Rd, Lansing, MI 48910

Remote participation by Zoom will be available. So, you are also invited . . .

to a Zoom meeting.

When: Apr 14, 2023, 09:00 AM Eastern Time (US and Canada)

Register in advance for this meeting:

https://us02web.zoom.us/meeting/register/tZEsd-irqDkvHtDpGOn_fRyKbkPzLx0lv7pY

After registering, you will receive a confirmation email containing information about joining the meeting.

*If you are calling in by phone, email your name and phone number to Angela Hentkowski
ahentkowski@stewardsheridan.com, we will put your name in a zoom user list that
will identify you by name when you call in.*

Please note that the Zoom feature of these meetings entails that they will be recorded.

This will be a regular in person and remote meetings of the Council of the Probate & Estate Planning Section. The Council meeting will be preceded by a meeting of the Council's Committee on Special Projects (CSP), which will begin at 9:00 AM. The CSP meeting will end at about 10:15 AM, and the Council meeting will begin shortly thereafter. The agenda and meeting materials will be posted on the Probate & Estate Planning Section page of the SBM website. Once those things are posted, you should be able to download them from: <http://connect.michbar.org/probate/events/schedule>.

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Section Secretary

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Supplemental Council Meeting Materials

Supplemental Attachment 1

MEMORANDUM

TO: SBM Probate and Estate Planning Council
FROM: Mark J. DeLuca, on behalf of the Tax Committee
RE: April 2023 Tax Nugget

This month's Tax Nugget is a summary of *Smaldino v. Commissioner of Internal Revenue*, T.C. Memo. 2021-127. *Smaldino* involves an IRS challenge of a series of gift transactions entered into by a husband and wife. The first gift was from the husband to his wife, the second gift (made the day after the first gift) was from the wife to an irrevocable trust created by her husband, and the third gift was from the husband to the same irrevocable trust he created. In *Smaldino*, the IRS successfully argued that the doctrine of substance over form should apply to these three gift transactions and effectively cause the gift from the husband to his wife to be ignored for tax purposes, so that both gifts to the irrevocable trust were treated as if they were made by the husband.

In 2013, Louis P. Smaldino ("Louis") and his wife, Agustina Smaldino ("Agustina") had a net worth in excess of \$80 million. For decedents dying in 2013, the federal estate and gift tax exclusion amount was \$5.25 million. Consequently, Louis and Agustina were facing significant estate tax liability exposure. In an attempt to reduce their estate tax exposure, Louis and Agustina, with the assistance of counsel, began to implement estate tax planning. Below are the pertinent facts regarding their planning:

- In 2003, Louis formed Smaldino Investments, LLC (the "LLC"). Louis conveyed ownership of several parcels of real property to the LLC in 2012.
- On December 21, 2012, Louis created the Smaldino 2012 Dynasty Trust (the "Dynasty Trust"). The Dynasty Trust is an irrevocable trust. The beneficiaries of the Dynasty Trust are five of Louis's children, and the descendants of those five children. Agustina is not a beneficiary under the terms of the Dynasty Trust. Louis named his son Allen as the trustee of the Dynasty Trust.
- Louis transferred a 40.95% ownership interest (Class B nonvoting units) in the LLC to Agustina. Louis and Agustina executed an assignment document that provided that the transfer of the 40.95% ownership interest to Agustina was "Effective: April 14, 2013."
- Agustina then transferred a 40.95% ownership interest (Class B nonvoting units) in the LLC to the trustee of the Dynasty Trust. Both Agustina and the trustee of the Dynasty Trust executed an assignment document that provided that the transfer of the 40.95% ownership interest to the Dynasty Trust was "Effective: April 15, 2013."
- Louis also transferred an 8.05% ownership interest (Class B nonvoting units) in the LLC to the trustee of the Dynasty Trust. Both Louis and the trustee of the Dynasty Trust

executed an assignment document that provided that the transfer of the 8.05% ownership interest to the Dynasty Trust was “Effective: April 15, 2013.”

- Louis filed a 2013 gift tax return and reported the gift of the 8.05% ownership interest (Class B nonvoting units) in the LLC to the trustee of the Dynasty Trust (valued at \$1,031,882 for purposes of the gift tax return).
- Agustina filed a 2013 gift tax return and reported the gift of the 40.95% ownership interest (Class B nonvoting units) in the LLC to the trustee of the Dynasty Trust (valued at \$5,249,118 for purposes of the gift tax return).

The IRS issued a notice of deficiency to Louis for his 2013 gift tax return. The IRS took the position that in addition to the reported gift of the 8.05% ownership interest in the LLC to the trustee of the Dynasty Trust, Louis also indirectly made a gift of the additional 40.95% ownership interest in the LLC to the trustee of the Dynasty Trust. Louis disagreed with the IRS and filed a petition with the U.S. Tax Court.

The main issue at trial, other than the valuation of the two gifts, was whether, for gift tax purposes, the gift of the 40.95% ownership interest in the LLC to the trustee of the Dynasty Trust should be treated as a gift made by Louis or Agustina.

At trial, the IRS argued that IRC Sec. 2523(a) should not apply under these facts, and instead, the doctrine of substance over form should cause the gift of the 40.95% ownership interest in the LLC from Louis to Agustina to be ignored for gift tax purposes. Louis argued that the gift of the 40.95% ownership interest in the LLC from Louis to Agustina was completed properly, and IRC Sec. 2523(a) should exempt this gift between a husband and wife.

The court ultimately held that IRC Sec. 2523(a) did not apply because Louis never actually transferred “an interest in property” to Agustina. The court went on to explain that “[t]ransactions which do not vary, control or change the flow of economic benefits, are to be dismissed from consideration.¹ The court found that Agustina was never treated as a member of the LLC, and further, the court did not believe that the parties ever actually intended Agustina to be a member of the LLC. Thus, the court held that Louis gifted the full 49% ownership (8.05% + 40.95%=49%) interest in the LLC to the trustee of the Dynasty Trust in 2013.

Although the facts in *Smaldino* were certainly not great for the petitioner, the court’s opinion does provide a few good reminders for estate planning practitioners.

- (1) Document Dates and Execution. The court seemed to take issue with the fact that the gift transaction documents did not provide an execution date (*i.e.* no evidence of when the documents were actually signed). The gift transaction documents only included an effective date. However, the court did not like the fact that the documents included an effective date of April 2013, but were likely not actually executed until August 2013.
- (2) Corporate Formalities. As noted above, the court found that the parties never actually intended Agustina to be a member of the LLC. This was based, in part, on a review of

¹ *Snyder v. Commissioner*, 66 T.C. 785, 791 (1976) (quoting *Higgins v. Smith*, 308 U.S. 473, 476 (1940)).

the organizational documents for the LLC. The organizational documents were never updated to include Agustina as an owner of the LLC. Additionally, pursuant to the terms of the LLC operating agreement, the purported transfer of ownership interest from Louis to Agustina required board approval to be effective. The gift transaction documents did not include the requisite board approval.

- (3) Income Tax Reporting. For the 2013 tax year, the LLC partnership income tax return reported that ownership of the LLC for the entirety of the 2013 tax year was as follows: (i) 51% owned by Louis; and (ii) 49% owned by the trustee of the Dynasty Trust. The court took issue with the fact that the 2013 LLC partnership income tax return did not report Agustina as an owner for any portion of the tax year. Income tax reporting should match the terms of the underlying transaction.

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Supplemental Attachment 2

M E M O R A N D U M

To: Council of the Probate and Estate Planning Section of the State Bar of Michigan
From: James P. Spica
Re: Chairperson Elect's Report
Date: April 5, 2023

Members of the Council, ex officio members, and liaisons, please save the date: the 2023 Chairperson's Dinner will be held **October 13, 2023** on the campus of my alma mater, the Interlochen Arts Academy at the Interlochen Center for the Arts. The October CSP and Council meetings will be held, at the same place, the following morning. Overnight accommodation on campus will be available. (Details to follow.)

JPS