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## ESTATE PLANNING NEWSLETTER

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### A Will Makes Estate Administration Simpler and Less Costly

Many people think they don't need a Will because they don't have much money, are young, or for other reasons. However, if you do not have a Will, the administration of your estate can be more complicated and expensive than necessary, even for a small estate, and your assets will be distributed as determined by state law which may not be as you would like or expect.

If you are married and do not have a Will, your assets may not all pass to your spouse.

- In New Jersey:
  - If you have children from a different relationship, your spouse will receive the first 25% of your assets (but not less than \$50,000 nor more than \$200,000); the balance will pass 50% to your spouse and 50% to your children.
  - If you have no children but have a surviving parent, your spouse will receive the first 25% of your assets (but not less than \$50,000 nor more than \$200,000); the balance will pass 75% to your spouse and 25% to your parents.
- In Pennsylvania:
  - If you have children from a different relationship, your spouse will receive 50% of your assets and your children will receive 50%.
  - If you have children all of whom are children of your current spouse, your spouse will receive the first \$30,000; the balance will pass 50% to your spouse and 50% to your children.
  - If you have no children but have a surviving parent, your

spouse will receive the first \$30,000; the balance will pass 50% to your spouse and 50% to your parents.

If assets would pass to minor children, this could create a number of problems.

- Minors cannot legally receive funds directly from an estate.
- The assets would not automatically be distributed to the child's parent. Instead, it may be necessary for the parent to apply for guardianship of the child's property.
- Generally, a child will be entitled to receive the inheritance upon reaching the age of 18 regardless of how much money that may be. The child may not be ready to handle the funds. A trust for a minor would be more appropriate.

Other problems may arise if you do not have a Will.

- There could be a conflict among family members as to who should administer the estate. You cannot verbally direct who should administer your estate.
- Not having a Will may result in costs that a Will would avoid. The administrator of your estate may have to pay a premium for a bond before being appointed, a nonrefundable expense to the estate which could be more than \$1,000.

It's important that a properly drafted Will is in place for everyone, including younger adults especially those with minor children. The benefits include: assets pass to beneficiaries you choose, less expense, proper asset protection for your beneficiaries, and less chance of family conflict.

### Titling Assets Must be Coordinated with Your Estate Plan

Assets titled jointly with another or with a TOD (transfer on death) or POD (pay on death) designation will pass directly to the named beneficiary regardless of the terms of your Will. These forms of titling assets supersede your Will and may not be consistent with your estate plan.

A TOD or POD to a minor child will create additional problems and expenses. Minors cannot legally receive assets directly. Once the child reaches the age of 18, he/she can receive those assets regardless of whether the child is ready to handle the amount. A trust for a minor is more appropriate.

Jointly titled property creates an ownership interest in that property. Assets that are titled jointly with another are subject to that other person's creditors even if all of the funds were contributed by you.

If the other joint owner dies, New Jersey presumes that the entire account was owned by him/her and that you are the beneficiary. Depending on your relationship to the joint owner, this may result in an inheritance tax being due.

Even if the jointly held, TOD, or POD assets pass to the intended beneficiary, by bypassing your estate, there may be insufficient liquidity to manage estate expenses, especially if there is real estate in the estate. It is better to have the assets go to the estate and allow the executor to distribute the assets according to your Will, retaining enough to administer the estate.

Some people title assets jointly so that the other person can assist with managing the assets. While it may not be intended that the joint owner receive the balance of assets at your death, that will be the result. A better alternative is to have a Power of Attorney in place. Your designated agent would not have an ownership interest in the property, just the ability to help manage the asset for you in your best interest. Upon your death, the assets will then pass as you directed according to your Will.

Some people title assets jointly to avoid probate. In New Jersey, this is unnecessary. Unlike many other states, in New Jersey probate is an easy process and will be necessary in most estates anyway due to some assets still titled in your name.

## Federal Estate Tax Changes are Looming; Large Gifts May be Prudent

The Federal Estate Tax Exemption for decedents passing in 2023 is \$12,920,000 for each person, \$25,840,000 for a married couple. The exemption will continue to increase each year based on the inflation index. However, under current law, in 2026, the exemption amount will drop to 50% of what it is at that time. We estimate this amount to be about \$6,500,000.

For clients who will be subject to the estate tax, it is prudent to consider making gifts before the exemption decreases. As background, the Federal Estate Tax is unified with the Federal Gift Tax. If lifetime gifts are made, the available Federal Estate Tax Exemption will decrease by the amount of the gifts. Since the Gift Tax Exemption is also currently \$12,920,000, gifts up to this amount can be made without the imposition of gift tax. The IRS has announced that individuals taking advantage of the increased gift and estate tax exemption amounts during lifetime in effect from 2018 to 2025 will not be adversely impacted after 2025 when the exclusion amount is scheduled to be reduced.

The increased Federal Estate Tax Exemption was enacted as part of the Tax Cuts and Jobs Act of 2017 which included 23 tax cut provisions. The tax cuts are slated to expire on December 31, 2025. Last year, legislation was proposed to make the TCJA permanent. While this legislation was not enacted, it is likely that Congress will attempt to make the law permanent before the end of 2025.

Individuals with an estate of \$6,000,000 or more, or couples with an estate of \$12,000,000 or more, should monitor the situation to consider if substantial gifts are warranted. Unfortunately, the only way to exploit the current exemption amount is to make a gift greater than the future exemption amount. This “all or nothing” concept is illustrated in the following example.

Assume a couple has a net worth of \$19,000,000. Under current law, no Federal Estate Tax would be due from the couple because the total exemption for the couple is \$26,000,000 (rounded). However, if the exemption is cut in half in 2026, only \$13,000,000 would be tax free, and the remaining \$6,000,000 would be taxed at 40% resulting in a \$2,400,000 tax.

If, instead, one spouse made a gift of \$13,000,000 prior to 2026, that gift would be tax free. If the second spouse’s death is after 2025, \$6,000,000 would be left and would be totally shielded by the \$6,500,000 exemption remaining, and no tax would be due.

Alternatively, if one spouse made a gift of \$6,500,000, that gift would again be tax free. If the second spouse’s death is after 2025, \$12,500,000 would be left and would be only partially shielded by \$6,500,000 exemption remaining, and 40% tax would be due on the unshielded \$6,000,000 resulting in a \$2,400,000 tax.

## Conversions from Traditional IRAs to Roth IRAs Can Save Income Tax

**Changes to Required Minimum Distribution (RMD).** The SECURE 2.0 Act of 2022 made changes to RMD. During your lifetime, you are required to withdraw the RMD from your IRAs based upon your age. Under the new legislation, beginning in 2023, the age that you must start taking RMDs increases from 72 to 73. Beginning in 2033, it increases to age 75.

**Roth IRA.** Contributions to a Roth IRA are made with income that has already been taxed, meaning there are no tax deductions for contributions, but the money you have in a Roth IRA grows tax free over time. Roth IRAs do not have RMDs at age 73 like a traditional IRA, so you can continue letting your money grow until you’re ready to access it. When you do decide to take distributions from a Roth IRA, neither you nor your beneficiaries will have to pay income taxes on the withdrawals.

**Conversion to Roth IRA.** A systematic conversion from a traditional IRA to a Roth IRA can result in significant income tax savings. There is a current tax cost because the amount converted from a traditional IRA to a Roth IRA is subject to income tax now but future distributions will be income tax free. The tax savings for this technique can be maximized for recent retirees as set forth in the following example.

Assume a 65 year old retiree has \$1,000,000 in a traditional IRA and \$500,000 in other savings. Social Security benefits do not have to be claimed until age 70 and the required beginning date for RMD is now age 73. As a result, for the next several years, the retiree’s taxable income will be temporarily low. As shown from the tax rates listed on the back page, for a married retiree, income tax rates are 12% or less for taxable income up to \$89,450, and the tax rate is 24% or less for taxable income up to

\$364,200. In addition, the first \$27,700 of income is shielded by the standard deduction.

Further assume that the retiree has no other taxable income and withdrawals of \$117,150 from a traditional IRA are converted into a Roth IRA each year. The total income tax due on the conversion is only \$10,294, computed as follows:

0-\$27,700	No Tax
Next \$22,000	\$2,200
Next \$67,450	\$8,094

If this plan is continued for five years, the Roth IRA balance can be greater than \$500,000 at a tax cost of \$50,000. Any appreciation on the converted IRA will be income tax free on withdrawal.

This example is based on perfect facts, but even with less ideal facts, the systematic conversion will almost always result in beneficiaries inheriting a greater amount. Other factors that must be considered in this analysis are the impact on the New Jersey pension exclusion and the tax effect on Medicare contributions.

ICI.ORG reports Total US retirement assets were \$32.3 trillion as of September 30, 2022. Retirement assets accounted for 30 percent of all household financial assets in the United States at the end of September 2022. The average retirement savings for those over 65 is \$216,720.

# Estate Planning Gifting Techniques Save Estate Tax

As we consider the potential changes in the Estate Tax Exemption in 2026, it may be prudent to delay a major gift until 2025 to give Congress a chance to enact legislation. It is a monumental decision to make a gift of \$12,920,000 to save estate tax. The senior generation must be fully prepared to lose control and ownership of the gifted assets and must consider non-tax considerations such as the ability of the beneficiary to handle the receipt of a large gift, even if it is in trust. In the meantime, the following estate planning gifting techniques should be implemented to reduce the taxable estate.

- **Annual Exclusion Gifts.** As background, the Federal Estate Tax is unified with the Federal Gift Tax. If lifetime gifts are made, the available Federal Estate Tax Exemption will decrease by the amount of the gifts. Since the Gift Tax Exemption is also currently \$12,920,000, lifetime gifts up to this amount can be made without the imposition of gift tax. However, each year, gifts of the "Annual Exclusion" amount, which is currently \$17,000, can be given to any beneficiary *without* reducing the amount of the Estate Tax Exemption. Exploiting the annual exclusion is a powerful estate tax savings technique.

For example, married grandparents with two married children and four grandchildren would each have eight potential beneficiaries. If both grandparents wished to make gifts, sixteen annual exclusion gifts of \$17,000, totaling \$272,000, could be made each year. If this gifting plan is implemented annually over ten years, \$2,720,000 would be gifted tax free. In addition, any appreciation on those gifts would also be outside the grandparents' taxable estates. As shown from the following table, and assuming an average investment rate of return of 5%, the estate would be reduced by about \$3,400,000 resulting in a tax savings of \$1,360,000.

Year	Gifts Made	5% Return	End Balance
2023	\$272,000.00		\$272,000.00
2024	\$272,000.00	\$13,600.00	\$557,600.00
2025	\$272,000.00	\$27,880.00	\$857,480.00
2026	\$272,000.00	\$42,874.00	\$1,172,354.00
2027	\$272,000.00	\$58,617.70	\$1,502,971.70
2028	\$272,000.00	\$75,148.59	\$1,850,120.29
2029	\$272,000.00	\$92,506.01	\$2,214,626.30
2030	\$272,000.00	\$110,731.31	\$2,597,357.61
2031	\$272,000.00	\$129,867.88	\$2,999,225.49
2032	\$272,000.00	\$149,961.27	\$3,421,186.77

- **Trusts for Minor Children and Young Adults.** If you have a minor child or young adult beneficiary who may not have the experience or maturity to manage gifts of \$17,000 or \$34,000 per year, or a greater lump sum, assets can instead pass to a trust to be invested and distributed to your beneficiary by a trustee of your choosing. When the beneficiary reaches a certain age (an age you choose), he or she could receive the remaining balance outright.

- **Life Insurance.** Life insurance is included in the taxable estate for Federal Estate Tax (even though it is not taxable for New Jersey Inheritance Tax if a beneficiary is named).

If a decedent owned a life insurance policy, the proceeds would be taxed as part of the taxable estate. Through the use of an Irrevocable Life Insurance Trust, the life insurance proceeds would be totally removed from the taxable estate thereby eliminating potential estate tax resulting in a very significant benefit to your children. For example, if a person owns assets over the \$12,920,000 limit and also owns a \$3,000,000 life insurance policy, that policy would increase the estate tax by \$1,200,000 (\$3,000,000 X 40%). If, instead, the \$3,000,000 policy is held in a properly drafted and administered trust, no estate tax would be due on the policy.

- **Qualified Personal Residence Trust (QPRT).** A QPRT is a trust to which a person transfers a personal residence retaining the right to continue to live in the residence for a stated term of years or until the person's earlier death. At the expiration of the trust term, the QPRT terminates and, subject to potential lease arrangements, the residence typically passes to descendants. If the person dies prior to the end of the trust term, the QPRT terminates and the property reverts to that person's estate and will be distributed according to the provisions of the Will. The transfer of a personal residence to a QPRT will result in dramatic estate tax savings if the person survives until the end of the trust term while there will be little or no effect on the person's right to use the residence.

The estate tax savings of a QPRT is generated because only the present value of the remainder interest would be deemed a gift. The present value is determined by the term of the trust and the applicable interest rate as set forth by the IRS. As the interest rate increases, the value of the right to use the property increases and the remainder interest, which is the amount deemed to be gifted, decreases. Since interest rates have recently increased, a QPRT is a more attractive estate planning tool.

- **Gifting with Discounts.** Making lifetime gifts is the centerpiece of an estate plan. While the benefit of making the lifetime gifts is substantial as illustrated above, benefits can be increased by "leveraging" gifts using minority and lack of marketability discounts. If a gift of a minority interest in a company is made, there would be a minority discount because the beneficiary does not have any control over how the property is invested or when distributions are made. In addition, there would be a lack of marketability discount because there is not a ready market to purchase a fractional interest in a company. As a result, if a gift is made of 40% of a \$10,000,000 company, the value for gift tax purposes could be discounted by 25% or more. This means that the value of the gift for gift tax purposes would not be \$4,000,000 (40% X \$10,000,000), but rather \$3,000,000 (40% X \$10,000,000 X 75%).

We can assist with the implementation of this gifting technique through the use of techniques such as Grantor Retained Annuity Trusts, sales to grantor trusts, family limited partnerships, and Spousal Limited Access Trusts.

Forbes Reports that Baby Boomers are expected to transfer \$30 Trillion in wealth to the younger generation over the next many years!

# TAX TABLES

New Jersey Inheritance Tax	
Class of Beneficiary	Tax Rate
Class "A": spouse, domestic partner, descendant, parent, step-child, mutually-acknowledged child	Fully exempt
Class "C": sibling, son/daughter-in-law	First \$25,000 - exempt Next \$1,075,000 - 11% Next \$300,000 - 13% Next \$300,000 - 14% Over \$1,700,000 - 16%
Class "D": people who do not qualify as Class "A", "C", or "E" including step-grandchildren	Under \$500 - exempt Over \$500: first \$700,000 - 15% Over \$700,000 - 16%
Class "E": Charities, other exempt entities	Fully exempt

Pennsylvania Inheritance Tax	
Class of Beneficiary	Tax Rate
Spouse	Exempt
Descendants & Lineal Heirs	4.5%
Siblings	12%
Other heirs, except charities and governmental entities which are exempt	15%

Federal Estate Tax Exemption		
Year	Exemption	Tax Rate
2022	\$12,060,000	40%
2023	\$12,920,000	40%

Federal Gift Tax Annual Exclusion	
Year	Exemption Amount
2022	\$16,000
2023	\$17,000

Uniform Lifetime Table (for RMD for IRA Owners)					
Age	Dist. %	Age	Dist. %	Age	Dist. %
72	3.65%	82	5.41%	92	9.26%
73	3.77%	83	5.65%	93	9.90%
74	3.92%	84	5.95%	94	10.53%
75	4.07%	85	6.25%	95	11.24%
76	4.22%	86	6.58%	96	11.90%
77	4.37%	87	6.94%	97	12.82%
78	4.55%	88	7.30%	98	13.70%
79	4.74%	89	7.75%	99	14.71%
80	4.95%	90	8.20%	100	15.63%
81	5.15%	91	8.70%	101	16.67%

New Jersey Retirement Income Exclusion		
Applies if 62 or older or disabled AND income up to \$150,000		
Single	Married, Jointly	Married, Separately
Income up to \$100,000		
\$75,000	\$100,000	\$50,000
Income \$100,001-125,000		
37.50%	50.00%	25.00%
Income \$125,001-150,000		
18.75%	25.00%	12.50%

Net Investment Income Tax 2023	
3.8% add'l tax on Investment Income	
Single	inc over \$200,000
Married, Jointly	inc over \$250,000
Estates & Trusts	inc over \$14,450

Long-Term Capital Gains Rates 2023			
Tax Rate	Single Income	Married, Filing Jtly	Estates & Trusts
0%	Up to \$44,625	Up to \$89,250	Up to \$3,000
15%	\$44,626-492,300	\$89,251-553,850	\$3,001-14,649
20%	Over \$492,300	Over \$553,850	Over \$14,650

New Jersey Income Tax Rates 2023			
Tax Rate	Single Income	Married Filing Jtly	Estates & Trusts
1.40%	Up to \$20,000	Up to \$20,000	Up to \$20,000
1.75%	\$20,001-35,000	\$20,001-50,000	\$20,001-35,000
2.45%	---	\$50,001-70,000	---
3.50%	\$35,001-40,000	\$70,001-80,000	\$35,001-40,000
5.53%	\$40,001-75,000	\$80,001-150,000	\$40,001-75,000
6.37%	\$75,001-500,000	\$150,001-500,000	\$75,001-500,000
8.97%	\$500,001-1,000,000	\$500,001-1,000,000	\$500,001-1,000,000
10.75%	Over \$1,000,000	Over \$1,000,000	Over \$1,000,000

Federal Income Tax Rates 2022 & 2023						
	Single		Married Filing Jointly		Estates and Trusts	
Tax Rate	2022 Taxable Income	2023 Taxable Income	2022 Taxable Income	2023 Taxable Income	2022 Taxable Income	2023 Taxable Income
10%	\$0-10,275	\$0-11,000	\$0-20,550	\$0-22,000	\$0-2,750	\$0-2,900
12%	\$10,276-41,775	\$11,001-44,725	\$20,551-83,550	\$22,001-89,450	---	---
22%	\$41,776-89,075	\$44,726-95,375	\$83,551-178,150	\$89,451-190,750	---	---
24%	\$89,076-170,050	\$95,376-182,100	\$178,151-340,100	\$190,751-364,200	\$2,751-9,850	\$2,901-10,550
32%	\$170,051-215,950	\$182,101-231,250	\$340,101-431,900	\$364,201-462,500	---	---
35%	\$215,951-539,900	\$231,251-578,125	\$431,901-647,850	\$462,501-693,750	\$9,851-13,450	\$10,551-14,450
37%	Over \$539,900	Over \$578,125	Over \$647,850	Over \$693,750	Above \$13,450	Above \$14,450