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WHAT'S NEW IN ESTATE PLANNING

2020 ANNUAL REVIEW

1. FEDERAL ESTATE TAX

A. **$11,580,000 Estate Tax Exemption** (Rev. Proc. 2019-44): The amount you can leave free of estate tax for a death in 2020 is increased by $180,000 as indexed for inflation. A married couples can leave double, which is $23.16 million.

B. **Sunset:** In 2026, the Exemption will return to $5,000,000, plus an amount indexed for inflation, unless the law is changed.

2020	$11,580, 000	+ 40% tax on amount over
2021-2025	same indexed	+ 40% tax on amount over
2026	$ 5,000,000	+ 40% tax on amount over

plus index for inflation (approx. $6 million)

C. **No Clawback** (REG-106706-18; §20.2010-1): The IRS issued final regulations that avoid potential claw back of gifts made before end of 2025 for those dying after 2025.-The result is that any potential claw back of gifts made before the end of 2025 is avoided for those dying after 2025. For example, if you gift $11 million this year, and then die in 2026 when the exemption returns to $5 million, the IRS will not "claw back" $6 million and charge a 40% tax.

D. **Use it or lose it?** In order to use all or a portion of your $11.58M exemption before you lose it in 2026, you would need to make a gift of more than $6 million (the approximate exemption amount in 2026). If you make a $7 million gift, you would preserve $1 million of your exemption ($7 million -$6 million). Since there would have been a 40% tax on the $1 million, the $7 million gift would save $400,000 in federal estate tax upon your death, which is 5.7% of the $7 million.

E. **Stepped-Up Income Tax Basis**: Most assets which you own at death receive a new income tax basis equal to the date of death value. This means that your lifetime gain and loss is eliminated. Assets which do not receive a new income tax basis are retirement plans, IRA's, annuities, and installment sale notes. If you gift assets in your lifetime, those assets will not receive a new income tax basis.

F. **Beneficiaries were liable for estate's unpaid tax liability** (U.S. v Ringling): Estate filed a Federal Estate Tax Return (Form 706)but did not pay the tax due. For 3 years, the IRS kept sending notices of the balance due. The US obtained a judgment against each beneficiary personally for the tax due (transferee is personally liable).

2. GIFT TAXES

A. **$11,580,000 Gift Tax Exemption (Rev. Proc. 2019-44)**

B. **No Clawback (REG-106706-18; §20.2010-1)**

C. **$15,000 Annual Gift Tax Exclusion ($30,000 per couple): unchanged**

D. **Unlimited Medical and Educational Expenses:** You can pay anyone's medical care and educational expenses if you make your payment directly to the provider of services. These transfers do not count against your Gift Tax Exemption.

E. **Carryover Income Tax Basis**: When you make a gift, you give your income tax basis (cost, plus improvements, less depreciation) to the recipient. In general, this means that your donee will continue to hold your capital gain or loss.

3. GENERATION SKIPPING TRANSFER TAX (GST)

A. **$11,580,000 Gift Tax Exemption (Rev. Proc. 2019-44)**
B. **No Claw back (REG-106706-18; §20.2010-1)-**assume same
C. **$15,000 Annual Gift Tax Exclusion ($30,000 per couple): unchanged**

4. RETIREMENT PLANS

The SECURE ACT- Changes to Retirement Plan Distribution Rule
The Setting Every Community Up for Retirement Enhancement (SECURE) Act was signed into law on December 20, 2019 and became effective January 1, 2020.

The aim of the Act is to prevent older American's from outliving their assets. Some of the cost of the bill will be paid for by the acceleration of the income tax due on an IRA after the death of the owner. The cost to support the older Americans will be paid by the younger Americans.

A. DEATH BEFORE 2020: OLD RULES APPLY

1. **Spousal Rollover:** A surviving spouse can "rollover" an IRA and take RMDs over their life expectancy (ex. 20 years). When the surviving spouse dies, however, the new 10 YEAR rule applies to the beneficiaries.

2. **Inherited (Stretch) IRA:** A surviving child can set up an Inherited IRA and take RMDs over their life expectancy (ex. 50 years). A surviving grandchild can set up an inherited IRA and take RMDs over their life expectancy (ex. 80 years).

   PLANNING OPPORTUNITY: Disclaimer by Spouse: A surviving spouse may want to disclaim all or a portion of the IRA within 9 months of the owner's death if the children are contingent beneficiaries so that the children can use the life expectancy "stretch" payout. (This would be as late as September 30, 2020 for a death on December 31, 2019).

B. EFFECTIVE DATE OF SECURE ACT

1. **Jan. 1, 2020**: Law passed Dec. 20, 2019 and affects death after 2019.

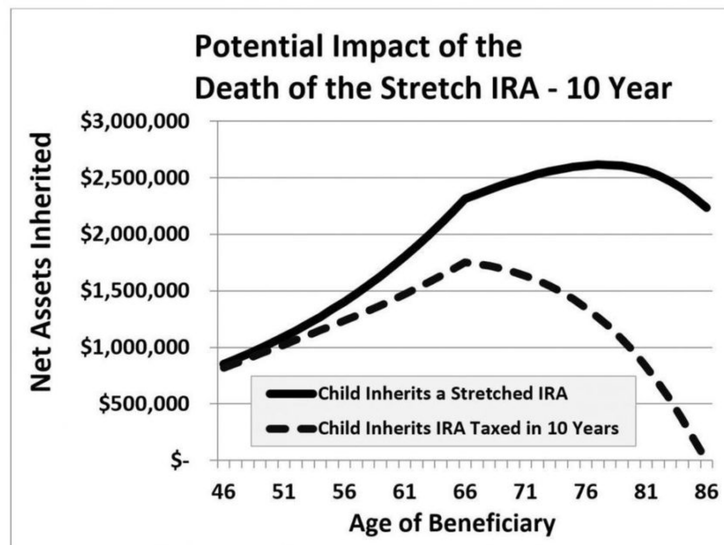
2. **Pre 2020 deaths**: The designated beneficiary can continue to use the life expectancy payout on an Inherited IRA.

3. **Post 2019 deaths**: The designated beneficiary must use the 10-year payout.

C. DEATH AFTER 2019: PAYOUT - 10 YEARS VS. LIFE EXPECTANCY

1. **Designated Beneficiary (DB):** 10-year payout.

   Stretch IRA is Gone: The "Stretch IRA" is gone and is replaced by a maximum 10 YEAR post-death payout. For example, children and grandchildren can no longer use their life expectancy for RMD payouts. They must receive the entire IRA by December 31st of the 10th anniversary of the Owner's death and pay the income taxes owing.



2. **Eligible Designated Beneficiary (EDB):** Life Expectancy Payout.

   i. Spouse
   ii. Minor Child of Participant (until majority, then 10-year payout)
   iii. Disabled Person
   iv. Chronically Ill Person
   v. Person not more than 10 years younger

3. **Non-Designated Beneficiary (Non-DB):** 5-year payout.

   i. Not naming a beneficiary
   ii. A named beneficiary doesn't survive
   iii. Naming the Estate as a beneficiary
   iv. Naming a trust as beneficiary that doesn't qualify for "see-through treatment"

D. LIFE EXPECTANCY PAYOUT

1. Spouse as beneficiary: Outright v. Trust

i. **Outright**: Spouse rolls over, names own beneficiaries, withdraws over life expectancy when deceased participant would have been age 72. At death of spouse, 10-year payout. Simple but no control over spouse's withdrawal or spouse's designation of beneficiaries.

ii. **Trust for Spouse**:

a. **Conduit Trust**: Treat like spouse and gets life expectancy payout. Special language in the trust. At death of spouse, 10-year payout to beneficiaries. Control over spouse's withdrawals and designation of beneficiaries. Use in second marriage or a spendthrift spouse.

b. **QTIP-Conduit Trust**: This trust requires that the greater of all income or RMD (life expectancy payout) must pass through to the spouse. In addition, this trust gets the marital deduction for federal estate tax purposes.

c. **Income Only Trust**: This is an accumulation trust with a 10-year payout. This could be a QTIP Trust or Trust B (Bypass/Credit Shelter/Exemption Trust) that lacks the "conduit language" to distribute RMD's to the spouse.

2. Minor Child (of Participant): Outright v. Trust

i. **Outright**: Name a Custodian (until age 25 in California) for the child under CUTMA as beneficiary, who will establish the inherited IRA account. Life expectancy payout until age of majority under state law, but once an adult, then 10-year payout. Under California law, this would be age 18 plus 10 years, which is age 28 as the end of the 10 years. Custodian would withdraw from IRA and pay expenses to or for the child. Custodian would establish another Custodial account to hold withdrawals not yet spent.

ii. **Trust**:

a. **Conduit Trust**: Life expectancy payout until age of majority under state law, but once an adult 10-year payout. All distributions from the IRA pass through the trust to the beneficiary.

b. **Accumulation Trust**: 10-year payout. Trustee can keep distributions from the retirement plan, i.e. accumulate distributions, and/or make distributions to the beneficiary. Health, education, maintenance and support. "See through trust" if all beneficiaries are individuals, both income and remainder beneficiaries. No charitable remainder beneficiary.

c. **Multiple Minor Beneficiaries:** If there are many minor children, when does the 10-year rule start? When the oldest or youngest attains majority?

3. **Disabled Person or Chronically Ill Person: Outright v. Trust**
   i. **Outright**: This get a life expectancy payout.
   ii. **Trust**:
      a. **Conduit Trust**: Life expectancy payout.
      b. **Accumulation Trust**: Life expectancy payout if a see-through trust with sole life beneficiary. This means there is no sprinkling to other beneficiaries.
   iii. **Definitions:** What is the definition of disabled or chronically ill person? Must they qualify for Social Security Disability benefits?
   iv. **Lower Income Tax Bracket**: Consider naming siblings and/or unmarried partner as beneficiaries if they are in lower income tax bracket than very successful children.

4. **Individual not more than 10 years younger (Siblings, Unmarried Partner):**
   i. **Outright**: This get a life expectancy payout.
   ii. **Trust**:
      a. **Conduit Trust**: Life expectancy payout.
      b. **Accumulation Trust**: 10-year payout.

E. <u>10-YEAR PAYOUT</u>

1. **Designated Beneficiary**: Individual

2. **Designated Beneficiary**: "See-Through Trust"

   i. **Conduit Trust:**
      a. Single Beneficiary
      b. All distributions from the retirement plan to the trust must "pass through" to the individual beneficiary. Special language in the trust.

c. Trustee loses control over all distributions from the retirement plan.

ii. **Accumulation Trust:**

a. Any other trust if trustee can keep any distributions from the retirement plan, i.e. accumulate distributions.

b. "See through trust" if all beneficiaries are individuals, both income and remainder beneficiaries.

IRA Termination vs. Trust Termination: IRA terminates at 10 years and must be paid to the trust. Can be severe income tax consequences since trust is in the highest income tax bracket. Trust does not have to terminate at 10th year.

PLANNING OPPORTUNITY - Amendment to Trust: If you have a conduit trust as your retirement plan beneficiary, consider changing from a conduit trust to an accumulation trust. Although the IRA must payout within 10 YEARS, The accumulation trust allows the trustee to continue to administer the trust for the beneficiary beyond the 10-year period.

3. **Example: Adult children or grandchildren as beneficiaries**:

i. **Outright**: Child/grandchild establishes "inherited IRA account" with a 10-year payout.

ii. **Trust for Child/Grandchild**:

a. **Conduit Trust**: 10-year payout. All distributions from the IRA pass through the trust to the beneficiaries. There is no life expectancy payout. The dynasty stretch IRA Trust is gone. Could wait until the end of the 10th year for distribution, when total income tax is owing unless Roth IRA.

b. **Accumulation Trust**: 10-year payout. Trustee can keep distributions from the retirement plan, i.e. accumulate distributions, and/or make distributions to the beneficiary. Health, education, maintenance and support. "See through trust" if all beneficiaries are individuals, both income and remainder beneficiaries.

c. **Trust Advantages/Disadvantages**: Creditor/divorce protection. Management for a spendthrift beneficiary. Control

distribution if beneficiary dies before 10 years. Trust tax returns and accounting must be filed annually.

F. CHARITY: ZERO INCOME TAX

1. **Outright**: There is no income tax when a retirement plan is distributed to a charity.
2. **PLANNING OPPORTUNITY - Charitable Remainder Trust Replicates the Stretch IRA:** A Charitable Remainder Trust (CRT) is a trust that is required to distribute a percentage of trust assets to an individual for life or up to 20 years, when the trust ends and the balance goes to charity. The payout to the individual can be between 5% and 50%, with 10% remainder to charity. While the 10 YEAR payout rule applies, if the IRA is payable to a CRT, the CRT isn't taxed on either the distribution from the IRA or the income and gains it earns. The result is similar to the "stretch IRA". Do the math.

G. OTHER CHANGES FROM SECURE ACT

1. **Eliminates 70 ½ Age Restriction on IRA Contributions:** With Americans living longer and working beyond the traditional retirement age, they can now contribute at any age as long as they have compensation.
2. **Increases the Age for Required Minimum Distributions (RMDs) to 72:** The law increases the age for Required Minimum Distributions (RMDs) from 70 ½ to 72 years of age. For individuals born on or before June 30, 1949, the old rules apply; they must begin taking RMDs as of April 1 of the year after they reach 70 ½. For individuals born on or after **July 1, 1949**, the first RMD is April of the year after they reach 72.

H. WHAT SHOULD I DO? REVIEW YOUR IRA BENEFICIARIES

1. **Beneficiary Designation Form:** Obtain a copy of your Beneficiary Designation form from each institution that holds your IRA or retirement plan (e.g., Schwab). For corporate pension plans, contact your plan administrator.
2. **Professional Review**: Bring the beneficiary designation form to meet with your estate planning attorney.

RESOURCE FOR PROFESSIONALS: Natalie B. Choate, Attorney and national expert on estate planning for retirement benefits: https://www.ataxplan.com/.

5. **INCOME TAXES**

A. **Key Provisions for 529 Accounts:** The law expands the definition of a tax-free qualified distribution from a 529 savings plan to include repayment of up to $10,000 in qualified student loans, and expense for certain apprenticeship programs. The SECURE Act makes this change retroactive to distributions made after December 31, 2018. Parents who may have funds remaining in an educational savings account may want to help a child who has already graduated.

B. **ABLE Accounts IRC 529A:** ABLE accounts are a special type of investment designed to allow persons with disabilities to control and grow money in a tax-free environment without jeopardizing their eligibility for public benefits like Supplemental Security Income (SSI), Medi-Cal, Section 8 ("HUD housing"), CalFresh ("food stamps"), and all other federal public benefit programs with a financial eligibility test.

C. **Can North Carolina Tax a Trust's Undistributed Income? (<u>North Carolina Dep't of Revenue v The Kimberley Rice Kaestner 1992 Family Trust</u>)**:

Grantor, a New York resident, established a family trust for his children and grandchildren. The trust gave the trustee "absolute discretion" to distribute the trust assets to the beneficiaries "in such amounts and proportions" as the trustee might "from time to time" decide. One daughter and her minor children moved to North Carolina. Based solely on the beneficiaries' residence in North Carolina, the state taxed the trust for the taxable years 2005-2008 in an amount exceeding $1.3 million. The US Supreme Court held that to satisfy the due process clause, there must be "some minimum connection, between a state and the person, property or transaction it seeks to tax." Significantly, the trust funds were undistributed and the beneficiaries had not received a distribution of trust funds during the relevant years.

California trust law taxes "the entire taxable income of a trust if the fiduciary or beneficiary (other than a beneficiary whose interest in such trust is contingent) is a resident, regardless of the residence of the settlor." Cal. Rev. & Tax Code §17742(a).

6. WILLS AND TRUSTS

A. **The Case of the Post-it Note (<u>Pena v Dey</u>).**Settlor sent a note to his attorney, including handwritten interlineations on one of the trust documents, making Friend beneficiary of the trust. But the handwritten interlineations were not signed and Settlor died before a formal amendment was prepared for his signature. Was it an effective amendment? A Post-it® note on the document, signed "Best, Rob," did not satisfy express Trust requirements that amendments "be made by written instrument signed by the settlor and delivered to the trustee." Although the court acknowledged that Settlor obviously intended to make Friend a beneficiary, here the interlineations

constituted a written instrument separate from the executed trust and did not satisfy trust modification provisions.

B. **Is this a Trust? (<u>Jones v Remark-Aripez</u>).** One of the six beneficiaries (Preferred Beneficiary) was designated as successor trustee and also given Grantor's house, "to use in [her] discretion for the benefit of all beneficiaries" of his living trust. Preferred Beneficiary intended to distribute all real property assets to herself, free of trust. The appellate court noted that Grantor used "quintessential trust language — 'for the benefit of all beneficiaries,'" which compelled a finding that Grantor intended the real property be held in trust for all beneficiaries. Further, the language did not include Grantor's wishes or desires, but instead was assertive and direct, placing an "imperative obligation" on Preferred Beneficiary to hold the real property in trust. Living trust beneficiary, given discretionary use of real property "for the benefit of all beneficiaries," must hold property in trust. All beneficiaries must receive equal value of property, whether it is rented, sold, or made productive in some other way.

C. **When does Medi-Cal get Reimbursement from a Trust? (<u>Gonzalez v City Nat'l Bank</u>).** A trust was formed with medical malpractice settlement assets to be used specifically to pay for the beneficiary's future medical expenses. After 21-year-old special needs trust beneficiary's death, Department of Health Care Services entitled to reimbursement under Prob C §3605 from trust remainder for beneficiary's Medi-Cal service payments. Public policy considerations favor DHCS's full reimbursement. However, if a parent creates a "3rd" party special needs trust to receive the beneficiary's inheritance, then Medi-Cal does not receive reimbursement from the trust after the beneficiary's death.

D. **When is Child Support payable from a Trust?** (**<u>Cleopatra Cameron Gift Trust</u>**) Husband was granted custody of two children His ex-wife received $40k per month from her parents' trust. The California family court ordered direct payments from the parents' trust to husband for child support. However, the trust was administered under South Dakota law and the trust's spendthrift provision prohibited direct payments of former wife's child support obligation to her ex-husband.

   Therefore, the South Dakota Court held that the enforcement power under California Probate Code §15305 did not compel direct payments from the trust in South Dakota because that self-executing enforcement method was prohibited by South Dakota law.

E. **What Happens if My Beneficiary Dies before Me? (<u>Estate of Stockird</u>)** Decedent left holographic (handwritten) will: 65% of the estate to the life partner and 35% to Aunt "by marriage". What happens to Aunt's share if she doesn't survive Decedent?

   If she was "kindred", it would pass to her heirs. In this case, since she was not "kindred" as she was an aunt-by-marriage, her share lapses and goes to life Partner.

F. **Did the Child "Contest" the Trust? (<u>Key v Tyler</u>).** Attorney daughter unduly influenced her aged mother to disinherit other children in an amendment to mother's trust. Another child contested the Amendment. The Court held that the "No Contest Clause" was enforceable against the attorney daughter for DEFENSE of the amendment. The beneficiary's defense of trust amendment obtained through undue influence in invalidity action met trust's definition of a contest triggering disinheritance and no-contest clause in trust.

7. <u>ADMINISTRATION</u>

A. **Transfer of Personal Property without Probate (PC 13100):** Increases, from $150,000 to $166,250, the maximum value of a decedent's estate for which an affidavit or declaration to collect decedent's personal property outside the formal probate process may be used.

B. **"Non-Marital" Biological Daughter Could not Sue for Wrongful Death of Father (<u>Stennett v Miller</u>):** Decedent man conceived daughter but he wanted no contact with the child. Mother never sought a court order of paternity. When the daughter was 10, Decedent was killed in an auto accident by drunk texting driver. Mother filed Petition to declare daughter as heir-at-law so she could pursue a wrongful death action. DNA proved daughter was decedent's child. The court held that the daughter had no right to inherit from her father under intestate succession because he "never openly held her out as his own child". Therefore, she had no right to sue for wrongful death as his heir. A state may validly impose different requirements for establishing natural parent status for birth mothers and biological fathers because mothers and fathers are not similarly situated when it comes to their role in becoming parents

C. **Granddaughter Removed as Administrator for Mismanagement (<u>Estate of Sapp</u>):** Granddaughter as administrator and personal representative of grandfather's estate could be properly removed under Prob C §8502(a), given her mismanagement of estate. Administrator's 15-year-long delay tactics in blocking the estate property sale, her denial of the court's instructions, and her attempts to buy out the heirs for much less than they would be entitled to from proceeds of a sale were done in bad faith and intentionally.

8. <u>ELDER LAW & ELDER ABUSE</u>

A. **Hospital Not Liable for Elder Abuse for failing to follow dying patient's health care directive (<u>Alexander vs. Scripps Memorial Hosp La Jolla</u>)**: 70-year-old woman transferred from a skilled nursing facility (SNF) to Hospital for end-state terminal pancreatic cancer care. Her Advance Health Care Directive stated that she wanted to prolong life. However, the Hospital health care professionals refrained from providing Patient with certain advanced life support measures because, in their view, such measures would have been ineffective and would have caused her

additional suffering. The Court found there this was not elder abuse and not a violation of health care directive.

B. **Financial Advisors are "Mandated Reporters" - (<u>Welfare and Institutions Code Section 15630.1</u>)**This new law adds securities broker-dealers and investment advisors to the categories of persons who are mandated reporters of suspected abuse of an elder or dependent adult; allows mandated reporters who report suspected abuse to notify a trusted contact person previously designated by the elder or dependent adult for that purpose, as specified; and allows mandated reporters to temporarily delay requested account transactions and disbursements of elder or dependent adults, as specified. Requires a mandated reporter of suspected elder or dependent adult financial abuse, who has direct contact with the elder or dependent adult, or who reviews or approves the elder or dependent adult's financial documents, records, or transactions in his or her role as a financial services provider, and who has observed or has knowledge of an incident that reasonably appears to be financial abuse, or who reasonably suspects such abuse, to report the known or suspected abuse as soon as practicably possible to the local adult protective services agency or the local law enforcement agency.

C. **What if You Marry your Caretaker? (<u>Probate Code 21380</u>)**. This law prohibits a surviving spouse from receiving a share of the decedent's estate, if the spouse was a care custodian of the decedent who was a dependent adult and the marriage commenced while the care custodian provided services to the decedent, or within 90 days after those services were last provided to the decedent, and the decedent died less than 6 months after the marriage commenced, unless the spouse can prove by clear and convincing evidence that the marriage was not the product of fraud or undue influence. This effectively closes a loophole that allowed care custodians to avoid the presumption of fraud or undue influence that applies to donative transfers made to certain beneficiaries.

9. <u>INSURANCE</u>

A. **Keep Life Insurance Beneficiaries Up to Date (<u>State Farm Life & Acc. Assur. v D'Allessandro</u>).** In a marriage dissolution, the Court ordered decedent to maintain insurance payable to kids but Decedent didn't change beneficiary from former spouse to kids. The Court awarded the death benefit to two of three minor children of decedent, who were by divorce decree named as insured beneficiaries.

B. **Cannot Use Power of Attorney to Change Life Insurance Beneficiaries (<u>Metropolitan Life Ins. Co. v Razo</u>).** Uncle named Nephew 1 as life insurance beneficiary. After Uncle was diagnosed with pancreatic cancer and medicated, Uncle signed statutory short from power of attorney (POA) naming Nephew 2 as agent. Nephew 2 signed change of beneficiary form under POA on life insurance and changed the beneficiary to himself. Uncle died two days later. The statutory short

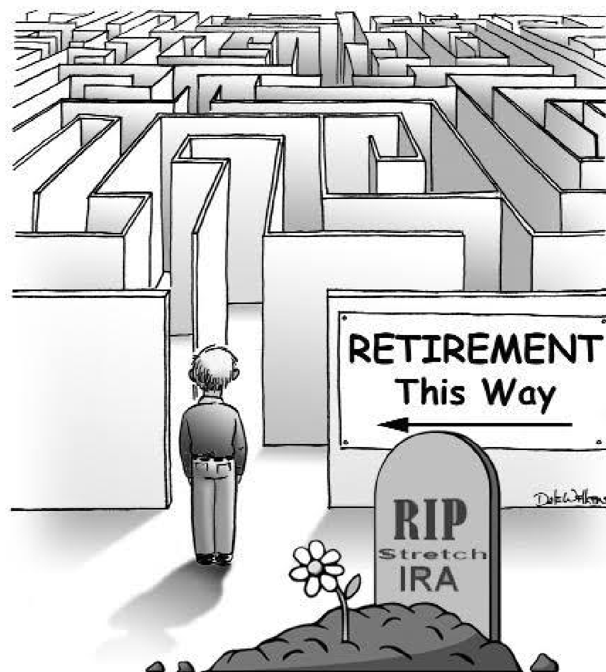
form power of attorney did not authorize agent to change beneficiary on grantor's life insurance, thus, change was invalid.

10. PROPERTY RIGHTS

A. When is Community Property "Transmuted" into Separate Property? (Marriage of Begian & Sarajian) Mother, Husband and Wife signed a deed transferring the property to Wife as "a bonafide gift". Husband and Wife divorced and Husband claimed the property was still Community Property. Wife claimed it was her Separate Property. The Court held that when the real property was conveyed to Wife by deed, the transaction lacked express declaration to constitute transmutation of Husband's community property interest into Wife's separate property. There was no express declaration of transmutation Fam C 852.

B. Premarital Agreement 7 Day Rule (In re Marriage of Clarke & Akel). Husband downloaded a premarital agreement from the internet and presented it to Wife, who took to her attorney. The attorney modified the agreement and returned to Husband and told Husband to get own Attorney. Husband signed the agreement the next day. Husband now claims the agreement is not enforceable because it was not presented to him seven days before marriage. The Court held that Wife could not enforce a premarital agreement when evidence showed Husband had not been provided seven calendar days to review the document, had not been advised of the rights he was giving up in the agreement, and had not executed a written waiver of those rights.

IN CONCLUSION….



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