Estate Planning Client Advisory

Winter 2020 - 2021

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

Tax Updates 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.

President-Elect Biden's Proposals: Although election issues are pending as of this writing, Joe Biden appears positioned to be the next President. His most significant estate tax objectives are set forth below.

1. Gift and Estate Taxes. Biden has affirmed support for a significant overhaul of the gift and estate tax system, most notably (a) reducing the estate tax exemption to $3.5 million without an index for inflation, (b) decreasing the lifetime gift tax exemption to $1 million, and (c) increasing the tax rate to 45%. Also, any changes could be retroactive to January 1, 2021. According to *FoxBusiness*, the amount of revenue potentially raised would serve to depress economic activity "*by nearly double what Biden's estate tax plan is expected to collect annually*."

2. Elimination of Basis Step-Up at Death. The "Biden plan" would also radically alter long-standing income tax law by taxing heirs on unrecognized capital gains (possibly limited to decedents with an earnings history of more than $400,000). Under present law, estate heirs pay no income tax on an inheritance and take a new "basis" of each estate asset (e.g. stock) equal to each asset's fair market value at 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 the heirs' tax liability for all pre-death appreciation.

Example: Mr. Smith purchased Apple stock for $100,000 which, at his death, was worth $500,000. If Mr. Smith's heirs sell the stock for $500,000, under present law they pay no tax. However, under Biden's proposal, the heirs would report $400,000 in capital gains and pay income tax.

3. Georgia Senate Races Crucial. The enactment of Biden's tax plan is contingent upon Democrats picking up both Senate seats in the January 5th run-off in Georgia. This would give Biden 50 Senate seats with Vice President elect Kamala Harris as the tie-breaker. However, according to *Forbes.com*, "*[i]f Republicans retain even one of the two seats, it's extremely unlikely Biden will be able to get any of his proposed changes…*" In such a case, almost any Biden proposal without minimal bipartisan support will face an uphill battle.

Exemptions Increased to $11.7 Million for 2021: The baseline exemptions are adjusted annually for inflation. For gifts and deaths occurring on or after January 1, 2021, the 2020 exemptions are set to increase from $11.58 to $11.70 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 2021 gifts, the tax-free amount remains at $15,000.

IRA News – SECURE 2.0 and Charitable Remainder Trusts: As many readers know, the 2019 SECURE Act raised the IRA required minimum distribution ("RMD") age to 72 but decreased the maximum withdrawal period by a non-spouse beneficiary to 10 years.

1. SECURE 2.0. In October, the "Securing a Strong Retirement Act of 2020" (or "SECURE 2.0") was introduced in the House by Ways and Means Chairman Richard Neal (D-MA) and Kevin Brady (R-TX). SECURE 2.0's main benefits are to (a) raise the RMD age from 72 to 75, and (b) exempt IRA owners from RMD requirements if the IRA balance is less than $100,000 on December 31st of the year before the owner turns 75. A bill similar to SECURE 2.0 is moving forward in the Senate. Our expectation is that SECURE 2.0 – in some format – will become law due to its broad bipartisan support.

2. Extending Beneficiary RMD Period Beyond 10 Years. As noted above, the SECURE Act limits a non-spouse beneficiary RMD period to 10 years. The good news is that an "end run" around this rule exists to significantly extend the tax-deferred status of the IRA funds and the beneficiary's withdrawal period – the Charitable Remainder Trust (or "CRT").

Example: Mr. Jones creates a CRT – which is tax-exempt – and designates his CRT as the beneficiary of his $1 million IRA. At Mr. Jones's death, the IRA transfers $1 million to the CRT without paying income tax. His son, Tom, manages the CRT as Trustee and receives a yearly payout of at least 5% (or a higher percentage pre–selected by Mr. Jones) of the CRT's annual value for life. Tom only pays taxes on the 5% as it is received. Hopefully the CRT principal appreciates substantially during Tom's life thereby increasing the amount of his 5% payment. Upon Tom's death, the CRT balance passes to the charity previously selected by Mr. Jones.

According to *Forbes.com*, under realistic economic and life expectancy assumptions, Tom will receive $400,331 more via the CRT option than if he had been the direct beneficiary of the IRA!

Giving a Grandchild a Savings Head Start – the Roth IRA: For grandchildren who are teenagers or young adults, a good option exists to set them on a path to accumulating a tax-exempt retirement fund. Specifically, if a grandchild has earned income, he or she can open a Roth IRA and the grandparent deposits $6,000 of his or her own funds in the IRA – up to the grandchild's earnings. Roth IRAs are tax-exempt, any funds withdrawn by the grandchild after age 59½ are tax-free, and a grandparent's "2020 contributions" may be made until April 15, 2021. Please note that contributions are gifts which count against the $15,000 annual tax-free gifting exclusion noted above.

Snowbird State Tax Update: Many states have massive debt issues yet continue policies which exacerbate these challenges. 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 survey of some noteworthy tax issues across the country.

SALT Deduction Limit in Play: The 2017 Tax Act's limitation of the state and local tax ("SALT") deduction to $10,000 is one of the biggest factors affecting northern state budgets, moves to Florida and audits of Florida residents by northern states. Prior to the SALT limitation, taxes paid to northern states (such as state income and property taxes) were deductible on the taxpayer's 1040 subject to phase-out limits. However, under a Biden administration the SALT limitation would be eliminated. According to *The Brookings Institute*, Senate Minority leader Chuck Schumer said: "*I want to tell you this: If I become majority leader, one of the first things I will do is we will eliminate it forever….It will be dead, gone and buried*." However, the report also noted that "*[l]ifting the cap on the SALT deduction would massively favor the rich, with most of the benefit going to the top one percent*."

Arizona Voters Approve 77% Income Tax Increase: In early November, Arizona voters approved a tax rate increase from 4.5% to 8%. Touted as a tax on the rich and heavily backed by the state teacher union, the additional 3.5% surtax applies to single persons at $250,000 and married persons at $500,000.

Illinois Voters Reject Income Tax Increase: While Arizonans raised their income tax rate, Illinois voters rejected a Constitutional Amendment which would have replaced the state's 4.95% flat tax with a progressive income tax rate of up to 7.99%. The Amendment was defeated 55% to 45%, reflecting a significant number of Democrat voters breaking ranks with Governor Pritzker and Senator Dick Durbin who supported the Amendment.

New Jersey Set to Enact Millionaire's Tax: As of this writing, New Jersey Governor Phil Murphy and legislative leaders are close to a deal to enact a "millionaire's tax" that would raise the tax rate on those earning more than $1 million from 8.97% to 10.75%. Yet only 2 years ago New Jersey imposed the 10.75% rate on those earning more than $5 million. According to *The Wall Street Journal*, the millionaire's tax is projected to raise $390 million annually and will fund $500 rebates to families earning less than $150,000.

Recovering Lost Funds: Given the geographic mobility of most Americans, it is not uncommon for an "old" asset or account to be forgotten. To address this concern, the National Association of Unclaimed Property Administrators has endorsed the website *www.missingmoney.com*. "Missingmoney" is a free website that can identify old bank accounts, insurance policies, stocks, bonds and safety deposit box contents. To utilize the website, simply enter your name and the state(s) in question.

Paralegal Michelle Taylor Joins Firm: We are pleased to announce that Michelle Taylor has joined the law firm as an Estate and Trust Administrator. Michelle was born and raised in Cleveland, Ohio, holds a B.S. degree in Legal Studies, is a Florida Registered Paralegal and has qualified as an Advanced Certified Paralegal by the *National Association of Legal Assistants*. Michelle has worked in the legal field for almost 20 years and handled hundreds of estates. Michelle and her husband have two children, ages 26 and 24. Outside of work, Michelle enjoys spending time with her family and training her dogs.

Words of Wisdom: "*So Peter opened his mouth and said…God anointed Jesus of Nazareth with the Holy Spirit and with power. He went about doing good and healing all who were oppressed by the devil, for God was with him. And we are witnesses of all that he did…[t]hey put him to death by hanging him on a tree, but God raised him on the third day and made him to appear, not to all the people but to us who had been chosen by God as witnesses, who ate and drank with him after he rose from the dead. And he commanded us to preach to the people and to testify that he is the one appointed by God to be judge of the living and the dead. To him all the prophets bear witness that everyone who believes in him receives forgiveness of sins through his name."* Acts 10:34-43.

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