

# Estate Planning for the Rest of Us

(For Estates Under \$10 Million)

*Presented To:*

Estate Planning Council, Inc. of Nassau County

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*Presented by:*

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# About Jordan . . .

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Jordon N. Rosen, CPA, MST, AEP® is a Director and shareholder in the Wilmington, Delaware CPA firm of Belfint, Lyons & Shuman, where he heads the firm's estate and trust practice. Jordon also provides tax consulting and compliance services to the firm's higher net worth clients and business owners. He is the Past President of the National Association of Estate Planners and Councils (NAEPC) and has served as president of the Delaware Estate Planning Council and the Chester County, PA Estate Planning Council. Mr. Rosen is also a member and past chair of the Delaware State Chamber of Commerce tax committee, is a member of the AICPA Trust, Estate and Gift Tax Technical Resource Panel, and is a member of the editorial board of Thomson Reuters Focus publication.

Jordon is a licensed CPA in Delaware and Pennsylvania and is a member of the Pennsylvania Institute of CPAs, Delaware Society of CPAs and the AICPA Tax Section. He also holds the designation of Accredited Estate Planner® and has been recognized as a 5-Star Wealth Manager by Philadelphia Magazine and Delaware Today.

Mr. Rosen is a frequently sought out speaker both locally and nationally on tax planning and related issues and has published more than 100 articles. He has been a frequent television and radio guest and a past host of Money Talk on 1450-WILM. He received his undergraduate degree in Accounting from Temple University and his Master's degree in Taxation from Widener University.

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# Taxpayers Are Re-Thinking the Need for Planning

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- Fewer are subject to the Federal Estate Tax since the exemption is so high
- Many states (i.e. Delaware) follow the Federal rules, thus eliminating any state death tax

However . . .

- Non-taxable estates today may become taxable in the future
  - Assets grow (naturally or by inheritance)
  - Laws change
  - Some people actually win the lottery
- As time passes and life events occur, most estate plans become hopelessly out of date

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# Excuses We Hear Why Clients Don't Think They Need To Plan:

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- If there are no taxes due, what is the need for planning?
- I'm too young
- All of my property is jointly held with my spouse
- Estate planning is only for the rich folks
- It's too expensive
- We had our wills drawn up when we were married (probably more than 15 or 20 years ago!)
- I don't want to think about it

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# Reasons Why Estate Planning is Critical for the Modest Estate Owner

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- Several States (i.e. MD and NJ) have estate exclusions well below the Federal level
- Several states (i.e. PA) impose a state inheritance tax
- Need to provide for surviving spouse
- Special needs family member
- Care for minor children
- Second (or third, or fourth) marriage
- Asset protection (predators and spend thrifts)
- Divorce planning

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# Reasons Why Estate Planning is Critical for the Modest Estate Owner – Continued

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- Closely held business/farming operations
- Provide for future education needs
- Charitable intent
- Family dynamics (potential divorce, drug addiction)
- Valuation issues
- Disposition of tangible personal property
- Dictate how YOU want to dispose of your estate
- Planning for pets

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# Conventional Planning Prior to 2011

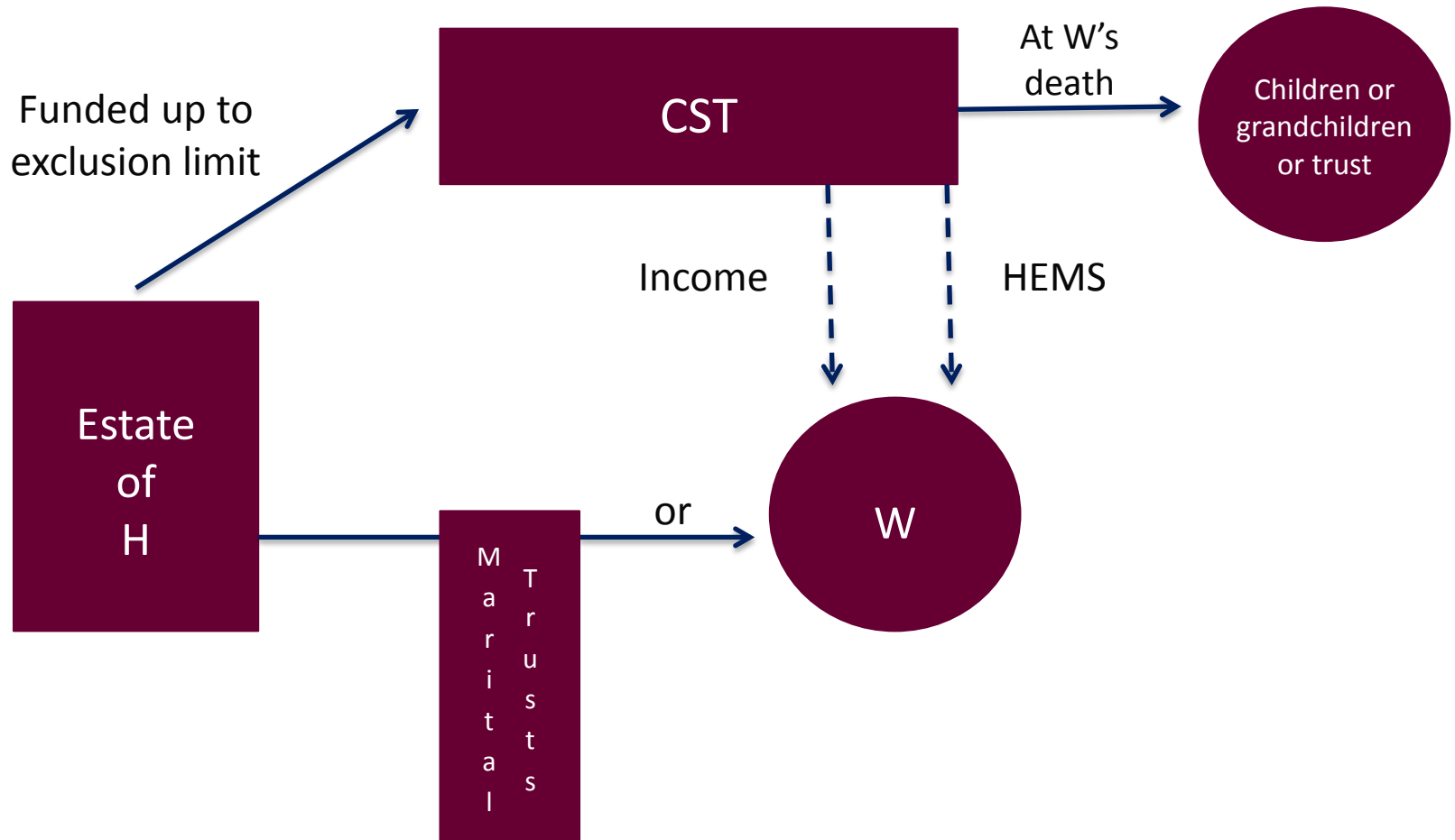
- Tried to equalize estates
  - Didn't always know who would die first
  - Some assets could not be re-titled
  - Re-titling in separate names could create creditor issues
- Each spouse created identical wills/trusts
  - Creating a credit-shelter trust
  - Creating a marital trust



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# Conventional Planning Prior to 2011



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# Conventional Planning Challenges

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- Not planning at all and wasting the first-to-die's estate exclusion
- Not being able to fully fund (balance) each spouse's CST at the first death
- Not requiring that the CST be funded or leaving the decision to the surviving spouse



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# With no Planning -Wasting the Estate Tax Exclusion Amount

	H	W
Total Estate	\$5,000,000	\$5,000,000
Marital Deduction at H's Death	(5,000,000)	5,000,000
H's Taxable Estate	\$-0-	10,000,000
W's Estate Exclusion at W's Death		(5,000,000)
W's Taxable Estate		\$5,000,000

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# IRC Section 2010(c)(4)

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## Deceased Spousal Unused Exclusion (DSUE) amount

- TRA 2010 – for decedents dying on or after 1/1/2011
- Estate and gift tax exclusions were reunited at the hip (“use it now” or “use it later”)
- “Portability” became permanent with the 2012 Tax Act
- Final regulation became effective on June 12, 2015



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# Applicable Exclusion Amount

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(Form 706, Line 9a)		Basic Exclusion Amount* (\$5,450,000 in 2016)
(Form 706, Line 9b)	+	DSUE**
(Form 706, Line 9c)		AEA

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\* \$5,000,000 in 2011 and indexed for inflation

\*\* Not indexed for inflation – it is frozen at date of death

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# DSUE = Lesser of

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- A. The basic exclusion amount, or
- B. The excess of
  - I. The applicable exclusion amount of the last such deceased spouse of such surviving spouse, over
  - II. The amount with respect to which the tentative tax is determined under Section 2001(b)(1) on the estate of such deceased spouse

## IRC Section 2010 (c)(4)

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	H	W
Total Estate	\$5,000,000	\$5,000,000
H's prior taxable gifts and bequest to good friend Jordon Rosen	(3,000,000)	
	2,000,000	
Bequest to surviving spouse	(2,000,000)	
H's taxable estate	\$ -0-	
"Ported" to surviving spouse		2,000,000
Surviving spouse's BEA		\$7,000,000*

\*Available for future gifts/bequests

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# Generation Skipping Transfer Tax (GSTT)

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No provision in law to “port” unused GST exemption



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# Making the Portability Election

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- Not an affirmative election. A deemed election is made if a timely and complete 706 is filed with DSUE and there is a surviving spouse
- Election is made by the executor (Form 706, Part 6)
- Not available to a non-resident surviving spouse who is not a U.S. citizen, except to the extent allowable by treaty with his or her country
- Assets transferred to a QDOT – calculation is preliminary (Form 706, Part 6, Section B)

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# Making the Portability Election – Continued

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- Election is effective as of date of death
- Election is irrevocable as of the due date of Form 706
- Uncertainty of exact amount of DSUE when filing the estate tax return where the election is (deemed) made, does not negate the election; only the amount of the DSUE will change.
- SOL is extended with regard to the determination of the DSUE amount until the expiration of the SOL of the surviving spouse's estate.

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# Requirements of Return When Making Election

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- Complete and properly prepared in accordance with instructions and regulations
- Reporting values on Form 706 that is not otherwise required to be filed
  - Property subject to marital or charitable deduction—only need to report
    - Description
    - Ownership
    - Beneficiary
    - Information to establish right of estate to the deduction

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# Requirements of Return When Making Election – Continued

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- Rule does not apply to property if
  - Value needed to determine value passing to another recipient
  - Value needed to determine eligibility under Section 2032 (alternate valuation), 2032A (farm valuation), or Section 6166 (extension of time to pay tax)
  - Less than the entire interest in the property is marital or charitable deduction property
  - A partial disclaimer or partial QTIP election is made with respect to property which is marital or charitable deduction property

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# Statement Required on Form 706

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- If executor exercises due diligence to estimate FMV of the gross estate
- Executor (under current regulations) can include his/her best estimate rounded to the nearest \$250,000
- Signed under penalties of perjury
- Will be considered a complete and properly filed return

**Regulation Section 20.2010-2T(a)(7)**

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# Who is Permitted to Make (or opt-out-of) the Election?

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- Duly appointed executor or administrator of the estate
- If no duly appointed executor – a non-duly appointed executor in actual or constructive possession of any property of the decedent
- Portability election made by a non-appointed executor cannot be superseded by a contrary election by another non-appointed executor of the same estate
- What if executor and surviving spouse do not agree?
  - See Vose case (OK S.C.)

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# Late Elections

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- No relief if estate was otherwise required to file Form 706
- If filing just to elect portability
  - Section 9100 relief may be available. See PLR 201722021.
  - Rev. Proc. 2017-34 - Simplified Method for Filing for Extension of Time to File
    - Effective 6/9/17
    - 706 will be due later of 1/2/18 or 2 years after death
    - Any prior PLR applications before 6/9/17 will be disregarded
    - If estate ultimately found to be taxable – extension is void
  - Treasury hesitating to make this relief permanent for fear of executors not making the election until after the surviving spouse's death

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# Opting Out of Portability

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- ✓ the box – Form 706, Part 6, Section A
- Small estates that otherwise do not have to file Form 706, simply do not file anything
- If a return is otherwise required to be filed, the filing of a late Form 706 is considered opting-out of the portability election (Prop. Reg. Section 20.2010-2(a)(3)(ii))
- Hazards of not electing portability
  - Assets grow
  - Some people actually win the lottery
  - Get client consent in writing if they choose not to elect portability

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# Last Deceased Spouse

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- Most recently deceased person who was married to the surviving spouse at the time of that person's death
- Identity as of day of taxable gift or the date of the surviving spouse's death
- Re-marriage does not alter the designation of last deceased spouse. Surviving spouse can apply DSUE amount to future lifetime gifts
- Apply DSUE first; then own BEA
- Multiple DSUE amounts

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# How Smaller Estates Will Be Affected By

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- Basis Consistency Rules
- New Form 8971 Reporting Rules

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A pair of red boxing gloves hanging from a chain against a brick wall. The gloves are positioned on the left side of the frame, with their straps and laces visible. The background is a dark, textured brick wall.

DSUE v. CST  
or  
Income Tax v. Estate Tax

# Estate Tax vs. Income Tax Planning

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- Highest Estate Tax Rate is 40%
- Highest Marginal Personal rate is 39.6%
  - New 3.8% surtax
  - State income tax
- Since most taxpayers will not be subject to the estate tax, more focus needs to be on the income tax aspects
- Planning on an asset-by-asset basis
  - “BASIS” planning is the new normal
  - Best assets to have in your estate (i.e. Roth IRA, tax-exempt bonds)
  - Worse assets to have in your estate (i.e. traditional IRA)
- Need to consider the tax implications to the beneficiaries
- May drive which assets to spend down first

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# Providing for Surviving Spouse

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- Use of trust
  - To provide income annually for life
  - To provide principal distributions for health, maintenance, support and welfare
  - To protect assets from creditors and future spouses
- Prior wills/trusts may provide that “credit-shelter” trust be funded up to the estate tax exclusion amount
  - Unintended consequences
  - Should re-visit provisions
  - Will not provide a second basis step-up as opposed to electing portability
- QTIP – discussed later in outline

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# Advantages of CST

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- Asset protection (generally not available using DSUE)
- Appreciation exempt from surviving spouse's estate (but no step-up)
- GST protection



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# Advantages of DSUE Election

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- Get a second basis step-up at surviving spouse's death
- Ultimate Federal and state capital gains tax savings
- Lower administrative expenses
- Allows for spousal rollover of IRA/retirement plan assets
- Allows for stretch IRA for non-spousal beneficiaries
- Control/GPA (limited for retirement plan assets)
- Income subject to individual tax brackets, not condensed trust brackets
- Could save/avoid NII tax for same reason

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# Using a QTIP Trust

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- No estate tax inclusion at first death
- Included in surviving spouse's taxable estate
- Assets get a second step-up
- Control-keeps assets in family
- General asset protection
- Can get GST protection with a reverse QTIP election

Treasury and IRS provide guidance . . .

A QTIP election made under Section 2056(b)(7) will not be disregarded and treated as null and void when an executor has elected portability of the DSUE amount under Section 2010(c)(5)(A). See Rev. Proc. 2016-49.

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# Community Property

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- Each spouse owns half the property
- DSUE is not as much of an issue



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# State Death Taxes

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- DSUE (portability) is a federal concept
- States have not yet adopted portability election statutes
- May need to be creative in states where estate exclusion is less than the Federal amount
- Use of CST to protect assets up to state exclusion
- Use of Marital Trust followed by gift to children's trust by surviving spouse (could have limited benefits in states such as CT and PA)

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# Qualified Domestic Trust (QDOT)

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- Allows for marital deduction for bequeathed property passing to a surviving spouse who is not a U.S. Citizen
- Estate tax is generally imposed under Section 2056A when distributions are made from the trust
- If DSUE amount
  - Executor determines a preliminary DSUE amount
  - Decreases as Section 2056A distributions are made
  - Not available to the surviving spouse against tax on lifetime gifts since final determination of DSUE is postponed until death of surviving spouse or termination of QDOT

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# Post-Mortem Elections

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- Portability
  - Reduces need to “equalize” estates
- May need to revisit older documents
- Use of credit shelter trust for clients living in states that do not recognize portability or have a lower estate exemption
  - Must file Form 706 (Estate Tax Return) to elect portability, even if no return is otherwise needed
    - Must be on a timely filed return
  - DSUE amount not indexed for inflation
  - Provides a second basis step-up opportunity
- EE/E Bonds
  - Can elect to report accrued but unreported bond interest through date of death on final 1040
  - Future interest reported by beneficiaries

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# Post-Mortem Elections – Continued

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- QTIP election – for the second family
  - Provides income for second spouse for life
  - Remainder goes to children from first marriage
  - Value of trusts includable in second spouse's estate
- Fiscal Year of Estate
  - Calendar
  - Fiscal - no later than last day of month preceding month of death

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# Post-Mortem Elections – Continued

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- Section 645 election
  - Allows calendar year revocable trust to file as part of estate's fiscal year
  - Can defer income
  - Saves administrative fees
  - Limited life
  - Made with timely filed return
- Disclaimers
- GSTT

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# Annual Gifts

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- \$14,000 per donee in 2016
- Lifetime exclusion now linked to estate exclusion (\$5.45 million in 2016)
- Direct payment of medical and education expenses to provider avoids ALL gift tax implications
- Making gifts in excess of annual exclusion amount may still have benefits
- State issues in PA –
  - Inheritance tax is still an issue
  - Gifts within 1 year of death are pulled back into estate
- Consider the non-tax reasons for making gifts

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# Income Tax Considerations for Making Annual Gifts of Appreciated Property

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- Carryover basis of gift vs. basis step-up at death will be a case-by-case consideration
- Donee gets donor's cost basis and holding period associated with gifted property
- Sale by donee will generally produce capital gain, taxed at 0% 15%, 20%
- Be mindful of Section 1411 Surtax of 3.8%
- Donee could be hit with recapture
  - Taxed at 25% (Unrecaptured Sec. 1250)
  - Ordinary tax rates

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# Valuation Issues

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- Discounts
  - Full basis step-up at death may be a better deal if estate is not taxable
  - Reconsider prior planning
  - It's all about basis planning and income taxes for smaller estates
- Use of FLPs
- Use of QPRTs



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# Basic Documents and Issues

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- Wills
  - Maybe a pour-over will is appropriate
  - Names executor and successors
  - Generally addresses payment of final expenses, funeral expenses and disposition of TPP
- Revocable Trust
  - A “will replacement” for assets titled to the trust
  - Critical to also name successor trustees
  - Provides privacy
  - Can provide separate disposition instructions for a different class of beneficiaries than in the will
  - In Delaware – avoids 1.75% probate fee

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# Basic Documents and Issues – Continued

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- Advance Medical Directives
- Durable Power of Attorney
  - Name of power holder and possible successors
  - Be careful who you name as power holder
  - Immediate or upon happening of an event
  - Generally preferable to adding a name onto an account

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# Beneficiary Designations

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- Applicable to
  - IRAs, Roth IRAs
  - Employer plans
  - Life Insurance
  - Annuities
  - Bank and brokerage accounts
- Review and update as needed
  - Birth
  - Death
  - Divorce
  - Marriage
  - Other



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# Beneficiary Designations - Continued

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- Consider providing copies to advisors
- “Per stirpes”
- Trusts as beneficiary
- Charity as beneficiary
  - Separation of accounts
  - Percentage of account balance
  - Best assets to leave to a charity

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# Estate Planning for Pets

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- Use of trusts
- Who pays the Income tax?
- Does Rover and Fluffy need ID numbers?
- Who is the trustee?
- Who cares for Fido?
- Leona Helmsley left \$12 million to her dog, Trouble.
- (court eventually reduced the inheritance to \$2 million)
  - Security - \$100,000/yr.
  - Grooming - \$8,000/yr.
  - Food – \$1,200/yr. (went from crab cakes to Alpo)
  - Medical - \$2,500-\$18,000/yr.
  - Guardian fee - \$60,000/yr.



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# Questions

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