The Blitz

April 2018

Information on Tax and Estate Planning from the
Masonic Charities of the Grand Lodge of Pennsylvania

Question 1: I recently got a call from my widow friend, Joan, who I see at my receptions in Reading, Pa. Her husband, Jack, passed away about a year ago, and she asked me if she should add her daughter, Sally, to the deed on her house while she still lived there. She also asked about including Sally on her savings and checking accounts, so Sally can help her out with her finances. She wanted to know if she should be concerned with sharing her assets with Sally.

Answer: During my time counseling surviving spouses with children, I have come across this fact scenario more than I would expect. There are several factors to consider when retitling your assets in a child's name. Let's review the issues I discussed with Joan.

1. Inheritance consequences: For Joan, adding her only child to the deed of her home as a joint tenant with rights of survivorship seemed logical, since she intended to give everything to Sally when she passed anyway, and this just made the process easier. As the surviving joint tenant at Joan's death, Sally would take immediate possession of the property without the need for probate through Joan's Will. The same outcome would seem attractive by adding Sally as a joint tenant to Joan's checking and savings accounts, but there are some consequences for this easier path to inheritance.

2. Income tax consequences: With regard to Joan's home or any appreciated assets such as securities, the loss of the step-up in basis for the entire home could have significant tax consequences upon death when the house is sold. The transfer could also disqualify Joan from use of part or all of her Principal Residence Tax Exclusion if her home is sold during her lifetime. If Joan lived in Bryn Mawr, her house could have increased a fortune in value over the years, and Joan or her heirs could have an unwelcome tax bill when the house is sold. Luckily (or maybe not), Joan lives in Reading, and her place hasn't appreciated much over the years, so she doesn't have to worry about this problem.

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3. Inheritance tax consequences: There is still an inheritance tax problem, since Joan is a resident of Pennsylvania. By including Sally as a joint owner of her house and accounts, Joan has gifted one-half the value of these assets to Sally and will avoid the 4½% inheritance tax imposed on that amount given away, PROVIDED that she survives for more than a year after the transfer of one-half the assets to Sally. If not, then any amount given away in excess of $3,000 for each asset will be subject to the 4½% inheritance tax, despite the fact it was given away prior to Joan's passing (and this tax would be 12% for siblings and 15% for all other individuals such as cousins, nephews and friends). I told Joan she needs to weigh the advantages of avoiding the inheritance tax on what she gives away versus Sally having to pay capital gains taxes on any appreciation when the house is sold after her passing.

4. Medicaid consequnces: Another problem with adding Sally to Joan's assets is Joan would be disqualified for Medicaid if she drained all her assets and moved into a nursing home within five years of making the gifts. The transfers could also prevent Joan from qualifying to go to Masonic Villages for any living option for the same reason. I told Joan she needs to see an elder law attorney to make sure she has sufficient assets to avoid this problem before she decides to add Sally to the accounts and home.

5. Creditor consquences: There is also the risk of other parties tying up the property and accounts. As a joint tenant, Sally now has legal access to the home and to the checking and savings accounts, and Sally's creditors have access, too. Heaven forbid, Sally drains the accounts for her own personal use or declares bankruptcy, and liens are placed on the assets. The assets could even get tied up in divorce proceedings, or, if Sally is held responsible for a serious accident, a victim could put liens on the property. Finally, if Joan wants to sell her place, she now needs Sally's consent to do anything. I told Joan these are all scenarios that may not happen, but lawyers have to tell their clients about all the bad things that could happen since most people believe it happens only to everyone else.

6. Reverse inheritance tax consquences: I told Joan that if Sally predeceased her for some reason, then the one-half of the assets given away that return to Joan as the surviving tenant will be subject to a 4½% inheritance tax, since Sally is a child older than age 21. I have seen this happen before, and it is devastating to the parent.

7. Consider alternatives: I confided in Joan that she really needs a good attorney to get proper advice before proceeding with adding Sally to the accounts and deed. I told her she might want to consider having the accounts setup for transfer on death to Sally, so they go right to her outside the Will. I advised her to just keep the house in her own name and go through probate, so she can keep control of it until she sells it or passes. Joan could prepare a financial power of attorney for Sally to handle her affairs if she became incapacitated, which is a lot easier than putting Sally on the accounts and deed. I then made some calls and sent Joan to an estate attorney who was recommended to me in the Reading area. Joan seemed overwhelmed by all my observations but was relieved that she talked to me and was put in touch with an attorney who could help her.

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Question 2: Recently, one of my clients wanted to give $100,000 to his son to help him purchase a new Ferrari. He asked me if he had to pay gift taxes on the gift to his son since it exceeded the annual gift tax exclusion.

Answer: My first question to my client was, "Why in the world would you even consider giving $100,000 to your son for a supercar?!" My subsequent response was that generally, no tax will be due. Here is why: Every individual is eligible for a lifetime estate and gift tax exclusion, which started in 2018 at $11.2 million, as amended by the Tax Cuts and Jobs Act of 2017. The annual exclusion for a gift to any individual is $15,000 in 2018. This means that you can give up to $15,000 to any individual in 2018, and it does not count toward your lifetime exclusion of $11.2 million. Since my client gave $100,000 to his son, he gets a free pass for the first $15,000 of his gift, and the remaining $85,000 must be applied toward his lifetime exclusion, thereby reducing it from $11.2 million to $11.115 million.

A married couple can give up to $30,000 ($15,000 for each spouse) to any other individual without having to reduce the lifetime exclusion for either spouse. Therefore, for individuals with less than $11.2 million or couples with less than $22.4 million in assets, the only obligation for making a large gift is the requirement to file a gift tax return reducing your lifetime exclusion, but you will never have to pay a tax. One caveat is that gifts paid to an educational institution for someone's tuition or payment of someone's medical expenses are subject to an unlimited exemption. So, if you are lucky enough to have over $11.2 million to give away someday, you may want to consider paying for tuition or medical expenses for your relatives first. For those residing in Pennsylvania, there is not a state gift tax to worry about, but if you give away more than $3,000 to someone less than one year before your passing, the amount in excess of $3,000 will be included in your estate for inheritance tax purposes and subject to a tax as high as 15%, depending upon the class of the beneficiary of the gift. This is the so-called called "anticipation of death rule."

Circling back to my client, he gave his son the $100,000 for a Ferrari provided that my client can use it on Sundays to go shopping. Hmm... Is that a retained interest which may result in an incomplete gift? We will save that issue for another day. Feel free to email me your gift tax question or suggest any other question to considered as a Blitz question of the month.

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As Chief Gift Planning Officer of the Masonic Villages in Pennsylvania, Alvin H. Blitz, Esq., serves the Masonic Charities of the R. W. Grand Lodge of Pennsylvania, which consists of the Masonic Villages, the Masonic Children's Home, the Pennsylvania Masonic Youth Foundation, the Masonic Library and Museum of Pennsylvania and the Masonic Charities Fund. Attorney Blitz holds a Bachelor of Science degree from the University of Scranton, a Master of Arts degree from Fairleigh Dickinson University, and a Juris Doctorate from Dickinson School of Law. He has given estate planning seminars throughout the country and is a member of Carlisle Lodge No. 260, Carlisle, Pa.

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