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WEBINAR

Tax-Saving Opportunities: *Mastering IRS Form 706*

WELCOME

Today’s Presenters

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Agenda

- Filing Requirements
- Understanding IRS Form 706
- Portability Election
- Strategies for Wealth Preservation
- Collaborations for Client Success
- Q&A

Filing Requirements

When is a 706 required and timeline for filing?

- For 2023, if the Decedent's *gross* assets plus lifetime gifts exceed $12,920,000 (for 2024 that amount is $13,610,000) an Estate form 706 is required
- For Decedent's with Gross estates under filing threshold leaving surviving spouse, a return may be filed to port/transfer the first to die's unused exemption to surviving spouse.
- Form 706 is due 9 months after the Decedent's death (may request a 6-month extension)
  - Key Takeaway: effective as of 1/1/2026 the lifetime exemption is reduced due to the "sunset" of the current law. Reversion back to $5,000,000 (adjusted for inflation)
  - Same due dates for Required and Portability filings generally.

State Estate Tax Filings

When to consider states?

- Married couples who reside in a state with an estate or inheritance tax or both
    - CT, HI, IL, IA, KY, ME, MD, MA, MN, NE, NJ, NY, OR, PA, RI, VT, WA and the District of Columbia
    - Key Takeaway: often potential State estate or inheritance taxes are overlooked. These taxes may apply if a taxpayer is domiciled in any of these states OR owns property in any of these states.
        - A tax may be assessed even up the first spouse to die, due to differences between Federal and State laws

Using qualified professional with the necessary expertise

Who prepares form 706?

- Generally, accountants and attorneys
- Form 706 is a unique form with a high audit rate (unlike an income tax filing)
- Executor/Personal Representative is personally liable for the estate taxes due, which can be significant
- Therefore, it's critically important to engage professionals with the necessary expertise and experience
- As accountants/consultants we are uniquely qualified to prepare all returns and assist with administration after someone dies:
    - Beginning with the 1040, to the 706, the post-death estate/trust form 1041 income tax returns through the distribution assets and funding of any trusts.
- Most importantly though this is a collaborative effort bringing together all of the client's advisors (attorney, financial advisor, banker, insurance agents etc.)

Filing Requirements

What assets are included in the Estate?

- In general, what determines ownership by a Decedent?
  - Individually owned, Separate property, Revocable Living Trust
  - Jointly owned property
  - Joint Revocable Living Trust
  - Community property
    - Key takeaway: if move from Community Property state may be able to retain the full "step-up" in basis upon the first spouse's death
  - Life insurance – did the Decedent at death have "incidents of ownership"
- Example of other assets included in the estate
  - Marital trust in which a prior QTIP election (Qualified Terminable Interest Property) was made – i.e. a trust setup for the benefit of the surviving spouse of which a marital deduction was taken to defer estate taxes until the death of the surviving spouse

Filing Requirements

What are some assets excluded from the Estate or reduce Estate taxes due?

- Certain qualified Irrevocable Trusts
  - Intentionally Defective Grantor trusts (IDGT's)
  - Irrevocable Life Insurance trusts (ILIT's)
  - Trust setup by someone other than the Decedent of which they only hold a beneficial interest
- Assets distributed to qualified charities
  - Planning Point: If a client has charitable intentions, consider taking advantage of the up to 100k per year direct from Traditional IRA to charity for those over age 70 ½ and for post-death charitable bequests, again the Traditional IRA is likely the most tax advantageous asset to use since IRA's do NOT receive a "step-up" in basis and could be subject to total taxes in excess of 80%

Audit of form 706

Form 706 scrutiny and IRS audit rate

- Every form 706 is hand reviewed by an attorney in the IRS Estate/Gift division
- General statute of limitations is 3 years from the original due date or when filed
- Per a recent IRS data book:
  - Overall audit rate for form 706 is about 7%
  - Taxable Estates, especially those with hard-to-value assets have a much higher audit rate
  - Estates larger than $10M are audited at about a 22% rate
  - Estates greater than $100M with hard-to-value assets are likely audited at a rate of 50% or more
- Generally do not find out whether an estate is being audited for 12-18 months after filing
- Can request a Closing Letter for $67

Understanding IRS Form 706

IRS Form 706 poses several complexities that often lead to common errors. These include, but are not limited to:

1) **Properly accounting for all gifts made during life:** A very common area in which there are estate/gift/generation-skipping tax issues are unreported gifts and incorrectly filed gift tax returns. Particularly Generation-Skipping Tax issues and elections.

   Key takeaway: Prior to death, have a qualified professional review all previously filed gift tax returns and address all potential issues, unreported gifts and any late elections needed. Much better to address pre-death and could save significant taxes

2) **Incorrect Valuation of Assets**: One of the most common mistakes is the misvaluation of the estate's assets. It's crucial to obtain accurate appraisals to avoid potential penalties.
3) **Missing Documentation**: Failing to provide necessary documentation can lead to issues and delays.
4) **Failure to Include All Assets**: All global assets must be included on Form 706, not just those in the US. Overlooking foreign assets is a common error.
5) **Incorrect Tax Calculations**: Errors in tax calculations can lead to significant discrepancies. It's highly recommended to use a qualified tax professional with the necessary expertise to prepare form 706 and all related calculations.
6) **Late Filing**: IRS Form 706 must be filed within nine months of death, with a six-month extension available. Missing these deadlines can result in penalties and interest.

Portability election

What are the basics of a Portability election?

- 2010 and prior if a Decedent had not used their lifetime exemption (during life or upon their death), any unused lifetime exemption was permanently "lost".
- Beginning 1/1/2011 an Executor or Trustee may make a "Portability" election for the Decedent to port/transfer to the surviving spouse the amount of any unused lifetime exemption
  - Key takeaway: Benefit is to the estate of the surviving spouse. Should be considered at the first death, looking at estate to be included in survivor's estate.
- If the surviving spouse remarries, the surviving spouse keeps the DSUE transferred from the deceased (first) spouse.

Portability - timing of the election

When must a Portability election be made?

- The election is made by filing form 706 and making the Portability election on a timely filed return (9 months after death or 15 months after death if a valid extension is filed)
    - For late filed returns, in *which the 706 is filed* *solely* *for making the Portability election,* form 706 may be filed *up to 5 years after the date of the Decedent's death. Top of return should include the following " filed pursuant to* Rev. *Proc. 2022-32 to elect portability under § 2010(c)(5)(A)"*
- Planning Point: when working with blended families and second marriages, you may need to address who pays for the preparation of form 706 as those benefitting from the election may not be those responsible for making the election. in some instances, provisions should be included in their Will and Revocable Living Trust.
    - For example, client with a taxable estate remarries after their first spouse dies. The second spouse also predeceases them and has assets of 1M. The second spouse named their child as executor. There is no form 706 required and the child of the second spouse may not want to pay for a 706 to be prepared.

Portability election

When should a Portability election be considered?

- Married couples with combined estate of more than $14,000,000 (or possibly less depending on your thoughts regarding the future of estate taxes)
  - Due to the "sunset" of the current law on 1/1/2026 married couples will only be able to shelter approximately $14M vs. $28M
  - A future administration may also reduce the current lifetime exemption
- Married couples primarily with assets that are not conducive to funding a credit shelter trust
  - For example, retirement plans (IRA's, 401(k)'s, 401(b)'s etc.), primary residence, annuities, deferred compensation etc.

Obvious Benefits of Portability election

- Obvious benefit of making the Portability election:
  - Estate/Gift tax savings - Avoids loss of the lifetime exemption of the first spouse to die
    - This benefit can be significant as every dollar of additional lifetime exemption saves estate taxes at a 40% rate!
    - Thus, every $1,000,000 of portability exemption saves $400,000 in estate taxes!
  - Income tax savings – applies to assets eligible for a "step-up" in basis that are included in the Surviving Spouse's Estate vs. Funding a Credit Shelter Trust
    - This eliminate the applicable taxes on the appreciation in value from the first spouse's death to the second's spouse death
    - Examples of eligible assets are: real estate, stocks, partnership interests and other non-tax deferred investments

Benefits of the Portability election

Not So Obvious Benefits of Portability election

- <u>Not so obvious benefits of making the Portability election:</u>
  - Peace of mind for the Surviving Spouse (this should not be underestimated/undervalued)
    - The portability of the lifetime exemption, for some clients, takes estate taxes off the table and the surviving spouse doesn't have to worry or talk about it again
    - For other clients, it allows for more flexible estate plans and the ability to transfer more wealth during life
    - In general, the Surviving Spouse benefits from a less complex estate plan

Benefits of the Portability election

Not So Obvious Benefits of Portability election

- Not so obvious benefits of making the Portability election:
  - Future costs saved/avoided:
    - Accounting and legal fees that would be necessary to continue to engage in discussions about estate taxes and planning to avoid them
    - If applicable, saves the annual compliance costs of filing a Credit Shelter Trust income tax return
- *Key Takeaway: Making the Portability election and filing form 706 is the equivalent of purchasing an "insurance policy" to cover Estate taxes. It's a small price to pay for significant benefits.*

Tools to assist with analyzing whether to make a Portability election

State of the Estate analysis

- Initial Questionnaire – this is to gather an initial understanding of what's important to you and what you want to accomplish with your estate plan
- Estate/Trust Summary
  - This compiles a concise list of all assets and liabilities and what is "in" and "out" of the Estate in order to determine any projected Estate tax and what assets will get an adjustment to basis at death
  - Review of titling of all assets, all beneficiary designations (retirement accounts, life ins etc.), review the "health" of life insurance policies, annuities etc.

Tools to assist with analyzing whether to make a Portability election

State of the Estate analysis

- Diagram of legal documents – this provides a "picture" of what your current documents say:
  - Last Will and Testament and any Codicils along with Durable Power of Attorney and Health Care Directive
  - Revocable Living Trust and any Amendments
  - Other Irrevocable Trusts
  - LLC/Partnership agreements
  - Stockholder's agreement, Buy/Sell agreement
  - Other pertinent legal documents
- List of follow up's and recommendations

Exploring The Various Tax-Saving Strategies Related to IRS Form 706

Tax-Saving Strategies

Marital Deduction: This is a tax deduction that allows the gross value of an estate to be reduced by the amount of its bequest to the surviving spouse, effectively reducing the taxable estate.

Unified Credit: This credit encompasses the lifetime gift tax exemption and the estate tax exemption, allowing a significant amount of wealth to be transferred tax-free.

Alternate Valuation Date: If elected, this allows the estate to be valued six months after death, which will result in lower estate taxes if both the estate's value and estate tax have decreased.

Special Use Valuation: This provision can allow for lower estate taxes for family farms and businesses by valuing them based on their actual use rather than their highest and best use.

Qualified Disclaimer: Allows for assets to pass to heirs without further tax consequences. May be used post-mortem to more efficiently transfer assets and/or accomplish goals. Generally, must be executed within 9 months of date.

Building Stronger Relationships with Clients

Collaboration and Communication are the Keys

Open Communication: Maintaining an open line of communication with your clients is crucial. It ensures that you stay updated on any changes to their financial situation and can adjust strategies as needed.

Understanding Client Goals: Every client has unique financial goals. Understanding these goals allows you to tailor your advice and strategies to their specific needs.

Utilize Technology: Technology can greatly enhance client collaboration. Using secure platforms to share documents and data not only improves efficiency but also transparency.

Regular Updates: Regularly updating clients on the progress of their estate planning keeps them engaged and contributes to a more trusting relationship.

Encourage Questions: Encourage your clients to ask questions. This not only helps them to better understand the process but also allows you to address any concerns or issues that may arise.

Personalized Approach: Remember that one-size-fits-all does not apply in estate planning. Always adopt a personalized approach to meet the unique needs of your clients.

Q&A

Thank you for attending

Additional Questions?

Reach out to us at

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