PHILADELPHIA ESTATE PLANNING COUNCIL

VOL. XXVI, NO. 2 • WINTER 2017

President's Message

Huldah A. Robertson, CFP®, AEP®

Happy New Year!!!

Hope you all enjoyed a happy and healthy holiday season and are ready to engage in our rewarding and vibrant PEPC community for 2017.

As we reflect on 2016, we shared many valuable moments together – our luncheons spanned topics of Family Business Ownership to Difficulties Opening Bank Accounts, and How the Basis is Reshaping Estate Planning. We kicked off our camaraderie with our Welcome Back Party at the Top of the Tower; toasted each other at our Holiday Celebration at Union Trust, and enjoyed Drop In networking events during our fall calendar.

We also became more engaged on a social network front as our LinkedIn communication and new website have provided endless opportunities to build and brand ourselves and our council – within the PEPC Community and beyond.

From an awards perspective, we honored our friend and colleague, William H. "Bill" Haines IV, with the Mordecai Gerson "Mordy" Meritorious Service Award.

Rich Schwartz and I also had the opportunity to attend the NAEPC Annual Conference where we formally accepted PEPC's "5-Star Council" Award and strengthened ties with councils across the country and NAEPC itself. Fellow councils and NAEPC offer tremendous benefits on a myriad of levels, and we look forward to pursuing conversations for mutual advancements.

Looking forward to 2017, we have a robust calendar of opportunities!! Our luncheon series begins in January with **Dana G. Fitzsimons Jr.** discussing "The Past Year's Most Significant, Curious, or Downright Fascinating Fiduciary Cases"; in February we have **Tara Thompson Popernik** presenting "GRAT to Great: Efficient Wealth Transfer with Grantor Retained Annuity Trusts", and in March we have **Marty Shenkman** speaking about "Estate and Financial Planning for Chronic Illness."

We hope you will also join us in recognizing our esteemed colleague, Nina B. Stryker, with our Distinguished Estate Planner Award at our January Luncheon.

In true PEPC tradition, our committees are creating opportunities for everyone to connect, engage, and excel. The spring calendar includes timely Roundtable topics, friendly Drop In gatherings, sportsmanly Golf and Tennis Outing, and not to be missed, the Annual Meeting at the Museum of the American Revolution.

We invite you to engage in committee work as a way to build lasting relationships and deliver meaningful impact within the council and community. Please take a moment to see which committees are interesting to you…and join the next meeting or reach on the website for more information.

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Changes to the New Jersey Tax Laws Warrant Immediate Attention!

Glenn A. Henkel, Esq.

On October 14, 2016, New Jersey Governor Chris Christie signed legislation raising the state's gas tax to help replenish the state's expired transportation trust fund. As a tradeoff, the law takes steps to encourage residents to remain in the state after retirement. First, it phases out the estate tax, effective January 1, 2018, and that will have a profound impact on the manner that our New Jersey clients will plan for their estates. Second, there is an enhanced retirement income exclusion that is phased in between now and 2020. This article will discuss estate planning issues for New Jersey residents and it will also highlight several issues that planners will need to know.

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COMING EVENTS

LUNCHEON PROGRAMS

The Union League
140 South Broad Street
Philadelphia, PA 19102
www.unionleague.org

11:45 – 12:00 p.m. Registration
12:00 – 12:30 p.m. Luncheon
12:30 – 1:45 p.m. Program

Dates:
Tuesday, January 17, 2017
Tuesday, February 21, 2017
Tuesday, March 21, 2017

Annual Golf & Tennis Outing

Monday, May 8, 2017
12:30 p.m. Golf Tee Time
2:30 p.m. Tennis Round Robin

Golf Outing:
Whitemarsh Valley Country Club
815 Thomas Road
Lafayette Hill, PA 19444

Tennis Outing:
Philadelphia Cricket Club/St. Martin's Clubhouse
415 W. Willow Grove Avenue
Philadelphia, PA 19118

Annual Meeting, Seminar & Reception

Thursday, May 18, 2017
3:00 – 3:30 p.m. Registration
3:30 – 6:00 p.m. Program
6:00 – 8:00 p.m. Reception & Museum Access
Museum of the American Revolution
101 South Third Street
Philadelphia, PA 19106

Please register at www.philaepc.org.

President's Message continued

On behalf of the entire council, we want to take this time to thank our many committee members, sponsors, and leadership team. Your volunteerism and support are essential to the strength and evolution of our community.

Wishing you all a happy and healthy 2017!

Cheers,

Huldah A. Robertson, CFP ®, AEP ®

Sign Up for a PEPC Committee

The Philadelphia Estate Planning Council offers many opportunities for member involvement. One of the most rewarding ways to get involved is through our many committees.

The committees encompass all activities of the council including planning our social events, publishing our highly informative newsletter, enhancing our website and developing our education programs.

All members are encouraged to actively participate on a committee. Committee participation provides the opportunity to expand your professional relationships and increase your leadership skills.

To sign up, please contact the PEPC Office at staff@philaepc.org.

New Jersey continued

While the major highlight in this new legislation is the repeal of the estate tax after 2018. It is really a "phase out" and there is always the potential that the tax may not, in fact, disappear. Moreover, the New Jersey *inheritance* tax is retained (a significant trap for unwary). The rules for 2017 decedents allow a $2 million exemption per decedent, including a change in the manner that the tax is computed. The way the law is drafted allows an easy fix to retain the tax if the state later decides to keep the 2017 tax format. The current tax law is a "cliff," meaning that the tax applies on all estates subject to tax but the new law provides a "credit" reducing the tax even on larger estates. The other provision is the enhanced pension exclusion that looks good, but it may not apply to some of our clients. Consider that the New Jersey estate tax repeal together with the other changes in the transportation trust fund law creates an unfunded hole in the New Jersey budget of more than a billion dollars in 2018. Before clients hurry home to New Jersey, they should look into the details.

Under the new law, the New Jersey estate tax will be phased out for decedents passing after January 1, 2018. Presently, the $675,000 exemption is the lowest in the country and will increase to $2 million for decedents who pass away after January 1, 2017. What does this mean for those living in New Jersey? What changes to planning and documents might be advisable to consider for New Jersey domiciliaries? Will it bring back former New Jersey residents who "changed" their domicile to a no-tax state? For many, it has been the INCOME tax that has caused clients to leave New Jersey (maybe climate too). Because the current law only allows a meager $20,000 pension exclusion (married filing joint), the new law adds an increased pension exclusion that is likewise phased in and makes New Jersey more competitive regionally.

The newly adopted pension exclusion increases the thresholds from $20,000 in 2016 to $40,000 in 2017, $60,000 in 2018, $80,000 in 2019 and to $100,000 for 2020 and thereafter (all married filing jointly). For single taxpayers, the current $15,000 exclusion goes to $30,000 (2017), $45,000 (2018), $60,000 (2019) and $75,000 (2020). However, this benefit is provided only to taxpayers who are below the gross income threshold. Even a mere $1 of gross income over the exemption, denies the taxpayer of the benefit. Under current law, the pension exclusion is denied if the taxpayer has New Jersey taxable income of more than $100,000. Thus, while the law is a step in the right direction, it is not that attractive to high net worth individuals.

For the estate tax, New Jersey law provides that there are no estate tax changes for 2016 decedents (leaving in place the $675,000 exemption threshold based upon the 2001 provisions in IRC Section 2011) and there is no tax for 2018 decedents. For 2017 decedents, the tax is imposed based upon the prior I.R.C. Section 2011 "credit" rate chart as it existed in 2001 that is now incorporated into the statute, but the computed tax is reduced by a "credit" of $99,600, the tax that would have been imposed on a $2,000,000 estate.

Whether the State will be financially able to forgo the estate tax revenues in 2018 and thereafter remains to be seen. That will be an issue for a future legislature and a future Governor. The lost revenue effects even just for the estate tax repeal are huge, almost $500 million in fiscal 2020 and more than $500 million in fiscal 2021 and fiscal 2022. As mentioned, the 2017 tax computation could be a precursor to future rules so they are worth studying.

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New Jersey continued

The *new* New Jersey tax computation for 2017 decedents is keyed to the definition of "taxable estate" contained in Internal Revenue Code Section 2051. That reference has raised an interesting interpretive question. When the existing New Jersey tax was keyed to the 2001 tax code, there was no deduction for state estate tax. (IRC Section 2058 that allows a state estate tax deduction is only effective for decedents passing after 2005). Now, because of the reference to the current tax code, the *state* tax to be paid is a *deduction* in arriving at the tax. Thus, there is a circular computation to arrive at the tax. Maybe, this will be fixed in a technical correction. However, as of now, the computation is a "circular," meaning you deduct the tax against the tax and need a computer or algebraic formula to determine the amount owed. The allowance of a deduction could also raise questions about taxes paid to other jurisdictions where an estate could attempt to claim both a credit for tax paid and a deduction.

One major benefit is that this definition of the tax base in IRC Section 2051 starts with the "gross estate" less deductions, which is *before* adding back prior gifts made. As a result, like it was for the pre-2017 rules, gifting still reduces the estate and thereby, using a gifting strategy reduces the estate tax. Before gifting, however, advisors should make sure that the assets being given away do not result in a higher income tax cost. When assets are gifted, the donee receives "carryover" income tax basis rather than the "step up" that can occur at death. It is usually not a good idea to save estate tax at a cost of an increased income tax, unless the tax is lower (analysis is needed before the gift) or the asset will not be sold (e.g., a vacation home or a family business). Another consideration with gifting is that under the old rules, the gifts escaped estate tax. However, there was still a tax on the assets remaining in the estate, so there would be some tax due. To avoid any tax at all, a donor had to gift all the way down to a retained asset base of just $100,000. Now, because of the "credit" on the first, $2,000,000, a retained asset base of $2,000,000 will escape the tax entirely. This is a great opportunity for deathbed planning however, while there is generally no "3-year" rule for *estate* tax, there remains a rule for *inheritance* tax that will impose an inheritance tax on all gifts within three years of passing.

Another benefit to the new system is that the pre-2017 "simplified method" of computing the estate tax will be repealed. This approach was not "simple" and often resulted in more tax than under the usual so called "706 method" named after the federal tax return Form 706.

In the end, the New Jersey estate tax change is welcome relief, but for clients with estates above the $2 million exemption amount, prudence would suggest that they retain their existing plans. With the potential that the Trump administration will repeal or modify the federal estate tax, many clients will be eager for simplification to their planning. However, let's not act too quickly for our New Jersey residents. If an estate is below the $2 million sum, then perhaps the simplification may be useful. However, for many others, immediate changes may not be warranted.

Another key factor to consider is that New Jersey also imposes an inheritance tax. The New Jersey inheritance tax is not repealed as a result of this effort. The New Jersey inheritance tax does not generally apply to transfers to a spouse, child, or grandchild who are referred to as "Class A" beneficiaries. Unfortunately, the New Jersey Inheritance tax subjects transfers to siblings, and children in law at a rate of 11% (on an amount over $25,000) known as Class "C" beneficiaries. This rate rises on transfer above $1.1 million reaching a high of 16%. Other non relatives are taxed at a 15% rate (16% over $700,000). While a "step child" is a preferred "Class A" beneficiary, the transfer to a "step *grandchild*" causes a 15% tax. The New Jersey inheritance tax remains a costly trap for unsuspecting taxpayers. As noted above, unlike the rules for the New Jersey estate tax, the inheritance tax carries with it a three-year inclusion of gifts in the tax base.

Many of the questions in a spousal estate tax planning structure relate to the plan in place from the passing of a first spouse until the passing of the survivor. A common approach taken in wills (or revocable trusts when used as the primary dispositive document), is to incorporate a 'credit shelter trust' and a marital disposition (either outright or in trust). The purpose of the credit shelter trust was generally to make assets available to the surviving spouse but to avoid them being included (or taxed) in the surviving spouse's estate for estate tax purposes. In other words, this technique to limit the tax seeks to allow the heirs to inherit assets tax free sheltered by the exemption of both parents.

In New Jersey, some families would employ a state exemption level credit shelter trust of $675,000, a "gap" trust funded with the difference between the federal exemption and the New Jersey exemption (then $675,000). The excess above the federal exemption would be bequeathed to a "Qualified Terminable Interest Trust" or "QTIP" as defined in IRC Section 2056(b)(7) or other marital deduction qualifying bequest. The estate, post-death, could then determine how to characterize the gap trust. For smaller estates some practitioners may have relied on outright bequests and the provision of a credit shelter trust that is created by a "disclaimer" by the surviving spouse. While that type of dispositive

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New Jersey continued

scheme might appear not to require any modification, that may be too superficial of an analysis. Practitioners must evaluate the plan in light of the recent legislative developments made, pending or anticipated. Because of the pending changes happening over time, a plan for a 90 year old client might differ from the plan for a 60 year old client. However, it may be beneficial to review existing documents, particularly those with tax driven formula clauses as tax thresholds change.

With the repeal of the New Jersey estate tax (or possible federal repeal), a "Disclaimer Trust" plan may become the default planning approach for moderate wealth taxpayers. If spouses have been married for a long time and the children are "common children" of the marriage, such that it could be anticipated that a surviving spouse would not be expected to disinherit the children of the predeceasing spouse, then a disclaimer trust may provide the greatest opportunity for flexibility. Disclaimer trusts, however, are not effective in achieving non-tax planning objectives.

A disclaimer trust estate plan would devise the entire estate to the surviving spouse. If the inheritance is "disclaimed' by the survivor, the will or revocable trust can direct the inheritance to a trust for the spouse as permitted by I.R.C. § 2518. By granting a surviving spouse this option, the surviving spouse can choose whether funding the trust with the estate of the first spouse to die is appropriate based upon a variety of circumstances at that time, such as (1) the size of the combined estates at the first death; (2) the applicable federal/state estate tax exemption; (3) the likelihood that the surviving spouse will reside in a state with a state estate tax; and (4) will a trust provide opportunities for income tax planning and "basis" shifting. While all of these uncertainties may remain at the death of the first spouse, this flexible plan is premised on the assumption that we may know more at that time than when the wills and estate plan were drafted.

Another issue to consider is that since the federal American Taxpayer Relief Act of 2012 (signed January 1, 2013) the federal government has permitted "portability" of the federal estate tax exemption. Portability was designed with an eye toward eliminating the need for the complexity of traditional "by-pass/ credit shelter/family trust" planning used to shelter tax by preserving the estate tax exemption of each spouse of a married couple. In general terms, "portability" of estate tax exemption allows one spouse to inherit the assets of their deceased spouse – which used none of the exemption permitted for non-marital and non-charitable transfers and also inherit the unused exemption. The technical term for this "unused" exemption is the "Deceased Spouse Unused Exemption" or "DSUE." In the context of planning for New Jersey domiciliaries, assuming the estate tax remains, the state does not allow for "portability" of exemptions.

Procedurally, the administration of a New Jersey estate has always been hampered by the process that protects the State collection of the tax. In New Jersey, there is a lien for estate tax on the estate of a decedent. The executor/personal representative could always access half of the funds without discharging the lien (known as a "blanket waiver") but the balance of the estate could be released only on receipt of clearance from the New Jersey Division of Taxation. The Division would issue "inheritance and estate tax waiver" forms that prove the tax has been paid and the institution holding funds would require these "waivers" to make final release of the estate assets. For estates where no tax is due, a "Self-executing waiver" process could be used. These are the forms L-8 (for cash/stocks/ bonds/intangibles) or form L-9 for real estate. Under new procedures, the "self-executing waiver" process will be updated to apply only where the estate is less than $2,000,000. However, there may be a delay in spreading the word since many institutions are aware of the pre-2017 $675,000 threshold. In other words, there may be some time before institutions will be aware to use the new rules.

Finally, another trap for unwary is that in 2015, the federal "Surface Transportation and Veterans' Health Care Choice Improvement Act of 2015" (H.R. 3236) relaxed filing due dates for federal tax returns placed on extension. For federal taxes, a fiduciary can get a 5 ½ month extension on income tax returns (Form1041) from April 15 until September 30. At present that rule will not apply for New Jersey purposes (Pennsylvania too). Thus, while federal tax returns can be extended to September 30 the New Jersey return will still be due Sept 15 (if extended).

In sum, the ever-changing tax landscape will cause our New Jersey clients to review their estate planning documents. For a change, the news from Trenton is good news, but before changes are implemented, advisors should carefully consider the fine print. Compound this with possible federal tax changes and clients will undoubtedly want to eliminate tax planning in favor of simplicity. Simplicity may be appropriate for some, but not all. Clients and estate planners will need to be ready to figure out which ones can or should change and which ones should not change. Be careful out there!

Glenn A Henkel JD, LLM, CPA is a tax and estate planning lawyer at Kulzer & DiPadova in Haddonfield NJ, is a member of the PEPC board and has been active in the New Jersey trust and estate community for over 30 years. Mr. Henkel is a frequent lecturer and has written extensively on estate planning topics.

Five of the Hottest Topics in International Estate Planning

Paula Jones

Multinational individuals and families are one of the most misunderstood segments of the wealth advisors' clientele. Planning for multinationals is not only applicable to the super-wealthy, nor only those who live in New York. The recent media storm surrounding the Panama Papers seemed to exacerbate the inaccurate stereotype that anyone holding assets "offshore" must be a tax cheat.

The real issues that all wealth advisors must be able to address for the multinational client, however, are usually far less dramatic. More and more multinational individuals and families are created by the significant increase in international travel to and from the United States, the creation of cross-border businesses, and the migration of employees to and from the U.S. As a result, the seemingly average client may turn out to have personal, business or financial connections to more than one country, such as:

- A U.S. resident's husband dies with an estate valued well above the federal estate tax exemption amount. His Will leaves everything outright to his wife. The wife is now faced with a large federal estate tax bill due to the lack of an unlimited marital deduction afforded to non-U.S. citizen surviving spouses.
- A married executive owns most of her assets in her own name. For estate planning purposes, it is best that she and her husband each own an equal amount of assets. She needs to make large transfers to her husband, who is a U.S. resident.
- A green card holder has been living in the U.S. for about 6 years. He plans on returning to his home country of Germany in the next few years. He is trying to decide when and how to accomplish his goal in the most tax-efficient manner possible.
- A wealthy Russian individual wishes to purchase real estate in the United States. She asks for advice on the best way to title the property prior to its purchase hoping to minimize U.S. income, estate and gift taxes while limiting her personal liability in regard to a tenant's use of the property.
- A couple left the U.S. several years ago without formally giving up their green cards. They also stopped filing U.S. income tax returns. The clients want to see if they are considered non-compliant with the IRS and if so, they want to weigh all of their options in order to become compliant and avoid significant penalties.
- A multinational couple, both born in India, are citizens of the United Kingdom. They own U.S. property and spending a good portion of their time here. The U.K. law deems them domiciled in India but the U.S. law deems them domiciled in the U.K. They look for advice on planning their estate in the U.S. under this scenario.

The U.S. income and estate tax laws operate differently for multinationals than for purely domestic clients. Every wealth advisor should have at least a passing knowledge of those differences in order to flag issues that must be incorporated into any plan.

1. U.S. Transfer and Income Taxes Have an Extended Reach

The basic rules for federal income and estate tax form the background against which many planning solutions are constructed. The U.S. has a broader reach of taxation than many other countries, even those countries from which U.S. laws have been derived. Here are the basics:

U.S. citizenship and U.S. residency subjects individuals to U.S. transfer tax (estate and gift taxes). U.S. transfer tax extends to all assets, wherever situated in the world, owned by said individuals.[1] For those individuals without either U.S. citizenship or residency but with assets deemed to have a U.S. situs (such as real estate and tangible personal property physically located in the U.S.) only those U.S. situs assets are subject to U.S. transfer tax.[2]

Individuals who have either renounced their U.S. citizenship or residency may still, under certain circumstances, be subject to U.S. estate tax on a portion or all of their future estate. One law applies to those individuals who renounced prior to June 17, 2008 while a different law applies to those renouncing on or after June 17, 2008. The imposition of estate tax applies under slightly different circumstances in the older law versus the newer one.[3]

U.S citizenship and U.S. residency subjects individuals to income tax in the U.S. as well and it extends to *all* income regardless of the country from which it is sourced.[4] For those individuals without either citizenship or residency in the U.S., but with U.S. source income, only the U.S. source income is subject to U.S. income tax.[5]

An exit tax may be imposed on 1) individuals who give up their U.S. citizenship or 2) long-term green card holders who give up their green cards, if the renunciation occurred on or after June 17, 2008 ("covered expatriates").[6] Capital gains tax is imposed on all unrealized capital gain on a covered expatriate's worldwide assets, after an exemption amount of $693,000 (in 2016) is applied.[7] Not everyone is subject to this exit tax, however. A further qualification needed in order to meet the definition of a "covered expatriate" is either a net annual

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Hottest Topics continued

income tax of $161,000 (in 2016) or a net worth of $2 million or more. The U.S. is only interested in imposing the exit tax on those who are considered wealthy.

The definition of "resident" for U.S. estate tax purposes is vastly different than it is for U.S. income tax purposes. A "resident" for estate tax purposes is, a "decedent, who at the time of death, had domicile in the United States." A person acquires domicile by living in a particular location, "for even a brief period of time, with no definite present intention of later removing therefrom."[8] A U.S. income tax resident, by contrast, is generally determined in a quantitative manner. Individuals count the number of days they are physically present in the U.S. and if greater than a certain number, according to a formula, they are deemed a tax resident. Green card holders are also automatically deemed U.S. income tax residents.

2. Tax Treaties Can Provide Welcome Relief

There are income tax treaties between the United States and most other countries in the world. However, there are less than twenty estate tax treaties between the United States and other countries.

Most treaties have "tie-breaker" provisions which define issues such as residency, domicile and asset situs - which may be otherwise difficult to discern. Since the laws of more than country may be in direct contrast, a treaty provision can itemize each element of these concepts in order to determine the residency and domicile of an individual and the situs of that individual's assets.

In any planning or administration of a multinational individual or family, the provisions of any applicable tax treaty are crucial. Such treaties can offer a marital deduction when there is none available otherwise; they can prevent double taxation on property otherwise allowed to be taxed under each country's law; and they can also prevent the avoidance of taxation on property that may otherwise fall through a loophole between the laws of applicable countries. The provisions of a tax treaty can negate the need for complex planning in certain areas of the estate. Always check the provisions of any applicable tax treaty before formulating any multinational's estate plan.

3. Non-Citizen Surviving Spouses Have Options

There is a limit to the marital deduction afforded to any transfer – during life or at death – between spouses when the recipient spouse is not a U.S. citizen.[9] Only transfers to U.S. citizen recipient spouses are afforded the unlimited marital deduction with which most advisors are familiar. Take note that the citizenship status of the donor spouse is irrelevant. Also, both U.S. citizens and U.S. residents are afforded the $5.45 million (in 2016) federal estate and gift tax exemption amount, so transfers above and beyond this amount are those in need of a marital deduction to minimize transfer taxes.[10]

The philosophy behind this law is to preserve the U.S.'s ability to tax the transfer of the surviving spouse's inherited assets at her death. Should the surviving spouse give up his or her residency, the U.S. can lose its authority to tax him or her. The U.S. would preserve its taxing authority for a U.S. citizen spouse, however, regardless of the country in which he or she physically resides, due to the reach of the U.S. estate tax upon a citizen's worldwide estate.

Fortunately, a non-citizen recipient spouse has some options to render the transfer of assets to him or her eligible for the marital deduction. First, there may be an estate tax treaty that will grant the marital deduction in the estate of the decedent spouse. Another option is for the surviving spouse to become a U.S. citizen.

Finally, a Qualified Domestic Trust ("QDOT") can be incorporated in the estate plan of the donor spouse to earmark any amount passing to the non-citizen recipient spouse that exceeds the applicable estate tax exemption.[11] Fortunately, if there has been a lack of planning on the part of the donor spouse, a post-mortem QDOT is available to the surviving spouse, if needed.

The QDOT must maintain a U.S. jurisdiction for tax purposes, so that regardless of where the surviving spouse may relocate, the U.S. maintains the authority to tax the QDOT assets upon their transfer out of the trust. Any transfer into, or attributed to, the QDOT from the donor spouse's estate is then afforded the marital deduction.

A QDOT does not replicate the same experience for the surviving spouse as obtaining citizenship and receiving all assets outright to manage in whatever way he or she seems fit. The QDOT pays out all current income to the surviving spouse but any principal distributions from the QDOT to the surviving spouse are subject to federal estate tax, except when considered "hardship" distributions.[12] A QDOT, while providing a welcome option for whom citizenship is not an option, can still feel restrictive to the surviving spouse.

4. Plan Your Client's Pop Over the Pond

When non-U.S. people wish to eventually become resident in the U.S., they have an opportunity to plan their estate while still exempt from the U.S. transfer tax system. Since non-U.S. people have neither U.S. citizenship nor U.S. residency they are subject only to estate or gift tax on U.S. situs assets (see above). Prior to establishing U.S. residency, therefore, unlimited transfers of assets

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Hottest Topics continued

to beneficiaries, outright or in trust, can be made without incurring U.S. gift tax. (These individuals would need to determine if the country of their citizenship or residency, or countries in which their assets are located impose any transfer or income tax on the transfer.) Once U.S. residency is obtained, these same individuals are subjected to the lifetime gift exemption amount of $5.49 million.[13]

To extend the benefits of this "loophole", it is recommended that the transferred assets are directed to a U.S. dynasty trust created in a jurisdiction in which the rule against perpetuities has been abolished. Such a trust can keep the benefit of the U.S. transfer tax-free transfer of assets going for many generations.

5. Get Compliant with Foreign Accounts and Assets

In the Spring of 2009, the Internal Revenue Service publicized their intent to enforce penalties against those who had failed to report income on their foreign accounts on their U.S. income tax returns. The Service also went after those who failed to file reporting forms regarding foreign accounts, even if all of the income from those accounts had been appropriately reported and paid in the U.S.

For those taxpayers who have not reported or paid income tax on their foreign income, the IRS's Offshore Voluntary Disclosure Program ("OVDI") may be an option to become compliant.[14] The most current OVDI, announced in 2012 and modified in 2014, has no current closing deadline. This program imposes a penalty of 27.5% of the highest balance of unreported accounts, in lieu of most other civil penalties if the IRS finds that the taxpayer acted willfully resulting in noncompliance.[15]

If, on the other hand, the IRS finds a taxpayer did not act willfully, they offered, beginning in September of 2012 and expanded in June of 2014, a Streamlined Program that imposes only a 5% penalty on the highest balance of unreported accounts, in lieu of most other civil penalties.

In order to prevent the need for either of these programs, advisors need to ensure their clients with any accounts or other assets offshore remain compliant. The Foreign Account Tax Reporting Act ("FATCA") was passed in March of 2010 and clarified the requirements of U.S. persons in reporting their financial holdings offshore. A result of that portion of FATCA directed at individual taxpayers, IRS Form 8938 was created to collect information from taxpayers who had not only bank accounts outside the U.S., but also foreign assets. Form 8938 is filed with a taxpayer's Form 1040 and was first required to be filed in tax year 2011.

Practitioners should also be mindful of the requirements of FinCEN Form 114 (often referred to as the "FBAR" and previously identified as Form TD F90-22.1), IRS Form 3520 and IRS Form 3520-A, which often impact individual taxpayers, trusts and estates in the foreign context, although these forms and reporting requirements have been in existence long before 2010.

Legal issues surrounding the compliance of U.S. persons with foreign accounts or with foreign assets have continued to be a major focus of the IRS. There continues to be ongoing activity and change in this highly complex area of the law, with the risk of stiff penalties at every turn.

Conclusion

As our global environment expands, more and more middle class Americans are venturing outside of U.S. borders in many ways - travel, trade, investment and emigration. Advisors should be in tune with the increasing number of clients who have international components to their personal, business or financial lives.

Footnotes:
1 IRC §2001(a), IRC §2031(a)
2 IRC §2101(a), IRC §2103
3 IRC §877, IRC §877A
4 IRC §2(d)
5 IRC §871
6 IRC §877A
7 IRC §877A(a)
8 Treas. Reg. §20.0-1(b)(1)
9 IRC §2523(i)
10 IRC §2010(a)
11 IRC §2056A
12 IRC §2056A(b)
13 IRC §2010(a)
14 https://www.irs.gov/individuals/international-taxpayers/streamlined-filing-compliance-procedures
15 https://www.irs.gov/uac/2012-offshore-voluntary-disclosure-program

Paula M. Jones has almost twenty years of experience advising clients on all aspects of domestic and international estate law for moderate to high net worth individuals and business owners. She opened her own practice in 2016. Paula is currently an adjunct professor at Western New England University School of Law where she teaches International Estate Planning and she has authored several articles in respected industry journals. In addition, she developed a workshop and companion workbook on estate planning basics, titled "Will Power: Wealthy or Not, Your Estate Matters." Her web site is www.paulajoneslaw.com.

A Litigator's Perspective

Thoughts on Drafting a Durable Power Of Attorney with an Eye Toward Preventing Agent Misconduct and Future Conflict.

Timothy J. Holman, Esquire[1]

Would you advise someone against turning on their home security system just because they have a front door with a deadbolt? Or would you say instead, "You can never be too careful. I know the chances are slim that you'll need it, but you should use the security system since it's available to you." Estate planners can give their clients a similar choice for adding extra security when it comes to drafting powers of attorney. Even though Principals trust their chosen Agents, and no Principal chooses an Agent expecting that person to steal from them, Agent misconduct happens all too often.

As an Orphans' Court litigator, I don't draft durable powers of attorney. I have, however, encountered countless situations in which an Agent has treated a power of attorney as a license to steal. I've also met many beneficiaries of a Decedent's Estate who did not know until after the Decedent's death that an Agent under the Decedent's power of attorney abused that power. Such beneficiaries often say they did suspect the Agent was up to no good, but they felt powerless to explore or to stop the Agent's conduct. In this article, I will outline a few steps that you can take, as drafters, to decrease the chance that an Agent will take advantage of your Principal client.

Clearly Explain Your Principal Client's Options

Act 95, Pennsylvania's Power of Attorney (POA) law, contains the following provision: "Except as otherwise provided in the power of attorney, an agent shall not be required to disclose receipts, disbursements or transactions conducted on behalf of the principal unless ordered by a court or requested by the principal, a guardian, conservator, another fiduciary acting for the principal, governmental agency having authority to protect the welfare of the principal or, upon the death of the principal, the personal representative or successor in interest of the principal's estate." 20 Pa. C.S. § 5601.3(d)(1).

This provision essentially codifies long-standing law that limits the class of folks who have the legal right to learn anything about an Agent's actions during the Principal's lifetime. Indeed, standing issues pervade POA dispute litigation. *See, e.g., Griggs Estate (No. 2)*, 2 Fiduc. Rep. 3d 354 (O.C. Chester Co. 2012). This decision held that only the Executor of a Decedent's Estate or the Trustee of Decedent's Trust had standing to compel Decedent's Agent under a POA to Account – expressly denying standing to Decedent's widow, who was not a beneficiary of her husband's Estate, but was the beneficiary of her husband's Revocable Trust, and in all events could have taken an elective share.

I urge you to focus, however, on this language in the provision: "except as otherwise provided in the power of attorney." Here, the Legislature emphasized that planners can modify their POA documents to suit each individual situation. This includes the ability to give a third person the right to receive information about an Agent's actions during the Principal's lifetime. As one who deals regularly with the tragedies that unfold from un-checked Agents, I believe that **every estate planner should speak with every Principal client about whether they wish to give a trusted child or other person the right to receive information about their Agent's conduct during the Principal's lifetime.**

Any given client may have a valid need or preference for allowing their Agent to conduct their affairs without interference or information requests from their children or others. But by expressly authorizing others to inquire into these matters, Principals can protect themselves and their ultimate heirs. Otherwise, no one other than the Principal will ever be monitoring the Agent during the Principal's lifetime. This can become particularly worrisome if the Principal loses capacity, which, in my experience, is when things tend to go wrong.

Once the Principal loses capacity, the Agent is truly a "free Agent." That is, unless your client has empowered another person to at least look over the Agent's shoulder by reviewing financial records periodically, no one is likely to know what the Agent is doing until the Principal dies. If the Agent has, in the meantime, looted and spent the Principal's assets, then an uncollectible surcharge verdict will certainly be dissatisfying to the Estate beneficiaries whose inheritance has been plundered.

Counsel Clients on their Ability to Set Limits on Designated Overseers

To avoid creating a scenario where the designated "extra set of eyes" abuses that privilege, consider placing limits on that right in terms of timing. For example, you might suggest to your Principal client that their designated relative or trusted friend might have the right only every 6 months or even annually to receive copies of records documenting the Agent's conduct. You can use Pennsylvania's statutory language as a springboard for a conversation with your client about this critical issue.

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Help Your Clients Understand What is At Stake

To get to the heart of the issue, and to help your client understand the stakes, you might ask your client a question like this: "If you are hit by a bus tomorrow, and are rendered fully incapacitated under the law, but will live another 10 years, do you want your chosen Agent to be the only person during that decade who knows what is happening to your money and other assets? Or do you want to consider giving someone else you trust the ability to look over the Agent's shoulder, by getting bank statements, receipts, or even a formal or informal Account from the Agent ?"

In addition to authorizing a designated person to review receipts or receive some sort of accounting, planners might consider customizing the Principal's POA to expressly confer standing upon the designated third person to seek and receive a Court Accounting of the Agent's conduct during the Principal's lifetime. Without such language in the POA, I tend to think that the Orphans' Court judges will likely continue to follow existing law, which denies legal standing to anyone other than the Principal to compel an Agent to file an Account.

If a Principal chooses not to authorize a third person who can compel a formal Account during the Principal's lifetime, he or she can at least designate a third person to receive financial information, such as bank statements and receipts. With this designation in place, the trusted third party will not be without a remedy if the information received is questionable or not received at all. Indeed, if the Agent of a legally incapacitated person fails to produce the required information or produces incomplete or otherwise "shady" information, then the Principal's designated third person would have a solid basis for filing a guardianship action. Among traditional oppositions to guardianship petitions is that the alleged incapacitated person previously identified an Agent, who steps up in Court as the proposed Guardian. But if that Agent has already proven that he is incapable or unwilling to provide essential information about his conduct as Agent, then he would seem to be ill-suited to serve as Guardian.

If you help your clients understand the stakes when they name Agents, and establish a logical and fair protocol for the periodic oversight of the Agent by another trusted person, then many of your Principal clients might well want their Agents to "account" periodically to that trusted person. Agents unwilling or unable to provide the requisite level of detail of their actions and expenditures on a regular basis should not be Agents at all. **By including language in the Powers of Attorney you draft for Principal clients that ensures one or more trusted persons will receive information about their Agent's actions, you will help to spare many families significant heartache, disappointment, financial loss and, of course, litigation.**

Speak Directly With the Agent… As the Principal's Lawyer

My sense is that lawyers who draft Powers of Attorney for Principals do not speak much, if ever, to their Principals' designated Agents. Ideally, drafters would hold a meeting or a conference call with both the Principal and the Agent to speak about the terms of the POA, the law's requirements as to Agents, and especially about the Principal's expectations for how the Agent will act under the POA. That conversation may clarify ambiguities in the POA or highlight language in it that should be more specific, to align with the Principal's expectations.

In that conversation with the Agent, it would be worthwhile to discuss the Agent's duties, and the importance of keeping records. Although 20 Pa. C.S. § 5601.3(b) allows a Principal to waive that requirement, along with various other so-called "waivable duties," you should never allow your Principal client to waive her Agent's obligation to maintain complete, contemporaneous and meticulous records of the Agent's conduct/transactions entered into with the Principal's funds.

I have heard lawyers opine that meeting with the Agent adds unnecessary expense to the estate planning process, especially when many sophisticated clients believe they have a solid grasp on how the POA works. They sometimes also note that the required statutory "Important Notice" language signed by the Principal and the Agent, which warns each of the importance and risks of granting the Agent the extraordinary powers contained in the document, essentially says it all. See 20 Pa. C.S. § 5601(c). By formally discussing the risks and consequences of Agent misconduct with both the Principal and the Agent as a routine part of your drafting process, however, you can truly drive home the message and avoid the risk that your client or the Agent are simply "signing the form where asked."

Related to this issue, I note that estate planners should not fear that by speaking with your Principal client's proposed Agent, then the Agent thereby becomes "your client." You can and should clearly state during the meeting that (1) you do not represent the Agent, and in fact only represent the Principal, and (2) you believe it is important for Agents to understand their legal obligations and the fact that if they violate those obligations, then severe repercussions may follow. **By making it your standard practice to meet or speak with each Principal client's chosen Agent before the Agent begins acting and to designate an "extra set of**

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eyes" to periodically review the Agent's conduct, then you can help your clients prevent financial abuse by their Agents.

Mr. Holman is a partner at the law firm of Smith Kane Holman, LLC, with offices in Malvern and Philadelphia. He limits his practice to fiduciary and commercial litigation. He lectures frequently for the Pennsylvania Bar Institute and others on fiduciary litigation topics. He recently finished a three year term as an elected member of the Executive Committee of the Philadelphia Bar Association's Probate and Trust Law Section, and is now the Philadelphia Probate Section Executive Committee's Liaison to the Board of Governors of the Philadelphia Bar Association. He has been recognized from 2013 through 2017 by the "Best Lawyers in America" (a Woodward/White, Inc. publication) in the field of fiduciary litigation, and has been recognized as a "Super Lawyer" in 2016 and 2017 in the field of estate and trust litigation.

Footnote:
1 Many thanks to my associate, Daniel R. Boose, Esquire, for his assistance with this article.

Exit Planning: The Reality Check

Frank Spezzano

What is my reality? Today. As of this moment.

This is the Question that every owner needs to answer at some point during their business endeavors. Where am I today? What am I doing? Where am I going? How long will this last for me? How long will I continue?

In the first article of this series (Philadelphia Estate Planning Council Winter 2014-2015 Newsletter), we introduced the idea of the necessity of creating an Exit Plan and then created a detailed outline of the various components and steps in the process.

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Throughout the article the Process was the key take away, the underlying bedrock of the discussion, the specific point emphasized and driven home. In this installment we will lay out when and how the Process might begin.

At some point the owner asks a series of questions which all boil down to when do I stop and, regardless of when stopping, how do I stop. There is that realization that now or soon might be the time.

This is the precise moment to do a Value Gap Analysis.

Value Gap Analysis

The Value Gap Analysis determines if the owner can exit the business or change the role played in the business while moving on to his or her desired lifestyle and other endeavors. The key component of this gap analysis is a clear vision of what life will and should be like in the ensuing years to come. Thought needs to be given to current and future health, probable longevity, residence and tax locations, other homes, travels, family responsibilities and, not to be ignored, passions. Other items not to be ignored are current lingering financial and familial messes which would be better handled sooner rather than later to avoid unforeseen distasteful and costly problems in the future. Based on this clear vision, a current annual cost and any necessary one time lump sum costs can be approximated and translated into a value which will drive the necessary income and leave behind whatever inheritances are desired for the family.

This calculated value can result in a simplistic amount of principal to be invested developing sufficient income to afford the vision and still leave behind whatever amounts may be desired for heirs. This value can also be calculated on a more rigorous basis by using the present value of an increasing annuity with adjustments for inflation, taxes, income derived from all other outside sources such as Social Security benefits, rents, expected inheritances, the illiquidity of certain assets and inheritances desired for heirs.

Once this value is obtained, a comparison can be made between what the owner has currently saved outside the business and what is needed based on the calculation above. The difference is often an eye opener but in some instances happily not. This difference is the Gap that can be made up by remaining in the business and continuing to develop savings or simply selling the business. That is if the business can command the necessary sales price. This prompts the question, what is the business worth.

Value

However the calculation for value is done, the actual number derived as proven by the sale of the business is ultimately the result of two seemingly non numerical variables, want and need.

Most texts will list three main ways to value a business.

Synergistic Value. This is what a competitor or roll up operation may be willing to pay in order to fold the business into an existing similar business, eliminate a competitor or produce economies of scale.

Investment Value. This is what a financial investor, such as a private equity firm, may be willing to pay in order to derive income or build the business and increase the key dashboard indicators in order to sell for a much higher value in the future.

Fair Market Value. This is what a willing buyer and seller free of constraints and pressures would agree to in order to transact the exchange of the business. This is commonly discussed when drafting buy sell agreements.

There is a fourth value not often cited as a value in the texts but is nevertheless commonly cited by owners. That is…

Value to the Owner. This is what the owner wants and needs to duplicate the lifestyle and also to assuage the ego. This value is the benchmark typically used by the owner when evaluating seemingly reasonable offers to buy the business.

For all intents and purposes, the fair market value is the value to use in our discussion. It is a useful benchmark, easily defensible and a good comparison point if a potential buyer materializes who may be either a synergistic or investment buyer. It is also a useful realistic pricing scenario for discussing intra- family transfers. With this value, the owner can now answer the question, What is My Reality?

Reality Check

What type of owner am I today? Which description fits?

Sell now at the highest price. I need the money and I need to go.

Stay and grow the business. I need to increase my personal savings and grow the value of the business.

Sell. I have sufficient personal investments and am ready to **move on** outside the business.

Stay. I have sufficient personal investments and want to **continue working.**

Determining what type of owner I am today is the key to proceeding along with the Process and the direction the process will take.

The Process for the Specific Type of Owner

Each type of owner will enjoy or be harnessed to a specific time frame and list of tasks to be handled. However a general list for all owners selling - asset or

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stock sale - or merging businesses is very similar. All sellers will have to produce for the buyer good records and documents which are neat, clean, clear and current. These will include accounting records, your typical Profit and Loss Statement (P&L's) and Balance Sheets for several years, loan documents, tax returns – both state and federal and in particular those returns regarding sales tax and so on. A clear enumeration and listing of add backs will also need to be produced. Also needed to be presented will be good corporate books and records , non-competes and non-disclosure agreements, compensation agreements, employee and benefit manuals, procedures and policies manuals and anything else which may be specific to the business. Also to be divulged will be a list of customers and clients, any financial measurements and data pertaining to those customers and clients along with product and fee pricing information.

For Sell Now, Need Money

For those owners who need to sell now and are in need of money and a quick exit for whatever reasons, the time frame is very short indeed. The items mentioned in the preceding paragraph will need to be produced. Note that sometimes sellers get sloppy and ignore a key item that needs to be handled, namely having a good solid non disclosure document signed by all those involved in the possible transaction. This is absolutely key. Not all transactions make it through the due diligence process and to the closing table. As is said haste makes waste and if a possible sale to a larger competitor falls through, the failed outcome can be disastrous if proper steps and documents were not secured. For these owners, selling is not an easy task for them or their advisors. Everyone needs to focus and work hard and with a great deal of coordination. A good strong respected team leader is absolutely necessary, especially in this case when all the players in the transaction will be moving quickly. This team leader task will be to keep all the advisors on track and communicating with one another.

For Stay and Grow

For those owners who need to continue staying in the business and growing it, the time frame is less stressful than our pressured need-to-sell owner. All the items mentioned for our seller above need to be created and available for the future. A reasonable time frame to accomplish the above items mentioned might be six months. Once the six month clean-up is accomplished, the focus can shift to growing the business in the most profitable direction for the time frame most appropriate for the seller's age, situation in life, health and other considerations. Some items to be considered to be improved and enhanced are:

- Cash flow and collections
- Reasons for selling
- The business position in the industry and the industry's short and long term outlook
- Diversification of the customer and client base
- Retention of customers and clients and their profitability and cross selling potential
- The business niche
- Growth opportunities
- Developing a turnkey business - less dependent on the owners everyday involvement
- Proprietary products and intellectual property
- Skilled, trained and devoted employees in sync with the development of the business

For Well Heeled and Ready to Go

For those owners who are sufficiently well heeled and ready to move on outside the business, the process can build on all the items mentioned for our sellers previously. It is important not to short cut any of these listed items. As for the owner specifically, more emphasis can be devoted to the personal aspects of the owner's future life and other business interests, if any. This emphasis should start to help shape the owner's time and activities after moving on from the business sale transaction. The business owner needs to be cognizant of the fact that once the transaction is completed; there may be a sense of loss, a feeling of importance, and the other common feelings and emotions that arise when something which has been so engrossing and all consuming is now absent. Of course all the possible and probable negativity will be hopefully neutralized with a quick glance at the personal checkbook. Nevertheless, time needs to be spent developing a picture and vision for daily life and future endeavors after the transaction is completed. This is terribly important.

For Well Heeled and Continuing

For those owners who are sufficiently well heeled and wish to remain in the business, the task and list of items to handle is similar to those owners who are well heeled and ready to go. At some point the owner will have to exit the business regardless of the desire to remain involved. Age and health will eventually force the issue. So while there is sufficient time, a solid comprehensive exit strategy can be developed while the owner is involved in pushing the business forward. Personality quirks aside, this can be the easiest owner to engage. A reasonable time frame can be developed to employ all the skills and tools utilized to enhance the value of the business

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and the personal wealth and affairs of the owner while creating a clear and manageable exit and succession plan.

Creating the Exit Plan

By this point, the owner and advisor have laid down a strong foundation to use in building a solid well thought out Exit Plan. The Value Gap Analysis and the determination of the actual current Value of the business give a clear answer to the actual affordability of exiting the business. The classification and recognition of the specific type of owner the client may be provides the context in which to think through and craft a Plan. At this point the owner now has enough clarity to answer The Question. The owner now knows how to answer the questions first raised in the opening paragraph. With these answers and insights the Process can now move further along to developing the most favorable exit model, options and timeframes.

Frank A. Spezzano, CLU, ChFC, MSFS, President, IRUS Advisory – The firm and Frank provide personalized strategies and tactics to enhance all aspects of your business and personal lifecycles.

October Luncheon Program

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M. Read Moore (speaker), Huldah Robertson (President) and Sam Freeman (sponsor)

The Philadelphia Estate Planning Council Welcomes New Members!

September, October and November, 2016

Mark Alvino	Pine Hill Valuation Services
Joann Gamble	BNY Mellon
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Marygrace Gilmore	Philadelphia Museum of Art
Jennifer Harding	Barilotti Wealth Strategies
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Bonnie Richards	UBS Wealth Management
Karen Robinson	Geneva Global
Jason Susini	Glenmede Trust Company, N.A.
Jason Thompson	PNC Wealth Management
Brad Weingart	Wilmington Trust

Welcome Back Party

The annual Welcome Back Party was held on September 22, 2016 at Top of the Tower. Attendees enjoyed a networking cocktail reception and food overlooking the city of Philadelphia at sunset. Thank you to Stedmark Partners at Janney Montgomery Scott for sponsoring this event!

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Sheila Gorman, Peggy Robus, Andrea Brockman and Amy Parenti

Christopher Borden, Kevin Manning and William Cotter

Shane Johnson and J.R. Burke

Huldah Robertson and Chuck Sterne

Networking on the outdoor balcony at sunset

Eileen Dougherty and Steven Mignogna

Annual Holiday Celebration

The 2016 Holiday Celebration was held at the beautiful Union Trust venue located on Chestnut Street. Over 100 attendees enjoyed an open bar, food stations and hors d'oeuvres. Monetary donations were collected on behalf of the Children's Hospital of Philadelphia Reach Out and Read program. Thank you to AIG and EisnerAmper for sponsoring this event!

Scott Isdaner, Jordon Rosen, Huldah Robertson, Doug Simon and Richard Schwartz proudly display the 5-Star Council banner awarded by the National Association of Estate Planners & Councils.

Laura Weiner, Huldah Robertson, Bill Haines and Jeannette Leighton

Joel Luber, Steven Leshner and Lee Zeplowitz

View from above the PEPC Holiday Celebration

Nina Stryker, Kate Rada, Sharon Greenberg and Peggy Robus

Jordon Rosen, Tom Forrest and Michael Friedberg

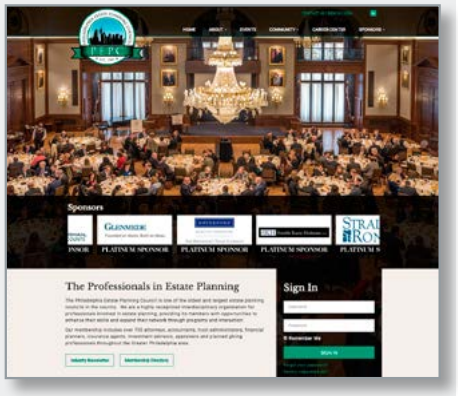
Mark Your Calendar

Tuesday, January 17, 2017
Topic: "The Past Year's Most Significant, Curious, or Downright Fascinating Fiduciary Cases"
Speaker: Dana G. Fitzimons, Jr.
Bessemer Trust
Atlanta, GA
Sponsor: Bessemer Trust

Tuesday, February 21, 2017
Topic: "GRAT to Great: Efficient Wealth Transfer with Grantor Retained Annuity Trusts"
Speaker: Tara Thompson Popernik, CFA, CFP®
Bernstein Global Wealth Management
New York, NY
Sponsor: Bernstein Global Wealth Management

Tuesday, March 21, 2017
Topic: "Estate and Financial Planning for Chronic Illness"
Speaker: Martin M. Shenkman
Shenkman Law
Fort Lee, NJ
Sponsor: The Law Offices of Peter L. Klenk & Associates

Be sure to visit the new PEPC website!



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