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TO: OUR CLIENTS AND FRIENDS  
FROM: JACKSON M. PAYNE  
DATE: NOVEMBER 1, 2011  
RE: FINANCIAL STRATEGIES FOR YOUR LIVES AND BUSINESSES

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**BUY DEPRECIABLE PROPERTY AND PLACE IT IN SERVICE  
THIS YEAR TO LOCK IN 100% BONUS FIRST-YEAR DEPRECIATION**

The 100% bonus depreciation allowance under Code Sec. 168(k) applies only for qualified property acquired and placed in service after September 8, 2010 and before January 1, 2012. For qualified property acquired and placed in service after December 31, 2011 and before January 1, 2013, the first-year bonus depreciation allowance is scheduled to drop to 50%. Thus, enterprises planning to purchase new depreciable property this year or the next should try to accelerate their buying plans, if doing so makes sound business sense.

The 100% first-year bonus depreciation deduction is permitted without any proration based on the length of time that an asset is in service during the tax year. As a result, a 100% first-year writeoff is available even if qualifying assets are in service for only a few days in 2011.

For example, Widget, Inc., a calendar-year business, needs to buy an additional \$500,000 of new five-year MACRS property. It is not eligible for expensing. If Widget makes the purchase before January 1, 2012, and places the property in service before that date, it may write off the entire \$500,000 cost in 2011. If it waits to buy the property and place it in service until 2012, it may only claim a first-year depreciation allowance of \$300,000 [ $(\$500,000 \times .50 = \$250,000$  bonus first-year allowance) +  $(\$500,000 - \$250,000 \times .20$  table percentage for 5-year MACRS property = \$50,000)].

However, accelerating a purchase into 2011 may not always be a good idea. For example, it may not produce good results for a taxpayer that has an about-to-expire net operating loss.

**TRUST MODIFICATION PREVENTS DRAFTING ERROR  
FROM RESULTING IN COSTLY TRANSFER TAX**

**PLR 201132017**

IRS has given its blessing to a court-approved modification to a trust containing a drafting error that could have triggered significant transfer tax to the surviving spouse. Specifically, IRS ruled that, as a result of the modification, the surviving spouse will not be considered (1) to possess a general power of appointment over the trust at his death, (2) to have released a power during his life, or (3) to have made a deemed gift of an interest in the trust under Code Sec. 2501.

Under Code Sec. 2041(a)(2), the gross estate includes property over which the decedent possessed at the time of death a general power of appointment created after October 21, 1942. For this purpose, a general power of appointment is a power exercisable in favor of the decedent, his estate, his creditors, or the creditors of his estate.

The exercise or release of a general power of appointment created after October 21, 1942, is deemed a transfer of property by the individual possessing such power.

Code Sec. 2501(a) imposes a gift tax for each calendar year on the transfer of property by gift during the year by an individual.

In this private letter ruling, Husband and Wife (Trustors) created an inter vivos revocable trust (Trust). They were Trust's original trustees, and the Trust provided that upon the death of the first Trustor to die, the trust assets were to be divided among the Marital Trust, the By-Pass Trust, and the Survivor's Trust.

Trust Article IV, Section 4.01 provided that on the death of the Surviving Spouse, the Trustee was to pay from the trust estate the Surviving Spouse's debts, expenses, and death taxes due by reason of the Surviving Spouse's death and charge them against property in the By-Pass Trust.

Wife died, survived by Husband and three children. Husband was appointed executor of Wife's estate and is the trustee of the Survivor's Trust, the By-Pass Trust, and the Marital Trust.

Attorney 1 drafted Trust. After Wife's death, Attorney 2 was consulted and discovered an error in Article IV, Section 4.01. The error was that the language charging the Surviving Spouse's debts, expenses, and death taxes against property in the By-Pass Trust should have referred to the Survivor's Trust.

In affidavits, Husband and Attorney 1 represented that it was the Husband and Wife's intent as Trustors to minimize estate taxes, including maximizing the use of the unified credit. Accordingly, the By-Pass Trust should have been drafted to ensure that the assets in the By-Pass trust would not be included in the Surviving Spouse's gross estate and the Surviving Spouse would not have any property or

other rights to the trust property that would cause the assets to be included in the Surviving Spouse's gross estate upon Surviving Spouse's death.

In order to correct the error in the Trust and to accurately reflect the intent of the Trustors, Husband, as the Trustee of Trust, filed a petition with a state court seeking authorization to modify Trust retroactive to the trust's inception. Husband, as the surviving Trustee, stated that it was at all times his intent and desire that the assets of the By-Pass Trust be administered so as to avoid taxation at Surviving Spouse's death. He advanced various arguments that the reference to the By-Pass Trust was a scrivener's error. The state court agreed and modified the trust in the manner sought.

IRS observed that the documentation submitted by Husband strongly indicated that he and his wife did not intend to have any control over the assets held in the By-Pass Trust, and that the provision in Section 4.01 of Trust to charge Surviving Spouse's debts, expenses and death taxes from the By-Pass Trust was the result of a scrivener's error. In reforming the By-Pass Trust, the state court found that the modification of Trust was an equitable reformation of Trust under common law and a state statute providing that when through fraud or mutual mistake of the parties, or a mistake of one party, a written contract does not truly express the intention of the parties, it may be revised on the application of the party aggrieved.

Consequently, IRS concluded that the state court order modifying the trust instrument based on a scrivener's error was consistent with applicable state law that would be applied by the highest court of that state. IRS found that section 4.01 of Trust, as modified by the court order, did not provide Surviving Spouse with a general power of appointment under Code Sec. 2041(b) over the assets of the By-Pass Trust. Therefore, IRS concluded that the value of the assets in the By-Pass Trust will not be included in Surviving Spouse's gross estate under Code Sec. 2041(a)(2) upon his death.

IRS also concluded that the modification will not (1) constitute the exercise or release of a general power of appointment by Surviving Spouse within the meaning of Code Sec. 2514(b) , or (2) be treated as a deemed transfer of an interest in Trust by Surviving Spouse for gift tax purposes under Code Sec. 2501.

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