# The Income Tax Is the New Estate Tax?

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**"I conceive that the great part of human miseries of mankind are brought upon them by false estimates they have made of the value of things."**
**Benjamin Franklin**

**"The future belongs to those who prepare for it."**
**Ralph Waldo Emerson**

**"Face reality as it is, not as it was, or as you wish it to be."**
**Jack Welch, Former Chairman GE**

**Basic Estate Planning Outline**

## I. Interdisciplinary Approach

- CPA, Attorney, Financial Consultant and CLU
- Process - requires series of actions
- Decision making - based upon information available at the present time
- A decision not to do estate planning now is a decision
- Importance of building relationships with the appropriate professionals. Need a network of individuals you and your family are comfortable with and trust.

## II. Importance of A Will

- Court-appointed administrator
- Court-appointed guardian for minor children
- Intestacy statutes

## III. What A Will Does

- Controls legal disposition of assets in the name of the decedent

- Governs appointment of fiduciaries
  - Executor/Executrix
  - Trustee
  - Guardian

- Tax Planning

## IV. What A Will Does Not Do

- Control the disposition of assets held in joint names
- Control the designation of life insurance proceeds
- Control the distribution of qualified retirement plan and IRA assets

## V. Federal Estate and Gift Tax System Unified in 1981/De-unified in 2001/Re-Unified in 2010 until the end of 2025.

- Gift tax annual exclusion $19,000 per donee.

- Estate and Gift tax life-time exclusion $13,990,000 in 2025.

- Direct payment of college tuition and medical expenses for donees are not counted as reportable gifts.

VI. • **Gross Estate:**

Assets pass by Will; By Contract; By Operation of Law.
Existence, Ownership and Valuation of decedent's assets.
Probate Assets vs. Non-Probate Assets.

- Internal Revenue Code Section 2033(a) provides in part that the gross estate of a decedent who was a citizen or resident of the United States at the time of his/her death includes the value of all property, whether real or personal, tangible or intangible, and wherever situated, **beneficially owned by the decedent at the time of his/her death {emphasis added}.**

  **Examples of Includible Assets:**
  -Assets in name of decedent
  -One-half of joint accounts with spouse [Be Aware of Gallenstein Case]
  -Transfers with retained interests (IRC Sec. 2036)
  -Retirement plan and IRA assets
  -Life Insurance owned by decedent
  -One-half of joint accounts with someone other than spouse
  -Power of Appointment Trusts

- Date of Death Value vs. Alternate Valuation Date

- **All decedent's assets in gross estate are stepped-up to fair market at the date of death IRC 1014(a).**

- **The basis of property received from a decedent is generally the fair market value of the property on the date of death. This is extremely favorable because it mitigates the gain on assets sold by the heirs.**

- Marital deduction – assets passing to surviving spouse

- Charitable deduction-assets passing by charitable bequest

- Administrative expenses-Executor Fee, Accountant, Attorney, Funeral

- **IRC 2010 allows the estate of the first spouse to die to elect to transfer any unused applicable exclusion amount, i.e. the deceased spouse unused exclusion, a/k/a DSUE to the surviving spouse.**

## VII. State Estate Tax Consideration

- New Jersey eliminated its estate tax effective January 1, 2018.

- New Jersey has retained its inheritance tax which is a tax on the transfer of assets to non lineal descendants. Tax is as high as 16%.

- Gifts made to non lineal descendants within three years of the decedent's death are brought back into the decedent's gross estate for New Jersey Inheritance Tax.

- New York State decoupled its estate tax from the Federal estate tax law.

- New York State Estate Tax exclusion is $7,160,000.

- Special rules apply to New York Estates which exceed 105% of the $7,160,000 New York Estate Tax Exclusion.

- New York State does not recognize portability.

## Income and Estate Tax Facts
## Tax Year 2024

| Income Tax Brackets | Rate | Estate Tax Brackets | Rate |
|---|---|---|---|
| Top Federal Income Tax Rate | 37.00% | Top Federal Estate Tax Rate | 40.00% |
| Top Federal Capital Gains Tax Rate | 20.00% | | |
| Net Investment Tax to Fund ACA | 3.80% | | |
| Top New Jersey Income Tax Rate | 10.75% | Top New Jersey Estate Tax Rate | 0.00% |
| | | Top New Jersey Inheritance Tax Rate | 16.00% |
| Top New York State Income Tax Rate | 10.90% | Top New York State Estate Tax Rate | 16.00% |
| Top New York City Income Tax Rate | 3.88% | | |

## Long-Term Capital Gains and Qualified Dividends Tax Rate
## Tax Year 2024

| Filing Status and Taxable Income | Rate |
|---|---|
| Single - up to $47,025 | 0.00% |
| Married Filing Jointly - up to $94,050 | 0.00% |
| Married Filing Separately - up to $47,025 | 0.00% |
| Head of Household - up to $63,000 | 0.00% |
| Single - $47,026 to $518,900 | 15.00% |
| Married Filing Jointly - $94,051 to $583,750 | 15.00% |
| Married Filing Separately - $47,026 to $291,850 | 15.00% |
| Head of Household - $63,001 to $551,350 | 15.00% |
| Single - over $518,900 | 20.00% |
| Married Filing Jointly - over $583,750 | 20.00% |
| Married Filing Separately - over $291,850 | 20.00% |
| Head of Household - over $551,350 | 20.00% |

**Case Study # 1**
**Nancy John**
**New Jersey Resident**
**Unmarried Indiviual**
**<u>Assets Passing To Nieces And Nephews (Class D Beneficiaries)</u>**

| Assets: | | Basis | Fair Market Value | Unrealized Gain |
|---|---|---|---|---|
| Personal Residence | | $ 500,000 | $ 2,000,000 | $ 1,500,000 |
| Partner Interest in FLP | | 200,000 | 1,000,000 | 800,000 |
| General Electric Stock | | 250,000 | 1,000,000 | 750,000 |
| Rental Real Estate | | 150,000 | 1,000,000 | 850,000 |
| | | $ 1,100,000 | $ 5,000,000 | $ 3,900,000 |

| Nancy Holds All Assets Until Her Death: | | |
|---|---|---|
| Federal Estate Tax | | $ - |
| New Jersey Estate Tax | | - |
| New Jersey Inheritance Tax [$ 5,000,000 Times 16%] | | 800,000 |
| Income Tax on Sale of Nancy John's Assets | | - |
| **Total Taxes** | | $ 800,000 |


| Nancy Gives Away All Her Assets And Lives More Than Three Years After Her Gift: | | |
|---|---|---|
| Federal Estate Tax | | $ - |
| New Jersey Estate Tax | | - |
| New Jersey Inheritance Tax | | - |
| Income Tax on Sale of Nancy John's Assets: | | |
| Federal Income Tax | 20.00% | 780,000 |
| ACA Surcharge | 3.80% | 148,200 |
| New Jersey Income Tax | 8.97% | 349,830 |
| **Total Taxes** | | $ 1,278,030 |


| Nancy Gives Away All Her Assets And Does Not Live More Than Three Years After Her Gift: | | |
|---|---|---|
| Federal Estate Tax | | $ - |
| New Jersey Estate Tax | | - |
| New Jersey Inheritance Tax | 16.00% | 800,000 |
| Income Tax on Sale of Nancy John's Assets: | | |
| Federal Income Tax | 20.00% | 780,000 |
| ACA Surcharge | 3.80% | 148,200 |
| New Jersey Income Tax | 8.97% | 349,830 |
| **Total Taxes** | | $ 2,078,030 |


***For Illustrative Purposes Only.***

## Definitions:

### Tenancy-in-common:

Undivided interest in real or personal property. Each co-tenant owns his/her proportionate interest in the entire property which extends beyond the death of any one co-tenant. Each co-tenant possesses the right to secure a partition of the property or to otherwise dispose of his/her interest.

**Example:** A, P and E acquire real property in New Jersey for $3,000,000 and build a Ritz Carlton Hotel across from Met Life Stadium in East Rutherford, New Jersey. A, P and E each contribute $1,000,000 to the cost of the property and each owns a one-third tenant-in-common interest in the property. A dies while owning a one-third tenant-in-common interest in this property. At the time of A's death, the property had a fair market value of $9,000,000. A's gross estate would include one-third of the $9,000,000 or $3,000,000 subject to minority interest discount. P and E continue to own their respective one-third tenant-in-common interest in this property along with the estate of A. **A's interest in this property passes to his heirs under the terms of his Last Will and Testament.**

### Joint Tenancy:

A joint tenancy in real or personal property exists where title to the property is held by each joint tenant with the right of survivorship. Upon the death of a joint tenant, the deceased joint tenant's rights terminate and title to the respective property rests in the survivor(s) by operation of law. During his or her lifetime, a joint tenant usually possesses the right of severance---the right to have the property partitioned or to sell his or her interest to another. In the event of severance, either through partition or sale, the right of survivorship ceases.

**Example:** A, P and E acquire real property in New Jersey for $3,000,000 and build a Ritz Carlton Hotel across from Met Life Stadium in East Rutherford, New Jersey. A, P and E each contribute $1,000,000 to the cost of the property and take title to the property as joint tenants with the right of survivorship. A dies while owning a one-third joint interest in this property. At the time of A's death, the property has a fair market value of $9,000,000. A's gross estate would include one-third of the $9,000,000 or $3,000,000, however, P and E would now own the entire property as title to the property rests in the survivors by operation of law. **A's Last Will and Testament does not control the disposition of this asset.**

## <u>Tenancy-by-the-Entirety:</u>

A joint tenancy between husband and wife with one salient difference-there is an absence of the right of severance, except by divorce. H (husband) may transfer his interest to W (wife), but he cannot sell to another or secure a partition of the property. H & W together can terminate their tenancy-by-the-entirety by selling or transferring their interest to a third party.

### Tenancies by the Entirety Created Prior to 1/1/1977:

Prior to Tax Reform Act of 1976, IRC Section 2040 provides that tenancies by the entirety are included in the gross estate of the first spouse to die **unless it can be proved that the surviving spouse contributed to the cost of the property (emphasis added).**

**Example:** H & W(husband and wife) acquire a summer home at the Jersey Shore in 1975 for a cost of $75,000. H dies in 2019.
The summer home's fair market value at the time of H's death is $4,700,000. You examine the recorded deed to the property and ascertain that H & W acquired the property as tenants by the entirety in 1975.

Based upon IRC Section 2040, you report the entire $4,700,000 in the Gross Estate of H for a 100% basis step-up. The surviving spouse's basis in this property is $4,700,000.

### Tenancies by the Entirety Created Post 12/31/1976:

IRC Section 2040, as amended by the Tax Reform Act of 1976, provides that one-half of the value of the tenancy will be included in the gross estate of the deceased spouse **regardless of who furnished the consideration for the property (emphasis added).**

**Example:**

H &W (husband and wife) acquire a summer home at the Jersey Shore in 1980 for $95,000. H dies in 2019. The summer home's fair market value at the time of H's death is $4,700,000. You examine the recorded deed to the property and ascertain that H & W acquired the property as tenants by the entirety in 1980.

Based upon IRC Section 2040, you report the one-half of $4,700,000 in the Gross Estate of H. The surviving spouse's basis in this property is $2,350,000 plus one-half of her original cost basis plus improvements.

# Elements of a Trust

**All trusts include three elements: a grantor, a beneficiary, and a trustee.**

## Grantor:

The person or institution who transfers assets into the trust. If you create a living trust for your children, you are the grantor.

## Beneficiary:

A person or institution who will receive money or other assets from the trust, according to the terms established in the trust documents.

## Trustee:

A person or institution with the duty to manage, invest, and distribute assets in the trust. Note that while all living trusts contain a grantor, beneficiary, and trustee, these need not be separate individuals. For example, a grantor might create a trust for tax or other purposes in which he or she is also the trustee and/or beneficiary.

## Irrevocable Trust:

A trust which, once created, generally may not revoked or amended by the grantor. Most trusts used for income, gift, or estate tax planning, are irrevocable in order to gain the tax advantages.

## Revocable Trust:

A trust that is subject to being revoked or amended by the grantor. Often used in cases when the primary objective is to maintain privacy during the grantor's life, or after his or her death.

**Living Trust (Inter Vivos Trust):**

Any trust created during the grantor's lifetime, for example a revocable living trust created to protect an estate should the grantor lose competence.

**Testamentary Trust:**

A trust created as part of a last will and testament that takes effect after the grantor dies.

**Charitable Remainder Trust:**

An irrevocable trust created to provide income or annuity payments for a beneficiary (often, the grantor). When the trust expires, the remaining assets are transferred to a charitable organization, which is usually determined by the grantor.

**Insurance Trust:**

An irrevocable trust that holds life insurance policies on one or more individuals. Often used to exclude life insurance proceeds from estate taxes. When the insured dies, the trust receives, manages, and/or distributes the proceeds.

## John M. Lisa

## Statements of Qualifications

John M. Lisa is a Certified Public Accountant in New Jersey and New York. He graduated from Saint Peter's University Jersey City, N.J. with a B.S. degree in accounting cum laude and has a MBA from New York University's Stern School of Business with a concentration in taxation and finance. His professional experience includes working in the audit and tax department of two "Big Four" CPA firms and has been in his own practice for the past forty three years. He was an adjunct professor of accounting at St. Peter's University. He has lectured before business and professional organizations, served as an expert witness, and has published articles in professional journals. Mr. Lisa is an active member of the New Jersey Society of CPAs [NJSCPA] and is the Past President of the Bergen Chapter of the NJSCPA. Mr. Lisa is a recipient of the Paul Harris Fellow from Rotary International. Mr. Lisa served as a coach for the North Caldwell Baseball Association and served on the North Caldwell Board of Adjustment.