

# The Advisor



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## ESTATE PLANNER'S TIP

The fact that not everyone has a will is no shock to most advisors. Even among those clients who do have wills, more than a few haven't reviewed them in the past five to ten years. Although a new will is probably in order for clients with "antique" wills, for many people, a codicil can suffice. Remember, however, that a codicil generally republishes an existing will, so the original document should be reviewed carefully to make sure all necessary changes are made. At the client's death, both the original will and the codicil must be admitted to probate, so the documents should be kept together in a safe place. And if a particular beneficiary's interest is eliminated in the codicil, he or she still will have to be notified of the probate proceedings, which could lead to discord or even a will challenge. If that possibility exists, the testator may want to execute an entirely new will.

## MAKING PORTABILITY ELECTION SIMPLER

Nearly every week, the IRS is issuing private letter rulings granting additional time for surviving spouses to make the portability election under Code §2010(c)(5)(A). The failure to make the election generally involves estates where no estate tax return was required. To reduce IRS staff time responding to the requests and also save taxpayers the fee involved with requests for private letter rulings, the IRS has announced a simplified procedure for requesting an extension of time.

Under Rev. Proc. 2017-34, the person allowed

to make the election on behalf of a decedent must file Form 706 on or before the later of January 2, 2018, or the second anniversary of the decedent's date of death. The form must also include "Filed Pursuant to Rev. Proc. 2017-34 to Elect Portability under §2010(c)(5)(A)" written at the top of the form. The simplified method is available only where the decedent was survived by a spouse, died after December 31, 2010, and was a U.S. citizen or resident at the time of death. In addition, the estate must not have been required to file an estate tax return under Code §6018(a) and did

not, in fact, file a return. This is the only method of obtaining an extension of time to make the portability election if the decedent and executor meet the requirements. For estates and surviving spouses not qualifying, a request for a private letter ruling is still available.

### REGISTER: YES, FEE: NO

Starting in 2010, only attorneys, CPAs and “registered tax return preparers” could prepare income tax returns for others. A preparer who was not an attorney or CPA was required to pass a one-time competency exam and a suitability check. All tax return preparers had to obtain a PTIN and pay an annual fee.

In 2014, the D.C. Circuit Court ruled that 31 U.S.C. §330 did not authorize the IRS to regulate tax return preparers [*Loving v. IRS*, 742 F.3d 1013]. The court invalidated the competency and continuing education requirements, but left in place the PTIN fee requirement.

The Independent Offices Appropriations Act allows agencies to charge a fee for a “service or thing of value.” The PTIN fee initially fell within

this category, because only a subset of the general public was entitled to a PTIN and the benefit of receiving compensation for preparing tax returns.

The U.S. District Court, District of Columbia, has now ruled that while the IRS was authorized to issue regulations requiring tax return preparers to obtain PTINs, it was no longer entitled to impose a fee. Several return preparers argued that the IRS lacks the authority to require the fees. The court noted that under *Loving*, the IRS may not require that return preparers obtain an occupational license. Because anyone can obtain a PTIN and prepare returns for compensation, the PTIN is no longer a “service or thing of value” for which the IRS may charge a fee, the court said (*Steele v. U.S.*, 2017-1 USTC ¶150,238).

### GIVING ISN'T TAXING

The trust established by Vera and Don became irrevocable at Vera’s death. The trust was divided into three separate trusts, one of which is a marital trust. Don is to receive all the net income from the marital trust, and as much principal as the trustees deem appropriate for his health and support. The couple’s two children are the trustees. Vera’s executor made a QTIP election for the marital trust.

The trustees of the marital trust propose to divide it into two separate trusts – Trust I and Trust II – with the same terms as the original. Don will then renounce any right, title or interest in Trust I. As a result, Trust I will terminate and be distributed to family beneficiaries. The IRS was asked to rule that Don will not be deemed to have made a gift of the property in Trust II and that his income interest in Trust I would not be valued at zero under Code §2702.

The IRS ruled that Don’s renunciation of his interest in Trust I will be considered a gift under Code §2511, but he will not be deemed to have made a gift of the property in Trust II. Because his interests in Trust II are not treated as a retained interest under Code §2702(a)(1), the

### PHILANTHROPY PUZZLER

Patricia purchased a deferred annuity contract in 2007. Payments are to begin soon, but she doesn’t really need or want the additional income. She received a newsletter from one of the charities she supports, explaining the benefits of charitable remainder trusts and how trusts funded with appreciated securities can avoid the capital gains tax when the shares are sold in the trust. Patricia would like to help the charity by using the annuity to fund the charitable remainder trust. Can she avoid tax on the growth within the annuity since 2007?

renunciation will not cause his interest in Trust I to be valued at zero. The IRS added that no part of Trust I would be included in Don's gross estate under Code §2044(b)(2) (Ltr. Rul. 201721006).

### TESTATOR DIDN'T EXCEED POWER OF APPOINTMENT LIMITS

Louise Bruce was given the testamentary power, under two trusts created by her mother, to appoint the trust remainders to any person other than her "creditors, her estate or the creditors of her estate." Relatives of the mother were to receive the remainders if Bruce did not exercise her power.

Bruce's will specifically referenced the power of appointment, directing that the trustees were to pay the remainders to her executor, to be added to the residue of her estate. The will also directed her executor to use the residue of the estate to create a private foundation in Bruce's name. The relatives who would have received the trust remainders in the absence of Bruce exercising her power to appointment claimed that Bruce did not have the power to direct the funds to her executor and therefore failed to appoint the remainders.

The Surrogate's Court of New York County said this was clearly not a case where Bruce was unaware of the existence of the power and therefore might have failed to honor its limits. Instead, said the court, she was not directing the trustees to distribute the funds to her executor as an agent of her estate, but rather as an agent of the foundation that the will directed the executor to establish. The court noted that although Bruce's intent was "inartfully expressed," it was a valid exercise of her power (*In re Will of Bruce*, 2017 NY Slip Op 30967(U)).

### DEDUCTION FOR UNREIMBURSED VOLUNTEER EXPENSES HITS DEAD END

The IRS disallowed the 2012 and 2013 charitable deductions of Adolph and Racquel Martinez, noting lack of substantiation. The couple conceded before the Tax Court that they had contributed

only \$220, but the court denied even that deduction, saying the purported donee was not listed on the IRS master list of §501(c)(3) organizations to which contributions are deductible.

The couple then argued that they were entitled to deductions of \$7,000 and \$5,825 for the year in question for unreimbursed volunteer expenses. Unreimbursed volunteer expenses of less than \$250 can be substantiated the same way as gifts of cash – with a canceled check, or receipt or other reliable written records showing the name of the payee along with the date and amount of the payment. For expenses of \$250 or more, the taxpayer must have a contemporaneous written statement from the charity containing a description of the services provided. Although the taxpayers provided a letter from the organization stating that Martinez was a volunteer and was not reimbursed for mileage, per diem, miscellaneous travel expenses or any other costs, the letter was dated June 1, 2015, meaning it was not contemporaneous [Code §170(f)(8)(B) and (C)]. The court determined the couple was not entitled to any deductions for unreimbursed volunteer expenses (*Martinez v. Comm'r.*, T.C. Summ. Op. 2017-42).

### PUZZLER SOLUTION

If the owner of a commercial annuity purchased after April 23, 1986, transfers it without full and adequate consideration, the owner is treated as receiving an amount equal to the excess of the cash surrender value over the investment in the contract [Code §72(e)(4)(C)]. Income is recognized even if the annuity is transferred outright to charity. Although Patricia could use the annuity to fund the remainder trust and receive an income tax charitable deduction, she would recognize income in the year of the transfer, reducing the benefit of the deduction.

### PHILANTHROPY – IT’S NOT JUST FOR “OLD PEOPLE”

The benefits of philanthropy aren’t limited to “people of a certain age.” True, charitable deductions are larger for charitable remainder trusts and other deferred gifts when beneficiaries are older, but there are several situations where charitable gifts in trust are appropriate for younger individuals.

#### *Retirement planning*

Many wage earners in the 33%, 35% and 39.6% tax brackets are frustrated by their inability to shelter as much income in qualified retirement plans as they would like. These clients can defer more income until their retirement years while claiming a partial deduction now, through the use of a net-income with make up charitable remainder unitrust [Reg. §1.664-3(a)(1)].

A 45-year-old client might fund a 6% net-income with make up unitrust with \$25,000 annually and take charitable deductions (\$4,167 in the first year, assuming quarterly payments and a 2% §7520 rate). The trustee invests primarily in growth stocks or mutual funds that produce little income. Each year that the donor does not receive 6% of the trust’s annual fair market value, a deficiency accrues. In 20 years, when the client is ready to retire, the trustee sells the growth stock (with no loss to capital gains tax), invests in high-yield securities and begins making up deficiencies from prior years.

Advantages of a “retirement” unitrust over other retirement plans:

- the unitrust may be established in addition to the donor’s other qualified plans;
- there is no maximum contribution;
- deductions for additional contributions increase as the donor gets older;
- there is no penalty if the donor begins receiving income prior to age 59½, and no requirement that withdrawals begin after age 70½;
- the client can fund the unitrust with appreciated securities, avoiding the capital gains tax, and;

■ a generous gift to charity occurs at the client’s death.

The same result is possible through a series of deferred payment charitable gift annuities.

#### *Family support*

Younger clients may be providing financial assistance to parents or grandparents, in most cases with after-tax dollars. A client in the 35% tax bracket who sends \$1,000 a month to a parent has to earn nearly \$18,500 to pay the taxes and make the \$12,000 gift.

Instead, the client could create a charitable remainder trust or charitable gift annuity that pays the parent the \$12,000 annually. The client receives a charitable deduction for the value of the remainder, based on the parent’s age and the payout rate of the trust or gift annuity. The gift to the parent is a present interest that qualifies for the \$14,000 annual exclusion.

#### *College expenses*

A similar gift is possible for a child about to enter college. A parent can create a term-of-years charitable remainder trust that pays the child income during college and until the child is established in a career – ten years, for example. A charitable deduction is available and the trust can be funded with appreciated securities for even greater tax savings.

#### *Capital gains reductions*

Clients in the 39.6% tax bracket are subject to capital gains at a 20% rate, rather than the 15% rate that applies to most taxpayers. In addition, the 3.8% net-investment income tax affects taxpayers with modified adjusted gross income in excess of \$200,000 for single taxpayers or \$250,000 for joint filers. Even with capital gains rates at 15%, younger clients may consider a charitable remainder trust a way to liquidate highly appreciated assets within a tax-exempt environment. They can retain payments for life, benefit from capital gains and net-investment income tax avoidance and receive an income tax charitable deduction.

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