WINTER 2022

Disability Planning with ABLE Accounts Made More Attractive in 2022

Increased Tax Exemptions in 2022

An Estate Planning Cautionary Tale

planning matters

PRACTICAL INSIGHTS INTO ESTATE PLANNING & WEALTH PRESERVATION

Compliments of Lindabury's Wills, Trusts & Estates Group

LINDABURY

McCormick, Estabrook & Cooper, P.C.

Attorneys at Law

You're thinking about succession planning, **and so are we.**

Lindabury, McCormick, Estabrook & Cooper has you and your family covered. The attorneys in our Wills, Trusts & Estates group have experience levels ranging from 10 to 40+ years in the field of estate planning and estate administration.

MEET THE PLANNERS

John R. Blasi, Esq.
Westfield
jblasi@lindabury.com

James K. Estabrook, Esq.
Westfield
jestabrook@lindabury.com

David G. Hardin, Esq.
Summit
dhardin@lindabury.com

Mary Patricia Magee, Esq.
Red Bank
mmagee@lindabury.com

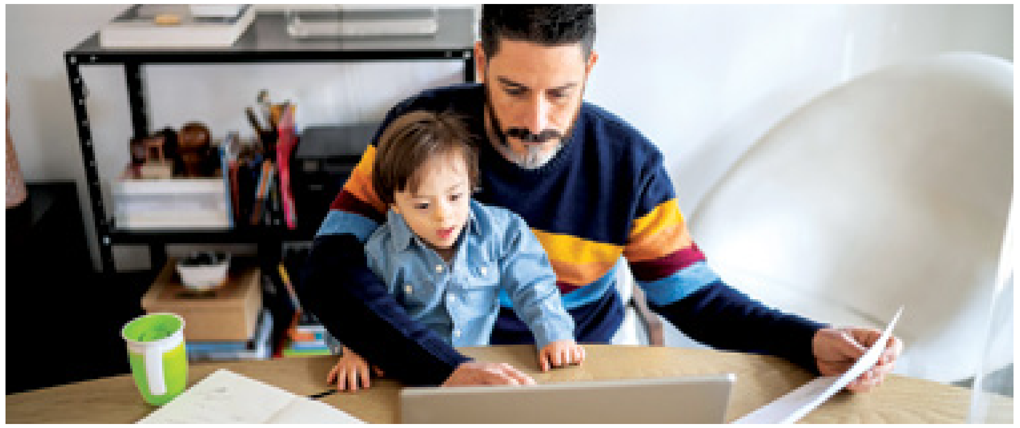
Elizabeth Engert Manzo, Esq.
Westfield
emanzo@lindabury.com

Lauren Mulcahy, Esq.
Westfield
lmulcahy@lindabury.com

Elizabeth Candido Petite, Esq.
Westfield
epetite@lindabury.com

Anne Marie Robbins, Esq.
Westfield
arobbins@lindabury.com

Maggie Spaziani, Esq.
Red Bank
mspaziani@lindabury.com



disability planning with ABLE accounts made more attractive in 2022

by Elizabeth Engert Manzo, Esq., CELA

While many may be familiar with Special Needs Trusts, some are still not familiar with tax-free Achieving a Better Life Experience (ABLE) savings accounts which were created under a 2014 federal law and currently available in New Jersey (and 46 other states). Funded correctly, ABLE accounts permit disabled individuals and their families to save money for disability-related expenses without compromising eligibility for needs-based benefits such as SSI, Medicaid, and other education, housing, health and food stamp benefits (such as FAFSA and SNAP). To establish an account, the designated beneficiary (and owner) of an ABLE account must be legally blind or have a medical disability that occurred prior to age 26. While interest earned on the account is tax-free, ABLE accounts with assets up to and including $100,000 are disregarded as a resource for SSI purposes. Distributions from the ABLE account may be made only to or for the benefit of the disabled individual for "qualified disability expenses," which broadly include education, housing, transportation, assistive technology, health and wellness, legal and funeral expenses, etc. Starting in 2022, and for the first time in four years, annual contributions to an ABLE account increased to $16,000 (matching the 2022 annual gift tax exclusion amount). While ABLE account balances are subject to Medicaid estate recovery upon the death of the disabled beneficiary, in certain disability planning circumstances the utilization of an ABLE account, either alone or in conjunction with a Special Needs Trust, may be an integral part of smart disability planning.

increased tax exemptions for 2022

by Anne Marie Robbins, Esq.

The federal estate and gift tax exemption (known as the "basic exclusion amount") has increased to $12.06 million per taxpayer in 2022. The exemption in 2021 had been $11.7 million. The increase means that in 2022, an individual can make gifts during life or at death totaling $12,060,000 without incurring gift or estate tax; a married couple can transfer $24,120,000 of assets. The annual gift tax exclusion has also increased, to $16,000 per donee (or $32,000 if spouses elect gift-splitting).

The gift tax annual exclusion for gifts to non-citizen spouses has also increased in 2022, to $164,000.

Note that the estate and gift tax exemption is slated to be reduced to $5 million, indexed for inflation, as of January 1, 2026. With this known reduction in the exemption approaching, we recommend consulting with your estate planning attorney to discuss possible strategies to take advantage of the large exemption presently available.

Smaldino v. Commissioner

an estate planning cautionary tale

by Margaret Spaziani, Esq.

A recent Tax Court case, *Smaldino v. Commissioner,* T.C. Memo. 2021-127 (November 10, 2021) emphasizes the need to ensure that the phases of transactions are completed properly and certain formalities are observed in order for an estate planning strategy to be successful. It is important to be careful even (and perhaps especially) in the case of emergency planning (i.e., planning because of health scares or impending tax law changes).

In the *Smaldino* case, rushed planning caused a tax deficiency that may have been avoided with a team of advisors working together to ensure that Mr. and Mrs. Smaldino's plan was properly implemented.

Mr. and Mrs. Smaldino were married in 2006. Mr. Smaldino had 6 children from a prior marriage and 10 grandchildren. Mr. Smaldino was a CPA turned real estate investor, with a real estate portfolio worth approximately $80 million. Mrs. Smaldino held a master's degree in economics and had worked in her husband's business for many years.

In 2003 Mr. Smaldino established Smaldino Investments, LLC, of which Mr. Smaldino was a member, as well as a revocable trust called the Smaldino Family Trust. In 2012 when he was 69, Mr. Smaldino had a health scare and transferred interests in 10 different parcels of real estate into the LLC. The LLC interests were then contributed to the Smaldino Family Trust.

The LLC's operating agreement distinguished a "Member" from an "Assignee." Mr. Smaldino was a member of the LLC; Mrs. Smaldino was not a member.

The LLC's operating agreement differentiated the assignment of economic rights in the LLC from the transfer of membership interests. It stated that "no member" was entitled to transfer or assign any part of the member's ownership interest "except as expressly provided for in Section 11.5(c)." Section 11.5(c) provided for transfers of membership interests without prior board approval only to (1) other members and (2) to trusts created for the benefit of a member's descendants.

On December 21, 2012, Mr. Smaldino established the Smaldino 2012 Dynasty Trust for the benefit of his children and grandchildren. On April 14, 2013, Mr. Smaldino transferred approximately 41% of LLC interests to Mrs. Smaldino. Mr. Smaldino's transfer to Mrs. Smaldino was not among the types of transfers expressly provided for in Section 11.5(c) of the operating agreement. Therefore, Mrs. Smaldino was an assignee of the LLC interests and not a member. The very next day, Mrs. Smaldino gave those same LLC interests to the Smaldino 2012 Dynasty Trust. The transaction was an attempt to use Mrs. Smaldino's federal estate and gift tax exemption in order to shelter a gift to the Dynasty Trust from federal gift tax. Mrs. Smaldino reported the gift to the Dynasty Trust on a Gift Tax Return and allocated her estate and gift tax exemption to the gift.

However, the Tax Court recharacterized the gift Mr. Smaldino made to his wife followed by her gift to the Dynasty Trust as if Mr. Smaldino **himself** had made the gift directly to the Dynasty Trust, deeming Mrs. Smaldino as no more than a straw person. Because Mr. Smaldino did not have sufficient exemption remaining to shelter the gift from the tax, the IRS assessed Mr. Smaldino a $1,154,000 gift tax deficiency, which was upheld by the Tax Court.

It is important to be careful even (and perhaps especially) in the case of emergency planning (i.e., planning because of health scares or impending tax law changes).

Some key steps that went wrong in *Smaldino*:

- Mrs. Smaldino held her LLC interests for only one day before she transferred those interests to the Dynasty Trust. The transaction may have passed muster had she waited longer. Some recommend a minimum of 30 days, others say 60 plus.
- Mr. Smaldino, who controlled the LLC, never amended the LLC documents to reflect that Mrs. Smaldino was the owner of some of the LLC interests. When a donee receives an interest in an LLC or other entity, the governing legal documents should reflect the change in ownership.
- Mrs. Smaldino was never formally recognized by the LLC as a member. The LLC documents made a distinction between an assignee and a member. Mrs. Smaldino was not a member of the LLC and arguably did not have the power to transfer her LLC interests according to the operating agreement.
- Following Mrs. Smaldino's transfer of interests to the Dynasty Trust, the LLC operating agreement should have been amended to reflect the Smaldino Dynasty Trust as owner.

The *Smaldino* case is a cautionary tale to ensure that the various phases of a plan are carried out in the proper order. If entities such as LLCs and partnerships are involved, corporate and partnership formalities should be observed. Transferors should have the authority under the documents to make any contemplated transfers. Transferees should be determined to be appropriate recipients of assets or interests **before** the transfers take place.

In the current estate planning climate, where large gifts are being made to spousal lifetime access trusts (SLATs) and other entities, it is extremely important to ensure that the components of a plan occur in the proper order in order to avoid a recharacterization similar to what occurred in *Smaldino v. Commissioner.*

LINDABURY

McCormick, Estabrook & Cooper, P.C.

Attorneys at Law

New Jersey | New York | Pennsylvania

lindabury.com

If you or your clients have questions about the issues discussed in this newsletter please contact a member of Lindabury's Wills, Trusts & Estates group. This newsletter is distributed to clients and professional contacts of Lindabury, McCormick, Estabrook & Cooper as a professional courtesy. The information contained in this newsletter is necessarily general and not intended as legal advice or as a substitute for legal advice. Any estate planning program should be undertaken only after consultation with a professional and an assessment of the relevant considerations.