



# WRN Newswire

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The *WRNewswire* is created exclusively for AALU Members by insurance experts led by Steve Leimberg, Lawrence Brody and Linas Sudzius. *WRNewswire* #15.04.15 was written by Howard M. Zaritsky, Esquire, Rapidan, Virginia. Howard and Steve Leimberg are the authors of the treatise entitled, [TAX PLANNING WITH LIFE INSURANCE: ANALYSIS AND FORMS: 2<sup>ND</sup> EDITION](#).

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**TOPIC: Annual Exclusion Allowed for 60 *Crummey* Beneficiaries, Despite No-Contest and Mandatory Arbitration Clauses**

**CITATION:** [Mikel v. Commissioner](#), T.C. Memo. 2015-64 (April 6, 2015); [Crummey v. Commissioner](#), 397 F.2d 82 (9th Cir. 1968); [Estate of Cristofani v. Commissioner](#), 97 T.C. 74 (1991); [Chief Counsel Advice 201208026](#).

**SUMMARY:** The Tax Court held that gifts to an irrevocable trust qualified for the gift tax annual exclusion because each of the trust's 60 beneficiaries had *Crummey* withdrawal powers, and *despite* the fact that the trust included both (1) no-contest clauses disinheriting a beneficiary who questioned a trustee's discretionary actions, and (2) a requirement that all disputes be submitted to review by a religious court.

**RELEVANCE:** This is a direct rejection of the contrary position taken by the IRS in Chief Counsel Advice 201208026, and it reinforces the utility of *Crummey* powers to qualify gifts to an irrevocable life insurance trust or other irrevocable trust for the gift tax annual exclusion.

It is noteworthy that there were 60 beneficiaries, and that the trustees had very broad discretion in their exercise of a power to distribute for health, education, maintenance, or support, and to help defray reasonable wedding costs, the costs of purchasing a residence, and the costs of entering a trade or business. With 60 beneficiaries, the interest of each beneficiary was relatively uncertain. However, the court did not question that the *Crummey* power created a present interest that qualified for the gift tax annual exclusion.

In drafting irrevocable life insurance trusts, no-contest clauses are often popular, because they make the trustee's job much easier by discouraging expensive, annoying, and time-consuming litigation. In this case, the clause was construed not to apply to the beneficiaries' ability to enforce the *Crummey* powers. However, drafters should consider expressly including in any no-contest clause used in a *Crummey* trust language such as the following:

No action to enforce the right of a beneficiary to withdraw a proportionate share of each contribution to the trust, as authorized under the article entitled "Annual Withdrawal Powers,"

shall be deemed a contest to which this article applies, and no such attempt shall result in the elimination of the trust interests of the beneficiary making such attempt.

It is also noteworthy that the court held that the provision in the trust requiring that disputes be adjudicated by a religious court did not alter the donor's gifts eligibility for the gift tax annual exclusion. The court noted that: (a) the religious court was required by the trust to interpret the trust in accordance with applicable state law and to give the beneficiaries those rights available under state law; and (b) a beneficiary who wished to do so could bring an action in state court, subject to the application of the no-contest clause.

Not many clients will prefer that matters be submitted to a religious court, but many want to require that disputes be submitted to binding arbitration. A drafter who wants to require binding arbitration should be aware that most state courts have held such clauses unenforceable when used in trusts. If the trust is controlled by the law of a state in which such clauses are enforceable or in which they have not yet been subject to judicial scrutiny, the trust language should state expressly that the arbitrator must apply the same state law that would be applied by a state court reviewing the same dispute, and give the beneficiaries the same rights that they would have had under applicable state law.

**FACTS:** Israel and Erna Mikel created and funded an irrevocable trust, the IEM Family Trust, for the benefit of their children, descendants, and the spouses of their children and descendants. In total, there were 60 beneficiaries, including many who were minors. The trust gave each beneficiary a *Crummey* withdrawal power, and the trustees gave the beneficiaries written notice of the gifts and their withdrawal rights. The trust provided that, if a beneficiary made a withdrawal demand, the trustee, must immediately distribute the demanded assets outright and free of trust. The trustee gave each beneficiary written notice of the gift. The donors claimed \$720,000 of annual exclusions for the gifts made in the first year.

Otherwise, the trustees had discretion to distribute income and principal to and among the beneficiaries for their health, education, maintenance, or support, and to help defray reasonable wedding costs, the costs of purchasing a residence, and the costs of entering a trade or business. The trustees were given very broad discretion in exercising these discretions.

The trust also included a clause requiring that any disputes regarding the interpretation of the dispositive provisions of the trust must be "submitted to arbitration before a panel consisting of three persons of the Orthodox Jewish faith," known as a *Beth Din*. The panel was directed to "enforce the provisions of this Declaration \* \* \* and give any party the rights he is entitled to under New York law."

The trust also included a no-contest clause that revoked the share of any beneficiary who takes any legal action to "oppose the distribution of the Trust Estate, or . . . [to contest] any distribution set forth in this Trust. . ."

The IRS disallowed the gift tax annual exclusion.

The Tax Court held for the taxpayers, finding that neither the no-contest clause nor the mandatory arbitration clause deprived the beneficiaries of their present interest under the *Crummey* power. The court reviewed the history of *Crummey* powers, and summarized the key rule from the original *Crummey* case was "all that is necessary is to find that the demand could not be [legally] resisted."

The court noted that the no-contest clause did not apply to the *Crummey* power, because that was not a discretionary action of the trustees. The court agreed that beneficiaries might be reluctant to contest *other* trustee decisions because of the no-contest clause—but they would not be prevented from enforcing their right to withdraw their share of each gift.

The court also noted that the religious panel was required to apply New York law and to give the beneficiaries the same rights they would have under New York law. Also, a beneficiary could still file a case in court, though that could trigger the no-contest clause if the dispute did not involve enforcement of the *Crummey* power.

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