

Evolving Trends & Changing Laws

Tulsa Estate Planning Forum
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Program Perspectives

FOCUS: PRACTICAL TAX & ESTATE PLANNING OPPORTUNITIES & TRAPS
(particularly the Impact of Tax Reform)

- General Discussion – Exceptions Apply
- Particular Facts can Change the Advice
- Every Possible Change & Issue are Not Discussed
- **HANDOUTS & UPDATES**

Memorable Quotes


“And I must say that the Republicans, I think, have been cutting taxes with borrowed money, and the Democrats have been spending with borrowed money. They agree only on the borrowed money.”

Alan Greenspan on PBS, September 24, 2010

5/7/2019

Prediction


Estate Planning & Probate Will Explode in the Next 30 Years



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Demographic Trend
Increasing Deaths

<u>Year</u>	<u>Total Deaths</u>
2010	2,400,000
2020	2,867,000
2030	3,316,000
2040	3,881,000
2050	4,249,000



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Demographic Trend
Looming Bequests

A 2003 Boston College report (that updated a 1999 report) projected that the largest intergenerational wealth transfer in history would occur by the year 2052, with a total transfer of approximately


\$41 trillion



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Prediction

TCJA will cause Increased Audits of Trust & Estate Income Taxes



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Tax Facts

It is anticipated that about **1,800 estates** will pay an Estate Tax in 2018

According to the IRS Data Book for Fiscal Year 2016:

Form	Returns Filed	Audits		Audit Rate
		Field	Letters	
1041	3,174,929	451	3,284	0.1%
709	238,324	1,843	-0-	0.8%
706*	3,631	1,365	-0-	37.6%

* Showing Gross Estate over \$10 million
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Tax Fact

Trust & Estate Income Taxes for 2019

If income of an estate or trust is	The income tax is
Not over \$2,600	10% of taxable income
Over \$2,600 but not more than \$9,300	\$260 plus 24% of excess over \$2,600
Over \$9,300 but not more than \$12,750	\$1,868 plus 35% of excess over \$9,300
Over \$12,750	\$3,075.50 plus 37% of excess over \$12,750


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The New Reality

(Divergent Federal Tax Thresholds)

Income Taxes are the New Confiscation Tax for most Moderately Affluent Taxpayers

- ✓ Annually Renewable (compounded Cost)
- ✓ Lower Tax Thresholds
- ✓ Paid Earlier



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The New Planning Environment

Estate planning is not Diminishing

Estate Planning is not getting Simpler – It is getting more Complex

Estate Planning is less about Taxes and more about LEGACY

Income Tax Planning Trumps Estate Tax Avoidance for **99.9%** of Clients

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Demographic Trend

Elderly and Insolvent

- Most retiring Baby Boomers are financially unprepared for their retirement.
- In 2011, the average 65 to 69 retiree had a median net worth (including \$125,000 of equity in their residence) of **\$194,266**.
- Retiree are outliving their meager retirement funds.
- A recent report shows that bankruptcies for those 65 and above has **tripled** since 1991, while retirees age 75 and older had a **10 time increase**

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Demographic Trend
Elderly and Insolvent




The Center for Retirement Research at Boston College estimates **that more than half of all American households** will not have enough retirement income to **maintain the living standards** they were accustomed to before retirement, even if the members of the household work until 65, two years longer than the average retirement age today

Demographic Trend
Elderly and Insolvent

The national annual median cost of a private room in a nursing home is **\$100,375**, according to a 2018 Cost of Care study



Memorable Quotes



“The OASI Trust Fund and the DI Trust Fund are projected to have sufficient reserves to pay full benefits on time **until 2034** and 2032, respectively. Legislative action will be needed to prevent reserve depletion in those years. In the absence of such legislation, continuing income to the trust funds at the time of reserve depletion would be sufficient to pay **77 percent of OASI** benefits and 96 percent of DI benefits.”


5/7/2019 2018 Social Security Trustees' Report

The Unexpected
Filial Support Laws

According to the **Statute of Frauds**, you cannot generally be held liable for the debts of another without agreeing to such liability.

24 states have adopted **Filial Support statutes** in which family members can be held legally liable for the support obligations of family members

In 6 states, failure to provide the necessary support to a spouse can be a **criminal Felony or Misdemeanor**



PLANNING OPPORTUNITY
Long Term Care Insurance

Encourage the children of financially challenged parents to purchase **Long Term Care Insurance** on their parents

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Wealth Transfer Planning From 2019 to 2026



Trap for the Unwary
(Its Temporary)

NEVER, EVER, forget that the TCJA Increased Transfer Tax Exemptions are

Temporary!

- ✓ January 1, 2026
- ✓ Democrats are in Control

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Trap for the Unwary
(Its Temporary)

Proposals for Federal Tax Increases on the Wealthy

- ✓ Annual Wealth Tax
- ✓ Reduction of Transfer Tax Exemptions
 - ✓ Increase in Transfer Tax Rates
 - ✓ Increase in Capital Gain Rates
 - ✓ Increased Social Security Taxes
- ✓ Increase in Income Tax Rates

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Tax Fact

The Wealth Transfer Exemption has not been Reduced since the Estate Tax was Re-enacted in 1916, except from 2010 (unlimited exemption) to 2011.

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Planning for Affluent Clients

- ✓ Greater use of Lifetime Gifts – Using Exemption Trusts
- ✓ Greater use of Sales to Defective Grantor Trusts
 - ✓ Increased Use of GRATs
 - ✓ Generation Skipping Trusts
- ✓ Move Appreciating Assets out of the Estate

PLANNING OPPORTUNITY
Does Clawback Occur?

Does the language of §2001(g)(2) make the use of Gift Exemptions before 2026 Permanent?

Proposed Regulations were released on November 20, 2018.

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PLANNING OPPORTUNITY
Planning for Wealthy Clients

Consider making significant gifts before the Exemptions are Reduced

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PLANNING OPPORTUNITY
The Portability Election

Making the **Portability Election** may be more Important, given the Possibility of a future Reductions in **Wealth Transfer Exemptions**

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PLANNING OPPORTUNITY
Late GST Elections

If a GST Election was not properly made, consider making a **Late Election** using the Higher Exemptions

Don't wait until 2025

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PLANNING OPPORTUNITY
Accumulating Wealth

Perspective: Given the non-expiring C Corporation 21% Tax Rate and the Simplicity of the rules (versus the pass through entity 20% deduction), do clients move toward the use of C Corporations to own **Appreciating Property and build Wealth?**

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Trap for the Unwary
Accumulating Wealth

Service businesses are limited in their use of the section 199A 20% tax deduction, which decreases their market value

Example: Paul Allen's ownership in the Seattle Seahawks and Portland Trail Blazers

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PLANNING OPPORTUNITY
Funding a Buy-Out

- Use the Lower C Corporation Tax Rate to Reduce the Tax Cost of **Non-Deductible Life Insurance** in a Family Closely Held Business
- Use the Insurance Proceeds to Equalize/Buyout **Family Members who are not Active** in the Business

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Valued Added Resource

Joint Committee on Taxation Blue Book (issued December 20, 2018) on THE 2017 Tax Cuts and Jobs Act at:
<https://www.jct.gov/publications.html?unc=startdown&id=5152>



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The Increased Significance of State Taxes



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Memorable Quotes

“With the shift to a \$10,000 limit on deductibility of State & Local Taxes against Federal income taxes for the 2018 tax year and into the foreseeable future, **state income tax planning** has become **one of the biggest sources of revenue** for estate planning attorneys, accountants, trust officers and financial advisors.”

Steve Oshins, LISI Newsletter (January 14, 2019)

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Inclusion of State Income Taxes

Revenue Ruling 2019-11

provides information on the computation of recovered state income taxes that were deducted in a prior year

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Proposed State & Local Taxes

(a sampling)

California: Estate, Gift and GST Taxes

Chicago: VAT tax on billings of large professional firms

New York City: a one time “Mansion Tax”

New York: Extension of Millionaire Tax in 2020 (“temporarily” enacted in 2009)

New Jersey: a “Millionaires Tax”

Massachusetts: a “Millionaire Tax”

Connecticut: Sales Taxes on previously exempt products, like groceries and medicine

Memorable Quotes

“Tax the rich. Tax the rich. Tax the rich. We did that. God forbid the rich leave.”

New York Governor Andrew Cuomo
Source, The Buffalo News, February 4, 2019

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Change of Residency

Reported shortfalls in projected New York Revenue:

State, FYE 2018 to 2019: **\$3.7 billion**


New York City: **\$935 million**

New Jersey has reported an income-tax **shortfall of 6%** so far for its June 2019 fiscal year. It had anticipated **growth of 5.4%**

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Prediction

TCJA’s Federal Taxable Income changes will Adversely Impact Residents of States with Higher Income Tax Rates and as a Result more **Residents will consider Moving** to Low or No Income Tax States



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Change of Residency

In 2015 New Jersey’s richest resident, hedge fund billionaire David Tepper, declared himself a Florida resident and moved his business to Florida. New Jersey was projected to **lose hundreds of millions in annual tax revenue.**

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Memorable Quotes

“Between 1992 and 2014, New Jersey **lost \$24.91 billion** in net adjusted gross income(net AGI). Nearly 60% of that net AGI (\$14.79 billion) went to – you guessed it – Florida.”

Source: Forbes, April 18, 2016

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PLANNING OPPORTUNITY

State Income Taxes

Example:

Moving a Client out of an 8% Tax State before a **\$10 million** sale, Saves **\$800,000.**

Make Sure to Move the Residency the Tax Year BEFORE a Sale!

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State Income Taxation on Business Sales

Corrigan v. Testa

- Ohio based LLC started business in 2000
- LLC was sold in 2004 for \$27,563,977
- Ohio assessed an income tax of \$674,924 on a percentage of the sale apportioned to Ohio (38.827%)
- *“Thus, if Mansfield Plumbing had made a bulk transfer of its business assets rather than having the business transferred through a sale of the L.L.C. ownership itself, then the gain from the sale would have been realized at the L.L.C. level, and the Ohio-apportioned share would have been taxed to Corrigan on a pass-through basis. “*

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Demographic Trend

Determining a Domicile

14% of Americans Move Each Year

As Baby Boomers Retire, this % will Increase

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Demographic Trend

Determining a Domicile

In 2009, the National Association of Homebuilders estimated that there were **6.9 million homes** that qualify as non-rental second homes



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PLANNING OPPORTUNITY

Minimizing State Taxes

For Clients with **Multiple Residences**, it is **Very Important** for them to Declare a State of Domicile and Take Steps to Perfect Such Residency



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The Unexpected

"Just the Facts Please"

Matter of Blatt

*"In reviewing the factors of a change in domicile, historically, the move of items near and dear tend to demonstrate a person's intention. As borne out by the evidence in this case, **Petitioner's Dog** was his near and dear item which reflected his ultimate change in domicile to Dallas."*


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Trap for the Unwary

State Wealth Transfer Taxes

Never Lose Sight of State Transfer Taxes

- 17 States have a Death Tax
- Connecticut has a Gift Tax



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The Unexpected

Contemplation of Death

As of January 1, 2018, **Iowa, Kentucky, Maryland, Nebraska, New Jersey, & Pennsylvania** have **Contemplation of Death** rules. The rules vary widely (e.g., the period of "contemplation") and in some cases are rebuttable.


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Trap for the Unwary

State Income Tax Claims

State Legislatures are getting increasingly Aggressive in imposing State Income Taxes and Sales Taxes on Out of State Taxpayers

State Courts sometimes Eliminate the Aggressive Income Tax Claims



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State Sales Taxes on Internet Sales

South Dakota vs Wayfair, Inc.
(issued June 21, 2018)

“Quill is flawed on its own terms.... the physical presence rule of Quill is unsound and incorrect.”

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Memorable Quotes

“The federal government should not intrude on state tax policy. Although Congress has a constitutional responsibility to ensure the orderly function of interstate commerce, it is also obliged to respect the sovereignty of the state to determine their own sales and use tax policies.”

Democrat Jerrold Nadler, House Judiciary Committee Chair

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The Consequences of Wayfair

Result: Continuing Confusion & State Tax Aggression

- Local Sales Tax Options & Tax Filing
- Minimal Associations with the State
- State sales taxes on Services
- Taxation of Non-Residents

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State Income Taxation of Trusts

Kimberley Rice Kaestner 1992 Family Trust

- Trust created in New York
- Sole Trustee is a New York resident
- Beneficiary moves to North Carolina
- No distributions to the NC Beneficiary
- Beneficiary could not compel Distributions
- North Carolina imposed an Income Tax on the Trust
- North Carolina Trial Court: The tax violates the Due Process Clause and Commerce Clause
- North Carolina Appellate Court and Supreme Court ruled in favor of the Taxpayer

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Valued Added Resource

Declaring your State of Tax Domicile Checklist at www.Scrogginlaw.com



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Valued Added Resources

To support your time of **residency** or **taxable travel** in another state consider these cell phone apps:

➤ <https://monaco.com/>

➤ <https://www.taxday.com/>

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Valued Added Resources

Latest State Estate Tax laws
see: <http://www.mcguirewoods.com>

Retiree State Income Taxes
See: www.Kiplinger.com/letterlinks/2018 map



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Valued Added Resources

Steve Leimberg's Income Tax Planning Newsletter #173
- Lad Boyle, Jonathan Blattmachr & Mitchell Gans -

Trust Planning to Save State Income Taxes



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The Complexities of Co-Habitation



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Celebrity Examples
Cohabitation




Goldie Hawn & Kurt Russell have lived together since 1983

Oprah Winfrey & Stedman Graham since 1986

Spencer Tracy & Katharine Hepburn for 27 years

Demographic Trend
Cohabitation



In 2016, **18 Million** people were Cohabiting (a 29% increase from 2007)

From 2007-2016, the number of Cohabiting adults over age 50 increased by **75%**

Source: Pew Research Center

Trap for the Unwary
The Tax Cost of Co-Habitation

Is a Transfer of Assets under a Co-Habitation:

- **Compensation** for Services?
- A **Settlement** of Claims under Palimony?
- A **Gift** that uses the Lifetime Exemptions?
- **None of the Above?**

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The Tax Cost of Love

Blagaich

- In the course of an 18 month relationship Lewis Burns (age 72) gave Diane Blagaich (age 54) \$743,819, a diamond ring and a \$70,000 Corvette.
- When she broke up with him, he sued for recovery of the assets and filed a 1099-MISC with the IRS for \$743,819
- The court awarded \$400,000 and he revised his 1099.
 - **Tax Court ruled against Ms. Blagaich:**
- Despite repaying the \$400,000 there was no offset against the original 1099 because the payment was made three years later
- The IRS was not bound by the local Court's determination

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Trap for the Unwary

Updating Documents after a Break-Up

Impact on the Estate Planning

- ✓ **No Automatic Termination of Inheritance Rights under Wills**
- ✓ **Continued Authority under Medical Directives and Powers of Attorney**

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Divorce Planning




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Demographic Trend

Divorce & Baby Boomers

According to a March 3, 2012 article in the Wall Street Journal, entitled "*The Gray Divorces*," the divorce rate for Baby Boomers' is skyrocketing, even while it is diminishing for other demographic groups.

"Among divorces by people ages 40-69, women reported seeking the split 66% of the time."



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Trap for the Unwary

Consequences of Remarriage

TCJA eliminates **Alimony Deductions & Income Taxation of Alimony Payments for Post-2018 Settlements**

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PLANNING OPPORTUNITY

Funding a Buy-Out

Replacement for Alimony:

- **Marital Trusts**
- **By-Pass Trusts**
- **CRTs**

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PLANNING OPPORTUNITY
 Funding a Buy-Out

Qualified Contingencies and 664(f)

For purposes of this subsection, the term “qualified contingency” means any provision of a trust which provides that, upon the happening of a contingency, the payments described in paragraph (1)(A) or (2)(A) of subsection (d) (as the case may be) will terminate not later than such payments would otherwise terminate under the trust.

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PLANNING OPPORTUNITY
 CRT Contingencies

Normally, the existence of a Contingency on a trust bequest to a surviving spouse voids any estate or gift tax marital deduction. However, Code **§2056(b)(8)** provides an exception for CRTs “If the surviving spouse of the decedent is the only beneficiary of a qualified charitable remainder trust ...” Similar language is contained in Code **§2523(g)**

A CRT for the spouse (or soon-to-be-former-spouse) can contain a provision that terminates the CRT upon the **Remarriage of the Spouse**, a **Contest of the Will** or upon other **Contingencies**

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PLANNING OPPORTUNITY
 Divorce and Transfer Tax Exemptions

A Wealthy Wife is required to make a Significant Property Settlement for the benefit of a Less Wealthy third Husband

She could create a **Lifetime Marital Trust** for the benefit of the soon to be Ex-Husband

At the Ex-Husband’s death, his Transfer Tax Exemption (which he might not otherwise have used in full) benefits her children by **Reducing the Transfer Taxes** and a **Step-Up** in Basis occurs

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PLANNING OPPORTUNITY
 Divorce and Transfer Tax Exemptions

View the Less Wealthy Spouse’s Transfer Tax Exemption as a Tradable Asset in Divorce Negotiations

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PLANNING OPPORTUNITY
 Divorce and Transfer Tax Exemptions

A Divorcing Entrepreneur wants to begin Transferring equity in her Family Business to children from a prior marriage.

She has a Pre-nuptial agreement which Restricts the rights of the current Husband.

The Appraiser has provided a discount in value of 40% for the Minority Interest she will transfer in the Business.

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PLANNING OPPORTUNITY
 Divorce and Transfer Tax Exemptions

If the couple elects Gift Splitting, the Donor/Wife can effectively transfer her and the Husband’s Exemption Amounts to a Generation Skipping Trust and save up to **\$7,600,000** in Estate Taxes

\$11,400,000 (spouse’s 2019 unified credit) discounted at 40% (\$19,000,000 in transferred value) times the federal estate tax rate of 40%

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PLANNING OPPORTUNITY
 Divorce and Transfer Tax Exemptions

Making up for the Traded Exemption:

The Wealthier Wife could provide a **Marital Trust** for the benefit of the Ex-Husband, or
 Provide a **Larger Property Settlement** to the Ex-Spouse, or
 Purchase a **Paid Up Life Insurance Policy**

“In return for saving me \$7.5 million in transfer taxes, I will agree to increase your property settlement by \$3.0 million.”

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PLANNING OPPORTUNITY
 Divorce and Transfer Tax Exemptions

Beware of the Reciprocal Trust Rules!

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PLANNING OPPORTUNITY
 Divorce and Basis

Divorce negotiations should take into account the **After-Tax Value** of an asset, not just its **Fair Market Value**

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Trap for the Unwary
 Divorce and Basis

A wife owns a tract of land that has a fair market value of **\$2.1 million**, a basis of **\$200,000** and secured debt of **\$1.5 million**. The husband receives the property as a part of the divorce and immediately sells it, thinking that he gets to keep the **\$600,000** in equity.

The recognized gain is **\$1.9 million**. Assuming a state and federal effective income tax rate of 30%, the taxes on the sale are **\$570,000**, leaving the husband with **\$30,000** after payment of the mortgage.

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Trap for the Unwary
 Divorce Planning

Automatic Statutory Revocations in Divorce

- Spouse “predeceases” “for all Purposes”
 - * May not apply to Step-Family
- Spouse as Trustee for Children
- Spouse is removed from GPOA
 - Any successor named?
- May not Apply to ERISA Accounts
- May not apply to Beneficiary Designations

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Trap for the Unwary
 Marriage and Divorce

In many States, Divorce (and sometimes marriage) **Revokes an Existing Will**


However, **Medical Power of Attorney** and **Financial Powers of Attorney** may Not be Revoked

Trap for the Unwary

Divorce and Basis

Critical Tax Information


The divorce decree should require that the transferor spouse provide the transferee spouse **sufficient records** to support both the **basis** of the property and its **holding period**



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Trap for the Unwary

IRAs and Asset Protection




In Clark v. Rameker, the US Supreme Court unanimously ruled that an **Inherited IRA** did **not** have the Bankruptcy protection afforded ERISA retirement accounts or a taxpayer's own IRA.

Huge **Implications for Spouses** – the Supreme Court did **not** make a distinction between an Inherited IRA for the Surviving Spouse and other Beneficiaries.

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Trap for the Unwary

IRAs and Asset Protection



In Lerbakken, the 8th Circuit ruled that when a divorcing husband received 401(k) and IRA assets from a former spouse in divorce, the retirement assets lost their special bankruptcy exemption

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PLANNING OPPORTUNITY

Adopting an Adult

In Goodman v. Goodman the divorced creator of a 1991 Irrevocable Trust for the benefit of “my children” adopted his 42 year old girlfriend so she could gain access to a portion of the \$300 million in trust funds. The ex-wife as legal guardian of the two current trust beneficiaries objected. The court terminated the adoption on a procedural basis.

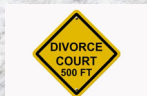
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Demographic Trend

Divorce & Baby Boomers

62% of divorced clients do not have a current **Will**

Even fewer have **Medical Directives** and **General Powers of Attorney**



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Valued Added Resources

- **Post-Divorce Practical Checklist**
- **Planning for Divorce from the Perspective of a Tax and Estate Planner**

at www.Scrogginlaw.com



PREPARE FOR THE CONSEQUENCES OF REMARRIAGE



Memorable Quotes

*Marriage is often due to lack of **judgment**, divorce to lack of **patience** and remarriage to lack of **memory***

Marriage Statistics

- 8% of newly married adults have been married three times or more
- Roughly 500,000 U.S. residents over age 65 marry each year



Demographic Trend

Dad's New Relationship

Widowers over age 65 are **10 times** more likely to marry than widows



Demographic Trend

Dad's New Relationship

61% of widowers are engaged in a new romantic relationship within 25 months of their wife's death, versus **19% of widows**



Demographic Trend

Dad's New Relationship

20% of men in second marriages marry someone who is at least **10 years Younger** than them



The New Reality
(Fear of Second Spouses)


Dad's marriage to a woman
20 years his junior has
created heartburn for a lot of
children who have been
anticipating a **larger and
quicker inheritance**

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Understanding the
**FIRST
CASSEROLE
RULE**




Central Point
**HEIRS OF REMARRIED
WIDOW/WIDOWERS HAVE
MORE TO FEAR FROM THE
REMARRIAGE THAN FROM
TRANSFER TAXES**



Trap for the Unwary
Spousal Rights

In Second and Third Marriages,
Spousal Rights may be more
Destructive to the Descendants'
Inheritance than any Taxes




The New Reality
(Fear of Second Spouses)

Wives are Increasingly
concerned about Family
Assets passing to their
Widower/Husband's
New Wife

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Trap for the Unwary
Consequences of Remarriage

In 49 states a Spouse has a
right to an "**Elective Share**"
and Other Rights against the
Estate – EVEN if the Spouse
is **Disinherited** by a Will!



Trap for the Unwary

Consequences of Remarriage

Spousal Elective Share & Years Support (Georgia)

- Elections against the **Homestead**
- **Intestate Claims & Pre-Marriage Wills**
 - **ERISA** Retirement Plans
- Elections against **Personal Property**
- Ownership of **Personal Property**
- **Decision Making** Authority
- **Filial Support** Statutes



Spousal Rights

Georgia is the only State without a Spousal Right to a Deceased Spouse's Assets

✓ *"A testator, by will, may make any disposition of property that is not inconsistent with the laws or contrary to the public policy of the state and may give all the property to strangers, to the exclusion of the testator's spouse and descendants."*

Intestate Rights

Spousal Intestate Rights


- No Will
- New Marriage with Old Will
- No Other Living Heirs



The Law

(New Spouses)

Georgia Statute 53-4-48(c): *"If the will was made prior the [the marriage of the testator],and does not contain a provision in contemplation of such an event, the subsequent spouse shall receive the share of the estate he or she would have received if the testator had died intestate."*



The New Reality

(Second & Third Marriages)

Even **Moderately Wealthy Clients** Need to Consider:


- ✓ **Pre-Nuptial** Agreements
- ✓ Post-Nuptial **Waivers** (ERISA Plans)
- ✓ **Updated Documents** for Estate Planning
- ✓ Documented **Ownership** of Personal Property
- ✓ The Use of **Conduit Trusts** for Spouses

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TRAP or OPPORTUNITY?

Change of Residency

Changing the State of Residency of an Incapacitated Spouse can Substantially **INCREASE** or **DECREASE** the Asset Rights and Power of the other Spouse




Pre-mortem Planning



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Planning for your Demise

In December 2018 Gerald Cotton (owner of a cryptocurrency platform) died unexpectedly at age 30 with **\$131 to \$190 million** in cryptocurrency (owned by over 115,000 people) held in “cold wallets” on his encrypted laptop – but without anyone else having the passwords to his computer.



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Trap for the Unwary

Capital Loss Carry-Forward

The IRS has ruled that the **Capital Loss Carry-forward** and **Net Operating Losses** Solely Generated by a **Decedent’s** Assets:

- Cannot be Carried Over to a Surviving Spouse – Even with a Joint Return
- Cannot be Carried over to the Estate
- Cannot be Carried over to the Heirs

Solution: Consider Accelerating Income in the Final Return



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PLANNING OPPORTUNITY

Obtaining a Higher Basis

If a **Discretionary “Spray” Trust** contains Appreciated Assets, then consider Distributing the assets to a **Terminally Ill Beneficiary** (e.g., spouse or descendant) before they Die to Obtain a Step-Up in Basis

§1014(e) should not apply because the Distribution came from the Trust, not a future Beneficiary

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PLANNING OPPORTUNITY

Obtaining a Higher Basis

A **Terminally Ill** client is the Beneficiary of a **Marital Trust** with substantial **Unrealized Capital Losses**

Upon the Beneficiary’s Death, the assets will **step down** to their lower Fair Market Value

However, if the trust sells the assets **before** the Spousal Beneficiary’s death, the Losses can be **preserved** for **Remainder Beneficiaries**
(See IRC §642(h)(1))

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PLANNING OPPORTUNITY

Understanding §1014(e)

Four Triggers

- ✓ An **Appreciated** Asset is Gifted
- ✓ **Donee Dies** within One Year of the Gift
- ✓ The Asset is **Reacquired** by the Donor or the Donor’s Spouse
- ✓ The Donor is **Entitled to Sale Proceeds**

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PLANNING OPPORTUNITY
Obtaining a Higher Basis Despite §1014(e)

Assume a donor gifts **\$1.0 million** in cash into an **IDGT** in which the donor is the deemed grantor and the donor's dying spouse is the sole lifetime beneficiary. Low-basis property owned by the grantor is sold into the trust during the spouse's lifetime. The donee/spouse holds a **Testamentary General Power of Appointment** over the entire trust and exercises the power of appointment in favor of the donor or a trust for the donor's benefit.

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PLANNING OPPORTUNITY
Obtaining a Higher Basis Despite §1014(e)

The sale by the grantor to the IDGT is not recognized for income tax purposes. §1014(e) would not apply because the gifted cash was not "appreciated."


The entire trust fund would be included in the donee/spouse's estate pursuant to IRC §2041(a)(2). Pursuant to IRC §1014(b)(9), a step-up in basis should be allowed because the trust assets were included in the donee/spouse's estate.

IRS Position?: **Step Transaction Doctrine** applies.

5/7/2019

PLANNING OPPORTUNITY
Planning for IRS Discounting

In Structuring any Tax Basis related Strategy, **Anticipate** the Methods the IRS might use to **Reduce** the Value of the Assets



5/7/2019

PLANNING OPPORTUNITY
Basis Opportunity in Family Businesses

The Adell Family Business

Issue: the Value of the Business at Father's death.


The Estate contended that the pivotal role that the decedent's Son played depressed the value of the Business—the son's "**Personal Goodwill**" greatly reduced the value of the Father's company. The Son was not subject to an employment agreement or covenant not to compete.

The Court agreed that a **Substantial Value** had to be assigned to the son's Personal Goodwill, reducing the value of the Father's Estate

5/7/2019

Trap for the Unwary
Basis in Family Businesses

Will the IRS use the Recent Decisions to provide that the "**Personal Goodwill**" of Family and/or Employees create an effective **Discount** on the value of the business for Tax Basis purposes?



5/7/2019

PLANNING OPPORTUNITY
Basis Opportunity in Family Businesses



If the Principal Family Business Owner does not have a Taxable Estate, do you place Key Family Members under **Restrictive Employee Covenants** to **Increase the Value of the Business?**

5/7/2019

PLANNING OPPORTUNITY
 Obtaining a Higher Basis

Planners should Consider How to Bust Discounting Techniques!




PLANNING OPPORTUNITY
 Intra-Family Sales & Chapter 14

IRC § 1014(a): *Except as otherwise provided in this section, the basis of property in the hands of a person acquiring the property from a decedent or to whom the property passed from a decedent shall, if not sold, exchanged, or otherwise disposed of before the decedent's death by such person, be (1)the fair market value of the property at the date of the decedent's death...*


Use Chapter 14 to Increase the Basis under Buy-Sell Agreements

5/7/2019

PLANNING OPPORTUNITY
 Arguing the IRS Positions

A client created an FLP over which she **Retained Authority**

At her death, do you argue that under IRC 2036, the gifted interests are **included in her Taxable Estate?**



5/7/2019

PLANNING OPPORTUNITY
 Eliminate the Potential for Discounting

Dad is dying and owns 60% of the LP units in a FLP owning a family farm. The children own the GP interests and all the remaining LP units.

DO YOU LIQUIDATE THE FLP?

5/7/2019

PLANNING OPPORTUNITY
 Determining the Basis

§1015(a) provides as follows: *"If the facts necessary to determine the basis in the hands of the donor or the last preceding owner are unknown to the donee, the Secretary shall, if possible, obtain such facts from such donor or last preceding owner, or any other person cognizant thereof. **If the Secretary finds it impossible to obtain such facts, the basis in the hands of such donor or last preceding owner shall be the fair market value of such property** as found by the Secretary as of the date or approximate date at which, according to the best information that the Secretary is able to obtain, such property was acquired by such donor or last preceding owner."*

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PLANNING OPPORTUNITY
 Gifting High Basis Assets

Gifting of High Basis Assets can Make Sense

5/7/2019

PLANNING OPPORTUNITY
 Gifting High Basis Assets

- ▶ A Terminally Ill Client owns a Family Farm with a Basis of **\$3.0 million** and a Fair Market Value of **\$1.5 million**.
- ▶ If the Client Dies, the **Basis Steps Down to \$1.5 million**



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PLANNING OPPORTUNITY
 Gifting High Basis Assets

If the Client **Gifts** the Property to her Children, the Children can use the **\$3.0 million FMV** as the Basis for any Gain on a later Sale (but not for Loss purposes)



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PLANNING OPPORTUNITY
 Gifting High Basis Assets

Gain on the Sale
No Gain or Loss
Loss on Sale

\$3,000,000

\$1,500,000



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PLANNING OPPORTUNITY
 Gifting High Basis Assets

If the asset is gifted to a **Spouse**, the High Basis is Carried Over for All Purposes (T.R.1.1041-1T(d)Q&A11)



5/7/2019

Valued Added Resources

- Partial Checklist for a Terminally Ill Client
- Income Tax Planning for Clients with Shorten Life Expectancies at www.Scrogginlaw.com



5/7/2019

Charitable Planning



5/7/2019

Demographic Trend

Charitable Bequests

A 2010 Bank of America Study of High Net Worth Philanthropy estimated that between **\$6.6 trillion** and **\$27.4 trillion** in Charitable Bequests would be made from 1998 to 2052

5/7/2019

PLANNING OPPORTUNITY

Maximize the Tax Benefits of Charitable Donations

Maximizing Charitable Donations after TCJA

- Direct IRA payments by those over 70½
- Payment of Marketing & Advertising expenses
- Using a Non-Grantor Trust to fund donations
 - Bunching donations every 2 years (using a Donor Advised Fund)



Taking Advantage of State Tax Credits for Charitable Donations

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Trap for the Unwary

IRA Direct Charitable Transfers - §408(d)(8)

The exclusion applies only if a Charitable Contribution Deduction for the entire distribution would otherwise be allowable. *“for example, if the deductible amount is reduced because of a benefit received in exchange, or if a deduction is not allowable because the donor did not obtain sufficient substantiation, the exclusion is not available with respect to any part of the IRA distribution.”*

JCT Report, p. 19.

5/7/2019

PLANNING OPPORTUNITY

Charitable Deductions vs. Marketing Expenses

- Charitable Deductions by individuals and businesses are subject to numerous Limitations and Deduction requirements
- Business owners should consider having their business make Payments as **Marketing and Advertising**
- The central issue in distinguishing the two is *a reasonable expectation of a financial return commensurate with the amount of the advertising payment*

Treas. Reg. § 1.162-15(b)

5/7/2019

PLANNING OPPORTUNITY

Charitable Deductions that Don't Impact the Standard Deduction

- ✓ Fund a Non-Grantor Trust and gave Non-Grantor Trustee(s) the **Discretion to make Distributions** to Charitable or Non-Charitable Beneficiaries
- ✓ §642(c)Charitable Deduction comes out before the Determination of DNI, reducing the potential taxation to Non-charitable Beneficiaries
- ✓ The Income is not reflected on the Grantor's Itemized Deductions, but **funds his or her Charitable Desires**

5/7/2019

PLANNING OPPORTUNITY

Funding Charitable Advancements

Provide for the Lifetime Advancements of Charitable Bequests

Example: Assuming a top state & federal income tax rate of 40%, replacing a **\$100,000** charitable bequest with a lifetime contribution could save up to **\$40,000** in federal income taxes

5/7/2019

PLANNING OPPORTUNITY
 Charitable Bequests

Consider having provisions in the Dispositive Documents that provide that **Charitable Bequests are NOT made if the Estate is not Taxable**

Instead, the **Expectation** is that the **Heirs will make the Charitable Contribution** and take the Income Tax Deduction

5/7/2019

PLANNING OPPORTUNITY
 "Philanthropic Business Enterprises"

If stringent requirements are met, a Private Foundation can own 100% of a business without having the Excess Business Holding rule apply

Code section 4943(g) was designed specifically for the "Newman's Own" Business Holdings

5/7/2019

Trap for the Unwary
 Charitable Deduction Supporting Documents

Belair Woods v. Comm'r,
 T.C. Memo 2018-159 (September 20, 2018)

Failing on a tax return to provide the tax basis for a charitable gift of an asset results in the denial of the charitable deduction

5/7/2019

Valued Added Resources

There are a number of web-based sources that evaluate public charities, including:

- ✓ <http://www.charitynavigator.org/>
- ✓ <https://www.charitywatch.org/>
- ✓ <http://www.guidestar.org/>
- ✓ <http://www.bbb.org/>


✓ To find a charity's recently filed 990 see: <http://foundationcenter.org/find-funding/990-finder>



5/7/2019

Valued Added Resource


- To See if a Charity has a Federal Income Tax Exemption go to:
- <https://www.irs.gov/charities-non-profits/exempt-organizations-select-check>



Note: Churches, synagogues, temples, mosques and government agencies are also eligible to receive deductible donations, even if they are not listed in this database.

5/7/2019

Incapacity Planning




5/7/2019

Demographic Trend

Looming Incapacity

<u>Year</u>	<u>Over age 65</u>
2010	40,200,000
2020	54,600,000
2030	71,500,000
2040	80,000,000
2050	86,700,000




5/7/2019

Demographic Trend

Looming Incapacity

A Lawyers.com study reported that only **29%** of Americans had either a Medical Directive or a General Power of Attorney



Control of the Family Business

The Lesson from Sumner Redstone

View Medical Directives and General Powers of Attorney as Part of the **Dispositional Part** of Estate Planning



Celebrity Example

Sumner Redstone’s granddaughter said that her aunt Shari Redstone and her three adult children had *“succeeded in reversing decades of my grandfather’s careful estate planning and are poised to seize control of Viacom and CBS.”*

New York Times, June 1, 2016

5/7/2019

The Law

(Testamentary Capacity)

- *“[a] man may believe himself to be the supreme ruler of the universe and nevertheless make a perfectly sensible disposition of his property, and the courts will sustain it when it appears that his mania did not dictate its provisions.”* Fraser v. Jennison, 3 N.W. 882, 900 (Mich. 1879)
- *“gross eccentricity, slovenliness in dress, peculiarities of speech and manner or ill health are not facts sufficient to disqualify a person from making a will”* In re’ Estate of Frazier, 131 Neb. 61, 73, 267 N.W. 181, 187 (1936)

5/7/2019

Decision Making

Decision Making


- ✓ Guardian over Person & Property
- ✓ Estate Personal Representative

Appointment of a **Guardian** can limit or revoke a General Power of Attorney



Celebrity Example

Glenn Campbell announced in 2011 that he had been diagnosed with Alzheimer's. In 2015, two of his eight children filed suit in Nashville alleging that his fourth wife (married since 1982) was refusing to let them visit their father or let them participate in his health care.



Document Review
Incapacity Planning

Make sure the Client's Parents and Adult Children have **Medical Directives** and **General Powers of Attorney**

5/7/2019

Personal Property – the Greatest Source of Family Conflict




Celebrity Example

On February 3, 2015, the front page of the Arts section of the New York Times reported that Robin Williams' widow and his three children from his two prior marriages were in conflict over the issue of how his assets, particularly his "*cherished belongings that include his clothing, collections and personal photographs*" would be divided up.

5/7/2019

Central Point
WHEN A CLIENT DIES, THE FIRST PRIORITY MAY BE TO **CHANGE THE LOCKS TO THE HOUSE**


5/7/2019



Understanding the **IN-LAW RULE**

Example

Each spouse had children from a prior marriage. The husband died in the car accident and the wife died the next morning. His Will passed all the tangible personal property and family heirlooms to the wife if she survived him - on the assumption she would return his family's heirlooms to his children. Her Will passed all of her tangible personal property to her husband if he survived her and, if not, to her children. Unfortunately, her children insisted that his personal property assets were their property because it belonged to their mother for the 12 hours she survived her husband.



The New Reality
(Unique Personal Property Assets)

- ✓ Firearms
- ✓ Stored Reproductive Assets
- ✓ Frequent Flyer & Hotel Perks
- ✓ Pets
- ✓ Digital Assets (e.g., Facebook)
- ✓ Passwords
- ✓ Inheritable Right of Publicity
- ✓ Contraband

Valued Added Resource

**Married and Single
Personal Property
Disposition Forms
at www.Scrogginlaw.com**



Valued Added Resource

**TANGIBLE PERSONAL PROPERTY:
THE MOST FORGOTTEN PART OF
AN ESTATE PLAN?
at www.Scrogginlaw.com**



A THOUGHT TO REMEMBER
According to Benjamin Franklin, only
death and **taxes** are inevitable.
So live your life **accordingly**.

