Estate Planning Client Advisory

Winter 2019 - 2020

The Law Office of Robert H. Eardley, P.A. is pleased to provide this *Estate Planning Client Advisory.*

Estate Tax Update and Recent Developments: In late 2017, Congress enacted legislation which affected the federal estate tax system as well as many other taxes. Most significantly, the 2017 Tax Act temporarily increased the estate, gift and GST tax exemptions to over $11 million apiece. However, the increased exemptions expire at the end of 2025 and revert to the $5 million base unless Congress enacts interim legislation.

Exemptions Increased to $11.58 Million for 2020: The baseline exemptions are adjusted annually for inflation. For gifts and deaths occurring on or after January 1, 2020, the 2019 exemptions are increased from $11.40 to $11.58 million apiece.

Annual Tax-Free Gifting Amount Remains at $15,000: The baseline tax-free gifting amount is $10,000 and is adjusted periodically in increments of $1,000. For 2020 gifts, the tax-free amount remains at $15,000.

Democratic Presidential Front Runners & Their Estate Tax Proposals: Much tax law will be affected if Democrats gain control of the White House and Congress next year. Below we highlight the estate tax positions of the 3 current Democratic front runners:

1. Joe Biden. Former Vice President Biden has largely remained silent with regard to his plans for the estate tax. However, in light of his stated goal of reversing much of the 2017 Tax Act, *Forbes.com* suggests it is likely Biden supports a return to the $3.5 million exemption and an increased tax rate above 40%.

Importantly, Biden's plan eliminates the income tax step-up in basis at death – at least for wealthier Americans. Under present law, the beneficiaries of an estate take a new basis of each estate asset (e.g. a home or stock) equal to each asset's fair market value at the deceased's date of death. "Basis" denotes the value from which the IRS determines gain or loss upon the sale of an asset. Basis step-up at death essentially eliminates tax liability for all pre-death appreciation.

Example: Mr. Smith purchases Apple stock for $100,000 which, at his death, is worth $500,000. If Mr. Smith's estate then sells the stock for $500,000, under present law it reports no capital gains tax. However, under Biden's proposal the estate would report $400,000 in capital gains.

2. Elizabeth Warren. For many months Senator Warren's signature tax proposal has been an annual tax on "the wealthy" of up to 3% of net worth. However, she recently doubled her wealth tax proposal to 6%. This tax would require the annual valuation of all assets including accounts, business interests, real estate and art. Tax experts see a serious question as to the constitionality of such a tax.

Interestingly, in 1990 twelve European countries had an annual wealth tax – but only three still do today, "largely because implementation problems and negative effects proved insurmountable" according to *The Wall Street Journal*.

And although Warren asserts that her wealth tax would apply only to the wealthiest Americans, history proves otherwise. A recent opinion piece in *The Wall Street Journal* noted skeptically that progressives who advocated for an income tax in 1913 used the same sort of claim. Even though the 1913 income tax applied to only 2% of households, by just 1923 the tax affected nearly 40% of households.

3. Bernie Sanders. Senator Sanders' proposal reduces the estate tax exemption to $3.5 million (with no annual inflation index) and imposes a graduated tax rate of 45% to 77%.

Sanders also proposes a Warren-style annual wealth tax with a top rate of 8% and buttresses enforcement with (1) a national wealth registry, (2) increased IRS funding, and (3) a 30% minimum audit requirement.

PLANNING POINTER – WATCH THE ELECTIONS: If a Democratic sweep occurs in 2020, significant estate tax increases will likely be enacted. Therefore, we recommend that individuals with a net worth in excess of $3.5 million monitor the legislative landscape and be prepared to take tax-savings steps.

Passing Airline Miles to Your Heirs – Most Airlines Aren't Your Friend: Airlines are quick to celebrate all the "benefits" of their credit cards and loyalty programs, but if you read the contract fine print you will find that most make it difficult, if not impossible, to transfer miles at death to loved ones. The following surveys some airline rewards programs:

- American & United. Miles are only transferable with airline consent and payment of a transfer fee.

- British Airways, JetBlue, Qantas & Singapore Air. Miles expire upon the original owner's death.
- Delta. Miles expire upon the original owner's death unless there is written transfer consent from a Delta vice president or higher officer.

- Southwest. Miles may be used for up to 24 months after the original owner's death if the family has the account login information.

A recent article in The Wall Street Journal entitled *The Thorny Issue of Inheriting Loyalty Points* provides tips to "improve the odds that your miles will outlive you:"

- Put an explicit bequest of your miles in your Will or Trust.
- Make sure your family has your account information and passwords to access your loyalty account.
- Refuse to pay a transfer fee.
- Do not let the account expire due to inactivity.

Snowbird State Tax Update: Many states have massive debt issues yet continue policies which exacerbate these problems. As emphasized in prior *Estate Planning Client Advisories*, Florida residents with a seasonal home in a northern state must vigilantly monitor their Florida tax residency status. The following is a brief survey of noteworthy tax issues unfolding across the country.

SALT Deduction Limit Upheld as Constitutional: Perhaps one of the biggest factors affecting northern state budgets – and the resulting audits of Florida residents – is the 2017 Tax Act's limitation of the state and local income tax ("SALT") deduction to $10,000. Until recently, states on the short end of the SALT deduction limit – including Connecticut, Maryland, New Jersey and New York – sought to have the SALT limit declared unconstitutional. However, on September 30th a federal district court upheld the law.

Texas Doubles Down on No State Income Tax: Although Texas has no state income tax, in November Texans took another step toward conservative tax policy by enacting Proposition 4. This Proposition amended the state constitution to require any tax legislation to pass by a two-thirds majority in both legislative chambers and a majority approval in statewide referendum.

Illinois's Financial Woes Continue: With the second highest property taxes in the country (after New Jersey), $134 billion in unfunded pension liabilities and 5 straight years of net population decrease, a super-majority of Democrats in the legislature voted to put a constitutional amendment on the 2020 ballot to convert the state from a 4.95% flat income tax to a progressive rate (the last state to do so was Connecticut in 1996). Additionally, on July 1st Illinois doubled its gas tax and enacted a 5-cent tax on plastic grocery bags.

Medicare Website Flags Nursing Homes for Abuse or Neglect: If considering a nursing home facility for yourself or a loved one, we recommend you first review the facility's ratings at Medicare's *Nursing Home Compare* website before making a final decision at www.medicare.gov/nursinghomecompare. On this website, each facility is rated between 1 and 5 stars in three areas: (1) health inspections, (2) staffing, and (3) quality measures, in addition to an overall 1 to 5 star rating assignment. Importantly, in October Medicare began adding a red circle enclosing a white hand warning by the name of each facility with a recent citation for abuse or neglect. For example, a recent search in Collier and Lee Counties revealed 2 facilities with red circle warnings.

The Durable General Power of Attorney – Have One and Keep It Current: A "Durable General Power of Attorney" – sometimes simply referred to as a "Power of Attorney" or "POA" – may be the most important component of an estate plan.

The POA is a document by which one person authorizes another person (the "Agent") to act on his behalf. The POA typically is used by the Agent to manage a client's daily personal affairs – such as bill payment – if the client experiences diminished mental capacity.

Perhaps surprisingly, the law does not automatically grant a spouse or adult child authority to handle finances and property. Rather, if there is no POA document, the family must institute a court guardianship to first have the loved one declared incompetent and then have a guardian appointed.

A Real-Life Example: A wealthy 90 year-old client with dementia has a POA designating his sister as Agent using her prior married name. The sister visited the client's local bank to access his safe deposit box. For weeks the bank refused to honor the POA. We resorted to escalation of the issue to the bank's national legal office and finally received approval to use the POA.

PLANNING POINTER: If your POA (1) is not current, (2) is too abbreviated (as is often the case with online forms), or (3) contains a mistake in the name – such as a woman's prior married name – the receiving" party (such as a bank) may not honor it. Our "best practices" recommendation is that correct and comprehensive POAs be executed every 7 to 10 years.

Changes to IRA 70½ Start Age & Beneficiary "Stretch" Expected: On May 23rd, the House passed the SECURE Act by a vote of 417 to 3. Although the Act has broad bipartisan support and is likely to pass into law, presently it is being held up by 5 Senators on procedural grounds for reasons unrelated to its retirement provisions.

The upside of the Act is that it raises the IRA required minimum distribution age from 70½ to 72. Unfortunately, the Act also requires the beneficiary (other than the spouse or a minor child) to withdraw all IRA funds within 10 years instead of over the beneficiary's life expectancy.

Words of Wisdom: *He [Jesus Christ] who comes from above is above all. He who is of the earth belongs to the earth and speaks in an earthly way. He who comes from heaven is above all. He bears witness to what he has seen and heard, yet no one receives his testimony. Whoever receives his testimony sets his seal to this, that God is true. For he whom God has sent utters the words of God, for he gives the Spirit without measure. The Father loves the Son and has given all things into his hand. Whoever believes in the Son has eternal life; whoever does not obey the Son shall not see life, but the wrath of God remains on him.* John 3:31-36.

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