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NEWSLETTER MAY 2018

To Our Clients and Friends:

In this Newsletter, we want to continue to update you by briefly covering topics of the most current interest to our clients.

HOW THE "TAX CUTS AND JOBS ACT" AFFECTS YOUR ESTATE PLAN

Estate Tax. The Estate Tax Exemption, for deaths on or after 1/1/18, has been doubled from $5.2M per taxpayer to $11.2M (i.e. $22.4M for a married couple) (reduced by lifetime taxable transfers, and indexed for future inflation). With Estate Tax no longer a concern for couples under this new $22.4M figure, many are opting for a simpler estate plan where all assets are bequeathed fully to the surviving spouse. Using a direct 100% bequest to spouse, "I Love You Trust," will, however, mean giving up the "anti-floozy" and "anti-Gigilo" protections that the prior standard A-B, or A-B-C, two-part, or three-part trust, provided for the children of the spouse who is the first to die. Many of our clients prefer to retain the two-part Trust, such that the one-half of the first spouse to die is irrevocable, but updating it to add provisions so that a full income tax basis adjustment can now occur at the death of the surviving spouse. For many of our clients, this requires more discussion, and a weighing of the pros and cons.

GST. Generation Skipping Transfer Tax ("GST") exemptions are also raised to the same $11.2M figure per person, meaning that more wealth can be directly or indirectly bequeathed to grandchildren and younger generations, without incurring an effective double tax. For instance, the Estate Tax bracket for taxable estates in excess of $22.4M per married couple is 40%; the generation skipping tax is an additional 40% tax when the grandchild or younger generation actually vests in the assets (i.e. when the children's generation dies). A danger can be lurking for those who simply planned to leave to their grandchildren "the most possible by law without incurring a GST tax"; in that case, for the estate of less than $22.4M, everything could be left to grandchildren, with nothing for children. All tax formulas in estate plans should be reviewed with these new, significantly larger, tax exemption figures, to be sure that dollars will flow as desired.

Gift Tax. The annual Gift Tax Exclusion was not changed by the new law, but was increased by an inflation adjustment in 2018 to $15,000 for each donor annually to gift to each donee. For instance, each married couple with 4 children (or in-laws) and 6 grandchildren, can gift up to $30,000 to the 10 individuals, totaling $300,000, without using either spouse's Estate Tax exemption and without needing to file a gift tax return. Additionally, tax-free gifts of any amount can be made to a spouse, to charity, and directly to an institution or provider for tuition or health care.

Stepped-Up Income Tax Basis. With all of these changes, the "Stepped-up Basis" rules at death have not changed. Whether or not Estate Tax is actually due at death, capital gain assets (such as real property, businesses, stocks) will adjust their cost basis to current death value for all community property assets, one hundred percent, even when only one spouse has died. This means that the family can sell assets after a death, avoiding payment of any capital gains tax, or choose to retain real property and claim new depreciation income tax deductions. So, for clients with less than $22.4M net estates, gifting assets during one's lifetime to save Estate Tax at death may not only be unnecessary, since there may be no Estate tax, but may also be unwise, since if the older parent retains ownership of the asset until death, it will receive a stepped-up cost basis for inheritance. Some individuals who have already gifted low-basis assets to children are having the children gift the assets back to achieve a cost- basis step up when the parent dies (pros and cons need to be considered, and the parent must live for at least a year after receiving the gift back).

Timing and Sunset of Law. Absent further legislation, the new Estate Tax Credit and GST Credits will return to their current level of $5M per person, adjusted for inflation, beginning January 1, 2026. Thus, clients who are fearful that the law will sunset while they are still alive, or that Congress will vote to reduce the tax credit even before that date, are still involved in gift-giving to reduce their estates. In fact, now that an individual can gift $11.2M before incurring any gift tax, some are gifting up to that limit now, hoping and expecting to be grand-fathered (without any "claw-back") when the current law expires or changes.

WHEN A CHILD TURNS 18, PARENTS OFTEN DON'T REALIZE THEY CAN NO LONGER MAKE LEGAL DECISIONS FOR THEIR NOW-ADULT CHILD, UNTIL TIME OF CRISIS.

Health Care Directive, including a HIPAA Authorization. Most clients only think of using this document for themselves and their older parents, but it can be equally important to be a designated Health Agent for their college-age children. The Directive can give parents a right to speak to a local hospital or health care provider about what may be happening to their child and to inquire about medical test results and treatment. Some college health centers have their own policies about release of private information, and you may also need your child to sign a local form.

Financial Power of Attorney. This document allows parents to manage their child's finances. It can be helpful, for instance, if a child becomes ill or has a car accident, leaving the child unable to make financial decisions. If bank accounts, a car or other assets are titled in the name of the student, the power of attorney can avoid the expensive and drawn-out court process of having a parent appointed as guardian or conservator of the student.

Education Record Release. Students must generally consent before education records such as grades, transcripts and disciplinary records can be shared with their parents. Many universities discuss this with parents at orientation, including a waiver form that could be signed by the student. Parents may be especially interested in having access to information related to scholarship, financial aid and tuition information, so they'll remain informed even if their student were to inadvertently ignore warning deadline letters about renewing financial aid.

BEWARE BENEFICIARY FORMS. NAMING THE WRONG PERSON OR FAILING TO UPDATE DOCUMENTS CAN CREATE UNNECESSARY EXPENSE FOR HEIRS.

Brokers and banks have provided an increased ability to name beneficiaries directly on a wide range of financial products, in addition to being able to designate beneficiaries of retirement accounts and life insurance. One needs to take care because those designations will override your Will and your Living Trust. Additionally, with the mergers of so many institutions, your beneficiary designation may be lost by the institution. We advise that you retain a copy of your beneficiary designation form that has been accepted by the institution, and re-confirm it every few years.

Accounts and property with beneficiaries designated should be reviewed from time to time, just like a will, to be sure that it's still who you intend and that the beneficiaries designated are still alive. Also beware that a marriage (or divorce) may automatically change or affect prior beneficiary forms that you've signed, so it's important to review and re-sign.

Be careful that you don't name minor (or not-yet-mature) or disabled children or grandchildren as beneficiaries, as they'll receive the funds directly at age 18, which may be splurged, spent unwisely, or provide a disincentive to college or work. Additionally, while the beneficiary is under age 18, a costly and cumbersome Court Guardianship must be instituted for the child.

One worse result is if no one at all is named as a beneficiary on a retirement account or life insurance, since it can be forced to go through probate. Especially for retirement accounts, the most inefficient tax impact could then occur, since children or other heirs/beneficiaries wouldn't be able to elect to "stretch out" treatment to defer income tax on IRA distributions for many years.

We generally advise designating the spouse as primary beneficiary, and a Trust for children as contingent beneficiary. For retirement plans, the Trust needs to include special language allowing acceptance of retirement account proceeds to achieve favorable income tax treatment.

ARE LIVING TRUSTS STILL IMPORTANT, IN A NO-TAX ENVIRONMENT? CHECK-UPS WITH THE ESTATE ATTORNEY EVERY 5 YEARS?

Avoidance of estate tax has always been just one reason for use of a revocable Living Trust. Living Trusts can also avoid the costs and time delays of a probate proceeding, including delays in accessing funds for continuing expenses, and ease of management of real property and businesses. Trusts, importantly, will provide rules and protections for young or immature children, with a selected Trustee in charge of management and distributions. Living Trusts can also continue to protect beneficiaries from creditors and divorce, making sure that grandchildren will inherit when their parent is no longer living.

We always recommend a "Check-Up" meeting to review the Living Trust and related estate documents to be sure there has been no marriage or divorce in the family, that designated Trustees and beneficiaries are still living, that assets are titled in the Living Trust to avoid probate (Very Important!), and that beneficiaries of life insurance, retirement plan accounts, and other such assets are not in conflict with the Living Trust beneficiaries. We also recommend, for clients who have given to us an Emergency Contact List, which can include contact information for your estate attorney, accountant, financial and insurance advisors, and physicians, that updated versions be sent to us every few years to be placed in your file, and also provide them to the person who you've named as first agent on your Health Care Directive and Trust documents.

PROP 13 – NEW PARENT-TO-CHILD PROPERTY TAX AVOIDANCE AND FLEXIBILITY AFTER DEATH

The California State Board of Equalization has provided families with a way to avoid Prop 13 when bequeathing the expensive family home to one child, even without sufficient cash or other assets in the estate to balance a bequest to the other child. Past rules could force a Property Tax Reassessment when the percentage of the house that one child wanted to keep was in excess of the child's proportionate share of the Trust (e.g. ½ when there are two children). There is, thus, an opportunity for us to update Trusts where one child may want the home or other real property in excess of her or her proportionate inheritance amount by adding to the Living Trust an option or right of first refusal, allowing the child to purchase 100% of house, while providing cash to the other child. (This is far simpler than the old method of arranging a loan to encumber the property prior to distribution.)

For families wishing to avoid sale of real property assets after death, and/or to bequeath property to one child instead of having co-ownership by all children, Prop 13 planning is crucial to avoid reassessment of property tax at death to the extent possible.

NEW MEDI-CAL RECOVERY LAWS

The law changed significantly during the past year, such that much or all of the estate of a Medi-Cal recipient might not be subject to recovery or repayment to the State if the Medi-Cal recipient has a spouse on death, or if there are no assets subject to a probate estate (i.e. if assets pass under a Living Trust, or directly to a designated beneficiary or joint tenant). If you have a family member with assets such as a home or car or life insurance who is receiving Medi-Cal, you are urged to investigate this law change.

FIRM RECOGNITION

We are pleased to be recognized for the quality of our work by an AV rating of our Law Firm (the highest) in Martindale Hubble for another year, and by inclusion of Vicki Magasinn as a continuing "Super Lawyer" in the Super Lawyers Magazine.

Attorney Amanda Morrison has now passed her tenth anniversary with the Firm, during which time she received her Tax Masters and also had a couple of babies. We are pleased that she's now become a partner in the Firm.

This Newsletter and those of prior years can be found on our Firm's website, www.magasinn.com. If you wish, however, to stop receiving this Newsletter, please call the office.

We send to all of you our best wishes.

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