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The Prudent Investor

December 2024

Planning your next will and testament

Would you recognize the person who signed your will?

If you haven't heard from your estate planning advisors lately, you soon may. In 2025, the amount exempt from federal estate taxes will grow to $13.99 million. For a married couple, should they both die in 2025, $27.98 million may be sheltered from estate taxes.

However, under current law that amount falls roughly in half in 2026. Some politicians are advocating for an even lower exempt amount, or a higher tax rate. On the other hand, there is some support for eliminating the federal estate tax entirely.

It's tough for any estate plan to be optimal for all tax environments.

Surprised heirs

A recent item in *The Wall Street Journal* noted the growing phenomenon of childless older adults ["People Without Kids Are Leaving Money to Surprised Heirs," October 2, 2024]. According to the Pew Research Center, 20% of U.S. adults never had children. In the absence of descendants, more distant relatives, as well as friends, become potential surprise heirs.

A study at Yale determined that people without descendants give an average of 10% of their estates to charity—the overall average is closer to 3%. Charities have taken notice.

Caring for pets after death can be a vexing issue for childless adults. The advent of pet trusts may resolve the problem, though laws on pet trusts

laughing heir. *Slang.* An heir distant enough to feel no grief when a relative dies and leaves an inheritance (generally viewed as a windfall) to the heir.

BLACK'S LAW DICTIONARY

vary from state to state. Typically, an individual agrees to care for the pet for the rest of its life, with support funds coming from a trust. After the pet dies, the caregiver may receive any balance left in the trust.

Other changes to consider

Taxes aren't the only reason for conducting a will review, they are just the spur to get the ride started. Obvious triggers include:

- birth of a child, grandchild or other potential heir;
- divorce;
- death of a beneficiary;
- marriage or remarriage;
- change in state of residence.

Other factors that can reduce the effectiveness of a will happen more gradually, over a longer period of time, and so may be less obvious.

Changes in a beneficiaries' needs or capabilities. Has a well-adjusted youngster become a troubled postadolescent? Is a troubled postadolescent of yesterday now making more money than you do? Changes in the lives of those around you need to be reflected in your estate plan.

Has your estate become less liquid? Will your estate have enough cash to meet expenses and tax obligations? If you have hard-to-sell assets, such as real estate or family business interests, you'll need special planning to avoid the forced asset sales from your estate at bargain prices.

Are you satisfied with your selection for executor? Estate settlement can be a demanding job. For the larger, more complex estate, the services of an experienced corporate fiduciary—a trust organization such as us—can be a welcome, cost-effective means to lift a difficult burden from the shoulders of a family member.

Review your ENTIRE estate plan

Your will only directs the disposition of the property that will pass through your probate estate. That may be only a portion—and perhaps a relatively small portion—of the total financial resources that will be available to your heirs. The most important types of nonprobate property are jointly held property, interests in qualified retirement plans and life insurance proceeds. You must take such assets into consideration as you evaluate the strength of your will.

Joint interests. Joint ownership of the family homestead with rights of survivorship has long been customary for married couples. It's possible to have too much of a good thing—when investment accounts are also held in joint name, flexibility in estate planning is lost. There is no estate tax savings for jointly owned property, and there can be income tax costs.

Retirement plans. In most cases, a surviving spouse will be the beneficiary of a pension or retirement account at the owner's death.

Life insurance. Insurance proceeds pass directly to designated beneficiaries unless the beneficiaries already have died. A good alternative to explore is naming a trust as beneficiary, to provide the heir with professional investment assistance for this important sum. Ask us for details.

Our invitation to you

We specialize in estate settlement and trusteeship. We are advocates for living trusts. If you would like a "second opinion" about your estate plans, or if you have questions about how trusts work and whether a trust might be right for you, we're the ones to whom you should turn. We'll be happy to tell you more.☐

Elements of estate settlement

Winding up the financial affairs of any affluent individual may prove surprisingly complicated.
The steps include:

- Inventory the assets;
- Obtain insurance as necessary;
- Manage investments;
- Collect debts owed to the decedent;
- Pay debts owed by the decedent;
- Raise cash;
- File death tax returns (federal estate tax and state estate or inheritance tax) if needed;
- File decedent's final income tax return;
- Distribute assets or fund trusts in accordance with the will; and
- Provide an accounting for the management of the estate.

Someone coming into this task for the first time is likely to find it daunting. There are companies, such as us, that include estate settlement as a core business function. We have the record-keeping systems in place, and we have the experience and expertise required to make estate settlement as painless as possible.

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Rookie mistake?

The following story is not hypothetical. The facts are drawn from a published IRS letter ruling.

Husband created a trust to manage his assets after his death. His two children, who were apparently from an earlier marriage, were named as the trustees. Husband owned a substantial IRA at his death, and the IRA named the trust as the beneficiary. After Husband died, the entire IRA was distributed to the trust's checking account.

Wife understood that she was entitled to 25% of that IRA. Evidently there was disagreement about what that amount would be, but on September 29, Wife and the children reached a settlement agreement. The trust would attempt to create an IRA rollover for Wife's portion of the proceeds. Wife established two IRAs for herself. On October 14, the trust sent the amount agreed to in settlement to Wife's IRA 1, and on October 22, she transferred everything to her IRA 2. The reason for having two IRAs is unclear.

When tax time came around early the following year, Wife received a notice from the trust that the distribution to her was taxable. This likely came as a shock to her, because she never had possession of the money, and the transfer was within 60 days of the agreement. Wife filed the letter ruling request, asking the IRS to waive the usual time requirements for an IRA rollover because of a mistake by a financial institution.

When did the 60 days for the rollover start?

The ruling does not state what the date was when the IRA proceeds were distributed to the trust. That was when the 60-day period for a rollover began, and evidently that was long before the settlement agreement was reached.

There was no financial institution involved here. Wife's complaint was that the trustees and their attorney advisor had a duty to her—a duty to preserve her opportunity for an IRA rollover of her inheritance, which they failed to do. After reviewing her argument, the IRS held, "The information you presented and documentation you submitted are insufficient evidence of financial institution error," without additional analysis.

Tax consequences?

The tax result is much worse here than the loss of a rollover opportunity. Wife will owe a 6% penalty tax on an excess contribution to an IRA for the amounts paid to her IRA by the trust. The penalty applies every year until the excess is withdrawn.

The trust will have to pay ordinary income tax on the entire amount of the IRA distribution in the tax year that it received the money. This could be a pretty substantial tax hit, because the income tax brackets for trusts and estates are much narrower than for individuals.

Normally, when a trust is a beneficiary of an IRA, only the Required Minimum Distribution will be paid to the trust each year, not the entire value of the IRA. If a surviving spouse is to receive a portion of an IRA, he or she should be named directly as beneficiary or percentage beneficiary, to preserve all tax options for deferral on the money.

Did the trustees, children of the earlier marriage, understand any of this when they authorized distribution of the IRA to the trust? The ruling offers no insight into this question, but it seems very unlikely. They acted out of inexperience, in a manner that seemed reasonable to them.

The better course to avoid unexpected problems in estate settlement is to hire professionals, a corporate fiduciary such as us. ☐

Cybersecurity

As "National Cybersecurity Awareness Month" came to a close, the IRS once again issued a warning for taxpayers to be vigilant with their electronic devices and online accounts. "It's important to remember that the IRS does not use unsolicited email and social media to discuss personal tax issues, such as those involving tax refunds, payments or tax bills." Suspicious emails should be forwarded to phishing@irs.gov. The Service also encourages taxpayers to use strong passwords and multifactor authentication. A virtual private network should be employed whenever one is on a public Wi-Fi network.

The IRS itself needs work on cybersecurity as well, according to the Treasury Inspector General for Tax Administration (TIGTA). The IRS has a Practitioner Priority Service for assisting professional tax preparers, and this service has been targeted by hackers. Over a period of eight months, ending on April 16 of this year, some $462 million worth of fraudulent refunds were filed through this channel. The Service stopped 4,254 of the false claims, but 574 got through, with $47 million in improper refunds.

Recommendations for beefing up security will be implemented. There's no word on whether the perpetrators have been found or will be held to account.

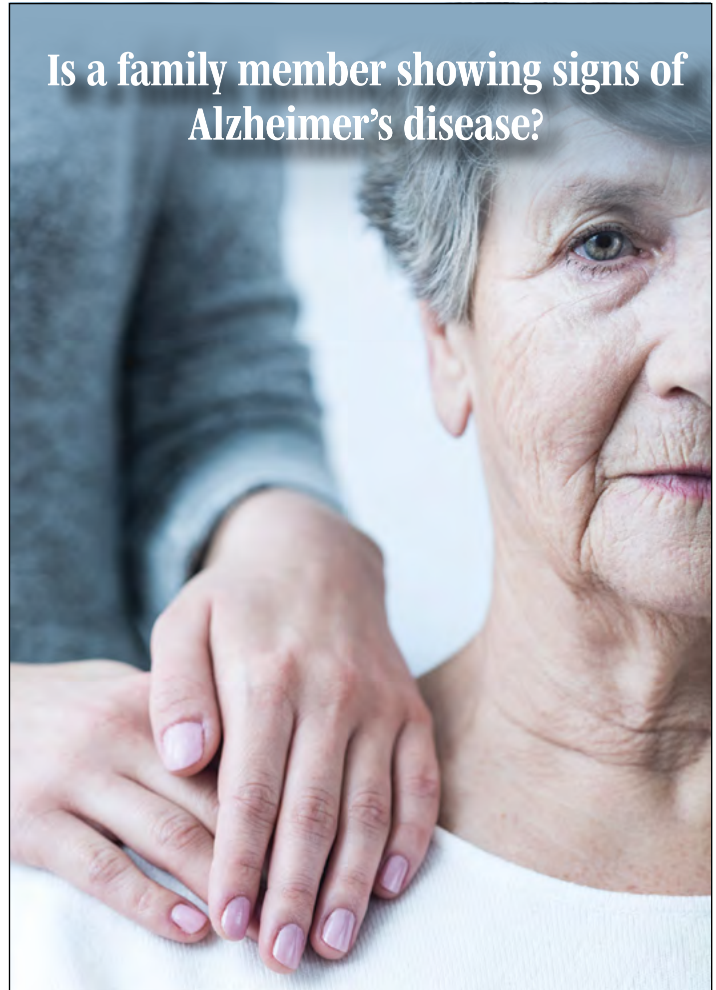
Adverse determinations

Recently the IRS denied tax-exempt status to an organization established to promote the development and growth of pickleball. The Service found that the organization was not operated exclusively for exempt purposes and that it furthered a substantial nonexempt purpose, that is, promoting recreational community pickleball events for its members. Income tax returns will be required for the organization.

They are in good company. Additional adverse determinations for tax-exempt status, issued the same day by the IRS, included:

- an organization founded to uplift rural communities through tourism because its tourism promotion activities further nonexempt purposes;
- an organization formed to operate and maintain a rural cemetery because its organizing document wasn't signed by at least two authorized individuals;
- a farming business;
- a group organized to promote physical fitness and a healthy lifestyle in the restaurant and service communities;
- an organization formed to promote the sport of purebred dogs, responsible dog breeding, and dog owners' rights;
- an organization established to help the less privileged and senior citizens with limited income after finding the organization's activities weren't limited to exempt purposes.

The amount of tax revenue at stake for these small organizations is likely to be minor, but the compliance cost may not be. ☐



Consider a living trust for comprehensive financial management. See our trust and investment professionals today.

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