Montgomery County Estate Planning Council

MCEPC Founded 1962

Charter Member

NEWSLETTER

Summer, 2020, Issue 58

Greetings from our new President

Leslie K. Heffernen, Esq., LL.M (tax), CPA

Esteemed Members of MCEPC:

I am very proud and honored to be a long-term member of MCEPC. I am even more excited to have the opportunity to serve as the President of our council for the 2020-2021 year. This year will bring with it much Board and member creativity and thoughtfulness as we navigate the unchartered waters of this pandemic. Although we have not had the opportunity to gather in person for several months, our council continues to grow. Your membership renewals and referrals of prospective members have strengthened our council and we look forward to its continued growth.

As we undertake a new meeting format for the foreseeable future, we hope that we will continue to be a relevant part of your professional development. The Board has been working hard behind the scenes. Next week we will be launching our Lunch and Learn Zoom programs which are intended to allow members to share ideas and experiences, and learn about relevant topics. We are continuing to develop other meeting formats as we approach the Fall.

On behalf of our Board I would like to welcome you into this new council year and we look forward to providing you with the education, fellowship, and resources of MCEPC. Please do not hesitate to reach out to me if you have any comments or suggestions.

Greetings from our outgoing President

Stephen A. Tulli, CFP®

To our valued Members and Friends….

It has been my honor to preside over the Council term of 2019-2020. I would like to thank our current Board, outgoing Board members and our Administrator, Wendy Rudolph, for tireless effort and counsel to me this past year. They are a wonderful group of colleagues for which I am grateful. I am excited about our incoming Board members as well as our new leadership. The Council is in great hands and we will navigate the “new normal” well, whatever it may be. The Board is moving forward with a full calendar of events, whether virtual or in-person, to continue to enhance your experience as members.

While our Council activity was altered by the COVID pandemic, your commitment to your clients and your respective professions never wavered. The MCEPC venues and meeting formats may have changed but what hasn’t changed is our mission to deliver timely educational content and provide peer professional networking opportunities to all of you.

If you haven’t done so, please renew your membership or join NOW at http://www.mcepc-pa.org ! Our 2020-2021 programs are content-rich and include some of the industry’s best speakers! As always, I invite you to participate in your Council by contributing ideas, volunteering for Committees, becoming Sponsors and considering a future Board position. The vibrancy of our Council and its future rests with YOU! Thank you for being part of the Montgomery County Estate Planning Council!

I look forward to seeing all of you this Fall. Please stay safe and healthy and enjoy your summer!

In This Issue:

WELCOME NEW MEMBERS AND
THANK YOU TO OUR REFERRING MEMBERS!!
Bode Hennegan—Membership Chair

We extend a warm welcome to our newest members as well as a big THANK YOU to our members who referred them! Please continue to spread the word about the great benefits of MCEPC membership – education, networking, camaraderie!

Brendan Flatow—Evergreen Settlements, LLC

Dean Fox—Kalejta Financial Management

Robert (Bob) Hart—Bernstein Private Wealth Management

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In the News

Congratulations...After thirty years, Charles Ingersoll has retired from The Haverford Trust Company!

Our Condolences... Long time member Marlyn Smith, Esq. passed in April. Our condolences go out to his family.

Asset Planning Services Elects Two New Board Members

Harleysville, PA (June 2020) – Asset Planning Services (APS) is pleased to announce the election of Daniel Esquirell, Director of Financial Planning at APS, and Bethany Landis, Director of Client Service at APS, to the Board of Directors.

"I am pleased to welcome Dan and Bethany as new Board members" said Richard Volpe, Founder and President of APS. "These individuals bring a wealth of experience and expertise and will be tremendous assets to our firm as we further our mission of providing financial direction to our clients and their families."

We're still working behind the scenes! We hope to connect soon, whether virtually or in person

What Is Interdependence? Why We Need to Plan for It

Bode Hennegan

When it comes to retirement and aging, many of us don't think twice about planning for our golden years. It can be exciting to look ahead and prepare financially for that time and place to do what we've always wanted to do like traveling, taking up a new hobby, visiting grandchildren or even starting a second career.

Aside of the enjoyable aspects of life in retirement, we also have to plan for the harsh realities of getting older and what that might entail. We plan for the time of increased dependence on others also known as "incapacity," which is defined as the physical or mental inability to manage one's affairs.

Of course, this planning involves drawing up legal documents including power of attorney, advanced directives and purchasing long-term care insurance. We also plan for the end of life with a will, life insurance policies and trusts.

But what about the time in between these two stages?

The time between newly retired independence and being dependent on others is known as ***interdependence***. It's a period that is often overlooked. Most of us don't plan for the interdependence stage but we should and here is why.

Benefits of Interdependence

This interdependent stage of aging is lasting longer because people are living longer with diminished capacity. It's the time when individuals need some assistance with tasks but they're still independent and able to live on their own. Most people want to stay in their home — in familiar surroundings and in their established community. Interdependence helps keep people in their homes longer.

And it's important to realize that just because someone might lose regular function in performing tasks, doesn't mean that individual can't stay in their home and live independently.

For example, think about the act of snow shoveling. At some point, an individual might realize he or she shouldn't shovel snow anymore because of a back problem or a heart issue or is simply afraid of falling. Just because that person shouldn't shovel snow, doesn't mean he or she stops being independent and is headed to an assisted living facility.

Instead, the person might consider getting help with snow shoveling, thereby extending his or her independence. That is exactly what interdependence is.

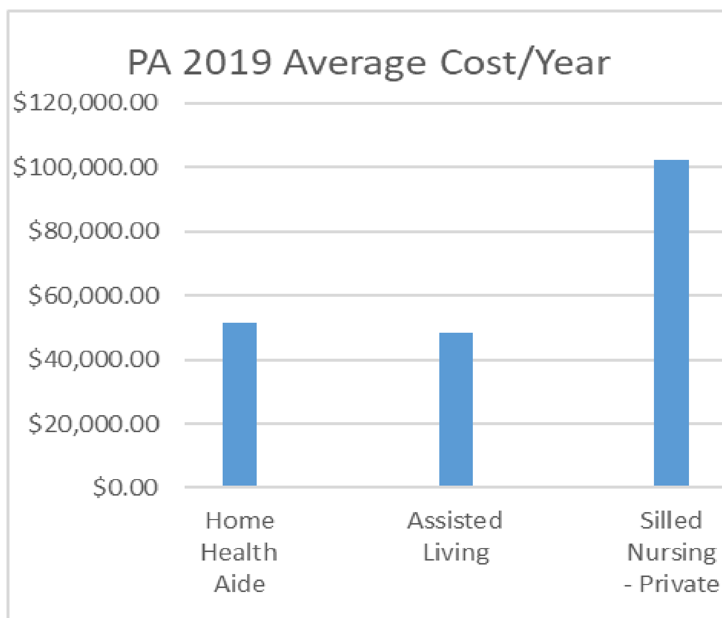
A more emotionally charged example is with daily money management. Unfortunately, research has shown that basic math is the first area to be affected by cognitive decline as people age. As the ability to comprehend math diminishes, money management becomes more challenging, sometimes resulting in checkbook mistakes or falling victim to money scams.

But similar to show shoveling, just because a certain task proves more challenging, it doesn't mean people can't remain independent in their homes. They can be interdependent (and stay in their home longer) if they seek help with the necessary bill paying and checkbook balancing.

What's more, two of the most common reasons aging adults leave their homes is because of the apparent risk of falls and medication errors. These two areas also have an in-home solution.

Professionals can be brought in to reduce the risk of falls by identifying problem areas and remove clutter and area rugs, add grab bars and railings, as well as enhance lighting throughout the home.

Aging individuals can also ask family or hire others to help them with sorting and distributing their daily medications to prevent harmful errors.



Data Source: Genworth.com

Interdependence - cont

This interdependent period is crucial to recognize because it can also mean delaying or preventing the often, astronomical cost of home care and institutional care that can come with aging (see chart).

Identifying Trigger Points

If we neglect to plan for interdependence, it can often be too late to get help and accelerate a person's need for costly care. Once people experience cognitive decline, it's often too late to plan. This is because people are not always conscious of their own decline and that's when life can get very complicated.

It's ***before*** we reach the interdependence stage, that we need to plan and identify "trigger points" for relinquishing responsibilities.

Trigger points are completely personal and depend on the individual. Examples of trigger points might include planning to take a driver's test annually and if that person fails, they know it's time to stop driving. Or if they have more than a couple significant checkbook mistakes, knowing it's time to ask someone else for help with money management.

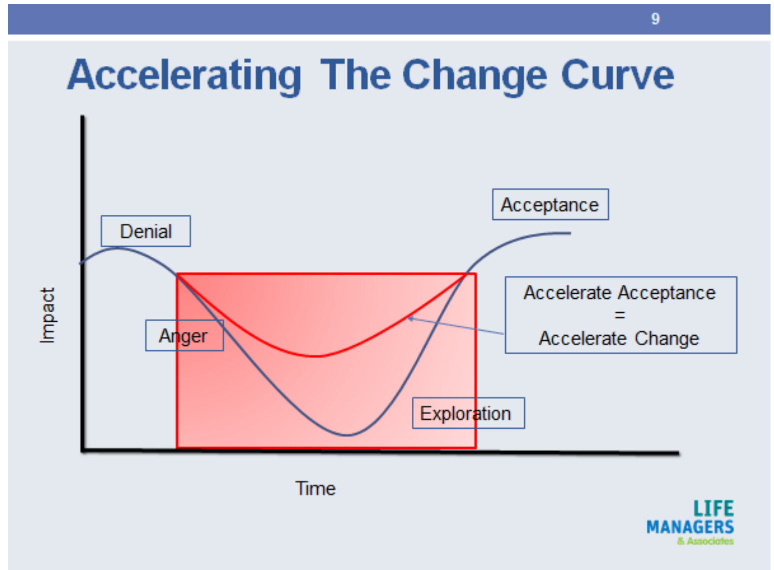
Planning for interdependence is like an insurance policy for staying at home. It allows individuals to have more control over their future and their needs instead of a family member deciding what's best for them.

Commonly Missed Planning Opportunity

Of course, it sounds like planning for interdependence makes sense on a personal and financial level. So why aren't we proactively planning for this stage of aging?

The first reason is that it is relatively **new**. Many older adults today lack a frame of reference. They may have never witnessed their parents' experience interdependence or at least do so for very long. It's likely that their parents did not live for years with chronic illness and diminished capacity.

The second reason we're not proactively thinking and planning for interdependence is our inherent **resistance to change**. As Elisabeth Kübler-Ross illustrated in 1969 regarding how people deal with their own death, a "Change Curve" exists (see box). This curve can apply to any significant change, not just death, and includes four stages: denial, anger, exploration and acceptance.



For instance, on your commute to work on a busy thoroughfare, you notice a new sign stating that the road will be closed the following Monday. But when Monday comes, you forget to leave early to accommodate for the detour and experience **denial**. As you sit in the traffic of the detour, you become annoyed because it is taking too long and you are going to be late for a meeting so you feel **anger**.

The next day you might remember the detour but you are annoyed that leaving so early caused you to forget your morning coffee, and you're still angry. It's not until the third day that you find there is a Starbucks on the new route, which is the **exploration** stage. It's at this point that you are on the upward trajectory of the curve. Once the road is back open, you decide to take the detour anyway so you can stop for your morning coffee and experience **acceptance**.

Any substantial change can take us through the Change Curve. Corporations have used this curve and realized that the bottom of the curve (the red box) is the "danger zone." This is where the most money is lost. In response, companies employ change management experts with the goal of changing the slope of the curve. If change is managed well, the curve can be can be accelerated and money is saved.

Interdependence - cont

The Change Curve to Increase Independence

But how does the Change Curve relate to aging and independence?

Denial is a leading reason that people don't plan for loss of function or death. We tend to deny our (potential or current) changing abilities. It's not until we **explore** how we can best live with limited abilities and then **accept** and ask for help that we are able to move in the upward slope (interdependence).

The longer we stay at the bottom of the curve in denial, the more dangerous and costlier it becomes for us. It is in this area of the curve that mistakes are more likely to happen, which may put us into the dependent stage prematurely.

For example, not recognizing one's own physical deficits may mean a grab bar wasn't installed to prevent a fall and as a result that individual might end up moving to an assisted living facility. Likewise, not accepting help with finances may lead to a devastating accounting error.

But recognizing and accepting potential deficits in daily functioning and knowing trigger points early is key to interdependent planning. When this happens, the Change Curve can be accelerated, keeping people in their home and money saved from having to move to a facility and all the costs that come with it.

In other words, knowing when to accept help (interdependence) from others early on is the way to extend independence. But most people need to understand interdependence options in order for it to benefit them.

Five Ways to Help Clients Plan for Interdependence

So how can you help your clients accelerate their Change Curve, become interdependent and stay in their homes?

Explain Interdependence: Change is inevitable. Let your clients know the dangers of not planning for interdependence.

Talk about Relinquishing Responsibility: Plant the seed at one meeting about what relinquishing responsibility (getting help) might look like but know that you will have to revisit it many more times.

Have Them Create a Trigger Point Plan: Have your clients establish the "trigger points" for when they will know to relinquish responsibility for tasks and who will assume those responsibilities.

Encourage Communication: Explain the value of discussing their interdependence plans with their families, friends or other supports.

Use a Professional Service: When necessary and when family can't be as readily available, it can make sense to call in professionals to help individuals carry out their interdependence plans.

Educating your clients on interdependence options early on can help them accelerate their own Change Curve into the acceptance stage of what might be ahead. This newly found awareness will help them confidently plan for the interdependent stage, identify their trigger points and do what most want to do: Stay in their homes as independently and as long as possible.

Bode Hennegan is the founder of Life Mangers & Associates, a company that provides personal assistant services to enable independent living. By empowering clients to age in place, Life Managers & Associates extends the time that they can safely live in their home, providing them with greater independence and flexibility. For more information, please visit www.life-managers.com.

Values Often Wrong in Estate Planning

by Leon Castner, ISA CAPP, Certified USPAP Instructor

One of the misconstrued problems in estate planning is the value of the personal property belonging to the client. It is often overvalued, leading to a surprising future shortfall of financial income or it has been overlooked altogether, either through careless mismanagement or through incompetence, neither of which are acceptable results for estate planning.

The main reason for this incongruity is that planners often accept the wrong methodology for appraising a client's or one's own personal property. This is based on the fallacious notion that property has a single value which is applicable for any intended use and for any time. This is simply not true. Valuations are based on effective dates and on intended uses (purposes). A valuation of an item for quick sale (need cash quickly or bankruptcy) is done at a "forced sale" value, one that is achieved on a cash basis usually very quickly, i.e. under 30 days. That is a much different value than one used for insurance coverage, which is normally the new replacement cost of an item in a top retail setting.

Another value sought is fair market value, a concept defined and codified by the IRS in their Treasury Regulations for estate taxes and charitable contribution deductions. It is set forth as "the price at which property would change hands between a willing buyer and a willing seller, neither being under any compulsion to buy or sell and both having reasonable knowledge of relevant facts" (Internal Revenue Section 1.170A-1©(2).)

This concept is used for appraisals for estate tax, gift tax, donations, or casualty losses. It is based on comparable sales and has little interest in what an item originally cost or what it might cost to replace with a new substitute. These sales are normally found through public auction results since they are readily available and are in a transparent marketplace. Forced sales (under compulsion) are usually excluded from consideration.

Most estate planners either ask their clients what their property is "worth" (a foolhardy question since the owners are not appraisers) or they use price guides, guidebooks (which have little to do with reality), or quick searches on the Internet. (Please do not believe everything you see on eBay.). Often, insurance policies are used to assess worth, which, once again, have little to do with potential liquidation value since they are based on replacement cost.

Estate planning on personal property should be done at either fair market value or orderly liquidation (arguably the same thing). What is needed is the amount the item would probably bring, in its current state and condition, under "average" time (marketing) and exposure, commonly delineated at 3-6 months. In the event the estate, trust, or heirs need to "cash out" or liquify assets, this is the amount they most probably would recover, minus any commission or related fees.

This is a far cry from what someone paid for something or what it might cost to replace with a new identical or suitable substitute. Using insurance schedules will only create havoc for future estate planning, although the listing of certain items may indicate potential high value (which should be investigated).

There are certain categories of personal property that seem to maintain or increase in value over time, oblivious to original cost. These have changed, however, and stalwarts like antiques and generic or decorative art have lost their luster. Many categories and styles have gone down drastically in recent years, due to public taste and decreased demand. For example, a tufted Victorian sofa that might have been valued at $3,000 ten years ago, could be worth only $300 today. The same is true for most antique glass, porcelain, and accessories, with few exceptions. (A good appraiser knows the exceptions.)

Most "cruise ship art" sinks as well, despite statements made at the time of purchase and/or certificates of authenticity that were given to fortify claims of investment potential. (C.O.A.s are only as good as the paper they are written on .) Most limited- edition prints, Franklin Mint type articles, and items sold for their "collectability" suffer the same fate, rarely surpassing original cost and usually fetching far less.

In addition, quality contemporary furnishings tend to depreciate rapidly, if not physically, at least economically. It would not be surprising to see a $25,000 dining room set bring only $1,500 after ten or twenty years of average use. (Think of the quick obsolescence of the wide screen television.) Most objects are like cars. Once you drive away from the showroom the car has already lost at least 10% of its value. You must wait a long time for it to become "historic" or antique, and that assumes it is still in great physical condition.

Volatile property like jewelry, coins, silver, and bullion rely on the current spot price of raw metal. Their values are joined to market fluctuations unless the property is of extreme rarity or has antique interest. A set of sterling silver for 12 by a well-known maker in an established pattern may cost well over $8,000 -$10,000 to purchase, but when selling that same identical set it will be weighed and evaluated in light of spot silver. It may bring as little as a tenth of that amount. Even Asian antiques such as

Values cont

porcelain, jades, ivory (a subject unto itself) have seen vast fluctuations in activity due to foreign markets and political instability. Appraisals from a few years ago may be totally out of date, especially for those type of items.

There is some good news. Certain items tend to maintain their value or even increase greatly over time. "Blue chip" art, the best of period furniture, and items with great provenance or pedigree fit that bill. Although not subject to any kind of inflation formula, they often follow a past track record, but not always. Periods and styles come and go, as do the flavor of art and artist.

Mid-century modern still sells well, far surpassing what owners paid for those items in the 1940s-1960s, as do the corresponding accessories, ceramics, porcelain, and glass. Paperware and ephemera (throw away paperware) are often overlooked since they were not originally purchased with huge funds. Autographs, historical documents, mementos of famous events and celebrations, sports cards, and even signed yearbooks can command amazing amounts. They tend to be overlooked when listing property, particularly by older owners.

The surprise in the world of personal property is amount of surprises that still occur, unplanned and unforeseen. The market may seem unpredictable, particularly to those not part of it, but it does have a recognizable flow. The best of the best usually remains that way, and the worst of the worst stays at the bottom. The middle is always moving, even in a pandemic.

The guidance for estate planners is to have their clients be honest in their declaration of valued property and to support or confirm it with appraisals done at the time. Since these will not be done for IRS estate tax purposes, appraisers have some flexibility in what they appraise and how they do it. (Note that estate appraisals done for probate or estate tax should be done the same way, but most estates have already planned on how to avoid the need for appraisals or any tax.)

Appraisal reports for estate planning can be tailored to the client, but still conform to uniform professional standards. Tell the appraiser to use fair market value or orderly liquidation. Do not use estimated replacement costs (unless you are advising your client to have proper insurance coverage.) This will give you a good and accurate view of the value of their possessions in a "where is" and "as is" state, not some pie in the sky notion based on unheralded and unsubstantiated claims that might torpedo future investment or liquidation plans.

Leon Castner is the new Estates & Trusts Specialist for Alderfer Auction, a full-service Hatfield based international auction company with stellar reputation having held nearly 200 auctions in 2019, including real property, fine art and antiques, collectibles, and estate residue. Mr. Castner is also Senior Partner at National Appraisal Consultants and is a Certified Instructor of the Uniform Standards or Professional Appraisal Practice of The Appraisal Foundation.

Considerations for Individuals and Closely Held Business Owners Resulting from the "CARES Act"

James Revels, Tracey Stone, Robert Keller, Sabrina Stimel

The recently enacted Coronavirus Aid, Relief, and Economic Security Act ("CARES Act") contains a number of important tax-related provisions. This article summarizes some of these provisions and also highlights a few planning considerations which are particularly relevant to individual taxpayers and owners of closely held businesses in the current environment. There continues to be further clarification to many areas of the CARES Act. Taking that into consideration, this article does not at times highlight additional clarification that may be available at time of printing.

Temporary Repeal of the Excess Business Loss Limitation

The CARES Act amended the excess business loss limitation regime under section 461(l) to have applicability for any tax years beginning after December 31, 2020, and before January 1, 2026. Prior to the amendment, the regime was applicable for any tax years beginning after December 31, 2017, and before January 1, 2026. Accordingly, the CARES Act amendment to section 461(l) effectively repeals the provision retroactively for tax years beginning prior to January 1, 2021. This impacts calendar years 2018, 2019, and 2020.

This temporary repeal of section 461(l) creates the potential for several different opportunities for individual taxpayers to access a refund of cash or pay a reduced tax liability in the future. In the near term, for taxpayers who may have been impacted by section 461(l) for 2018 or 2019 (or both), the retroactive repeal may allow for greater losses to flow through the taxpayer's return for those years, even though such losses occurred prior to the economic downturn. The repeal of the provision likewise creates opportunities for taxpayers to utilize losses from the recent economic downturn.

The repeal of the excess business loss regime may also result in the possibility of increased net operating losses ("NOLs") for the tax year, and may therefore also result in the possibility of increasing the amount of losses available for the taxpayer to carry back to a prior year (as discussed more fully in the section below). In some cases, this may include the possibility of carrying back a loss to a tax year prior to January 1, 2018, in which the taxpayer may have maintained a higher effective tax rate (i.e., when the highest marginal rate was still 39.6%).

It is important to note that in the case of a taxpayer with a loss limited under section 461(l) for the 2018 tax year (or for the 2019 tax year if a return has already been filed, and if the return can no longer be superseded), the retroactive repeal requires a taxpayer to amend their return to access a refund. It is important to also note that the failure to amend the taxpayer's return in situations where the excess business loss otherwise would have been utilized against non-business income of the taxpayer may result in the potential loss of the taxpayer's section 461(l) NOL carryforward in a subsequent year.

The repeal of section 461(l) was also coupled with a few technical corrections to the Tax Cuts and Jobs Act (the "TCJA"), some of which are outside of the scope of this article. However, a quick summary of these changes is provided below. The section 461(l) calculation now excludes items which are attributable to the trade or business of performing services as an employee. In addition, NOL deductions under section 172 and qualified business income deductions under section 199A would not be taken into account in determining excess business losses.

Section 461(l) has also been amended to provide that deductions for losses from the sale or exchange of capital assets would not be taken into account in increasing a section 461(l) limitation. Certain gains from the sale or exchange of capital assets may continue to be taken into account in reducing a potential section 461(l) limitation. Unfortunately, the technical corrections to the statute did not address whether a capital gain on the sale of a partnership interest or S corporation stock could be considered attributable to the taxpayer's trade or business. It should also be noted there are current provisions in the Heroes Act recently passed by the House of Representatives that contain provisions that would reverse these aforementioned changes.

Net Operating Loss Changes

The TCJA generally eliminated the carryback of NOLs (except for certain farm losses). However, the CARES Act grants taxpayers (including individual taxpayers) a five-year carryback period for NOLs arising in tax years beginning after December 31, 2017, and before January 1, 2021 (i.e., tax years 2018, 2019, and 2020).

The CARES Act also temporarily suspends the TCJA-imposed 80% of taxable income limitation on the use of NOLs for tax years beginning before January 1, 2021 (again, implicating tax years 2018, 2019, and 2020). For tax years beginning after December 31, 2020, the CARES Act re-imposes the 80% limitation with respect to the use of post- TCJA NOLs (i.e., NOLs arising in

CARES Act—cont.

tax years beginning after December 31, 2017), with two significant changes. First, incorporating a technical correction to the TCJA, the CARES Act determines taxable income for purposes of the 80% limitation after giving effect to the use of pre-2018 NOLs. Second, taxable income is determined without giving effect to the deductions for qualified business income, foreign-derived intangible income (FDII), and global intangible low tax income (GILTI) under sections 199A and 250.

Taxpayers are allowed to elect out of the five-year carryback rule, with the election being irrevocable. Procedurally, for NOLs arising in tax years beginning in 2018 and 2019, the election to forego the five-year carryback period would be required to be made by the due date (as extended) for filing the first tax return for the tax year ending after the date of enactment (i.e., with the 2020 tax return for calendar year filers), and for NOLs arising in a tax year beginning in 2020, by the due date (as extended) for the return for that year.

It is important to consider the character and rates of income in years prior and subsequent to a loss year before making the irrevocable decision to carryback an NOL or to forego the carryback.

Modification of Limitations on Charitable Contributions during 2020

The CARES Act enhances a taxpayer's ability to take a deduction for charitable contributions. Individuals who itemize their deductions can deduct up to 100% (as compared to 60%) of their adjusted gross income for certain cash contributions. For corporations, the 10% of taxable income limit is increased to 25%. To obtain this increased limitation, the contribution must be made in cash in 2020 to a public charity or certain foundations described in section 170(b)(1)(A). Donations to non-operating private foundations, supporting organizations, or donor advised funds do not qualify for this increased deduction amount.

Allowance of Partial Above-the-Line Deduction for Charitable Contributions

The CARES Act allows individual taxpayers who do not itemize their deductions the ability to deduct up to $300 of cash contributions made to a public charity or certain foundations described in section 170(b)(1)(A) during 2020. Most notably, contributions to non-operating private foundations, supporting organizations, and donor advised funds do not qualify for this deduction.

Special Rules for Use of Retirement Funds

The CARES Act waives the 10% early withdrawal penalty for distributions up to $100,000 from qualified retirement accounts for coronavirus-related purposes from January 1, 2020, until December 30, 2020. Income attributable to such distributions will be subject to tax over a period of three years. The taxpayer may recontribute the funds to an eligible retirement plan within three years without regard to that year's cap on contributions. The provision provides flexibility for loans from certain retirement plans for coronavirus-related purposes.

A coronavirus-related distribution is a distribution made to an individual:

- Who is diagnosed with COVID-19
- Whose spouse or dependent is diagnosed with COVID-19, or
- Who experiences adverse financial consequences as a result of being quarantined, furloughed, laid off, having work hours reduced, being unable to work due to lack of child care due to COVID-19, closing or reducing hours of a business owned or operated by the individual due to COVID-19, or other factors as determined by the Treasury Secretary.

The CARES Act also increases the amount an individual can borrow from their qualified retirement plan from $50,000 to $100,000 and also delays any 2020 loan repayment due date by one year or 180 days from the date of enactment, whichever is later.

Temporary Waiver of Required Minimum Distribution Rules for Certain Retirement Plans and Accounts

The CARES Act waives the required minimum distribution requirements for certain taxpayers for calendar year 2020. The waiver would generally apply to required minimum distributions from:

- A defined contribution plan described in section 401(a) or in section 403(a) or 403(b)
- A defined contribution plan which is an eligible deferred compensation plan described in section 457(b), but only if such plan is maintained by an employee described in section 457(e)(1)(A), or
- An individual retirement plan.

Delay of Payment of Employer Payroll Taxes

The CARES Act allows employers and self-employed individuals to defer payment of the employer share (6.2%) of the Social Security tax they otherwise are responsible for paying to the federal government with respect to their employees. This relief is effective for 2020 payments due after March 27, 2020. The provision requires that the deferred employment tax be paid over the following two years, with half of the amount required to be paid by December 31, 2021, and the other half by December 31, 2022.

The CARES Act provides a refundable payroll tax credit for 50% of wages paid by employers to employees during the COVID-19 crisis. The credit is available to employers whose operations were fully or partially suspended due to a COVID-19-related shut-down

CARES Act—cont.

order, or whose gross receipts declined by more than 50% when compared to the same quarter in the prior year. Once the gross receipts return to 80% when compared to the same quarter in the prior year, the credit will no longer be available. The credit is not available if the employer also received a Small Business Interruption Loan. Careful consideration should be given to whether a business should claim this credit or obtain the loan (a portion of which may be forgivable).

The credit is based on qualified wages paid to the employee. For employers with greater than 100 full-time employees, qualified wages are wages paid to employees when they are not providing services due to the COVID- 19-related circumstances described above. For eligible employers with 100 or fewer full-time employees, all employee wages qualify for the credit, whether the employer is open for business or subject to a shut-down order. The credit is provided for the first $10,000 of compensation, including health benefits, paid to an eligible employee. All persons treated as a single employer under sections 52 (a), 52(b), 414(m), or 414(o), would be considered one employer for these purposes.

The credit is provided for wages paid or incurred from March 13, 2020, through December 31, 2020.

Modification of Limitation on Business Interest

The CARES Act temporarily increases the amount of interest expense businesses are allowed to deduct on their tax returns from 30% to 50% of adjusted taxable income ("ATI") for 2019 and 2020. A taxpayer may elect to use 2019 ATI for purposes of calculating this limitation for the 2020 tax year.

For partnerships, the increased limit only applies for 2020 and not 2019. However, 50% of the partnership's 2019 excess business interest expense ("EBIE") will not be subject to the section 163(j) limitations (and will be automatically deductible by the partners in 2020), whereas the other 50% would still be subject to the section 163(j) limitations.

A partnership may elect out of the 50%-of-ATI provision in 2020. A partner may also elect out of the 50%- deduction-of-EBIE rule.

Technical Correction Regarding Qualified Improvement Property

The CARES Act includes a technical correction which would change the recovery life of qualified improvement property ("QIP") to 15 years under the general deprecation system, thereby making it eligible for bonus depreciation, retroactive to the enactment of the TCJA. This provision would allow for an immediate write-off of these costs instead of having to depreciate those improvements over the 39-year life of a commercial building. With the temporary repeal of the excess business loss regime under section 461(l) and the modification to allow for NOL carrybacks, this increased deprecation deduction may result in an immediate benefit to the taxpayer.

A real property trade or business that elected out of the interest limitations under section 163(j) is required to use the alternative depreciation system ("ADS") and cannot claim bonus depreciation. The ADS recovery period for QIP is now 20 years

If QIP was placed in service in 2018 and the 2019 return has not yet been filed, the taxpayer may correct the depreciation method with an amended return. Otherwise, an automatic accounting method change would need to be filed.

Other Disaster-Related Planning Considerations

Qualified Disaster Relief Payments

As a general rule, amounts provided by an employer to an employee are considered taxable compensation to the employee and a deductible business expense for the employer. However, when a federal "qualified disaster" has been declared, an employer may make "qualified disaster relief payments" ("QDRPs") to employees, and the assistance may be excluded from employee income under section 139 (while also being deductible to the employer). QDRPs can include reimbursements of certain reasonable and necessary expenses incurred as a result of a qualified disaster. For these purposes, a "qualified disaster" includes a disaster or emergency that the President has determined warrants assistance by the federal government, such as the coronavirus pandemic.

QDRPs do not include payments for expenses that are already being reimbursed by insurance (or otherwise) and generally do not include income replacement such as lost wages (see section 139(b)).

Qualified Disaster Losses

In addition to these emergency relief measures provided under the CARES Act, section 165(i) permits taxpayers to claim losses attributable to Presidentially declared disasters on the prior year's original or amended return. As such, a loss in 2020 can be claimed on the 2019 tax return.

Examples of such losses incurred in 2020 that may be treated as incurred in 2019 include, but are not limited to:

- Closure of store and facility locations
- Abandonment of leasehold improvements
- Permanent retirement of fixed assets
- Abandonment of pending business deals for which costs have been capitalized
- Disposal of inventory, supplies and other property that has become unsellable

CARES Act—cont.

- In certain circumstances, termination payments for executory supply or customer contracts, leases, or licenses
- Worthless securities (but not business bad debts)
- Impaired securities if the taxpayer uses the mark-to market method, and
- Loss from a sale or exchange of property.

The provision does not apply to ordinary and necessary deductible expenses under section 162(a), bad debts that are deductible under section 166, or net operating losses under section 172. Due to the requirement of a deductible loss under section 165(a), the provision only applies to the extent the taxpayer has remaining tax basis in an asset or capitalized intangible that can be written off.

With all of the above losses, it will be important to document causation (i.e., sufficient evidence that directly associates the loss with the COVID-19 disaster). Keep in mind, the amount of the loss could be affected by indemnification or insurance recovery.

The election to claim this loss must be made no later than six months after the original due date of the taxpayer's federal return for the year the loss is sustained (i.e., October 15, 2021, for calendar year taxpayers). Upon making the election, the taxpayer would be required to carryback all of its section 165 losses attributable to COVID-19. Revocation of the election can be made up to 90 days after the due date for making the election.

Estate Planning

For individuals whose assets may have temporarily declined in value due to the recent downturn in the markets caused by the COVID-19 disaster or otherwise, it may be an especially beneficial time to consider estate planning.

The availability of the enhanced lifetime exemption of $11.58 million had already made 2020 an ideal year to make gifts while minimizing exposure to federal transfer tax. Given the scheduled sunset of the doubled exemption at the end of 2025 and the possibility of a reduction in the exemption amount even earlier depending on the outcome of the 2020 elections, individuals were encouraged to consider using this benefit in the near term before it was lost.

Now, to the extent a taxpayer's assets may be somewhat undervalued, and in light of the extremely low-interest rate environment, the impetus for making gifts and establishing trusts is even greater. Transferring assets today, when they are lower in value than they are anticipated to be in the future, rather than holding those assets until death, can minimize estate and gift tax liability; this is because all future income and appreciation attributable to the transferred assets is removed from the taxable estate. In addition, interest rates are at historic lows. This is important because the success of a number of estate planning strategies (e.g., Sales to Intentionally Defective Grantor Trusts, Charitable Lead Annuity Trusts, Grantor Retained Annuity Trusts) depends on the performance of the gifted assets exceeding a specified interest rate benchmark. Thus, the current lower interest rates help maximize the amount of wealth an individual can transfer to younger generations without exposure to transfer tax.

Roth IRA Conversion

Given the fact that some investments may have declined in value as a result of COVID-19 and recent economic news, an individual taxpayer may want to consider converting a traditional individual retirement account ("IRA") into a Roth IRA. A conversion results in current taxation of any earnings/appreciation as ordinary income. A taxpayer may convert a portion or all of one or multiple accounts, but only a pro rata portion of the basis may be attributed to the amount converted and reduce taxable income accordingly. Thereafter, any earnings/appreciation in a Roth IRA can be distributed tax-free, and a Roth IRA is not subject to required minimum distributions as with a traditional IRA.

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Using a CRT to Outstretch the SECURE Act

Dean A. Mioli, CPA, CFP, CIMA, CLU

The SECURE Act brings new challenges and new planning opportunities. Under the SECURE Act, qualified plans (i.e. 401(k), 403(b), etc.) and individual retirement account benefits generally have to be distributed within 10 years after the year of the IRA owner's death. The one question we keep hearing, "How do I get the stretch back on IRA inherited assets?" That is the question we plan to tackle with a tried and true financial planning vehicle, the Charitable Remainder Trust (CRT). Let's review the basics of a CRT.

A CRT is an estate and gift tax exempt, irrevocable trust vehicle with "split interest" properties (1):

- There is an Income Interest held by a person or persons; and
- A Remainder Interest held by a charity or charities.

There are two main types of CRTs:

1) Charitable Remainder Annuity Trust (CRAT) (2) – The income beneficiaries receive a stated amount per year, $50,000 for example, of the initial trust assets and the amount will not change.

2) Charitable Remainder Unitrust Trust (CRUT) (3) – The income beneficiaries receive a stated percentage, 5% for example, of the trust's asset each year.

This article focuses on the Charitable Remainder Unitrust which is the more flexible of the two options for planning purposes. I will use CRT and CRUT interchangeably as the discussion continues.

For clients looking to enhance wealth transfer, a CRT can provide tax deferral which is very powerful. Other CRT benefits include, tax bracket management within the family, fulfill charitable goals, convert ordinary income to tax favored income (long term gains and qualifying dividends) and manage state income taxes.

Leaving retirement assets to a CRT can provide cash distributions to children for a period greater than 10 years (the normal payout period for designated beneficiaries). On the other-hand, inheriting a large IRA ($1M) with only the ability to spread income over 10 years could potentially vault a single beneficiary from the 24% tax bracket into the 35% tax bracket. Also the additional income opens up the door to the Medicare Surtax of 3.8% on net investment income. Note: IRA distributions are not subject to the 3.8% Medicare Surtax but will increase adjusted gross income (AGI).

Other CRT features and benefits include:

- The donor will generally NOT realize gain or loss if and when the transferred assets are subsequently sold by the CRT Trustee
- The CRT lasts a term of years or life/lifetimes
- Flexible payout potential
- Can function like a spendthrift trust
- Principal protection
- Reduce or eliminate estate taxes

If an IRA owner leaves their IRA to a CRT at death, will that be a taxable event? The answer is no, based on PLR199901023. Also, there is no taxable income to the beneficiaries until they receive distributions from the CRT.

For a standard CRUT the minimum payout is 5% and the maximum payout cannot exceed 50% (4). Using a term of years, the maximum term is 20 years. The actuarial value of the charity's remainder interest must be worth at least 10% of the value of the trust as of the funding date.

The CRT functions like a "see through" trust to the income beneficiaries, "Pre-SECURE Act". A CRT can have the payout based on the life expectancy of the beneficiaries. I was able to verify that a CRUT with a 5% payout and two income beneficiaries (a male and a female, age 39) passed the 10% remainder test (5).

At the 1.2% Section 7520 rate (6), it's not possible to create a CRUT for the life of a beneficiary under age 27. However, an IRA owner could create a 20-year CRUT with the highest permissible payout (10.98% payable annually) for a beneficiary regardless of age.

Using a term of years CRUT is one way to get around having beneficiary age issues, another way would be to consider multiple CRUTs when there are multiple beneficiaries of varying age. A CRT may not be advisable as the IRA beneficiary, if the CRT beneficiary has health issues or of advanced age.

On the next page is a CRT illustration. Here the IRA owner (Donor) at death leaves some or all of their IRA to the CRT. In this case the income beneficiaries are the children but the surviving spouse could be a beneficiary too. At the end of term (up to twenty years) or lives, anything left in trust would go to charity.

Charitable Remainder Trust (CRT)

Let's now cover CRT distributions, which have particular ordering rules.

Trust Distributions – Four Tier System

- The character of income received by the recipient is subject to and controlled by the tier rules of IRC 664(b). Worst in First out (WIFO)
  - First, distributions are taxed as ordinary income (current and accumulated)
  - Second, distributions are taxed as capital gains (current and accumulated)
  - Third, distributions are taxed as tax-exempt income (current and accumulated)
  - Finally, distributions are assumed to be the non-taxable return of principal
- Because of the above income tax rules, it is not possible for a donor/grantor, to simply convert ordinary income into capital gain or

CRT—cont.

tax exempt income [7].

- Funding a CRUT with IRA assets, the CRUT is going to be paying out ordinary income potentially for many years. Equities would certainly be appropriate in the CRT asset allocation with a 20 year time horizon or greater. As time goes by there will be an opportunity to exhaust the Tier 1. Once that happens, distributions can move to Tier 2, long gains and qualifying dividends, accordingly tax favored income will be paid out of the trust. What we are doing here is spinning straw into gold but that is going to take time.

- Distributions from the CRT to the income beneficiary usually represent taxable income. Tax information is reported on Form K-1.

CRT Income Tax Deduction -
Funding a CRT generates a charitable deduction,

- In this case, the estate (normally the donor/grantor) can claim an income tax deduction equal to the present value of the charity's future remainder interest.

- The charitable income tax deduction for a gift to a CRT is subject to the same percentage limitations and carryforward rules as an outright gift. Five year carryforward limit on charitable deductions.

Setting up a CRT one needs to consider the following:

- Is the owner charitably inclined? I believe some charitable intent is necessary.
- What CRT structure should be selected, CRUT, NIMCRUT or CRAT.
- How long? Should a term of years be selected or life?
- Choosing a Trustee – consider a corporate trustee
- What are the trust administration costs and does that include trust tax preparation (Form 5227)?
- Choosing a Charity – consider a donor advised fund
- How much to leave to a CRT? Does a CRT make sense for less than $250k? $500k?
- An attorney will be needed to draft the CRT document
- Consideration should be given that the document drafting should take place while the IRA owner is alive. The CRT can lie dormant until funded with IRA assets.

Other Options

The children could be the outright beneficiaries of the IRA. As beneficiaries, the children can take voluntary distributions for the first nine years after the year of death of the owner and take the final required minimum distribution in year ten. Managing the income tax bill could present some problems especially with a large IRA. Also, amounts distributed into the beneficiaries' estates exposes them to the beneficiaries' creditors and predators. For smaller IRA balances, leaving the IRA directly to the beneficiaries probably makes sense.

IRA owners, while living and married, could take advantage of what I would consider very favorable tax brackets and do Roth conversions. For a married couple filing jointly, the 24% income tax bracket tops out at $326,600 for tax year 2020. An IRA beneficiary inheriting a Roth IRA could wait until the final year before taking the RMD and enjoy ten years of tax free growth.

An accumulation trust is another option as an IRA beneficiary. An accumulation trust has flexibility on trust distributions where a CRT does not. An accumulation trust is a taxable trust. RMDs and income not distributed to the beneficiaries will be taxed at very compressed trust tax rates.

Concerns & Issues

Best to avoid problematic assets in a CRT like partnership interests and debt encumbered real estate. Also naming a private foundation as the charitable beneficiary would be a violation of the self-dealing rules.

There are factors which we will not know, like how long a beneficiary will live, what the Section 7520 rate will be when the CRT is funded and what the future tax rates will be. It's important to be cognizant of the unknowns and account for them as best you can in the planning.

Two states Pennsylvania and New Jersey don't exempt CRTs from state income tax purposes. New Jersey and Pennsylvania state income taxes are not based on federal income tax. A knowledgeable estate attorney can guide clients on how to set up a CRT to avoid NJ and PA income tax.

Summary

The potential for increased future income tax rates seems to be growing every day. For families looking to enhance wealth transfer and provide a vehicle to maximize tax deferral a CRT is definitely worth a look. Also other potential problems can be minimized like beneficiary overspending, divorce, lawsuits and poor investments. Some level of charitable intent should be present and the trust can be used as a teaching vehicle for the family.

"Planning is bringing the future into the present so that you can do something about it now" – Alan Lakein

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Endnotes:

1. Section 664(c)(1)

2. IRC Sections 664(d)(1)(A) and 664(d)(2)(A).

3. Section 664(d)(1).

4. Section 664(d)(2).

5. Per Crescendo Interactive Software version 2020.1. I used the April Section 7520 rate of 1.2%. The beneficiaries had a joint life expectancy (JLE) of 57.3 years

6.To review historical Section 7520 rates, here is a link: http://leimberg.com/freeResources/keyRates.html Secure Act - H.R. 1865 (116th Cong., 1st Sess.), P.L. 116-94

7. Treas. Regs. Section 1.664-1(d)(1)(b).

Long Term Care Planning

Michael C. DeFillipo, CLU, ChFC

A critical aspect of the financial planning process for long term care is determining how to allocate resources for what may be a significant future cost. According to the 2019 U.S Department of Health and Human Services (05/08/2019), nearly 70% of individuals over the age of 65 will require some type of long-term care during their lifetime. The average duration of care is 3 years, with 18% of all seniors requiring more than one year in a nursing home[1].

The Pennsylvania Health Care Association estimates that annual spending on long term care in the United States (excluding unpaid family care) has reached nearly $275 billion. Generally, health insurance does not cover these expenses, nor does Medicare (unless certain requirements are met through Medicare Part A for hospital service); Medicaid may provide some coverage, but only for individuals with very small countable assets. Roughly 23% of that $275 billion - $63 billion – is paid out-of-pocket.

For insurance purposes, Long Term Care (LTC) is defined as the loss of 2 of the 6 of the Activities of Daily Living (ADL) or cognitive impairment that requires substantial supervision. The ADLs are defined as:

• "Bathing" – washing oneself in either a tub or shower, including getting into and out of the tub or shower, or by sponge bath.

• "Continence" – ability to control one's bowel and/or bladder function, or the ability to perform associated personal hygiene (including caring for a catheter or colostomy bag) when unable to control one's bowel and/or bladder function.

• "Dressing" – putting on and taking off all items of clothing, and attaching any necessary braces, fasteners, or prosthesis.

•"Eating" – feeding oneself by getting food into the body from a receptacle (such as a plate, cup or table) or by a feeding tube or intravenously.

• "Toileting" – getting to and from the toilet, getting on and off the toilet, and performing associated personal hygiene.

• "Transferring" – means moving in and out of a bed, chair, or wheelchair.

The original form of protecting against long term care needs was self-insuring, either through portfolio assets or from the family structure. Over time, increased cost of care and the separation of generations within families put increased pressure on liquid assets to cover the cost of care until governmental programs become available. In addition, as we have seen with recent market events surrounding COVID-19, market fluctuations can force liquidation of assets at depressed valuations.

The individual LTC insurance marketplace started in the late 1970's and ramped up significantly in the late 1980's and early 1990's. The timing in the spike of traditional LTC policies coincided with a widening spread in the difference between the Medical Care CPI and Core CPI annual increase. Combined with the improvement in life expectancy – particularly in the mass affluent and affluent segment of the population, those who bought the insurance product – put pressure on these contracts. The impact of the early stage mispricing began to filter through to consumers in the late 1990's and early 2000's, as these policies were structured with non-guaranteed annual premiums. It was common to see annual price increases in excess of 30% in order to maintain coverage to support the liabilities of issuing companies.

In 1987, Lincoln Financial Group launched the first "hybrid" product, MoneyGuard. MoneyGuard is designed as a Modified Endowment Contract (MEC) universal life insurance policy with an LTC rider component build in. Though it is a life insurance policy, the policy is structured to provide long term care benefits, through a 2-year benefit period that can be increased through additional riders, much greater than the stated death benefit.

Unlike the previous traditional "stand alone" LTC insurance policies, the hybrid product provides a death benefit – the minimum amount allowable, but still something should the insured have the good fortune of living a long and healthy life and not needed. In addition, there is an equity component which, depending upon the desired tradeoff of lessening the potential LTC benefit, can be a full return of premium after the 10th policy year.

Since the innovation by Lincoln, several insurance carriers have replicated the hybrid product, including but not limited to Nationwide, Pacific Life, and Securian. OneAmerica adapted the universal life design to a Whole Life chassis. Each carrier added their own product differentiation, whether it be the difference between reimbursement or indemnity, the ability to extend a benefit period for lifetime and adding additional premium duration options (though the most common funding scenarios are single or 10-pays). The policies are guaranteed and fully paid once the original premium design is satisfied.

Underwriting is generally "pass / fail" based upon a personal health history interview and prescription check – some providers will offer various underwriting classes and may collect medical records for approval. For these policies, the focus is on morbidity rather than mortality.

The next phase of evolution in the LTC marketplace has been the proliferation of either Long Term Care or Chronic Illness Accelerated Benefit (CIAB) riders onto permanent insurance policies. Whereas the hybrid product is LTC first, the life insurance strate-

Long Term Care Planning—cont.

gy is primarily death benefit focused with the ability to accelerate the death benefit for long term care needs. In our firm, we've begun to refer to this the "Bucket of Money" strategy … the death and potential long term care benefit come from the same source, either dollar-for-dollar or pro-rata depending upon the carrier and type of rider.

In general, the significant difference between the LTC and CIAB rider – from a product and positioning standpoint, not in terms of licensing or under which section of the Code allows for the benefits to be received income-tax free – is the type of underwriting at application and cost. True LTC riders are built into the scheduled premium and include morbidity underwriting along with traditional mortality underwriting. It is possible to have separate underwriting classes for the base life insurance policy and the rider – in our practice, we had an individual qualify for the best available life insurance rating but be denied the LTC rider due to a history of arthritis and orthopedic surgery.

In most cases, CIAB rider is not underwritten at the time of application and is not incorporated into the premium schedule. (As you can see, this is a good way to get some form of coverage for that individual with physical injury history which does not impact life expectancy.) In the event the rider is activated, there is a reduction of death benefit in the amount of claim, interest and mortality factors. Based on non-empirical observation, that total amount of death benefit that can be accelerated is 70-80% when the rider is used for insureds between Age 80-90.

Whether using the LTC or CIAB rider, we encourage our clients to seek guidance from their tax advisor on the potential income and gift tax consequences of using the rider for a policy owned by an Irrevocable Life Insurance Trust. Since the benefit is paid to the owner, in this case the Trust, based upon the condition of the insured, the challenge is to determine how the benefit goes from the Trust to insured, who is generally the Grantor. One solution is to determine whether or not an existing Trust contains language that enables the Grantor/Insured to access trust assets through a series of demand loans that are secured by property pledged by the Grantor/Insured, with interest payable at a fair market rate. In addition, there is a lack of guidance as to whether having a rider (elective or not) on a life insurance policy owned by an ILIT insuring the life of the Grantor could be deemed an implied agreement between the trust and the Grantor that he or she has retained a beneficial interest under Internal Revenue Code § 2036 (a), regardless of whether the rider benefits are activated prior to death. As a matter of current best practice, we advise holding policies with LTC riders outside of the Trust.

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1. Pennsylvania Health Care Association https://www.phca.org/for-consumers/research-data/long-term-and-post-acute-care-trends-and-statistics

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7/23/2020	Webinar - Status of Probate and the Orphans' Courts	Bernard J. McLafferty, Jr., Esquire
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9/21/2020	Drafting Substance Abuse Trusts	Martin Hagan
10/26/2020	The Secondary Market for Life Insurance; Current Trends and New Applications	Jack Elder; Coventry
11/23/2020	Using LinkedIn and Social Media Effectively in your Practice	Brynne Tillman
1/25/2021	2021 Economic/Market Update	Ed Boehne; Haverford Trust
2/22/2021	Heckerling Update	Richard Greenberg

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