CUMMINGS & LOCKWOOD LLC

2023 PRIVATE CLIENTS GROUP ANNUAL UPDATE

December 14, 2023

It is hard to believe another year has passed and, as is customary, we are writing our annual letter to provide you with an update on various tax and estate planning issues and to highlight some items which may be of interest.

As has been the case for the last several years, we are still in a state of uncertainty regarding potential changes in the tax law. Although there is no comprehensive tax bill looming as we write this letter, many of the proposed tax law changes from prior years remain on the table for lawmakers to revisit in due course. We will, of course, endeavor to keep you posted on those developments in future updates as warranted.

The balance of this letter covers some tax and non-tax topics we believe are relevant to many of our clients and will end with a review of gifting issues you may wish to consider in the coming year.

CURRENT AND FUTURE FEDERAL ESTATE, GIFT AND GST TAX RATES AND EXEMPTIONS

Year	Exemption	Tax Rate on Excess
2023	$12,920,000	40%
2024	$13,610,000	40%
2025	$13,610,000*	40%
2026	$ 5,490,000*	40%

*as indexed for inflation

Under the federal gift tax laws, individuals can give a certain amount annually ($17,000 in 2023) to any number of people without exhausting any portion of their lifetime exemption from estate and gift tax. This “annual exclusion” amount is indexed for inflation and is set at $18,000 in 2024.

RECAP OF CHANGES AFFECTING RETIREMENT ASSETS

Recent changes to Retirement Plan rules: As a reminder, the Setting Every Community Up for Retirement Enhancement (“SECURE”) Act, enacted at the end of 2019, significantly changed the rules for inherited retirement accounts, including increasing the required beginning date for a plan participant/account owner to age 73 as of January 1, 2023.

Retirement account owners who have reached age 70½ can transfer up to $100,000 (indexed for inflation for the first time beginning in 2024) each year from their IRA directly to a qualified charity or charities and that distribution will be tax-free and count towards the required minimum distribution amount for that calendar year. Under the SECURE Act, account owners of that age also can make a one-time qualified charitable distribution up to $50,000 to fund a charitable gift annuity.

From an estate planning perspective, the most notable change under the SECURE Act was to require beneficiaries of IRAs inherited after the adoption of the Act, other than a surviving spouse, to draw down the entire account balance no later than the last day of the 10th year following the participant/account owner’s death, rather than over the beneficiary’s life expectancy. Although the Act, as written, did not include schedule for required distributions during the 10 year period, regulations proposed by the IRS in 2022 interpret the statute to require

annual distributions of a minimum amount based on the beneficiary's life expectancy and to require that the entire balance of the account be withdrawn by the earlier of the end of year 10 or the final year of the beneficiary's life expectancy. These proposed regulations would apply to accounts for which the original account participant died after the beginning date for his or her required distributions. There are some exceptions for minor children of the participant (whose 10 year draw down window begins when they reach the age of majority), disabled or chronically ill beneficiaries, and beneficiaries not more than 10 years younger than the deceased owner.

CORPORATE TRANSPARENCY ACT

Recent regulations implementing the U.S. Corporate Transparency Act require most companies, including limited liability companies and corporations, to file a report with the Financial Crimes Enforcement Network (FinCEN) of the U.S. Department of the Treasury identifying the company's ultimate beneficial owners. The beneficial ownership will not be publicly available and is generally available only to law enforcement and, in certain limited circumstances, financial institutions (in lieu of requesting the same information from the company directly).

It is likely that the persons managing or otherwise running any companies formed with the help of Cummings & Lockwood will be required to report their company's beneficial owners to FinCEN. The obligation to report will be on the companies and those persons in substantial control.

These regulations take effect on January 1, 2024 with respect to any company formed on or after that date. However, such regulations also require each non-exempt company formed prior to such date to file a report identifying their beneficial owners.

Filing exemptions are generally available to companies that are otherwise highly regulated (e.g., banks, publicly traded companies, registered investment advisors and broker-dealers and "large" operating companies with more than 20 full-time employees and more than $5 million in annual recorded gross receipts or sales on the prior year's tax return).

The regulations do not distinguish by purpose or complexity. Most of the entities formed with the help of Cummings & Lockwood will not fall under an exemption. It is likely that most of the companies identified below will be required to report their beneficial ownership to FinCEN:

- Entities formed to hold real estate (whether for rental, lease or personal use)
- Entities formed to manage publicly-traded securities or hold private equity investments
- Entities formed to hold tangible assets (e.g., horses, boats, artwork)
- Entities formed to run consulting businesses
- Entities formed to run family businesses
- Entities that are family offices
- Entities that have only one member or shareholder
- Entities that have only immediate family as members or shareholders
- Entities that only have trusts as members or shareholders

Please do not hesitate to contact your Cummings & Lockwood attorney if you have any questions or need our assistance in complying with the Corporate Transparency Act regulations, including what information must be filed and whether protective changes to your organizational documents are warranted.

CONSIDER ESTABLISHING AND FUNDING YOUR REVOCABLE TRUST NOW

As we did last year, we are again highlighting the advisability of creating and funding a Revocable Trust (sometimes referred to as a "Living Trust" or a "Revocable Living Trust") to help streamline the management of your assets should you become incapacitated and at your death. Delays in the courts, brought on by and made worse by Covid shutdowns, continue and these delays make the Revocable Trust structure even more valuable as

a way to avoid or reduce court involvement in settling your affairs.

A Revocable Trust is a popular and effective multi-purpose trust that will operate very differently at three distinct points in time:

1) While you are alive and capable of managing your affairs, you generally will be the sole beneficiary and the sole trustee or a co-trustee with your spouse of your Revocable Trust. During this time, your Revocable Trust serves simply as your "alter ego," and you control and use the trust property much the same way you would without the trust.

2) If you become incapacitated, your named successor trustee steps in to manage the trust assets on your behalf. You remain the trust beneficiary and trust assets remain available for your use and care.

3) After your death, your Revocable Trust acts like a Will by disposing of the trust funds to or for the benefit of your named successor beneficiaries. This use of Revocable Trusts is becoming more important as we are seeing increasing probate and surrogate's court delays in processing and effectuating Wills.

When someone dies without first establishing and funding a Revocable Trust, assets in the decedent's name which pass under the decedent's Will are essentially frozen until the Will is accepted and the named executor officially appointed by the court. Delays of several weeks to several months may occur. On the other hand, assets held in the name of a Revocable Trust at death may be managed by the trustees promptly after death. This allows the trustees to immediately respond to market and other economic factors to preserve and safeguard assets. This is particularly important when market conditions are volatile and the need to quickly access and manage investments becomes crucial to preserving the value of the assets.

There are other benefits to using a Revocable Trust arrangement and funding it before death, including minimizing court oversight and expense, keeping the terms of the estate plan more confidential, potentially reducing the likely success of any challenge to the estate plan and avoiding state income tax in some instances. There essentially is no downside to using the Revocable Trust structure. If you already have a Revocable Trust but have not yet transferred your assets into the name of your trust, you should discuss doing so with your Cummings & Lockwood attorney at your next periodic estate planning review. Likewise, if you do not have a Revocable Trust but would like to explore creating one, please ask your Cummings & Lockwood attorney for our client memo on the subject and any additional information relevant to your particular situation.

SELECTING A FIDUCIARY TO ADMINISTER YOUR ESTATE AND TRUSTS

Following an individual's death, his or her assets will be collected, debts paid, business affairs settled, necessary tax returns filed, and assets distributed as the deceased individual (generally referred to as the "decedent") directed. These activities generally will be handled on behalf of the decedent by a person acting in a fiduciary capacity, as an "executor" (in some states called a "personal representative"), an administrator or a "trustee," depending upon how the decedent held his or her property and whether or not he or she had a Will. The appointment of a fiduciary is crucial to the successful administration of an estate or trust.

Summary of a Fiduciary's Responsibilities: Executors and trustees generally are required to perform various duties involving the distribution and administration of property, which may involve some or all of the following:

- Understanding and implementing the terms of the Will or trust
- Knowledge of the applicable state and federal laws governing the Will or trust
- Filing the current Will with the probate court
- Locating, collecting, securing and appraising all estate or trust assets
- Confirming that there is sufficient insurance coverage for all assets
- Handling the payment of debts and expenses and settling creditors' claims against the estate or trust

- Locating heirs and beneficiaries and funding any bequests
- Managing the estate or trust, including record keeping, investment management, and collection of dividends and interest
- Obtaining a new tax identification number, preparing all necessary tax returns, and paying all taxes in a timely manner
- Preparing a detailed final account for presentation to the probate court
- Distributing the estate or trust corpus, settling business affairs and closing the estate

Selecting a Fiduciary: When selecting an executor or trustee, it is important to take into account the many responsibilities inherent in the position. With many small estates, the fiduciary's responsibilities may be straightforward and the designation of a family member may be appropriate. However, larger estates are often much more complex and require extensive knowledge of and experience with estate and trust administration.

Who Can Act as a Fiduciary: Fiduciaries can include family members, non-family members such as friends or colleagues, business advisors, accountants, attorneys, investment advisors, banks and trust companies.

A family executor or trustee may be appropriate in the case of smaller and less complicated estates and trusts, particularly where it is expected that the fiduciary will be assisted by an experienced trusts and estates attorney.

Occasionally there will be a family friend or a business associate available and willing to act as a fiduciary or as a co-fiduciary with a family member. Assuming that the individual is well-acquainted with the process of estate settlement and trust administration, this can be an ideal arrangement.

A trust company or a bank with a trust department can provide all of the administrative and investment services necessary for the efficient settlement of an estate and management of ongoing trusts.

An estate planning attorney who knows the client's goals and wishes in establishing a particular estate plan, as well as the client's family members and the client's financial or business interests also may be a good choice for a fiduciary. Although an attorney may be named as a sole fiduciary, often he or she serves as a co-fiduciary with a surviving spouse or other members of the client's family. If long-term trusts are created for the client's children, those children often become co-trustees with the attorney when they reach an appropriate age of maturity.

GIFTING CONSIDERATIONS FOR 2023-2025

As outlined at the beginning of this letter, under current law, the estate, gift and GST exemptions are scheduled to be reduced at the end of 2025. For clients who have not yet used their lifetime gifting exemptions, these historically high exemption amounts make this an excellent time to consider making lifetime transfers to "lock-in" the remaining exemption before the phase out.

- Connecticut has a separate state gift tax and the Connecticut gift and estate tax exemption now matches the federal exemption of $12,920,000 in 2023. This means that if a Connecticut resident who has not used gift tax exemption in the past makes a $12,920,000 gift to take full advantage of the federal gift exemption available in 2023, no Connecticut gift tax will be due. The Connecticut exemption will continue to match the federal exemption, whether it increases or decreases, going forward. Remember that gifts of real property and tangible personal property located outside of Connecticut are not subject to Connecticut gift tax and do not use Connecticut gift tax exemption. Conversely, gifts by non-Connecticut residents of real property and tangible personal property located in Connecticut are subject to Connecticut's gift tax.
- New York does not have a gift tax but does have an estate tax with an exemption of $6,580,000 in 2023. This means a New York resident who has not used any federal gift tax exemption in the past can gift up to $12,920,000 during 2023 and pay no gift tax at all, while the same transfer at death would incur roughly $1,534,000 of New York estate tax. (However, note that gifts made within three years of death are brought back into a New York resident's taxable estate for calculating New York estate taxes.)

- Florida has no separate state gift or estate tax.

When making gifting decisions, remember to consider capital gains and state tax implications. For example, under current law, gifting can result in a trade-off of capital gains tax savings versus estate and gift tax savings because the gifted assets retain the donor's cost basis and would not qualify for a stepped-up basis at death.

WHY SHOULD CONSIDER GIFTING BEFORE THE END OF 2025 OR SOONER IF ONE FEARS TAX LAWS MAY CHANGE BEFORE THEN?

- Clients who are certain they will never need the gifted assets and can maintain financial independence without those assets and the income they may generate.
- Clients who believe the property they gift will appreciate in value before death.
- Clients who believe and are willing to proceed on their belief that federal tax exemptions soon will be reduced below the current level for a prolonged period of time.
- Clients who are willing to gift the entirety of their exemption now, or at least the majority of it. Because the exemptions may be decreased later, you must give enough now to use what might be taken away. For example, if you have $12,920,000 in exemption and use $4,000,000 on gifts now, and the exemption is later reduced to $5,000,000, you will only have $1,000,000 of exemption left after the reduction. The $4,000,000 you use in gifts now will be applied against whatever exemption is left after the reduction. In other words, the gift will not be taken "off the top" of the higher exemption amount; it will simply be applied to whatever lower exemption exists later. That means making large gifts now is the only way to capture or "lock in" the difference between the historically large exemption amount, and whatever reduced exemption may be in place.

IN CONCLUSION

We recognize changes to tax laws may come at any time. We continue to monitor federal and state tax law developments as well as other trust and estate law proposals and post alerts on our website (www.cl-law.com) with any major developments, as well as a summary of the relevant provisions of any final tax law that is enacted. As always, please feel free to contact your Cummings & Lockwood attorney with any questions.

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