



Estates and Trust Tax Planning Overview

December 5, 2023
2023 Federal/State Tax Institute

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Key Take-Aways

- > Planning for smaller (non-taxable) estates is crucial
 - > Everyone should have basic documents
- > Focus shifts from estate tax planning to income tax planning
- > It is not just how much you leave your heirs; it is also the character of assets that you pass along to them
- > Portability is a game-changer
- > Use of elections can save \$\$\$



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Taxpayers are Re-Thinking the Need for Planning

- > Fewer are subject to the Federal Estate Tax since the exemption is so high (\$12,920,000 in 2023)
- > Many states follow the Federal rules, thus eliminating any state death tax

However, . . .

- > Non-taxable estates today may become taxable in the future
 - > Assets grow (naturally or by inheritance)
 - > Laws change
 - > Some people actually win the lottery!
- > As time passes and life events occur, most estate plans become out of date



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Excuses We Hear Why Clients Don't Think They Need To Plan

- > If there are no taxes due, what is the need for planning?
- > I'm too young
- > All of my property is jointly held with my spouse
- > Estate planning is only for the wealthy taxpayers
- > It's too expensive (cost v. value)
- > We had our wills drawn up when we were married (probably more than 15 or 20 years ago!)
- > I don't want to think about "it"



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Reasons Why Estate Planning is Critical for the Modest Estate Owner

- > Several states have estate exclusions well below the Federal level
- > Several states (i.e., PA) impose a state inheritance tax
- > Need to provide for surviving spouse
- > Special needs family member
- > Care for minor children
- > Second (or third, or fourth) marriage
- > Asset protection (predators and spend thrifts)
- > Divorce planning
- > Life insurance planning
- > Recent changes in law
- > Planning for IRAs and employer plan benefits
- > Roth conversion opportunities



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Reasons Why Estate Planning is Critical for the Modest Estate Owner – Continued

- > Closely held business/farming operations
- > Use of discounts
- > Hard to value assets
- > Provide for future education needs
- > Planned charitable giving
- > Family dynamics (alcohol and drug addiction)
- > Disposition of tangible personal property
- > Dictate how YOU want to dispose of your estate
- > Planning for pets
- > Long-term care planning
- > Medicaid planning



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Basic Estates Planning Documents

- > Will
- > Durable Power of Attorney
- > Advance Medical Directive
- > Revocable Trusts (Living Trusts)
 - > Depends on individual situation and state probate laws
 - > When owning out-of-state real estate
 - > Provides privacy
- > Other trusts to accomplish specific goals
 - > Special needs
 - > Asset protection

Everyone ages 18 and over should have these basic documents



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Beneficiary Designations

- > Applicable to
 - > IRAs, Roth IRAs
 - > Employer plans
 - > Life Insurance
 - > Annuities
 - > Bank and brokerage accounts
- > Review and update as needed
 - > Birth
 - > Death
 - > Divorce
 - > Marriage
 - > Other



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IRC Section 2010(c)(4) – “Portability”

Deceased Spousal Unused Exclusion (DSUE) amount

- > TRA 2010 – for decedents dying on or after January 1, 2011
- > Estate and gift tax exclusions were reunited (“use it now” or “use it later”)
- > “Portability” became permanent with the 2012 Tax Act
- > Final regulation became effective on June 12, 2015



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Portability Election

- > The election is made on a timely and complete 706 showing DSUE and there is a surviving spouse
- > Election is made by the executor (Form 706, Part 6)
- > Not available to a non-resident surviving spouse who is not a U.S. citizen, except to the extent allowable by treaty with his or her country



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Estate Tax vs. Income Tax Planning

- > Highest Estate Tax Rate is 40%
- > Highest Marginal Personal Income Tax Rate is 37%
 - > 3.8% surtax
 - > State income tax
- > Since most taxpayers will not be subject to the estate tax, more focus needs to be on the income tax aspects
- > Planning on an asset-by-asset basis
 - > "BASIS" planning is the new normal
 - > Best assets to have in your estate (i.e., Roth IRA, tax-exempt bonds)
 - > Worse assets to have in your estate (i.e., traditional IRA, E/EE Bonds)
- > Need to consider the tax implications to the beneficiaries
- > May drive which assets to spend down first



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1041 Income Taxation

- > Income
 - > Interest, dividends, capital gains and loss, rents, royalties, & partnership income, business income, ordinary gain, farm income, and other income
- > Deductions
 - > Interest expense, taxes (\$10,000 cap), fiduciary fees, charitable deductions, attorney and accountants, and other deductions
- > Extremely compressed tax brackets in comparison to individuals
- > Consideration for annual distributions
 - > Does trust agreement allow for distributions?
 - > Does it fit in with the beneficiary's estate planning?
 - > Does the beneficiary have creditor issues to worry about?
 - > Will the income taxes be less?
- > State income tax residence



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Fiduciary Tax Elections

- > Taxable year of the estate
- > Section 645 election to treat revocable trust part of the estate
- > Deducting administrative expenses on fiduciary tax return
- > Disclaimers
- > Section 643(g) allocation of estimated taxes to beneficiaries
- > Treatment of charitable donations made in subsequent year
- > Recognition of gain upon distribution of in-kind assets



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Creating or Terminating a Fiduciary Relationship

- > Use Form 56 to create or terminate the fiduciary relationship (Section 6903)
- > Notifies IRS of Trustee/Executor's address
- > Avoid notices being sent to incorrect address and missing statutory response dates
- > Form 56 vs. Form 8822-B



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Administrative Elections

- > Use Form 4810 to request a prompt assessment of the decedent's income tax and gift tax liability (Section 6501(d))
 - > Filed by the executor or administrator
 - > Filed within 3-year statute of limitations
 - > Filed after Forms 1040 and 709 are filed
 - > IRS assessment of tax or court proceeding must be made within 18 months after filing of form
- > Use Form 5495 to request discharge of executor from personal liability of decedent's income and gift taxes (Section 6905)
 - > Filed after Forms 1040 and 709 are filed
 - > Upon payment of taxes as notified by IRS, or, if no notice within 9 months of filing, executor is discharged from personal liability



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Partnerships

- > Section 754 election allows step-up in basis to be assigned to assets inside of partnership
- > Section 732(d) election alternative to be made by estate



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Estate & Trust as Shareholder of S Corporation

- > General Rules
 - > Estate can own S Corporate stock indefinitely
 - > Only certain trusts can own S Corp stock
 - > Testamentary trust can only own S Corp stock for 2-years
 - > Exception – QSST and ESBT
- > Estate is the owner, not the beneficiaries
 - > Beneficiaries, if otherwise ineligible shareholders, do not negate S status



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Qualified Subchapter S Trust (QSST)

- > Requirements
 - > Trust can only (and is required to) distribute all income annually to only one (1) beneficiary, who must be a U.S. citizen or resident
 - > Only the income beneficiary can receive principal distributions
 - > The income beneficiary's interest must terminate upon the earlier of the death of the income beneficiary or the termination of the trust
 - > Upon termination, all trust assets go to the income beneficiary
 - > The income beneficiary must elect to be treated as the owner of that portion of the trust consisting of the S Corporation stock
 - > QSST status terminates at the time any of the above requirements are not satisfied

Section 1361(d)



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QSST Election Made By The Income Beneficiary

- > Separate election required for each S Corporation owned by the trust
- > Generally, the election must be made within 2 ½ months after the S Corporate stock is transferred to the trust or from the time the S election is made
- > The election is irrevocable
- > Covers successive beneficiaries unless they affirmatively refuse to the consent within 2 ½ months of becoming an income beneficiary



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Electing Small Business Trust

- > Can have an estate as a beneficiary
- > Election made by trustee within 2½ months of the later of the S stock being transferred to the trust or the beginning of the first tax year which the S election is effective (Reg. 1.1361-1(m)(2))



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Qualified Beneficiaries of an ESBT

- > TCJA allows a nonresident alien individual to be a potential current beneficiary of an ESBT (in addition to resident individuals, estates, and certain charitable organizations)



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Thank You!

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