FAMILY OFFICE TAX ROUNDTABLE

McDermott Will & Emery

October 21, 2020

mwe.com

PRESERVING PRIVILEGES IN FAMILY OFFICES

SPEAKERS

JENNY JOHNSON WARE
Partner

ATTORNEY-CLIENT PRIVILEGE

- To be protected by attorney-client privilege, a communication must be:
  - Confidential
  - Between client and legal advisor
  - For purpose of giving or receiving legal advice
- *Key considerations for family offices:*
  - Waiver
  - Extension to agent of attorney (Kovel) or agent of client
  - Extension to others with common interests and their attorneys and agents
  - Differentiating legal advice from other advice
  - Application to fiduciaries

TAX PRACTITIONER PRIVILEGE

- To be protected by the tax practitioner privilege in IRC § 7525, a communication must be
  - Between a taxpayer and a federally authorized tax practitioner
  - Privileged if it were between a taxpayer and an attorney
  - Related to tax advice other than tax shelter advice
  - Sought in a non-criminal federal tax proceeding
- *Key considerations for family offices:*
  - Limited to practitioners authorized to practice before IRS
  - Limited to US federal civil tax proceedings
  - State accountant-client privileges differ and do not apply in federal proceedings

ATTORNEY WORK PRODUCT DOCTRINE

- To be protected by attorney work product doctrine, materials must be
  - Prepared by or at the direction of an attorney
  - In anticipation of litigation or for use in current litigation
- *Key considerations for family offices:*
  - Anticipation of litigation must be objectively reasonable
  - Triggers obligation to preserve evidence
  - Stronger protection for opinion work product

PRIVILEGE AGAINST SELF-INCRIMINATION

- For the 5th Amendment privilege against self-incrimination to apply, the anticipated communication must be
  - Testimonial
  - Incriminating
  - Compelled
- *Key considerations for family offices:*
  - Act of producing documents may be testimonial in certain circumstances
  - Only individuals, not collective entities, possess 5th Amendment rights
  - Invocation is complex judgment call with potential negative consequences

SPOUSAL COMMUNICATIONS PRIVILEGE

- To be protected by spousal communications privilege, a communication must be
  - Confidential
  - Made during marriage
- Either spouse may invoke privilege, even after divorce
- *Key considerations for family offices:*
  - Must be expectation of confidentiality
  - Destroyed by presence of anyone outside marriage

SPOUSAL TESTIMONIAL PRIVILEGE

- For the spousal testimonial privilege to apply
  - The proceeding must be criminal
  - The non-defendant spouse must invoke
  - The marriage must exist at time testimony is sought
    - Note that numerous states have repealed this privilege
- *Key considerations for family offices:*
  - Do not confuse testimonial privilege and communications privilege

PHYSICIAN-PATIENT PRIVILEGE

- For a physician-patient privilege to apply, in most states, there must be
  - A confidential physician-patient relationship
  - During which the physician acquired information
  - Necessary for medical diagnosis or treatment
- *Key considerations for family offices:*
  - Intersection with HIPAA
  - Scope of consent / waiver
  - Common exception when mental capacity / validity of will is disputed

CROSS-BORDER PRIVILEGE ISSUES

- Privilege a function of each country's laws
  - Relevant factors
    - Location of attorney, client, pending case, relevant documents
    - Where attorney is licensed
    - In-house or outside counsel
- *Key considerations for family offices:*
  - Know law of relevant jurisdictions
  - Border searches of devices – laptop, thumb drive, phone
  - Disclosure in one jurisdiction, voluntary or involuntary, may waive in others

IRS ATTACK ON PRIVILEGE

- ***Estate of Morrissette***, Tax Court Docket No. 4415-14
  - Estate argued bona fide sale exception to §§ 2036, 2038 and bona fide business arrangement exception to § 2703
  - IRS moved to compel production of estate planning attorneys' legal files
    - IRS argued waiver of privilege resulted from merely asserting exception
    - Estate asserted no reliance on advice of counsel, so no waiver
    - Court rejected broad waiver
  - IRS moved to compel production of communications shared with insurance broker and appraisal firm
    - Estate asserted attorney work product
    - Court required disclosure because broker working independently

BEST PRACTICES

- Educate
  - Describe benefits and scope to privilege-holders and their advisors
  - Explain waiver with examples
- Establish good habits
  - Clarify identity of client
  - Limit participants in calls and meetings
  - Identify privileged documents with headers or subject lines
  - Segregate legal advice into communications separate from business advice or return preparation
  - **DO NOT FORWARD** outside circle of privilege

BEST PRACTICES

- Maintain documents appropriately
  - Consistent with expectation of confidentiality
  - Segregate return preparation work papers from privileged advice
- Understand limitations of ***Kovel***
  - Professional assisting attorney in rendering legal advice
  - Engaged and directed and by attorney
  - Accountants – No protection for preparation of returns intended for filing
  - Appraisers – Consider intended use

BEST PRACTICES

- Keep wide audience in mind when future waiver may be advantageous
  - Reliance on advice of counsel
  - Reasonable cause and good faith defense to penalties
  - § 2036 and § 2038 exception for bona fide sale for full and adequate consideration
  - § 2703 exception for bona fide business arrangement, not a device to transfer property to members of decedent’s family for less than full or adequate consideration, terms comparable to arm’s-length transaction
  - Other situations where attorney’s records may be best evidence of intent

BEST PRACTICES

- Produce documents only after due consideration of privilege issues and careful review
  - Consider scope and impact of potential subject matter waiver
  - Weigh pros and cons of positions that trigger waiver
  - Review descriptions in bills and invoices
  - Consider all relevant privileges, not just attorney-client
  - Remember that client controls attorney-client privilege, but attorney controls attorney work product

THANK YOU