WADE ASH
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NEWSLETTER

February 2015

NEWS OF THE FIRM

5280 Magazine published its list of the 345 Top Lawyers by area of practice in Colorado in its January, 2015 issue. Laurie Hunter was included in the list of top 10 attorneys in the area of Trusts & Estates!

James Wade has been appointed as a member of a Task Force between ACTEC (The American College of Trust and Estate Counsel) and the National College of Probate Judges. He is also chairing a Sub-Committee of the Joint Editorial Board for Uniform Trust and Estate Acts to study the question of the determination of appropriate interest rates on obligations under the Uniform Probate Code.

Herb Tucker and Bob Horen were nominated as Fellows of the Colorado Bar Foundation and join James Wade, Laurie Hunter, Alison Zinn, Keith Lapuyade and Steve Schumacher as current Fellows. James Wade was also a previous chair of the Colorado Bar Fellows. Selection as a Fellow of the Foundation is in recognition of a lawyer as one whose professional, public and private career has demonstrated outstanding dedication to the welfare of the community, the traditions of the profession and the maintenance and advancement of the objectives of the Colorado Bar Association.

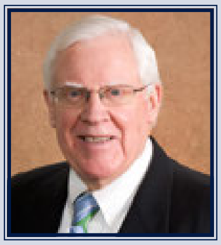
Alison Zinn will be speaking at a local GRIT Project seminar sponsored by the Colorado Bar Association and the Colorado Womens Bar Association to be held at the law firm of Wheeler Trigg O'Donnell LLP on March 5, 2015. The American Bar Association GRIT Project is aimed at educating and inspiring women to succeed.

Josie Faix and Merry Balson have formed Balson & Faix, LLP and will be leaving the firm at the end of February. We have enjoyed our time with Josie and Merry and extend our best wishes for the success of their new firm!

Keith Lapuyade is currently a panel speaker in a 9-Program Series called Understanding and Using Trusts which is sponsored by the Trust & Estate Section of the Colorado Bar Association. The Program is a practical series of CLE programs on understanding and using trusts. Each Program in the Series is dedicated to a key area of trust law and Keith will be speaking specifically on the topics of liabilities of trustees who do not properly administer their estates, liability factors, unforeseen consequences of failure to adhere to required duties, and pitfalls for the unwary.

Keith Lapuyade is also speaking at the Estate Planning Retreat in June, 2015 in Santa Fe, New Mexico, which is sponsored by the Trust & Estate Section of the Colorado Bar Association. Keith will be speaking on the topic of "I'm Not Dead Yet: The Conservator-Created Will and the Pre-Mortem Will Contest."

THOUGHTS ABOUT DEATH AND TAXES



James Wade

President Obama's recent tax reform proposal, which he referred to in his State of the Union message, includes a repeal of the so-called step-up basis rule.

Under the present law, the income tax basis in a person's assets is based on his or her historical cost (acquisition price). But at death the basis is adjusted to fair market value at date of death (as determined for federal estate tax purposes). Because of inflation and the general growth in the economy, normally we adjust the basis upwards (thus the reference to "step-up"); the opposite may be true - assets with a higher cost basis may be stepped down to fair market value. This arrangement under the tax reform proposal is characterized as a loop-hole.

THOUGHTS ABOUT DEATH AND TAXES (CONT'D.)

In the context of decedent's estates, there are several possibilities with respect to the impact on income tax basis. One is to treat the event of death as a disposition of the assets, thus triggering the capital gain or loss; the second is to avoid the taxable event but have the decedent's historical income tax basis carry-over to his successors (carry-over basis); and the third is the present system adjusting the basis to date of death value.

The first approach, which is the current Canadian system, would allow the recognition of capital gains and losses to occur in the context of estate administration. It would add a taxable gain and loss to the mix of assets and liabilities which have to be sorted out at death. Under this approach one could determine whether the gain or loss would be recognized in the decedent's final return or in the return of the estate or other successors. This approach would aggravate liquidity problems in estates holding other than traditional "financial" type assets (liquid stocks, bonds, bank accounts, mutual funds, and the like).

The second "tax reform" approach (carry-over basis) is not new to the tax code. We had a period of carry-over basis in the 1970s. The elimination of capital gains under the present step-up in basis system may be seen as an unnecessary anomaly which tends to give tax breaks to those wealthy enough to pass accumulated assets with substantial value. Carry-over basis does not put liquidity pressures on an estate, and it allows the decedent's successors to keep control over, plus an opportunity to plan for, capital gain or loss recognition.

The present system of "step-up in basis" is generally favorable to the taxpayer since a majority of assets is deemed to have appreciated in value during the period prior to death. A part of the current estate planning process is to determine the best utilization of the federal transfer tax exemption (presently $5,430,000). At death, unless the estate is taxable, we like to obtain valuations at the upper end of the range of fair market value. Also, knowing that the exemption can be utilized in part by lifetime giving, we try to select assets for gifting which are apt to appreciate in value, but if we have a choice between a high basis asset and a low basis asset we select the higher basis asset. The reason is that, for gift tax (as opposed to estate tax) purposes we have a carryover income tax basis in the gifted assets. Thus, if a low basis asset passes at death the capital gain is eliminated; if it passes by gift the capital gain is preserved.

The math depends upon respective tax rates. Until recently the capital gains rate had been reduced to 15% maximum and the estate tax rate was 45% with an increase to 55% for large estates. Thus, the difference might be as large as 40%. The present estate tax rate is 40%; and if the capital gain rate increased to 25% the differential would be only 15%. Should capital gains be taxed at ordinary income rates, the income tax rate might exceed gift and estate tax rates.

It is interesting that, so far as I am aware, there has been no recent comprehensive public policy debate on estate and gift tax rates. We know that historically the estate tax was established to pay war time costs. We also know that the gift tax was added to provide symmetry to a transfer tax system and that without a gift tax, inter vivos gift making could eviscerate the estate tax. We also know that historically the federal estate tax allowed a state death tax credit (i.e., providing that a small percentage of the federal estate tax could be shifted over to the states, including Colorado). Many states, like Colorado, enacted a death tax provision imposing a tax equal to the allowable federal credit. The state income tax credit was, however, eliminated from the federal tax, resulting in no estate or inheritance tax in Colorado. We also know that the federal estate tax has basically been a flat tax (at a relatively high rate but with growing exemptions) and has continued an unlimited charitable deduction.

The design of the tax may seem a bit random, but we have come to live with it. My experience with client reaction to the estate and gift tax system is inconsistent (if not random). Some clients want to do everything possible to avoid taxes; most are comfortable with the present estate tax exemption of $5,430,000 (plus the ability to utilize in the second estate any portion of the exemption unused in the first estate); many feel that the unlimited charitable deduction encourages their own charitable giving and feel that an elimination or substantial reduction of the estate tax would negatively impact charities in a significant way. A client or two, appreciative of the opportunities which America has given their immigration ancestors, have made the federal government

THOUGHTS ABOUT DEATH AND TAXES (CONT'D.)

(or a subdivision) a beneficiary of their estate.

This is not to take sides with respect to the tax reform proposal, but rather to contribute some information to the discussion. Going back to a carry-over basis system would bring the estate tax into line with the gift tax. If carry-over basis was applied to all decedents (and not just those whose estates are subject to federal estate tax) the tax would cast a very wide net and equally effect both low bracket and high bracket income taxpayers who owned appreciated assets at death. The revenue gathered would be substantial and not necessarily consistent with the announced goal of burdening wealthy taxpayers to assist an endangered middle class. In one sense the tax reform proposal would not create a new tax, but resurrect a previous system. The problem with the previous system, however, was that it was not easily workable. Measuring taxable gains at death based on historical acquisition data pre-supposes that the historical information is available. It is often hard enough to gather the basis information on assets which you yourself purchased. The problem is exacerbated by having to provide financial information on a transaction which may have occurred 50 or 100 years ago by your ancestor and not yourself.

Stay tuned.

DON'T FORGET PORTABILITY!

Laurie Hunter

I have met with two surviving spouses so far this year who did not file a federal estate tax return in their deceased spouse's estate. The deceased spouse did not have sufficient assets to *require* the filing of a return, but an opportunity was nevertheless lost. The deceased spouse's unused estate tax exemption is only "portable" to the surviving spouse's own exemption (added on to it) if the Form 706 is ***timely*** filed (within 9 months after date of death, or 6 months after that if an extension request is timely filed). Treasury granted a one-time extension until December 31, 2014 for couples who had failed to file, but that was because with the federal recognition of same-sex marriage, a lot of couples who did not think they could have portability, now could after the Supreme Court's *Windsor* decision. Whether Treasury will grant another similar extension in the future is unknown. But remember that in order to possibly double the surviving spouse's estate tax exemption through portability, an estate tax return ***must be filed***.

FACEBOOK'S LEGACY CONTACT

Facebook now lets users designate a person who can have access to their account after their death, as part of the security settings. In the past, Facebook and other on-line services have resisted permitting one's agent under a financial power of attorney or a personal representative of one's estate from accessing accounts. Partly, this is because federal law prohibits anyone other than the "user" from accessing an account. The Uniform Fiduciary Access to Digital Assets Act authorizes fiduciaries under state law to access accounts, but there is still a conflict with federal law. This Uniform Act may be introduced in the Colorado legislature this session. Stay tuned!

CONGRESS AUTHORIZES NEW ACCOUNTS FOR DISABLED INDIVIDUALS

Late December 16, 2014, Congress passed (and the President signed) the Achieving a Better Life Experience Act (ABLE), creating a new type of tax-advantaged savings account to help meet financial needs of disabled individuals and their families. The ABLE Act authorizes states to create these accounts (similar to 529 plan accounts for paying higher education expenses) starting in 2015. Persons could make contributions to the accounts for named beneficiaries, and the accounts grow tax-free, similar to 529 plan accounts. The accounts would not be considered "available assets" that would limit a beneficiary's qualification for Medicaid or other needs-based government benefits. Contributions to an account each year are limited to the gift tax annual exclusion (not five times that, as for 529 plan accounts), and if distributions are made for "qualified disability expenses" the beneficiary is not taxed on the distributions as part of his or her income. The beneficiary must be disabled or blind under Social Security, and that condition must have occurred before the beneficiary reached age 26.

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