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Portability extension requests simplified

ESTATE PLANNING: Executors who miss the deadline for making an estate tax portability election now have a little extra time.

By **Renée Rodda, J.D.**
Associate Editor

Estates that are filing an estate tax return only to make a portability election now have until the later of January 2, 2018, or the second annual anniversary of the decedent's date of death to make the election on the estate tax return.¹ No fee will be required to use this simplified extension procedure, which became effective on June 9, 2017.

Estates that miss this deadline will be required to request a private letter ruling to make the portability election.² The fee for these letter rulings is currently \$10,000.³

However, if a PLR request was pending on June 9, 2017, the IRS will close the ruling request and refund the user fee, and the estate may request relief under the new procedure.

Making the election

Prior to the availability of this extension procedure, a timely filed Form 706, United States Estate (and Generation-Skipping Transfer) Tax Return, had to be filed to make a portability election to preserve the deceased spouse's unused exclusion (DSUE) for estate tax purposes.⁴ This meant that the executor was required to file a return making the election within nine months of the decedent's date of

Additionally, the contribution is not deductible unless it constitutes a completed gift, meaning the donor “must do everything reasonably permitted by the nature of the property and the circumstances of the transaction in parting with all incidences of ownership.”⁴ This means that the donor must completely relinquish “dominion and control” over the contributed property; the donor may not retain any right to direct the disposition or manner of enjoyment of the subject of the gift.⁵

However, if a condition is placed on the contribution that may otherwise invalidate the contribution, and the condition is so remote as to be negligible, the charitable contribution deduction will be allowed.⁶



¹ *Fakiris v. Comm.*, TCM 2017-126

² See *Stark v. Comm.* (1986) 86 TC 243; *Knott v. Comm.* (1977) 67 TC 681; *Waller v. Comm.* (1963) 39 TC 665; Treas. Regs. §1.170A-4(c)(2)

³ See *U.S. v. Am. Bar Endowment* (1986) 477 US 105

⁴ *Coffey v. Comm.* (1944) 141 F.2d 204

⁵ See *Rosano v. U.S.* (2001) 245 F.3d 212

⁶ Treas. Regs. §1.170A-1(e)

REACT — What to do when you are a first time executor or trustee

ESTATE PLANNING: Give this to your clients.

By Richard B. Malamud, CPA, J.D., LL.M.
Guest Contributor

When a parent or someone close to you dies and you are the executor or trustee (“fiduciary”), it is often for the first and only time. It is likely you have no idea what must be done. The process varies by state and depends on how the title to the decedent’s property is held and who are the heirs. Some estates must go through probate while others won’t due to the size (exemption for small estates) or title (joint tenancy, community property with rights of survivorship, designated beneficiaries accounts, and property held in a trust) or type of property involved (cars, boats, and motorhomes).

As a nonprofessional fiduciary, you must quickly REACT:

Read the will, trust, other documents, and any other available financial information.

Engage professional representatives to assist you (tax professional, lawyer, financial, real estate, insurance).

Analyze the issues and process — learn on your own or have the professionals explain the issues and the process that will lead to the work you need to complete.

Complete all administrative tasks — find assets, pay bills, send notices, sell assets, go to court, and finally, make distributions to the heirs.

Take a vacation — you deserve it.

Read and review what you can find

Everything starts with the will and trust. They are the roadmaps. Find them and read them as soon as possible. It can be confusing as there is a lot of legalese and extraneous language, but do your best.

Next, find the rest of the financial information: bank accounts, brokerage accounts, insurance policies, credit card and other bills, and even the car pink slip. In the old days, “gathering” was fairly easy. Everything was printed and usually kept in a filing cabinet. If not,

within a month the postal worker would deliver the ongoing bills. Many bills are now either sent by e-mail or are on auto pay, and if you are lucky, you can find the password.

A good place to start looking for clues to everything else is the decedent's income tax return. It lists the interest bearing bank accounts, brokerage accounts, and business entities such as partnerships¹ and S corporations.

If you know you will be a fiduciary, have "the conversation" with Mom or Dad before they die: "What are your assets and liabilities, and what are your passwords?" Unfortunately, it is never the right time to ask. "I will know when its time to give you the information, and anyhow, it's all on my computer" is often the response. Even when you do get involved early, things change — new accounts are opened and passwords are changed.

It is time to review whatever you found in order to get a general idea of the size and nature of the estate and to talk to a tax professional and an attorney to find out how to proceed. Alternative resources are books² and web research, but most first-time fiduciaries should seek outside help. Do you really want to figure out the California Probate Code on your own? It won't be easy to be a fiduciary.³

Engage professionals

Reviewing the will and trust will raise many questions, as will making a quick list of assets and liabilities. Does the estate need to be probated, is an annual accounting required, how soon must the heirs be notified, do heirs receive a copy of the will or trust, and if so, when? Which bills should be paid now, which can wait? These are just a few of the questions.

You will probably figure out that either everything goes in trust until the decedent's spouse dies, or if unmarried, you get half of the estate and your sibling gets the other half, after giving the Hawaiian art collection to the next door neighbor.

Yet, confusion abounds. What does it mean to set up a qualified terminable interest property (QTIP) trust, a qualified subchapter S trust (QSST), or a bypass, spendthrift, or exemption trust? And what is a Uniform Gifts to Minor's Act (UGMA) or Uniform Transfer to Minor's Act (UTMA) account? What do you do with the house that's now empty, and how do you comply with the Uniform Prudent Investor's Act⁴ when reviewing the investment portfolio and the IRA account? That's why you may need to consult with various professionals including a tax professional, attorney, financial advisor, and insurance agent, to help you figure this all out.

First-time fiduciaries won't know the process of administering the estate or trust. It isn't common knowledge, and it certainly isn't described in the will or trust. In California, the trustee is required to notify the beneficiaries within 60 days of death,⁵ and an executor should start the probate process with the court within 30 days of notification of the death.⁶ Check with the a tax professional or attorney to find out if the assets need to be transferred into an administrative trust. Remember, everything earned after death is taxed to someone other than the decedent. So, hop to it.

Analyze the issues and get started

The next step is for the fiduciary to understand the process and start doing. Figure out what needs to be done immediately and what can wait a few days, weeks, months, or even years. Common questions are whether there will be a probate of the estate and whether an estate (federal or state) or inheritance (state) tax return must be filed.

In California, probate may be required if the decedent had real estate in his or her own name or certain tangible or intangible personal property without a designated beneficiary that totaled more than \$20,000 or \$150,000 depending on the type of property. Probate is time-consuming and expensive, and that is why in California property is often held in a revocable living trust — to avoid the time, cost, and public records that result from probate. (An issue that often comes up when married at the time of death is whether the house and other property are community property or separate property.)

An estate tax return is due nine months after death (plus a six-month extension). It is required for 2017 decedents if their gross estate exceeds \$5.49 million ("exemption amount"). No federal estate tax will be owed unless the taxable estate exceeds the exemption amount.

Fortunately, California has no inheritance tax no matter the size of the estate or to whom the estate is left. Thirty-one other states do not impose a death tax, but that leaves 18 states and some foreign countries that do, and a tax may be due there if the decedent was a resident of one of those states or if they owned real estate or a business in one of those jurisdictions.

Estates with a value exceeding the exemption amount will not owe any estate tax if any amounts over the exemption amount are left to a surviving spouse (directly or in a QTIP trust) or to charity. If not, and there is a tax, it is effectively a flat 40% tax on the net taxable value of the estate over the exemption amount (including prior taxable gifts).

If a return is required, Form 706, United States Estate (and Generation-Skipping Transfer) Tax Return, must be filed with the IRS, and Schedule A of Form 706 must be sent to each of the heirs to inform them of their tax basis in each of the assets received. It must be sent within 30 days of the due date of the estate tax return and must be updated if there are any changes.⁷

Even if an estate tax return is not required, if the decedent had a surviving spouse, the estate can elect "portability," which requires the filing of an estate tax return. Portability allows the unused exemption amount to be transferred to the spouse.

EXAMPLE 8-6: If the decedent had an estate of \$3 million, by electing portability, the remaining \$2,490,000 (\$5,490,000 - \$3,000,000) exemption amount can be passed to the surviving spouse, thus allowing the spouse to transfer their own exemption amount plus the additional portability amount to the heirs on the second death without incurring an estate tax.

Thus, even nontaxable estates may file an estate tax return. If a timely filed return isn't filed, a late portability election return may be filed the later of January 2, 2018, for 2011 or later years or the second anniversary of a decedent's date of death.⁸ Whether to make a portability election requires professional advice due to the cost involved compared to the probable lack of benefit for small estates.⁹

Complete all administrative tasks

Now it's time to gather up all the assets and pay the liabilities. Unless you became the trustee prior to death, you need to notify the banks and brokerage firms that as the fiduciary you can now sign the checks.

Decisions must be made and actions taken. Should you keep or sell the assets or combine bank accounts? Who are the beneficiaries of the IRA, Keoghs, pension, etc.? The life insurance won't pay itself. Someone must inform the insurance company of the death and provide a death certificate. It is a good idea to get at least six and probably a dozen copies of the death certificate. Most financial institutions will require a certified copy.

You will also need to notify the Social Security Administration, the military if the decedent served, insurance companies including life, health, car, and home, pension administrators, and many others.

Death won't stop the IRS. There's still a final income tax return to file. When you file the tax return, you must decide if you want to ask the IRS for a quick assessment because if you distribute the estate's assets to the heirs and it turns out the IRS or another creditor wasn't paid, you can be personally liable. Until all the creditors have been paid, make sure there are sufficient assets to pay them before making beneficiary distributions.

Making current beneficiary distributions (or not making them) is complicated by the fact that when the estate or trust earns income during the administration, it will be taxed to the trust or estate unless it is distributed each year it is required to be distributed. Fiduciary returns impose the highest tax rate, currently 39.6% on taxable income over \$12,500. Plus, the 3.8% net investment income tax will often apply to investment income.

If instead, the current income or any portion of it is distributed annually or within 65 days of year-end, that amount will be taxed to the beneficiary rather than to the trust or estate

almost always at a far lower tax rate. It can't be at a higher rate! Once all the creditors have been paid or it is obvious there are sufficient assets to pay them, maybe it is time to make some distributions to the beneficiaries, but check with the tax professional and attorney first. Remember, all creditors, including the IRS, must be paid first.

Will you decide to sell the house or will the kids keep it and rent it out? All this must be decided before the estate can be finalized and the assets distributed. Ask the attorney if an accounting is required before the final distribution.

Once you think everything is taken care of, all debts have been paid, and all assets have been identified, it is time to pay the heirs or fund the trusts. It is not uncommon to get final medical bills well over a year after death, and under the normal statute of limitations the IRS has three years and California four years to audit and assess a tax liability. Consider keeping a bank account open with reserve for any contingencies, and if a refund somehow shows up late, it's nice to have a bank account to make a deposit for a check with the decedent's name on it.

Take a vacation

Take a well-deserved vacation, possibly funded by a portion of your trustee fees. The bad news: They are taxable. The good news: They are not subject to self-employment tax if you aren't a professional trustee.¹⁰ If you are the sole heir, generally you shouldn't take a fee, because you will get the same amount without income taxes.

Final note

Don't throw the will, trust, death certificates, or estate tax returns away. Years later, notices could be sent to you about escheated property that wasn't identified earlier. To get the assets transferred to you or the heirs, some of those documents will be required. That is why you get the big bucks for doing all this; more likely you get nothing lest your siblings raise a stink.

About the Author

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Need more information?

For a primer on trust basics, including an overview on the different types of trusts and a walk-through on preparing the 1041 trust return, Spidell offers an eight-hour on-demand webinar. Go to www.caltax.com, click on Webinars, and find 2017 Basic Trust Webinar for details and to order.



- ¹ If there is an appreciated partnership interest, consider making a §754 election. See "Using the IRC §754 election in a partnership," *Spidell's Federal Taxletter*®, May 2016
- ² A quick web search found two books: "Estate and Trust Administration For Dummies" and "How to Probate an Estate in California," plus the California courts have lots of information on their websites
- ³ Cal. Probate Code §§16000–16504; see also "Understanding The Duties and Responsibilities of a Trustee" at: www.estateplanning.com/Duties-and-Responsibilities-of-a-Trustee/
- ⁴ Cal. Probate Code §§16045-16054
- ⁵ Cal. Probate Code §16061.7f
- ⁶ Cal. Probate Code §8001
- ⁷ See "IRS Form 8971 and Schedule A finalized — estate tax basis reporting," *Spidell's Federal Taxletter*®, April 2016
- ⁸ For details, see Rev. Proc. 2017-34
- ⁹ The problem is determining what is "small"
- ¹⁰ Rev. Rul. 72-86

Checklist of things to do

Things to do quickly

- ☐ Notify the Social Security Administration, pensions, and annuities of the death
- ☐ Find or request (and review) copies of:
 - ☐ Will
 - ☐ Trust
 - ☐ Birth certificate
 - ☐ Social Security card
 - ☐ Death certificate — get 5–10 copies
- ☐ If living alone:
 - ☐ Take care of any pets
 - ☐ Notify U.S. Postal Service to forward mail to you
 - ☐ Talk to the landlord about the lease
 - ☐ Cancel: cell and landline phones, newspapers, cable TV, magazines, electric, gas, etc. and unneeded insurance (some insurance like homeowner's will be needed until the house is sold or transferred)
 - ☐ Go through the house to look for important papers and secure valuable assets

Things that can wait a short while

- ☐ Call all advisors with relevant information or who can provide advice:
 - ☐ Tax professional
 - ☐ Attorney
 - ☐ Insurance agent
 - ☐ Stock broker/investment advisor
- ☐ Check with the employer/union/military about:
 - ☐ Final paycheck
 - ☐ Death benefit
 - ☐ Pension
- ☐ Check for personal property at an employer, health club, country club, volunteer office, etc.
- ☐ Locate all assets and liabilities that are easy to find (often they will appear as monthly statements in the mail, but increasingly this information will be sent by e-mail)
- ☐ Check old and ongoing e-mails for vital information, and check the account on a regular basis for new information for the following (including the monthly statements):
 - ☐ Bank accounts
 - ☐ Brokerage accounts
 - ☐ Life insurance policies (don't forget to notify the company)
 - ☐ Pink slips for cars
 - ☐ Real property
 - ☐ Stocks, mutual funds, exchange-traded funds, and bonds

- ☐ Businesses interests including partnership, LLC, LLP, corporation, or sole proprietorship
- ☐ Safe-deposit boxes and keys
- ☐ All credit card and other short-term debts
- ☐ Mortgages, loans, student loans, and other long-term debts
- ☐ Prior-year income tax returns
- ☐ Pensions — IRA, SEP, Keogh, Roth, 401(k), 403(b), 457, etc.
- ☐ Personal property: car, boat, jewelry, furniture, clothing, books, art, etc.
- ☐ Leases — for a car, mobile home, etc.
- ☐ Marriage certificate and divorce decrees
- ☐ California Secretary of State – Unclaimed property list
- ☐ Copies of prior gift tax returns

File claims for

- ☐ Any reimbursement for health-related final illness that can be repaid by health insurance
- ☐ Life insurance
- ☐ Any reimbursement for IRC §125 flexible-spending arrangements

For attorney or tax professional or both

- ☐ If there is a trust, determine who the new trustee is and what must be done
- ☐ If there is a will or property held in decedent's name alone, determine if probate is required
- ☐ Determine if an estate or inheritance tax return or income tax returns should be filed

Other things to do

- ☐ Pay debts that are due
- ☐ Determine if any bank CDs should be closed, as most will not have a penalty for early withdrawal
- ☐ Determine whether you are required to notify current and contingent beneficiaries of their potential inheritance
- ☐ Gather all information for the final income tax and fiduciary income tax returns
- ☐ Get appraisals for real estate or business interests
- ☐ Gather all information for the estate and/or inheritance tax returns
- ☐ Talk to your advisors before making any distributions to heirs
- ☐ Keep a reserve — decide how much and for how long

Finally

- ☐ Ask yourself and your advisors: What isn't included on this list?

Checklist of Topics to Discuss with Experts

Item	Yes	No
Final tax return (Form 1040)	<input type="checkbox"/>	<input type="checkbox"/>
Estate tax return (Form 706) and inheritance tax return (state) and portability election	<input type="checkbox"/>	<input type="checkbox"/>
Life insurance	<input type="checkbox"/>	<input type="checkbox"/>
Community property or separate property if married	<input type="checkbox"/>	<input type="checkbox"/>
Provisions in the will and revocable living trust	<input type="checkbox"/>	<input type="checkbox"/>
Funding of trust(s)	<input type="checkbox"/>	<input type="checkbox"/>
Title to real estate/partnerships/autos	<input type="checkbox"/>	<input type="checkbox"/>
Fund future trusts	<input type="checkbox"/>	<input type="checkbox"/>
Pay debts	<input type="checkbox"/>	<input type="checkbox"/>
Make distributions to beneficiaries	<input type="checkbox"/>	<input type="checkbox"/>
Fiduciary income tax returns (Form 1041)	<input type="checkbox"/>	<input type="checkbox"/>
Notifying Social Security, pensions, annuities, insurers, landlords, etc., of the death	<input type="checkbox"/>	<input type="checkbox"/>

Important Financial Contacts

	Name	Contact info
Tax professional		
Attorney		
Insurance – life/home/car		
Stockbroker		
Financial planner		
Banker		
Pension plan administrator		