

2023

National Income Tax Workbook

CHAPTER 2: TRUSTS & ESTATES

PP. 49 - 81



Learning Objectives

P. 49

- Annual gifts which qualify for exclusion, Estate planning
- Family limited partnership may produce discounted values
- Recognize & avoid challenges to the tax benefits of family limited partnership
- Understand Medicaid eligibility rules
- Know what tax benefits must be preserved in a decanted trust
- Understand when executor or transferee still has liability for a decedent's unpaid tax & mitigation of responsibility



Annual Exclusion Planning

Basic Exclusions

P. 50

- Nonspouse gift tax annual exclusion = \$ 17,000 (X 2 if Joint gift)
- Spousal gift tax annual exclusion = unlimited
- Non-citizen spouse gift tax annual exclusion = \$ 175,000
- Estate tax annual exclusion
 - \$ 12,920,000 unmarried taxpayers
 - \$ 25,840,000 married taxpayers

Completed Gift

PP. 50-51

- Transfer of beneficial interest & title to the property
- Partial interest transfer – less than complete interest
- Example 2.1 – car titled jointly (litigation now has 2 people to sue)
- Example 2.2 – joint tenants with right of survivorship

Bank Accounts & Joint Ownership

P. 51

- Completed gift when co-owner exercises control
- Example 2.3
 - Alexander & Olga co-owners
 - Olga draws on account
 - Completed gift when Olga withdraws funds

Retained Interest

P. 51

- Incomplete gift
- Partially incomplete gift
- Reserves any power over disposition of property
- Example 2.4
 - Transferred property to irrevocable trust (why not grantor trust?)
 - Trustee maintains discretion to pay or accumulate
 - Trustee retains testamentary power
 - Not a completed gift

Donor Retains Powers

P. 51

- Not a completed gift if donor retains:
 - Power to revest beneficial title to the property in himself or herself
 - Power to name new beneficiaries (unless it is a fiduciary power that is limited by a fixed or ascertainable standard)
 - Power to change the interests of the beneficiaries as between themselves (unless it is a fiduciary power that is limited by a fixed or ascertainable standard)
- Treas. Reg. 25.2511-2(d) – donor can reserve power to change the manner of time or enjoyment of property and still make a completed gift (legal opinion needed?)

Practitioner Note

P. 51

Ascertainable Standard

- The holder of a power is legally accountable
- Power to distribute trust income & principal for Health Education Maintenance Support
- Not ascertainable standard:
 - Use trust property for pleasure of beneficiary
 - Use trust property for happiness of beneficiary

- Example 2.5 – Retained Right to Change Time of Enjoyment
- Relinquishment of Powers
 - Treas. Reg. 25.2511-2(f) – living donor retain unlimited right
 - Can relinquish or terminate the right (complete gift)
 - Example 2.6 – Relinquished Power
- Donor as Trustee
 - Transfers property with no powers
 - Except fiduciary power to change beneficiaries
 - Completed gift if trustee's powers are limited by fixed or ascertainable standard
 - Treas. Reg. 25.2511-1(g)

■ Example 2.7 – Trustee’s Powers Limited by Ascertainable Standard

Practitioner Note: Gifts of Stock

- Completed gift when donor delivers properly endorsed stock certificate to donee/donee’s agent
- Date of completed gift is date stock is transferred
- Treas. Reg. 25.2511-2(h)

Gift in Contemplation of Death

PP. 52-53

- I.R.C. §2035(a)
- Decedent transferred interest in any property or gave away property in last 3 years before date of decedent's death
- AND value of the property would have been included in the decedent's gross estate under I.R.C. §§2036, 2037, 2038 or 2042 if the decedent had retained the transferred interest or relinquished power on the date of death
- I.R.C. §2035(b) –includes gift tax paid by decedent, estate, or spouse
- Bona fide sale – not subject to §2035

Present Interest

P. 53

- Not a future interest
 - Does not qualify for annual exclusion
 - Treas. Reg. 25.2503-3
- Example 2.8 – Gift of Future Interest
(ex. Michigan tuition purchase over 5 years)

Family Limited Partnership Interest

P. 53

- *Hackl v. Commissioner*
 - No substantial present economic benefit
 - No qualified gift
- *Estate of Wimmer v. Commissioner*
 - Partnership agreement restricted transfers
 - Primary purpose – investments
 - PTR's reported income on assets & qualified as completed gift
- Planning Pointer – Gift Tax Return – starts statute
- Planning Pointer – Client Objectives-(When receiving discounted Interest)

Transfers for the Benefit of Minors

P. 54

- Crummey Trust – Discussed last year’s chapter
- I.R.C. §2503(c)
- Treas. Reg. 25.2503-4(a)
 - The trust income & principal can be used for the benefit of the donee before he/she turns age 21
 - To the extent that the income & principal are not used, they are distributed to the donee at age 21
 - If the donee dies before age 21, the trust income & principal are payable to the donee’s estate or to someone the donee appointed under a general power of appointment
- Example 2.9 – Gift to Grandson of Present & Future Interests

- Practitioner Note – Custodial Account is Present Interest
- Crummey Trust
 - Gift of present interest qualifies for annual exclusion
 - Trust required accumulation of income
 - Required distributions to children – age 21-35
 - Discretionary distributions to children – after age 35
 - \$4,000 demand income per year
 - Completed gift
- Practitioner Note – Lapse of Power of Appointment

Annual Exclusion Planning

P. 55

- Gift Splitting – (consider this even if no taxable estate)
- Pattern of gifting – great example on pp. 56 & 57
- Make payment directly for
 - Education
 - Medical (examples on pp 57 & 58)



Family Limited Partnerships

Benefits of Family Limited Partnership

- Protection from creditor's claims
- Preservation of wealth to next generation
- Valuation discounts
- Reduce gift/estate tax liability
- Practitioner Note – Family LLCs

Benefits of Family Limited Partnership

- Structuring FLP
 - Two classes of owners
 - General partner - manages
 - Limited partners – economic interest
- Asset owner contributes assets in exchange for general or limited interest
- Discounted value for limited partners – lack marketability
- Example 2.16 – Gifting FLP Interest at a Discount – (keep doing it)

Pitfall of Family Limited Partnership

- Court cases discussed in text give examples of how FLP failed
- Discounting for Lack of Marketability
- Discount for Lack of Control
- Indirect gifts of property contributed to PTS (land)
- Step Transaction (end results)
- Retain control of family business §2036(a) p.61-63

Full & Adequate Consideration

P. 63

- I.R.C. §2036(a) – bona fide sale for adequate & full consideration
- Not included in gross estate
- *Estate of Harper*, T.C. Memo 2002-121
 - Assets transferred
 - Not arm's length transaction
 - Not motivated primarily by legitimate business concerns
 - No consideration for the transfer

I.R.C. §2703

P. 63

- Disregard restrictions in FLP
- Eliminate the discounts on the restrictions
- Exceptions:
 - It is a bona fide business arrangement
 - It is not a device to transfer such property to members of the decedent's family for less than full & adequate consideration in money or money's worth
 - Its terms are comparable to similar arrangements entered into by persons in an arm's length transaction

Holman v. Commissioner

P. 64

- FLP to maintain control of family assets – Business purpose
- Discounted minority interests
- Court found no business, only holding stock so no discount was applied
- Buy-sell agreements can be legitimate to maintain control
- Court reduced discounts on the gifts



Medicaid Planning

Medicaid Eligibility

P. 65

- Federal & state program
- ACA – expanded benefits
- Income Testing
- Asset Testing
- Practitioner Note – Non-Financial Eligibility

Medicaid Eligibility

PP. 65-66

- Income Test
- \$914 per month
- \$1,371 per month married & both spouses apply
- Wages, SS benefits, pensions, workers comp, & unemployment
- Spousal Impoverishment Rule
- Spend-down adjustment
- **Practitioner Note – Eligibility standards vary by state**
- **Consult an experienced Medicaid planner**

Medicaid Eligibility

P. 66

- Asset Test
- Resources less than \$2,000
- Resources less than \$3,000 married & both spouses apply
- Practitioner Note – Conditional Assistance
- Resources: cash, bank/brokerage accounts, savings bonds, land, life insurance, personal property, vehicles
- Excluded Resources: no ownership interest, no legal right, authority or power to liquidate, no legal right to use

FIGURE 2.2
Excluded Resources

Excluded Resource	Social Security Program Operations Manual Citation	No Limit on Value and/or Length of Time	Limit on Value and/or Length of Time
Home serving as the principal place of residence, including the land on which the home stands and other buildings on that land*	SI 01130.100	X	
Funds from the sale of a home if reinvested timely in a replacement home	SI 01130.110		X
Jointly owned real property that cannot be sold without undue hardship (due to loss of housing) to the other owner(s)	SI 01130.130	X	
Real property for so long as the owner's reasonable efforts to sell it are unsuccessful	SI 01130.140	X	
One vehicle used for transportation	SI 01130.200	X	
Life insurance, depending on its face value	SI 01130.300		X
Burial space or plot held for an eligible individual, his/her spouse, or member of his/her immediate family	SI 01130.400	X	
Burial funds for an individual and/or his/her spouse	SI 01130.410		X
Certain prepaid burial contracts	SI 01130.420		X
Household goods and personal effects	SI 01130.430	X	
Property essential to self-support	SI 01130.500– SI 01130.504		X

Medicaid Eligibility PP. 66-67

- Example 2.18 – Family Business
- Excluded Resources

FIGURE 2.2 (Continued)
Excluded Resources

Excluded Resource	Social Security Program Operations Manual Citation	No Limit on Value and/or Length of Time	Limit on Value and/or Length of Time
Resources of a blind or disabled person that are necessary to fulfill an approved plan for achieving self-support	SI 00870.000 SI 01130.510		X
Funds up to and including \$100,000 in an Achieving a Better Life Experience (ABLE) account	SI 01130.740		X
Federal disaster assistance received on account of a presidentially declared major disaster, including interest accumulated thereon	SI 00830.620 SI 01130.620	X	
Cash (including accrued interest) and in-kind replacement received from any source at any time to replace or repair lost, damaged, or stolen excluded resources	SI 00815.200 SI 01130.630		X
Certain items excluded from both income and resources by other federal statutes	SI 00830.055 SI 01130.060	Varies	
Victims' compensation payments	SI 00830.660 SI 01130.665		X
State or local relocation assistance payments	SI 00830.655 SI 01130.670		X
Tax refunds related to earned income tax credits	SI 00830.060 SI 01130.676		X
Grants, scholarships, fellowships, and gifts	SI 01130.455		X

* An individual's home continues to be excluded if the individual leaves the home but intends to return to it. If a spouse and certain relatives remain in the home, all or part of the home value may be excluded.

Medicaid Eligibility P. 68

- Excluded Resources
- Consult expert

Asset Transfers

P. 69

- 5-year lookback (**STATE LAW VARIES**)
- Assets transferred less than FMV
- Example 2.19 – Gift in Lookback Period
- Example 2.20 – Gift before Lookback Period
- Practitioner Note – Excluded Transfers

FIGURE 2.3
2023 SSI Spousal Impoverishment Standards

Minimum monthly needs allowance	\$2,288.75	All states (except Alaska and Hawaii)
Maximum monthly needs allowance	\$3,715.50	
Community spouse monthly housing allowance	\$686.63	All states (except Alaska and Hawaii)
Community spouse minimum resource standard	\$29,724	
Community spouse maximum resource standard	\$148,620	
Minimum home equity limit	\$688,000	
Maximum home equity limit	\$1,033,000	

Source: www.medicaid.gov/federal-policy-guidance/downloads/ssi-spousal-cib-01-2023-508.pdf

Spousal Impoverishment PP. 69-70

- Protect income & assets of spouse not on Medicaid
- Protect beneficiary who needs long-term care
- Spouse must live in community

Estate Recovery

P. 70

- Recovery of certain benefits paid on behalf of the enrollee
- Reimbursement of benefits received
- No recovery if:
 - Survived by spouse (recovery postponed)
 - Child under age 21
 - Blind/disabled child of any age
 - Hardship waiver

Medicaid Planning

PP. 70-71

- Gift before 5-year lookback
- Transfer assets out of taxpayer's control
- Practitioner Note – Medicaid Facilities
- Increase Value of Excluded Resources
 - Purchase new or more expensive personal residence
 - Purchase household furniture & furnishings
 - Pay off a mortgage
 - Make home repairs or improvements
 - Upgrade a vehicle
 - Prepay funeral/burial costs



Life Estate

P. 71

- Primary residence is excluded asset but is subject to estate recovery
- Life estate in real property
- Gift the remainder interest
- Limited to life estate owner's life or to another's life
- Ceases upon death (check your state rules)
- Not subject to estate recovery
- Example 2.21 – Creating a Life Estate

FIGURE 2.4
Unisex Life Estate Interest Table

Age	Life Estate Factor	Age	Life Estate Factor	Age	Life Estate Factor
54	.81054	55	.80046	56	.79006
57	.77931	58	.76822	59	.75675
60	.74491	61	.73267	62	.72002
63	.70696	64	.69352	65	.67970
66	.66551	67	.65098	68	.63610
69	.62086	70	.60522	71	.58914
72	.57261	73	.55571	74	.53862
75	.52149	76	.50441	77	.48742

Medicaid Trust Planning

P. 72

- Potential exclusion of assets & income
- Supplemental Needs Trust (Special Needs Trust)
 - Disabled individuals
 - Provide for extra needs
 - Self-settled
 - Third-party

Self-Settled Trust

PP. 72-73

- Pooled Trust
 - Established & managed by nonprofit organization
 - Maintains separate account for each beneficiary
 - Investment assets pooled
- Payback Trust
 - Contains the assets of an individual under age 65 & disabled
 - Is established for the benefit of such individual by someone else
 - Provides that the state(s) will receive all amounts remaining in the trust upon death of individual up to total amount Medicaid paid

Self-Settled Trust

P. 73

- Example 2.22 – Personal Injury Award
- Third-Party Trust
 - Established with third-party assets
 - Not available to beneficiary
 - Only available for beneficiary's supplemental needs
 - No estate recovery
- Example 2.23
- Practitioner Note – Trust Decanting

Decanting a Trust

Decanting Basics

P. 74

- Decanting – the distribution of assets from one trust into a second trust
- Strategy for changing outdated terms of an otherwise irrevocable trust
- Provide for beneficiary who becomes disabled after grantor executed the first trust
- Uniform Trust Decanting Act (UTDA)
 - Prohibits decanting if it will interfere with tax benefits first trust

Uniform Trust Decanting Act

P. 74

- Allows for reform of an irrevocable trust
- Irrevocable or revocable with consent of a trustee
- Does not apply to charitable purpose trust
- Decanting power – authorized fiduciary can distribute property, or modify the terms of first trust
- Authorized fiduciary – trustee or other fiduciary (not grantor) that has discretion to distribute or direct trustee to distribute
- Practitioner Note – Trust decanting may trigger Medicaid repayment

Exercising the Decanting Power

P. 74

- Exercised without consent of anyone
- No court approval needed
- Must provide notice of decanting to grantor, beneficiaries, trustees & certain others
- Example 2.24 – Disabled Beneficiary

Tax-Related Limitations

P. 75

- Qualified marital deduction property
- 2nd trust cannot include or omit any term that would prevent transfer from qualifying or would have reduced deduction amount
- I.R.C. §2056(b)(5) – power of appointment
 - Surviving spouse must be entitled to all income
 - Must be paid annually or more frequent intervals
 - Spouse has testamentary power of appointment
- I.R.C. §2056(b)(7) – qualified terminal interest property (QTIP)
 - Surviving spouse must be entitled to all income
 - Must be paid annually or more frequent intervals
 - No person has power of appointment

Tax-Related Limitations

P. 75

- Example 2.25 – QTIP Marital Deduction Trust
- Example 2.26 – Power of Appointment Trust
- Charitable Deduction
- Example 2.27 – Crummey Trust
- Example 2.28 – Trust for Minor
- S corporation Electing small business trust (ESBT) or Qualified subchapter S trust (QSST)
- Generation-Skipping Transfer Tax (GSTT)

Grantor Trust

P. 77

- Grantor – US citizen, resident of US or a domestic corporation

- Exception: (discussed in text)

Distributions may be made only to the grantor and the grantor's spouse during the life of the grantor. However, maker can withdraw assets.

(Consider pension assets transfer to beneficiaries outside of grantor trust)

Grantor Trust

P. 77

- Catch-all provision preserves any tax benefits
- 1st trust expressly indicates an intent to qualify for tax benefit
- 1st trust clearly designed to qualify for the tax benefit
- Prohibition on eliminating a tax benefit in 2nd trust does not apply to a future benefit
- Example 2.29 – Credit Shelter Trust



Fiduciary Liability for Taxes

Executor or Trustee of Estate

P. 79-80

- Personally liable for decedent's taxes
- Priority is to government claims
- I.R.C. §3713 – government debts paid first
- Distributions before government debts = personally liability
- Practitioner Note – defense = Knowledge of Federal Claim
- Consider Form 4810 Prompt Assessment & Form 5495 Request for Discharge from Personal Liability

Lien for Estate Taxes

P. 80

- I.R.C. §6324 – lien on gross estate of a decedent
- 10-years from date of death
- Closing letter to confirm estate tax liability has been satisfied
- Cross Reference – Federal Tax Lien
- Transferee Liability – personal liability to
 - Spouse
 - Transferee
 - Surviving joint tenant
 - Other person(s) in possession of property

Continuance after Discharge

P. 80

- I.R.C. §2204 – discharge of fiduciary from personal liability until after tax determination
- I.R.C. §2033 – property transferred to purchaser or holder of a security interest if executor has been discharged from §2204 (See 2022 National Workbook reference)
- The lien attaches to the consideration received (PA 116, farmland preservation valuation issue)

Estate Tax Closing Letter

P. 81

- \$67 User Fee
- Letter 627, Estate Tax Closing Letter
 - Confirms estate tax return has been accepted by IRS as filed, OR
 - Has been accepted after an adjustment by the IRS
 - IRS examination of estate tax return is closed
- Reopening or reexamining the estate – listed in text

Estate Tax Closing Letter

P. 81

- Portability of deceased spousal unused exclusion (DSUE)
- IRS can examine estate tax return of decedent for purpose of determining the transfer tax liability of surviving spouse
- Request estate tax closing
- 9 months after filing Form 706 (706-NA)
- 30 days from completion of examination
- Practitioner Note – Form 56

Estate Transcript

P. 81

- Notice 2017-12 & Notice 2017-5 I.R.B. 742
- Account transcripts – instructions on how to request one
- Form 4506-T, Request for Transcript of Tax Return
- Find Code 421 – closed examination of tax return

- Cross-Reference – Account Transcript in 2022 Tax Workbook



Questions?

2023 NATIONAL INCOME TAX WORKBOOK

CHAPTER 13: TAX RATES & USEFUL
TABLES



Tax Rates & Tables – topics

P. 477

- Tax Rates 2023 p. 478,
- Capital gains zero with Taxable Income under \$40,400 p. 479
- Car Expenses \$.655 2023 p. 483
Medical/Military Moving \$.22 Charity \$.14
Depreciation built in rate for trade-in basis reduction \$.28
- Amount for various lease values p. 485

2023 Medicare Part B Premiums based on 2021 MAGI

P. 501

<u>Single, HoH, QW</u>	<u>MFJ</u>	<u>MFS</u>	<u>Beneficiary's Premium*</u>
\$97,000 or less	\$194,000 or less	\$97,000 or less	\$164.90 2023
\$97,001-\$123,000	\$194,001-\$246,000	N/A	\$230.80
\$123,001-\$153,000	\$246,001-\$306,000	N/A	\$329.70
\$153,001-\$183,000	\$306,001-\$366,000	N/A	\$428.60
\$183,001-\$499,999	\$366,001-\$749,999	\$97,001-\$403,000	\$527.50
\$500,000 & above	\$750,000 & above	\$403,000 & above	\$560.50 *

*The standard premium will be \$164.90 (or higher) however, some who get SS benefits may pay less than this. IRA Rollovers will be counted in the calculation.

RETIREMENT PLANS

P. 511

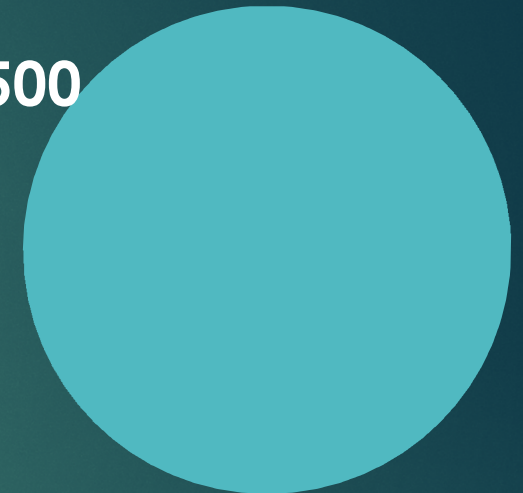
- ▶ **2023 IRA Limits Maximum \$6,000**
- ▶ Roth Example MJF modified AGI \$218,000-228,000 phase out, raised for **2023 \$6,500**
- ▶ **Retirement Plan Contribution Limits**
- ▶ Table for all plans – Consider max. if
- ▶ more than one employer
- ▶ Catch up remains \$7,500 over 50



RETIREMENT PLANS

P. 408

- ▶ **2023 401(k), 403(b) & SARSEP Maximum \$22,500 (only 14% use this per Vanguard)**
- ▶ Amounts are adjusted for inflation
- ▶ 2023 Maximum 401(k) 22,500
catch up 50 & over 7,500
Total 30,000
2023 IRA including Roth max. 6,500
- ▶ **SIMPLE 457 401(k) Defined cont./benefit comp.**



Chapter 13 Tax Rates & Tables

Social security & Medicare

P. 514

MAXIMUM earnings for Social Security **2023**
\$160,200

2024 not released yet

AMOUNT TO EARN A QUARTER OF COVERAGE

2023 \$1,640



IRS Hotlines & Toll-free Numbers

- ▶ See chart in text P. 516-517

