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**Steve Leimberg's Estate Planning Email Newsletter - Archive Message #2467**

**Date:** 19-Oct-16
**From:** Steve Leimberg's Estate Planning Newsletter
**Subject:** Martin M. Shenkman, Richard Greenberg & Glenn Henkel: The New Jersey Estate Tax Has Been Repealed, What's Next?

On October 14th, New Jersey Governor Chris Christie signed legislation raising the state's gas tax by 23 cents per gallon, from the 49th highest in the nation to the sixth, to help replenish the state's expired transportation trust fund. As a trade off, the bill will lower the New Jersey sales tax but will also phase out the estate tax on January 1, 2018. Now, **Martin M. Shenkman**, **Richard Greenberg** and **Glenn Henkel** provide members with their analysis of this important development.

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**Richard H. Greenberg** is Senior Partner of **Greenberg & Schulman**, Attorneys at Law in Woodbridge, New Jersey, where he focuses on estate planning and estate administration, tax matters and business and corporate matters. A Fellow of the American College of Trust and Estate Counsel (ACTEC), Mr. Greenberg is the Former Chair of the Taxation Law Section of the New Jersey State Bar Association, the Former Chair of the Board of Consultors of the Real Property, Trust and Estate Law Section, Co-Chair of the Estate and Gift Tax Committee of the Taxation Law Section, a member and former Chair of the Corporate Tax Committee and a member of its Inheritance Tax and Partnership Tax Committees. He is the former President of the Tri-County Estate Planning Council and member and Former Chair of the Essex County Bar Association Tax Committee, a member of the New York State Bar Association and its Tax, Trusts and Probate Committees, the Estate Planning Council of Central New Jersey and the Tax Committee of the Middlesex County Bar Association. Named as one of New Jersey's Top 100 Lawyers, he is a frequent lecturer and author on numerous estate planning and estate administration topics. Mr. Greenberg received his B.B.A. from Case Western Reserve University, his J.D. from St. John's University and his LL.M. in Taxation from New York University.

**Glenn A. Henkel, JD, LLM (tax), CPA, AEP,** is a shareholder in the Haddonfield New Jersey tax and estate planning firm, Kulzer and DiPadova. Mr. Henkel is a Fellow of the American College of Trust and Estate Counsel and is on the Board of Directors of the Philadelphia Estate Planning Council. He is a Past Chair of the Real Property, Trust and Estate Law Section and Taxation Section of the New Jersey State Bar Association. Mr. Henkel is the author of New Jersey Estate Planning Manual: Theory, Practice & Forms – 2007 (with Steven K. Mignogna and Gerard G. Brew). He was an editor and a contributing author and editor of New Jersey Estate and Trust Litigation: 2nd Edition – 2012 (by Steven K. Mignogna) and New Jersey Probate Procedures Manual – 2009 (by Gerard G. Brew) all published by the New Jersey Institute for Continuing Legal Education (available at www.NJICLE.com). In 2015 Mr. Henkel received the Dorothy G. Black award for distinguished service from the Real Property, Trust and Estate Law Section of the New Jersey State Bar Association. In 2009, he received the prestigious Alfred C. Clapp award from the New Jersey Institute for Continuing Legal Education. In 2005 he received the "Founders Award" for lifetime achievement from the Estate and Financial Planning Council of Southern New Jersey. He earned his J.D. degree at Rutgers University School of Law, where he graduated with honors and was awarded the Prentice Hall Award for outstanding performance in the area of taxation and his LL.M. in Taxation at New York University.

Here is their commentary:

## EXECUTIVE SUMMARY:

The New Jersey estate tax will be phased out. The New Jersey estate tax exemption, presently $675,000, the lowest in the country, will increase to $2 million after January 1, 2017 and will then be eliminated after January 1, 2018. What does this mean for those living in New Jersey? What changes to planning and documents might be advisable to consider for New Jersey (and in some cases other state, such as New York) domiciliaries? What will it mean for those that use to live in New Jersey but "changed" their domicile to a no-tax state? What might this repeal mean to those living in nearby states that have an estate tax (e.g., New York)? What changes to planning and documents might be advisable to consider?

While this newsletter focuses on the recent New Jersey changes and planning in New Jersey the guidance in many instances will be useful to practitioners in other jurisdictions as well.

## FACTS:

A deal was reached on September 30, 2016 between the Governor and key legislative leaders regarding funding for the Transportation Trust Fund ("TTF").

The highlights are as follows:

- Re-authorization of TTF for 8 years - $2 billion per year (which aggregates $32 billion when combined with all State and Federal funding).
- 23 cent increase in the gas tax.
- Increase earned income tax credit from 30% of the federal limit to 35%.
- Increases the New Jersey gross income tax exclusion for pensioners and retirees, reportedly to $100,000.
- Eliminates the New Jersey estate tax in phases by 2018.
- Sales tax is phased down to 6.875% (effective 1/1/2017), and then to 6.625% (effective 1/1/2018).

On Friday October 7, 2016, both houses of the State Legislature were called into a special committee hearing and voting session and approved the legislation. As of this writing the legislation still awaits the signature of Governor Christie, which is expected, at which time it would become law. The cuts amount to a $1.4 billion tax cut by full implementation in 2021, according to the Governor's office.

## COMMENT:

**Planning in a Decoupled State**

New Jersey is one of a minority of states that retained a state estate tax after the changes to the Federal Tax Code after the Economic Growth Tax Relief and Reconciliation Act of 2001 (commonly referred to as the first "Bush tax cuts"). As a result planning in New Jersey has been complex and quite different from states that had not decoupled. Since 2002, New Jersey imposed a separate estate tax. In New Jersey, spouses could leave assets tax free to their spouse or tax-free to charity, but a tax would be imposed on transfers to others to the extent the value of those transfers exceeded $675,000. While the New Jersey estate tax rate has been much lower than the federal rate, it was and is still significant with the marginal rate reaching 16%, and as a result has caused planning issues with respect to inter-spousal planning for New Jersey clients.

In addition to the estate tax, New Jersey also imposes an inheritance tax, but the tax does not generally apply to transfers to a spouse, child, or grandchild who are referred to "Class A" beneficiaries. Unfortunately for taxpayers, the recent legislation does not appear to have changed the New Jersey Inheritance tax, which generally subjects transfers to siblings at a rate of 11% and to many others at a 15% rate. The New Jersey inheritance tax may thus remain a costly trap for unsuspecting taxpayers.

Another issue to consider is that since the federal American Taxpayer Relief Act of 2012 (signed January 1, 2013). The federal government has permitted "portability" of the federal estate tax exemption. Portability was designed with an eye toward eliminating the need for the complexity of traditional "by-pass/credit shelter/family trust" planning used to shelter tax by preserving the estate tax exemption of each spouse of a married couple. In general terms, "portability" of estate tax exemption allows one spouse to inherit the assets of their deceased spouse – which used none of the exemption permitted for non-marital and non-charitable transfers and also and inherit the unused exemption. The technical term for this "unused" exemption is the "Deceased Spouse Unused Exemption" or "DSUE." In the context of planning for New Jersey domiciliaries the low New Jersey exemption created challenges and the need to evaluate or employ complex options to maximize the benefits of the first spouse's DSUE.

**Wills and Revocable Trusts May have to be Updated**

A common approach taken in wills (or revocable trusts when used as the primary dispositive document), is to incorporate a credit shelter trust and a marital disposition (either outright or in trust). The purpose of the credit shelter trust was generally to make assets available to the surviving spouse but to avoid them being included in the surviving spouse's estate for estate tax purposes. In New Jersey this was often addressed with a state exemption level credit shelter trust of $675,000, a "gap" trust funded with the difference between the federal exemption and the New Jersey exemption (currently $675,000). The excess above the federal exemption would be bequeathed to a QTIP or other marital deduction qualifying bequest. The estate, post-death, could then determine how to characterize the gap trust. For smaller estates some practitioners may have relied on outright bequests and the provision of a disclaimer credit shelter trust. While that type of dispositive scheme might appear not to require any modification that may be too superficial of an analysis. With this backdrop, practitioners must evaluate what might need to be done to update documents for the recent legislative developments.

What might need to be done to modify an existing will (or revocable trust) will depend on what provisions that document contains. Consider that the credit shelter trust and related planning could be structured in a number of ways:

- Fund the credit shelter trust with the amount that will not create a federal or state estate tax. If the New Jersey estate tax exemption was $675,000 and the federal exemption $5 million, then $675,000 would be transferred to a credit shelter trust. But if the New Jersey exemption increases to $2 million then that amount, not $675,000, should pass without further need for change, into the credit shelter trust. In 2018 if the New Jersey estate tax is repealed the amount might increase to the federal exemption amount which is $5 million inflation adjusted - $5,450,000 in 2016. It seems that the 2017 threshold will rise to $5,490,000, a modest increase. A key consideration for many people is what they anticipated their will accomplishing when it was written. If the credit shelter trust included children or other heirs (especially from a prior marriage), the result might not be the intent for them to have so much value directed to a trust for their benefit. Others might have only used a trust to save state estate tax which would no longer be relevant. The key is that it is important to determine what the objectives were when the document was completed, what the client's current objectives are now, and what the result of the provisions and new law may be.

- Some old wills might fund the credit shelter trust with a specific dollar amount, e.g., $600,000 for very old wills, or perhaps $675,000 to fund the New Jersey lower exemption amount. In these cases, you might need to modify the will to reflect the client's current intent. There may be no need or desire for a credit shelter trust under the new scenario (for smaller estates now desirous of the protections of a trust), or perhaps a higher amount might be warranted. These wills in particular should be updated. For smaller estates a disclaimer or other approach may be preferable.
- Other old wills might fund the credit shelter trust to the maximum amount that will not create a federal estate tax. Under current New Jersey law and through 2018 when the New Jersey estate tax is repealed, this type of formula could trigger a New Jersey estate tax which might not be intended or desirable. In these instances, it has been and continues to be imperative to revise the document immediately to avoid an unintended state estate tax. If the testator who signed the will does not have capacity to sign a will perhaps the title (ownership) of assets can be modified to avoid the tax, or a reformation proceeding may have to be brought in court to modify the document to reflect current law.
- For smaller estates, the entire estate might be bequeathed outright to the surviving spouse and the surviving spouse might be given the right to disclaim (renounce) any portion of that bequest into a credit shelter trust. This might avoid any tax issues. This is because the surviving spouse can simply opt to retain all assets on the first spouse's death and not trigger the transfer of any assets into a credit shelter trust. In this way whatever the New Jersey estate tax exemption may be the surviving spouse can control the tax consequences. While a disclaimer might provide ultimate flexibility, for many it is an overly simplistic and inadvisable plan as there is no protection afforded to the assets passing outright to a surviving spouse. With the incidence of elder financial abuse, divorce, lawsuits, etc. protecting the inheritance, not tax planning, could be of paramount importance. It is not only about taxes.
- Some Wills or trusts use a Clayton QTIP approach in which assets are bequeathed to a marital or QTIP trust and the executor may elect which portion qualifies for the marital deduction and the remaining non-elected portion passes to a credit shelter trust. In some instances this might remain a viable technique, in others not.
- For clients that are ill or of advanced age a more complex approach might be desirable to provide flexibility not only for the implications of the New Jersey repeal but the possible changes that might follow a Clinton victory of the White House (e.g., reduction of the gift exemption to $1 million and the estate exemption to $3.5 million).

There are many other variations, but certainly the safest approach is to review how each client's documents were structured. With so many variations and ancillary considerations (how assets are owned, asset protection, divorce planning, and other concerns) relying on an old document even if you believe it was drafted to account for the repeal of the New Jersey estate tax is simply not prudent. The real challenge for practitioners will be to convince clients to spend the money on an update meeting. This will be particularly difficult for those clients who believe (correctly or not) that there estate is below the federal exemption.

**Credit Shelter Trust Planning and How NJ Repeal Impacts It?**

One solution to the question of how to plan involves a tried and tested planning technique is flexibility. Building flexibility into an estate plan is an approach that has long been advocated, not only because the values of assets may fluctuate after the execution of the estate planning documents. Also the tax laws seem always to be subject to the political winds of change. Many plans have involved the use of a trust for the surviving spouse that can allow for the "sheltering" of assets from the potential taxation at the passing of the survivor. This trust, as noted briefly above, was often modified to address the New Jersey estate tax.

The following is a general discussion of credit shelter trust fundamentals practitioners are familiar with. This will set the foundation for a later discussion of the impact of the New Jersey repeal on credit shelter trust planning in New Jersey. The credit shelter trust (sometimes referred to as either a bypass trust, residuary trust, or family trust) has historically been utilized when considering a plan for a married couple, in order to preserve (before portability) the estate tax exemptions of each spouse. The credit shelter trust can generally:

- Allow the survivor to be sole trustee (with a HEMS standard).
- Grant the survivor the right to all income.
- Grant the spouse the right to receive principal for health, maintenance and support in reasonable comfort (the so called "ascertainable standard"), or a discretionary standard with an independent trustee.
- Grant the spouse a right to withdraw the greater of 5% or $5,000 (whichever is greater).
- The power to grant a power to re-allocate funds in the trust among a "special" or "limited" class, called a limited power of appointment ("LPOA").

Even with all of these powers being granted to the surviving spouse, the corpus of the credit trust should not be "included" in the taxable estate of the surviving spouse. This would hopefully generate an estate tax savings by "sheltering" the credit (or exemption amount) of the first spouse to pass away. In other words, if the exemption of one spouse is sheltered by one exemption, the survivor's exemption is available to shelter additional assets from tax. The trust can be crafted with fewer powers and rights depending on the family situation. However, because the trust was not included in the estate of the survivor, the basis would not be adjusted or stepped up. For many moderate wealth taxpayers domiciled in New Jersey, even if the increase in the federal estate tax exemption may have obviated worries about the federal estate tax, the continued risk of a New Jersey estate tax may have justified that planning. Once repeal is fully implemented in 2018 if there is no potential of a federal estate tax for the client, the absence of a New Jersey estate tax may assure no estate tax benefit from the application of a credit shelter trust, but serve to deny a basis step up.

Another approach to crafting a trust could be to provide that the surviving spouse is the sole beneficiary of the trust, that the survivor has the right to all income of the trust (in a manner that the requirements for a 'qualified income interest for life' are met). Under I.R.C. §1014(b)(10), a family can choose to place assets in a trust when the first spouse passes and, if an election is made to elect "Qualified Terminable Interest Property" ("QTIP") treatment under §2056(b)(7), the trust can receive "step up" in basis at the death of the surviving spouse. Thus, this plan could give the surviving spouse/surviving parent an option of determining whether or not it is better to utilize a credit shelter trust to remove assets from the survivor's estate, or elect QTIP treatment and portability at the death of a predeceased spouse. More specifically, Section 1012 of the Internal Revenue Code defines the "basis" of an individual's asset for purposes or resale as cost.
Under I.R.C. §1014, the basis is "stepped-up" or adjusted to the fair market value at the time of a decedent's passing.

In the event a married couple holds assets and has the option of placing assets in a trust in order to capture the estate tax exemption of both spouses, the basis would be adjusted or "stepped-up" to the fair market value on the date of death of the first or predeceasing spouse. However, the basis would not receive a second step-up to occur at the death of the surviving spouse. If there is substantial appreciation between the first death and the second death, that appreciation would not be subject to estate tax however, it would be subject to an income tax on liquidation of the underlying investments. Once the New Jersey estate tax is fully repealed the calculus for many taxpayers will change. The marginal aggregate federal/state estate tax rate will be lower and the relationship of the marginal estate tax rate to the capital gains rate will shrink. Thus, the benefit of basis step-up versus estate tax exclusion will change.

As a result of the opportunity to receive a second "step-up" in income tax basis, planners have recommended that clients forego the use of a credit shelter trust for the benefit of the surviving spouse/surviving parent because portability affords the family the right to receive the benefit of the estate tax exemption while simultaneously receiving an opportunity to receive a second adjustment or "step-up" in the income tax basis in all assets at the death of the surviving spouse/surviving parent.

**Flexibility Planning**

Incorporating this type of plan into a couple's estate plan provides, at the time of the death of the first (or predeceasing) spouse, the executor with the option to determine, when filing an estate tax return, on whether or not to incorporate the benefits of §2056(b)(7) of the Internal Revenue Code which would grant the estate a "marital deduction" over assets held in trust. In that event, the estate tax rule would treat the inherited assets as if they were owned by the surviving spouse. In that event, the DSUE can carry over to the surviving spouse. However, for income tax purposes the family would be afforded the opportunity to receive a step-up in income tax basis occurring at the second death.

By contrast, should the family choose to utilize the alternate approach whereby the credit shelter trust is funded and the assets are excluded from the estate of the surviving parent. In that case, no election to qualify under Section 2056(b)(7) of the Internal Revenue Code for marital deduction would be made. Setting forth a plan which calls for the creation of a credit shelter (or family) trust in the Will, a planner can be assured that the decision can be left for a later date to determine whether or not the portability and second step-up approach is warranted or whether the credit shelter plan (with the removal of all appreciation from the estate of the surviving spouse) would constitute a better approach.

One of the difficulties with the possible use of portability for estates that will not be "taxable" under the federal law (because the combined estate is less the federal $5,450,000 exemption- the 2016 threshold) is that there are many assumptions that need to be considered to determine whether a family plan should shelter the estate tax exemption from tax or not. How long will the surviving spouse live? How much will the assets appreciate? To the extent assets appreciate, will they be sold to incur the income tax? Will the family continue to reside in a state subjecting the estate of the surviving parent to tax? What will the income tax rates be on any future sale? Will the estate tax be reinstated at a state or federal level?

**QTIP Election**

Following the decoupling of the New Jersey estate tax in 2002, practitioners have grappled with the possible impact of Revenue Procedure Rev. Proc. 2001-38, 2001-24 IRB 1335, 2001-1 C.B. 1335, on New Jersey estate tax planning. Specifically, at issue in Rev. Proc 2001-38 was a situation where a trust would be sheltered the decedents by exemption. The Ruling held that the QTIP election would be ignored and the surviving spouse would not be subject to estate taxation on the trust corpus if no federal estate tax benefit will be achieved. Practitioners worried that if a New Jersey decedent funded a New Jersey bypass trust to $675,000 and a QTIP for the remaining estate to qualify for the state estate tax marital deduction, would that QTIP qualify since there was no reduction in federal estate tax. Under some interpretations of Rev. Proc. 2001-38 it was not certain that such a QTIP would qualify for the federal estate tax marital deduction, and hence for the New Jersey estate tax marital deduction. Once the New Jersey estate tax is repealed this issue would be obviated. However, the concerns about funding a New Jersey state only QTIP have been obviated by a recent Rev. Proc.

On September 27, 2016, the IRS announced Rev. Proc. 2016-49, which essentially, reversed Rev. Proc 2001-38. In effect, this new rule indicates that when an estate is filing an estate tax return, the QTIP election will be respected even if the election to be made is not necessary in order to avoid federal estate taxes. Rev. Proc. 2016-49 provides a procedure by which the IRS will disregard the QTIP election and treat it as null and void. Under §4.02 of that ruling, the taxpayer must file a Supplemental Form 706 and notify of request to treat the prior QTIP election as null and void. Without that request to nullify the QTIP election, it would generally be respected. Moreover, the ruling indicates that where a portability election is made, the QTIP election will be respected. Thus, for existing New Jersey only QTIPs, and for New Jersey only QTIPs formed until 2018, the issue raised by some commentators has been obviated by Rev. Proc. 2016-49.

**Disclaimer Trust Planning: More Likely in Many Situations**

With the repeal of the New Jersey estate tax for many taxpayers a disclaimer plan will become the default planning approach for moderate wealth taxpayers. Unfortunately, the default plan for most taxpayers below the federal exemption may be "I love you wills," outright bequests with no trusts. The move to simplistic wills may well fuel a growth in clients using on-line legal services rather than attorneys, or general practice attorney rather than estate planning specialists. The result will likely be a significant decline in the use of trusts and the protective benefits they afford.

For moderate wealth clients who use counsel there will likely be a greater reliance the use of a disclaimer trust. For example, if husband and wife have been married for a long time and the children are "common children" of the marriage, such that it could be anticipated that a surviving spouse would not be expected to disinherit the children of the predeceasing spouse, then a disclaimer trust may provide the greatest opportunity for flexibility. Disclaimer trusts, however, are ineffective in achieving non-tax planning objectives.

A disclaimer trust estate plan would devise the entire estate to the surviving spouse. If the inheritance is "disclaimed' by the survivor, the will or revocable trust can direct the inheritance to a trust for the spouse as permitted by I.R.C. § 2518. By granting a surviving spouse this option, the surviving spouse can choose whether funding the trust with the estate is appropriate based upon a variety of circumstances at that time, such as (1) the size of the combined estates at the first death; (2) the applicable federal estate tax exemption; (3) the likelihood that the surviving spouse will reside in a state with a state estate tax. While all of these uncertainties may remain at the death of the first spouse, this flexible plan is premised on the assumption that we may know more at that time than we did when the wills and estate plan were drafted. Without the New Jersey estate tax and with the potential of a high Federal estate tax exemption, this will be a plan that will retain its popularity. If the spouses plan to utilize a "disclaimer" trust option, it is still important to title the assets to divide the family estate equally between the husband and wife. While a one-half interest in real property can be disclaimed pursuant to both Treas. Reg. § 25.2518-2(c)(4)(ii) and *N.J.S.A.* 3B:9-2, other intangibles should be divided between the spouses.

Using this type of plan will provide for greater ease of administration if the spouses have a plan in mind as to how the disclaimer trust will operate at the death of either spouse. Some estate planners dislike the use of disclaimer trusts because they are concerned that a surviving spouse, in an emotional state, may be unwilling or emotionally unable to make the required evaluation of the need to disclaim in the short time permitted for a disclaimer. Others feel that if properly addressed in the planning phase, the surviving spouse will be able to carry through with this task as an entirely financial matter (not emotional). As a general rule, the disclaimer must be completed and filed (in the County Surrogate's office) within nine months of death. For real estate, it must also be filed in the Recorder of Deeds. Note the New Jersey disclaimer statute does not require that the disclaimer be filed within nine months. The only limitation under New Jersey law is that the disclaimant cannot accept the property. N.J.S.A. 3B:9-9. For federal tax purposes, the disclaimer must be completed within nine months. I.R.C. § 2518.

If the disclaimer meets the requirements of I.R.C. § 2518, it is a "qualified disclaimer" (a tax sensitive term). The transfer is not treated as a gift by the disclaimant for gift tax purposes and it is treated as a gift/bequest directly by the decedent as if the disclaimant had predeceased. The nine-month time frame is usually a sufficient period of time to deal with the emotional aspects of death of a loved one and make a financial choice — particularly if it has been considered earlier in the planning phase. Certainly, it is not something that must be considered shortly after the first spouse's death. However, assuming the spouse does not retitle assets into his/her individual name (which tends to be a natural desire), there should be adequate time to meet, discuss the financial options and make an informed choice about whether or not to execute on the disclaimer trust plan.

This planning option provides substantial flexibility. Obviously, the couple must be comfortable that the surviving spouse will carry through with the testamentary desires of the predeceasing spouse. Thus, it may not be appropriate in the second marriage where there are alternate heirs (*i.e.*, children of a previous marriage). If the spouses have planned to leave their entire estate to the survivor or the purpose of establishing a trust was simply related to the tax opportunities, then this type of plan may need reconsideration. Another consideration may be whether the surviving spouse will need the entire balance of the funds received from the predeceasing spouse. There are two mechanisms to consider in connection with this plan. First, if the surviving spouse feels that he/she does not need the entire estate, the survivor can also, likewise, disclaim an interest in the disclaimer trust, either in whole or in part. Thus, for purposes of testamentary disposition, this will be treated as if the property passed directly from the predeceasing spouse to the alternate heirs (presumably children/grandchildren). An alternate plan would be to devise the disclaimer trust in a fashion which allows principal to be used for the benefit of the heirs in addition to the surviving spouse. This is explicitly permitted by Treas. Reg. 25.2518-2(e)(2), assuming that the power of distribution is limited by an ascertainable standard.

The challenge for many New Jersey practitioners post-repeal of the New Jersey estate tax is to convince clients with wealth levels under the federal exemption of the need for better planning. The threat of a New Jersey estate clearly was a driver pushing clients to estate planners. Absent that starting in 2018, practitioners will have to educate clients about a range of considerations that would justify the cost of professional planning. These might include:

- With increased longevity the likelihood of remarriage following the death of a prior spouse will increase. The need for trusts on the first death to protect those assets is more important than most realize.
- Elder financial abuse is burgeoning. The use of on-line document preparation services is unlikely to provide the independent guidance to address this significant risk.
- If Hillary captures the White House she may succeed in pushing through her tax increase agenda. A reduction of the gift exemption to $1 million could have a chilling effect on asset protection and other planning.

**Life Insurance Trusts May Need to be Revisited**

Some taxpayers may have life insurance trusts that were created to hold life insurance to pay an estate tax. Even if the increases in the federal estate tax exemption eliminated the federal estate tax, some taxpayers may have retained an insurance trust in place to fund the New Jersey estate tax. If the New Jersey estate tax is in fact repealed perhaps there is no longer an estate tax justification for the insurance trust, but for some estates a New Jersey inheritance tax may still support such a plan if the inheritance tax is not repealed. While in many instances insurance trusts and life insurance serve a range of other purposes, if the elimination of the New Jersey estate tax eliminates the last relevant purpose, options could be explored for both the insurance coverage and the trust owning it.

Life insurance may have been purchased to pay an estate tax that might be eliminated but insurance may provide long term care benefits, an alternative asset class to provide ballast for other investments that are more risky, a fund to borrow in retirement and more.

**Durable Power of Attorney (and Revocable Trusts) Gift Provisions Might Warrant Reconsideration**

If a taxpayer’s power of attorney has a gift provision and the sole purpose of that gift provision was to save estate tax, then the power of attorney (or revocable trust if that too had a gift provision) should be evaluated. If there is no other purpose for the gift provision, consideration should be given to revising the document to reduce or eliminate the gift provision. Given the incidence of elder financial abuse using a durable power of attorney, if there is no reason to retain a gift provision, it may be preferable to revise the document and eliminate it.

**Title to Assets Should Be Revisited**

Some taxpayers intentionally divided assets so that either spouse could have assets to fund a credit shelter trust no matter who died first. If this was done for taxpayers with estates under the federal estate tax exemption, it may not be feasible to again change the ownership of assets back to whatever would be preferable without regard to the estate tax. So for example, if a couple in New Jersey had a $5 million estate, they were well below the federal estate tax exemption. They may have divided assets to fund a bypass trust under each of their wills. Assume the wife was a physician and the husband a teacher. It might be preferable to have all assets in the husband’s name to minimize liability exposure in the wife’s name. The repeal of the New Jersey estate tax might warrant changing title to those assets back to only the husband’s name.

Some taxpayers intentionally divided assets so that either spouse could have assets to fund a credit shelter trust no matter who died first. This may have been planned for taxpayers with estates under the federal estate tax exemption, e.g., to save New Jersey estate taxes by funding a New Jersey limit bypass or credit shelter trust. It may now be feasible to again change the ownership of assets back to whatever would be preferable without regard to the estate tax.

**Example**: A couple in New Jersey had a $5 million estate they were well below the federal estate tax exemption. They divided assets approximately equally in each spouse's name to fund a bypass trust under each of their wills. Assume the wife was a physician and the husband a teacher. It might be preferable to have all assets in the husband's name to minimize liability exposure in the wife's name. If the New Jersey estate tax is in fact repealed perhaps assets can be changed back to only the husband's name.

**Example**: A better but more complex approach might be to use some of the assets to fund an inter-vivos QTIP trust so there is protection and more control over disposition. If the inter-vivos QTIP is formed in a state that permits self-settled trusts or has express language permitting a bypass back to the grantor spouse, on the death of the first spouse the assets will return to the settlor spouse in a bypass trust, thus permitting both spouse's to benefit from the assets while providing asset protection. The practical issue is that absent the threat of a federal or state estate tax will the couple undertake the planning? Will the possibility of a Democratic win of the White House and a harshening of the estate tax motivate the planning now? If not will the couple revisit that planning depending on the outcome of the 2016 election?

The title to assets can be relevant to estate tax planning, and in particular to obtain an increase (step-up) in income tax basis on death (if the first to die holds the assets the income tax basis will be increased and the survivor can sell that asset without a capital gain). Assets might be retitled into the name of the spouse that is anticipated to die first, but not within one year (unless further planning is undertaken). Alternatively, a community property trust could be created in Alaska, South Dakota or Tennessee so that whichever New Jersey (a non-community property state) spouse dies first arguably all assets should qualify for an estate tax update. If the appreciation potential in the estate is large enough perhaps this might be advisable.

Be cautious about a myriad of ancillary issues before changing title to assets. What are the matrimonial implications to retitling assets? Even if there are arguably only limited legal implications because equitable distribution there might be a strategic impact? Should a post-nuptial agreement be created to address the retitling of assets?

Changing the title to a house might affect property taxes (e.g., senior citizen or veterans benefits), insurance coverage, and other matters.

Changing a legal document such as a will, without addressing title to assets, may accomplish nothing. Taxpayers need to understand that the elimination of the tax does not eliminate the need for planning and follow up. For professionals of all stripes this is going to be a hard sell: "I need to bill you to do work that may not save your heirs taxes." The key to this pitch will be all advisers echoing the same mantra. But will all players on the team really cooperate? Will wealth managers really do the right thing and push clients back to their estate planners?

**New Jersey Inheritance Tax Trap**

Will the New Jersey inheritance tax also be repealed? It does not appear so. Perhaps the revenue loss from both the repeal of the estate and inheritance tax at one time was deemed too costly. For those taxpayers bequeathing assets to beneficiaries subject to inheritance tax, gifts prior to death, and/or retaining life insurance to pay inheritance tax may be worthwhile. This will remain a trap for the unwary. Taxpayers will likely assume that since the estate tax has been repealed there remain no New Jersey death taxes until their estates are tagged with a costly New Jersey inheritance tax.

Perhaps durable powers of attorneys (and/or revocable trusts if those are the primary dispositive document) should be revised to permit advancement of testamentary gifts that might trigger a New Jersey estate tax.

**Personal Goals Become More Important**

Estate planning should never be only about estate taxes. There are a myriad of important personal goals that should be considered. One dimensional planning rarely is effective. Plans that were implemented merely to avoid New Jersey estate tax for taxpayers with estates under the federal exemption should be revisited to assure that robust and broad based planning was addressed, not merely a tax fix that is no longer needed provided. Did the documentation and planning address personal goals and issues? Was later life planning addressed if relevant? What steps were taken to reduce the risks of elder financial abuse? Does the client have religious goals or personal financial objectives for heirs that were overlooked in the focus of planning on taxes?

**Does New Jersey Repeal Matter to the Ultra Wealthy**?

Yes. Many estate plans for wealthy persons domiciled in New Jersey estate plans might have funded three trusts: a New Jersey credit shelter trust up to $675,000, a gap trust with the difference between the federal estate tax exemption in the year of death, and a QTIP for the remaining estate. The issue was how the gap trust might be characterized for estate tax purposes. Once the New Jersey estate tax is full repealed there will be no detriment to fully funding a bypass trust to the federal estate tax exemption. Until that time the multiple trust approach might still make sense.

For some wealthy taxpayers an outright bequest might have been provided for to the surviving spouse. The surviving spouse may have, according to the plan, intended to receive all assets outright from the deceased spouse and then make a gift to a self-settled trust. In that way no New Jersey estate tax would be incurred and the full federal exemption for the first to die spouse could be used. While this plan still has an advantage in that the irrevocable trust using the exemption will be a grantor trust as to the surviving spouse, providing ongoing tax burn for his or her estate. However, the calculus of the advantages and risks of that plan will change substantially if the New Jersey estate tax is repealed. It may be preferable to have the will or revocable trust of the first to die spouse fully fund a credit shelter trust on death and avoid the risk of the surviving spouse not carrying through on the intended plan, creditors of the surviving spouse reaching the assets bequeathed outright, etc.

Language in wills and revocable trusts should be reviewed to assure that it accomplishes the planning goals during the phase out of the tax and following the repeal.

**Should the Client "Repatriate?"**

Many wealthy taxpayers established domicile in states without an estate tax, e.g., Florida. Some of these clients really moved and changed their nexus out of New Jersey, others may maintain that they do, but may not have really made sufficient changes. In a few cases the taxpayer merely were taking a position that they were no longer domiciled in New Jersey to avoid the New Jersey estate tax. In the latter cases, and perhaps in the former, these taxpayers might wish to revisit their domicile decisions and status in light of the repeal. In such cases not only might all estate planning documents have to be updated to reflect a New Jersey domicile but a range of other decisions and steps might have to be modified as well.

**Other Considerations Make Changes Complicated**

There are a host of other considerations that should be factored into the analysis. Before documents, planning, insurance, asset title or other matters are changed consider:

- Nothing in the tax world is certain. What changes today may change tomorrow. Planning should have been and should remain flexible. If current documents were done designed with flexibility in mind perhaps they should be revised on that basis alone.
- Will the New Jersey estate tax repeal actually take effect as indicated?
- What will happen with the federal estate tax after the election? Will it be repealed or will instead the exemption be lowered significantly and other restrictive changes made?
- Asset protection, elder financial abuse and other considerations may be relevant.
- Mobility is important to consider too. Where might the taxpayer move in the future?

**Conclusion**

If the New Jersey estate and inheritance tax are in fact repealed, it is a welcome relief to those affected and might actually increase tax revenues to the State of New Jersey given how many taxpayers move out of the state (or say they do) to avoid the estate tax. Planning will be significantly simplified for those with estates near or under the federal estate tax exemption. In light of this everyone should review their existing estate planning documents, title to assets, life insurance coverage and anything else affected. The disturbing part of the repeal is tax on the wealthiest are being reduced while sales and gas taxes that disproportionately weigh on those of more modest means, where the additional dollars involved can create a real hardship, have been increased. The pros and cons of the estate tax repeal coupled with the other tax changes are debatable; the need to revisit and potentially revise estate planning documents in light of those changes is not.

**HOPE THIS HELPS YOU HELP OTHERS MAKE A *POSITIVE* DIFFERENCE!**

*Marty Shenkman*

*Richard Greenberg*

*Glenn Henkel*

**CITE AS:**