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Trust UPDATE

Stillman BANK

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A lawyer writes candidly about living trusts

The American Bar Association, a trade group whose roots go back to 1878, has a variety of subdivisions that its members may participate in. One of these is the Senior Lawyers Division, aimed at older lawyers in any specialty as well as lawyers of any age who specialize in elder law practice. The group publishes a magazine, *Experience*, four times each year.

In the October/November 2019 issue, attorney Mark Cianciulli addressed the question "Should You Put Your Property Into a Trust?" He was writing as one lawyer to another, and as one who has experience with probate and with handling real estate in trusts.

Good reasons for a living trust

The key trust benefit mentioned by Mr. Cianciulli is probate avoidance. He practices in Los Angeles, and reports that in California the minimum cost to probate a $1 million estate is $23,000 each for the personal representative (the legal name for the executor of the estate) and for the probate attorney who will guide the process. The probate attorney may also be entitled to "extraordinary fees" for any work that is considered to be outside the scope of a typical probate process. For example, if a house needed to be sold during probate, the attorney might be entitled to an additional fee if he provided coaching to the real estate agent who handled the transaction. There will also be court fees and other administrative expenses.

Avoiding probate also saves time. "Most probates take a year or more," Mr. Cianciulli writes. The administration of a trust, in contrast, continues without interruption even when the creator dies.

A trust gives an individual much greater control over the disposition of property. Examples listed by Mr. Cianciulli include:

- naming a guardian for children should they be minors at a parent's death;

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A trust gives an individual much greater control over the disposition of property.

- setting an age for children to be in full control of their financial assets;
- providing an alternative to conservatorship for handling one's own assets upon incapacity.

The flexibility of the trust drafting stands in contrast to the rigid rules that the state provides in the absence of planning. "I think the last thing people want is state law to decide who gets what of their estate, and that's exactly what happens when there's no trust and no will," he writes.

Finally, trusts offer financial privacy, they don't ordinarily become public documents as do wills. Says Mr. Cianciulli, "Most people don't realize how beneficial this last feature is until they open a probate matter and are inundated with people calling them to offer their services."

There are some downsides

There is no current cost to ignoring one's estate planning. Having a will drafted costs money immediately, and having a trust prepared may cost more. Mr. Cianciulli suggests that a trust will cost $2,500 or more to create. And it may not be a one-time cost, because there will be new fees if the trust needs to be amended later to take into consideration changes in circumstances.

For the trust to be effective, the real and personal property being placed in the trust must be retitled. That's administrative work, and new deeds may need to be prepared and recorded, which triggers more fees.

Once the property is in the trust, the creator of the trust no longer owns the assets. That fact must be disclosed in any contracts related to the assets. Lenders may require additional administrative procedures before trust assets may be used as collateral.

Finally, trust administration is not free. Whoever is seeing to it that the trust terms are adhered to will have to be paid.

On balance

While acknowledging the costs of creating and managing trusts, Mr. Cianciulli concludes that the benefits are far larger. "In my opinion, the relatively small amount of money and time you'll initially invest to create the trust outweighs the many times larger cost and longer time commitment by the estate and the persons administering the estate. I don't see the sense in spending tons of money on administrators and executors and court fees and expenses if my other option could be to leave more to my beneficiaries."

Our thoughts

Additional points to keep in mind, not mentioned by Mr. Cianciulli, include that when one chooses a professional trustee, such as us, one is also buying investment expertise for the supervision of the trust assets. We take the worry out of portfolio management for our clients. We are also well versed in the fulfillment of the fiduciary duties that are imposed upon trustees by the government. We'd be pleased to tell you more about our capabilities at your earliest convenience.

We'll give the last word to Mr. Cianciulli, because we're not bragging when he says it:

"The sad truth is that many people overlook the decision to create a living trust simply because they aren't aware of all the benefits it can provide them and their family, especially in light of all the negative consequences of not having one." ☐

Good candidates for a living trust

Just one of these qualifications makes you an excellent candidate for a living trust

- ☐ Worried about financial management upon illness or incapacity
- ☐ Owns substantial assets
- ☐ Owns assets in more than one state
- ☐ Family will need immediate access to assets after owner's death
- ☐ Wants financial privacy

Will and won't of the living trust

A living trust CAN	But a living trust WON'T
Help manage your financial life in case you become ill or incapacitated	Reduce or avoid taxes
Transfer assets to your beneficiary	Affect jointly owned property or accounts payable to a beneficiary
Protect your privacy	Protect assets from creditors
Avoid probate	Make a will unnecessary

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Making the move

On October 31 President Trump tweeted: "1600 Pennsylvania Avenue, the White House, is the place I have come to love and will stay for, hopefully, another 5 years as we MAKE AMERICA GREAT AGAIN, but my family and I will be making Palm Beach, Florida, our Permanent Residence." The President explained that he felt badly treated by the authorities in New York. "I hated having to make this decision, but in the end it will be best for all concerned," he concluded. Not coincidentally, Florida is one of seven states with no income tax, while New York has both city and state income taxes. Florida also has no estate tax, while New York does.

It takes more than a tweet to officially change one's residence for tax purposes, of course. Earlier the President and his wife signed declarations of domicile in Florida. That is only the start of the process, however. New York will collect an income tax on anyone who spends 184 days or more in the state. They may try to impose the tax if an individual who travels widely spends more days in New York than in any other location, even when the number is well short of 184. The tax authorities also will look to the location of businesses, art collections, family heirlooms, even pets to determine whether connections have been sufficiently severed to create a change of domicile.

Attending to details is important, because it is quite possible to be taxed as being domiciled in more than one state.

Billionaires on the move

Academic studies have demonstrated that many other billionaires have changed their domicile to avoid state death taxes, just as the President is proposing to do. Beginning in 2001, many states began dropping their estate and/or inheritance taxes. All but one have dropped taxes on gifts. Economists at the National Bureau of Economic Research tracked the movements of people on the Forbes 400 list after 2001 and found:

- The number of billionaires in states with estate taxes fell by 35% after 2001.
- Billionaires' sensitivity to estate taxes increases with age.
- About 43% of billionaires 65 and older originally in an estate-tax state moved to a state without a death tax.
- When a billionaire dies in a state that has an estate tax, the average contribution to state tax revenue is $165 million.
- In looking at the distribution of billionaires in 2001 and in 2010, nine years later, 21.4% of those in states with estate taxes had moved to a state without death taxes, while only 1.2% had done the reverse.

Planning needed

If you own residences in more than one state, you have some planning to do. You don't want to share the fate of John Dorrance, the founder of Campbell Soup. After he died in 1930, both Pennsylvania and New Jersey claimed him as a resident, requiring the payment of an estate tax to each state. The U.S. Supreme Court declined to hear his estate's plea that one may only have one domicile. ☐

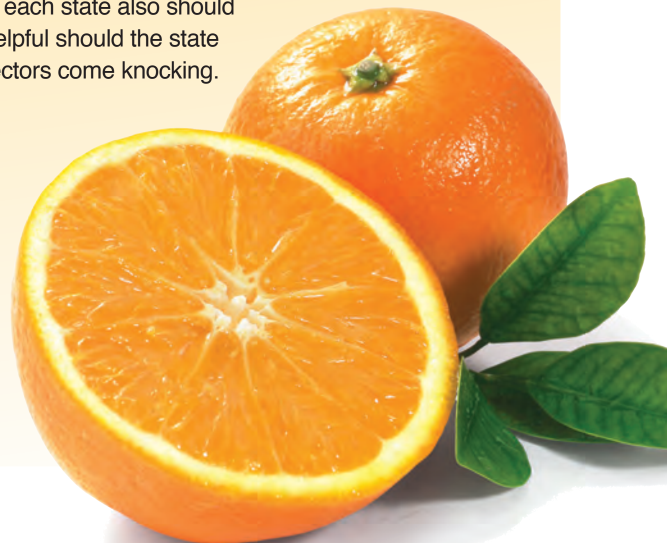
How to change a domicile

The federal income tax cap on state and local tax deductions has further motivated the rich to flee their domiciles in high tax states. It also has motivated the high-tax states to fight back. In addition to checking for pets and family treasures, states may examine cell phone records and Facebook posts.

Some of the steps commonly recommended to prove a change of domicile include:

- registering to vote in the new state;
- obtaining a new driver's license;
- registering one's car in the new state;
- updating estate plans, noting the new residence;
- joining a new church or temple;

Carefully documenting the days spent in each state also should prove helpful should the state tax collectors come knocking.



The "lock-in" debate returns

In the history of the U.S. estate tax, the amount exempt from the tax has never been reduced. Rather, the threshold of taxation has been increased from time to time, so as to keep targeting the federal estate tax on only the largest estates. At present, the exempt amount is indexed to inflation, and it stands at $11.58 million for 2020.

However, that exemption is slated to fall roughly in half in 2026 under current law. That has led some estate planners to recommend making large taxable gifts before 2026, so as to "lock in" the larger exemption amount—the federal exemption shields both gifts and estate transfers from tax. In November the IRS issued new Regulations that show how this strategy will work.

Basic example. Elizabeth made a $5 million taxable gift in 2018, and so used up that much of her basic exempt amount. If she dies in 2020, her estate tax exemption will be reduced by that $5 million, and so it will be $6.58 million. If she dies in 2026, assuming that the exemption has then fallen to $6.8 million, her basic exclusion amount will be $1.8 million.

Larger gift. Now assume Elizabeth makes $10 million worth of taxable gifts in 2020 and survives to 2026, when the exemption has fallen to $6.8 million. The estate tax is determined by bringing taxable gifts back into the calculation and allowing whatever credits were granted for those lifetime gifts. That means Elizabeth's basic exclusion amount in 2026 will be $10 million, even though under the statute it will have fallen much lower for anyone who made no taxable gifts at all.

Married couple. When Fred died in 2019, his executor elected to have Ethyl inherit his unused exemption amount, then $11.4 million. If Ethyl dies this year, she has her own exempt amount of $11.58 million, plus the exemption she inherited from Fred, for a total basic exempt amount of $22.98 million.

What happens if Ethyl survives until 2026? The exempt amount inherited from Fred does not change, but her own exemption will fall. Assuming that it's then $6.8 million, her basic exempt amount would be $18.2 million.

Is locking in the larger exemption with a taxable gift a good idea? At the current 40% tax rate on estate and gift transfers, the tax savings comes to roughly $2.5 million, which is real money. There are strategies available to leverage that number higher, and there is the chance that the estate tax rate goes higher in the future, which also magnifies the potential savings.

On the other hand, planners were in much the same position in 2012, when an exemption of $3.5 million was scheduled to fall to $1 million. Many recommended lock-in strategies then, only to be confounded when the Congress instead *raised* the amount exempt to $5 million!

Death and taxes may be certain, but the details are subject to change. ☐

Why are they so relaxed?

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Call us today to learn if a trust might be right for you!

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