Estate Planning for Same Sex Couples

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Estate planning for same sex couples presents special considerations. The estate planning goals of gay and lesbian couples are the same as those of heterosexual couples, but unfortunately, current aspects of Federal and state law present obstacles to the achievement of those objectives by same sex couples. Individuals usually desire that at death, their assets pass to their loved ones in a manner that is quick, easy, and results in the least amount of taxation. Estate taxation is particularly onerous for gay and lesbian couples if a proper estate plan is not established.

In the United States v Windsor discussed later on in this article, the Supreme Court determined that the federal government must recognize all marriages validly performed no matter who the parties to the marriage are, same sex or opposite sex couples. On October 21, 2013, Governor Christie signed a bill which allowed same sex marriages in New Jersey as of that day. Despite the Windsor case and the passage of the bill legalizing marriage, many same sex couples are still in civil unions or domestic partnerships. Furthermore, many long term same sex couples are not in any form of legal union. Therefore, while it is important for everyone to take steps to ensure that his or her lifetime intentions are enacted at the time of

death, it is especially crucial for gay and lesbian couples to plan proactively and with counsel both sensitive to and familiar with their needs.

CONTROL ISSUES

A significant problem facing gay and lesbian couples is that each member usually desires to benefit his or her partner, but often meets with or anticipates resistance from family members. At present in New Jersey, the law favors blood relatives, unless partners are legally married, have registered as Domestic Partners under the New Jersey Domestic Partnership Act [P.L. 2003, c. 246 (26:8A-l et seq.), as amended] or have entered into a Civil Union [P.L. 2006, c.103 (37:1-30, et seq.)]. A discussion of these "Acts' impact on estate planning will follow as issues are presented. There are a number of important estate planning documents every individual should have, but these are even more crucial for gay and lesbian individuals, whether or not they have entered into a legal marriage, civil union or domestic partnership.

1. LAST WILL AND TESTAMENT

A Last Will and Testament provides for the legal transfer of assets after death, names a person to settle the estate, names a trustee to administer any trust established and names a guardian for any minor children. A Will is the first but not the only estate planning document to be considered. The legal term for not having a Will at the time of death is "intestacy." In this situation, the state writes a Will for the decedent, and state law controls which individuals become beneficiaries of the estate and which individuals administer the estate. The intestacy laws in New Jersey now take into consideration gay and lesbian relationships, but only for those couples who have legally married, entered into registered a Domestic Partnership or Civil Union. New Jersey's intestacy law now provides that assets go to spouses, domestic partners and civil

union partners as well as children and blood relatives in certain combinations, depending on the facts. See NJ.S.A. 3B:5-4. However, nothing exists under New Jersey intestacy law that provides for a lifetime partner to inherit any property, unless the parties registered their domestic partnership prior to its sunsetting in February, 2007 or entered into a Civil Union or marriage. Therefore, if a person dies without a Will and has not formalized his or her relationship, his or her partner would receive nothing under New Jersey's intestacy law. Additionally, even if registered, a domestic partner or partner in civil union sits in the same position as would a husband or wife, potentially being forced to share in an estate with children of the deceased partner. Therefore, for the practitioners, discussions of the benefit of entering into Civil Unions have become an integral part of estate planning and knowledge of the Civil Union law and the process for formation is essential.

Furthermore, without a Will, a person cannot designate an Executor, Trustee or Guardian. If a person dies without a Will, the statute designates who will fill these positions. [See NJ.S.A. 3B: I 0-2] The statute lists blood relatives over unregistered gay or lesbian domestic partners. Again, an amendment took effect on January 12, 2006, permitting a registered domestic partner equivalent status to a spouse in an Administration proceeding and the Civil Union law treats partners in Civil Union similarly, but without making a Will even a registered domestic partner or partner in civil union is not assured of appointment as a Trustee or Guardian in an Administration proceeding. Therefore, under current law, a surviving unregistered partner will not be the person handling the administration of the estate without litigation and a court willing to set aside the statutory preferences. A surviving unregistered partner may not be able to plan funeral arrangements and may not even be invited to attend the funeral [see N.J.S.A. 45:27-22 and 3B:10-21.1]. In addition, absent a Last Will and Testament, the courts will favor biological

family members over any partner as a guardian for minor children whom the survivor has not adopted or by some other litigation process has been deemed the parent of the children. Guardianship of minor children remains a statutory requirement of placement with a child's surviving biological parent, regardless of their prior involvement, leaving a surviving same-sex partner, registered or unregistered, to seek, probably at best psychological parent status to secure even parenting time rights.

There are steps that can be taken to prevent these problems from occurring. The first step is to have a Will. The Will should address who has authority to make funeral arrangements [see NJ.S.A. 45:27-22 and N.J.S.A. 3B:IO-21.1], which requires such designations be made in a Will and not in any other writing as prior law permitted], intentions for jointly held property and it should appoint a trustee and a guardian for minor children.

Additional amendments to the Domestic Partnership Act and provisions of the Civil Union law include, notably to this topic, the inclusion of registered Domestic Partners and partners in Civil Union in respect to elective share claims. Registered domestic partners and partners in civil union may claim an elective share as would a spouse and so careful drafting and planning is required to assure that the testator has considered the ramifications of failing to leave their domestic partner/partner in civil union sufficient assets to meet the requirements set forth in N.J.S.A. 3B:8-1, et. seq. Further, for a couple registered or civil unioned in New Jersey, who later move to another state leaving property in New Jersey, N.J.S.A. 3B:8-2 applies the elective share law of the resident state therefore a surviving registered domestic partner or partner in civil union may be protected if their partner dies a resident of New Jersey, but not protected if he/she dies a resident of another state that will not recognize the domestic partnership or civil union.

A concern for gay men and lesbians who have a Will is the possibility that a family member can challenge it as invalid. Generally, a person challenging a Will must prove a defect in execution. Examples of execution defects include that the testator was not of sound mind at the time the Will was executed, the testator was under duress or undue influence, or that the Will was a product of fraud. The burden of proof is on the person challenging the Will, unless the claim is one of undue influence- there the burden shifts quickly to the person with the confidential relationship to the Testator who the family claims exerted the undue influence. If a Will is challenged, a court must decide the outcome. Certain precautions should be taken in anticipation of a challenge:

a) Execute a Will early on in life before competency becomes an issue. This point is magnified if a person suffers from a serious illness;
b) Specify in a Will which family members are being disinherited and why;
c) Do not have a partner present in the room when a testator executes a Will;[1]
d) Do not have a partner be a witness to the signing of the document;
e) Be honest with family members during life with respect to sexual orientation, relationships, and dispositive intentions.

We note that, generally, New Jersey law does not consider a spouse a confidant such that a claim of undue influence would shift the burden of proving no undue influence to the spouse. As no such case law exists to deal with the issues of registered domestic partners or partners in civil union, the litigator much look to Lewis v. Harris, 188 N.J. 415, 463 (2006), to argue that

[1] Opinions differ on this issue, as husbands and wives have confidential and often adverse interests in estate planning and attorneys usually permit married couples to execute documents together. This should be discussed with the client to determine whether their sensibilities will be offended by forcing them to deal separately. An attorney's notes should reflect the discussion if the documents are to be executed concurrently.

said couples have the same relationship as their heterosexual counterparts in respect to presumptions that there can be no undue influence assumed when leaving property to each other in their wills.

Careful documentation of the client's assets and family structure are also helpful in proving testamentary capacity. We have the client complete a very detailed information sheet, which will certainly prove they a) know the extent and general composition of their assets and b) know the "objects of their bounty," the two traditional pillars of testamentary capacity. My firm is careful never to destroy these files, no matter how old, in the event of a future contest.

2. TRUSTS

There are two types of trusts, inter vivos and testamentary trusts. Living Trusts (also known as inter vivos trusts) are established during life. Assets are transferred into a Living Trust at the time of its creation, and the trust operates during a person's lifetime. On the other hand, testamentary trusts are created in a Will and become operative at the time of death. Pour-over trusts are created while a person is alive but can be funded at death.

Another important characteristic of a trust is its permanency. A trust can be considered to be revocable or irrevocable. With a revocable trust, the person establishing the trust (hereinafter referred to as "the settlor") reserves the right to amend or revoke the trust, change the conditions under which the assets are held, or reclaim the assets for his or her own use. Because a revocable trust is distributed in accordance with the terms of the trust, it is not subject to the jurisdiction of the probate court upon death. This makes revocable trusts an important estate planning tool for people who seek to avoid probate.

In contrast to a revocable trust, in an irrevocable trust, the settler relinquishes rights to the assets in the trust. The settler cannot alter the terms of the trust at a later date. Assets

placed into irrevocable trusts not only avoid the jurisdiction of the probate court, but they sometimes are removed from the gross estate for estate tax purposes. This makes irrevocable trusts a valuable tool for estate tax planning.

a) Revocable Trusts

One of the most common uses of a revocable trust is to avoid probate. At death, a Will has to be probated in the surrogate's office of the county in which the decedent resided. New Jersey is considered a probate friendly state (i.e. low cost and prompt processing and issuance of Letters Testamentary). Nevertheless, some people still desire to avoid probate. There are some benefits to avoiding probate. If there is a revocable living trust, at death, a successor trustee would distribute all of the trust assets to named beneficiaries without the supervision of the probate court. The process is quicker and more private, unlike probate, it is not a matter of public record. If assets pass through probate, anyone can go to the surrogate's office and read a copy of a Will. A living trust prevents this from occurring. For some gay and lesbian couples who like or need to keep their relationship private this is extremely important.

Revocable trusts allow individuals to avoid ancillary probate for real estate owned outside the state. A successor trustee is named to act, in essence, as an attorney-in-fact, or agent, in the event of incapacity. Many people operate under the mistaken assumption that revocable living trusts save taxes. They are essentially tax neutral. While there are many benefits of revocable trusts, such trusts will not reduce estate tax liability or state inheritance tax. The major benefit of a revocable trust for gay and lesbian clients is that it keeps their intentions private and may make it more difficult for a family member to hold up the administration of the estate.

b) Irrevocable Trusts

An irrevocable trust generally is used for estates in excess of the federal credit shelter amount (presently $5,430,000) and/or the New Jersey exemption amount of $675,000. The benefits of most irrevocable trusts are that the assets contained within the trust are usually excluded from the settlor's estate. The downside is that once the trust is established it cannot be altered, amended or revoked. For estates that exceed the credit shelter amount serious consideration should be given, to the use of irrevocable trusts. This is extremely important for our New Jersey clients. The New Jersey estate tax applies to estates exceeding $675,000. If a person has $675,000 of assets and a $325,000 term life insurance policy, their estate for tax purposes would be $1,000,000. This will trigger a New Jersey estate tax of $33,200. If the term life insurance policy was placed into an irrevocable trust, it could be removed from the decedent's New Jersey estate. Therefore, it could avoid the $33,200 of tax. At present, couples remaining in New Jersey registered domestic partnerships are still subject to the New Jersey estate tax, while those entering into Civil Union or legal marriages have acquired the “spousal” exemption from the estate tax.

3. DURABLE POWERS OF ATTORNEY

A power of attorney authorizes another person to act as an agent on your behalf for financial and business transactions. It usually gives a named financial agent access to bank accounts, brokerage accounts, the power to sell property, deal with insurance companies and handle any other financial transactions. Most people tend to give their agent broad authority; however, this is not required. An agent's power can be limited to specific acts. A power of attorney can be revoked at any time assuming the grantor of the power is competent.

Unless the document specifies otherwise, a power of attorney is effective upon execution. However, a document can be drafted that doesn't become effective until the principal becomes incompetent or disabled. If a power of attorney has a delayed, or "springing effect", it only becomes effective upon certain conditions set forth in the power. Couples who are not concerned about each other's trustworthiness may choose to make the powers effective immediately upon execution as a matter of convenience.

For gay and lesbian couples, a power of attorney has even greater significance. Presumably, one's life partner would be the preferred decision maker in the time of a crisis, but this choice must be planned in advance. Absent a power of attorney these decisions might be taken over by a family member who may not be supportive of alternative life styles. In the absence of a serious partner, consideration should be given to naming a friend or trusted advisor as agent.

Additionally, a well-crafted Power of Attorney can avoid the necessity for a guardianship proceeding in the event of long-term or permanent incapacity. Gay men and lesbians have had significant problems over the years obtaining the right to act as a guardian of an incapacitated partner. With amendments to the Domestic Partnership Act, and Civil Union Statutes, registered partners will no longer have those difficulties, as the Statute puts them on equal footing with a spouse and thus, priority for appointment [NJ.S.A. 3B: 12-25]. For unregistered partners, the problems still exist and blood relatives, even remote, might be counted closer in status to the incapacitated person that an unregistered domestic partner. We have included in our materials a sample Power of Attorney for both financial matters and health care matters. Note the provision in the financial power with reference to the Banking Law [Section 2 of P.L. 1991, c. 95, amending N.J.S.A. 46:2B-8 et seq.], which provides that a New Jersey banking institution may

decline acceptance of a Power of Attorney if it was executed over ten (10) years before presentation if the agent is other than a spouse. Note that the banking law was not expressly amended by the Civil Union law and the extension of the “spousal” recognition is not express to civil union couples. This requires gay and lesbian couples to continually "refresh" their Powers over the years. Further, any power of attorney that grants powers concerning children are limited by statute to six (6) months in duration, so they, too, need continual re-execution [N.J.S.A. 3B:1239].

4. HEALTH CARE POWER OF ATTORNEY AND LIVING WILL

A Health Care Power of Attorney, is a document that every person should have to prepare for the following situations:

a) Providing instructions for the conditions when life-sustaining procedures should be utilized;
b) Designating who will make appropriate health care decisions;
c) Ensuring that the individual chosen to make these decisions has access to the principal and his or her medical records during incapacity.

In the absence of a health care power of attorney, the medical profession sometimes ignores even family in decision-making. Therefore, it is imperative that everyone have a Health Care Power of Attorney and Living Will which designates to what extent life should be prolonged in the event there is no reasonable hope of recovery or regaining a meaningful quality of life. A health care power of attorney should stipulate what medical treatments should be provided, whether feeding tubes should be used, and whether organs are to be donated.

A health care power of attorney can designate a health care representative to make these decisions on behalf of the principal. If no health care proxy exists, hospitals might decide to turn to the biological family to make these decisions, thereby completely shutting out

domestic partners. It should be noted that the Domestic Partnership Act does provide for the following in this regard:

a) Registered Domestic Partners/Partners in Civil Union are authorized as a matter of law to give authorizations for treatment for their partners and to accompany them to the hospital and to have access to their partner in hospital.

b) Unregistered partners, stating they are domestic partners, are authorized to make emergency authorizations for treatment and to accompany the partner to hospital.

c) It is unknown the extent of recognition, training and acceptance of these provisions amongst New Jersey health care providers and first responders. Therefore a Health Care Power, even if registered partners, is essential.

d) These grants of authority under the Domestic Partnership Act are only recognized in New Jersey, except as other States with similar recognition of same-sex couples may have statutes that recognize New Jersey's law under their own. It is unclear of the status of registered domestic partners and partners in civil union in states in which same-sex relationships have been afforded similar recognition. For example, in Massachusetts, same-sex couples can marry. They do not recognize New Jersey civil unions as being equated with Massachusetts marriages, therefore, New Jersey visitors to the Bay State would most likely be without “spousal” benefits and recognition. In those situations where there might be statutory recognition, it will of course be unclear as to whether the average first responder or health care provider will understand or be willing to recognize the grant of authority without a Power.

A health care power of attorney also should specify which individuals have visitation rights in the hospital and to receive personal property taken from the patient. Absent a power of attorney, hospitals tend to look to biological families first to make this decision. Accordingly, it is possible for a family not to allow a partner to visit in the hospital. Gay and lesbian couples should consider giving their power of attorney a "priority of visitation" which gives a partner priority to visit them before anyone else, including the biological family members. See a sample Priority of Visitation Statement and Health Care Power of Attorney attached.

In addition, purchase of a prepaid funeral should be considered. Therefore, a couple can plan their own funerals. Otherwise, this decision might be entirely left up to the family, and a person may not be buried near his or her partner. Careful consideration should also be given as to

who has control of an individual's remains. If the intention is for a partner to be in control then this should be specified in a Will (see above).

5. DOMESTIC PARTNERSHIP ACT

On or about January 12, 2004, the Domestic Partnership Act (hereinafter "DPA") was enacted in New Jersey. Under the statute N.J.S.A. 26:SA-I to 10, same sex couples age 18 and older can go to any municipal hall and for a $28 fee register as domestic partners. With the enactment of the Civil Union law, new registrations after February 12, 2007 are restricted to couples over the age of 62, both same-sex and opposite-sex. No new registrations for younger same-sex couples are available. Domestic Partnership status provided a few of the rights of spouses to gay couples, as well as to unmarried heterosexual couples at least 62 years of age. They can sue under the state's antidiscrimination law, visit each other in the hospital, make medical decisions for an incapacitated partner, file joint state tax returns and avoid the New Jersey Inheritance Tax. The provision for older heterosexual couples to register as domestic partners permits them to enter into a legally committed relationship without jeopardizing their Social Security or pension benefits, or disrupting estate planning. The DPA acknowledges and provides for rights and obligations of domestic partners while they are in the relationship, but appears to limit the right to the division of property and the right to support upon the termination of the domestic partnership. Two specific sections which address these issues are as follows:

Section 4(b) -discusses the requirements for establishing a domestic partnership, which includes, the agreement by both parties to be jointly responsible for each other's basic living expenses during the domestic partnership.

Section 6(b) _ "upon termination of a domestic partnership, the domestic partners, from that time forward, shall incur none of the obligations to each other as domestic partners that are created by this or any other act."

Note: The Act does not address any support obligation upon termination of the domestic partnership, and it appears that all rights a domestic partner has or may have terminate automatically upon termination of the partnership.

Furthermore, Section 10(3) of the DPA provides that the "superior court shall have jurisdiction over all proceedings relating to the termination of a domestic partnership established pursuant to Section 4 of the DPA, including the division and distribution of property.

6. DOMESTIC PARTNERSHIP AGREEMENT

As the Domestic Partnership is now restricted to only senior couples now and for the future, we will restrict our comments on formation. We do note that practitioners must inquire as to whether clients have entered into pre-domestic partnership agreements that in any manner altered the rights and obligations of domestic partners under the Act. These should be reviewed for impacts on inheritance. The practitioner should also review the Domestic Partnership Act as it concerns equitable distribution issues – anecdotally, the Courts have been equitably distributing property in termination of domestic partnership matters, but the statute is clear that alimony is not authorized.

7. CIVIL UNION – PRE-CIVIL UNION AGREEMENTS

Same-sex couples entering into civil union may contract prior to the civil union, as would an opposite-sex couple, to limit the rights and obligations imposed by law upon them. As with their heterosexual counterparts, the pre-nuptial agreement or pre-civil union agreement may be used to alter statutorily required rights and obligations such as alimony, equitable distribution, etc. The estate planning practitioner must inquire as to whether the parties entered into any such agreement to properly evaluate planning and tax issues.

Whether to enter into a pre-civil union agreement may be one of the most difficult decisions for a gay or lesbian couple to make. While some may perceive that such an agreement indicates a pessimistic assumption that the relationship will eventually end, it is actually a mechanism for ensuring that assets will be protected if the relationship fails to work out. It is usually used in connection with a relationship that is expected to be long term.

People usually think of pre-civil union agreements as being signed early on in the relationship, certainly before the civil union has been solemnized. But in truth, they can be executed at any time during the relationship. It is never too late to sign an agreement. A civil union agreement should address certain categories of property in the agreement. The first category is the property each party brings into the relationship. Usually, the agreement stipulates that such assets are the separate property of the individual who owned them initially. The second category of assets is those received by inheritance or gift during the relationship. Usually, these assets also remain the property of the remaining partner. The third category is assets acquired during the relationship. Usually a civil union agreement stipulates that these assets will be divided equally or in proportion to each partner's contribution towards obtaining them.

In addition, a civil union agreement should specify the payment of debt, living expenses and medical expenses. Specific reference should be made to who is employed and who is paying for the medical benefit.

The enactment of the Civil Union law incorporated an amendment to the pre-marital agreement laws to include pre-civil union agreements [see N.J.S. 37:2-32]. Adherence to this statute is now required, as disputes will be tried in a court of equity and failure to make disclosures, to have separate counsel, to execute within a reasonable period of time of the marriage, etc., may lead to the voiding of an agreement more informally entered into. In other

words, the Courts may lean toward a position of "what's good for the goose is good for the gander," substituting straight couples and same-sex couples for proverbial goose and gander.

8. CIVIL UNION FORMATION

Civil unions are formed in exactly the same manner as marriages. Licenses are available from the municipal registrars. A license must be obtained in the home town of one of the parties if they are New Jersey residents or in the town where the ceremony is to be performed if neither are New Jersey residents. Any person authorized to perform a marriage ceremony may perform a civil union ceremony. Public officials who perform weddings are required to also perform civil unions [see Attorney General Opinion Letter, December 21, 2006] or face discrimination charges under the Law Against Discrimination. As with marriage, there is a 72 hour waiting period between the making of the application for a civil union license and the issuance of the license. If a client is ill and cannot wait that period – application may be made to the Superior Court for a waiver from the waiting period.

9. UNITED STATES v WINDSOR

In United States v Windsor, decided by the U.S. Supreme Court in June 2013, Section 3 of the Defense of Marriage Act (DOMA) was declared unconstitutional. In this case, a woman married in Canada to another woman was denied the same estate tax benefits that married couples receive. The benefits were denied under a federal law called the Defense of Marriage Act (DOMA), passed in 1996. DOMA's Section 3 defined a marriage for federal purposes being solely between a man and woman - hence, why the federal government denied Edith Windsor the death tax benefits in her marriage. In a 5-4 ruling, the court declared that Section 3 of DOMA is

unconstitutional. Thus, the federal government cannot fail to recognize an otherwise legal union between a same sex couple for purposes of interpreting and applying federal law.

The Windsor ruling also clarifies the meaning of marital terminology. The term "spouse" "husband" and "wife" include an individual married to a person of the same sex if the individuals are lawfully married under a state law. The term does not include registered domestic partnerships, civil unions or other formal relations recognized under state law. The ruling will be applied prospectively as of September 16, 2013.

After the Windsor Decision, the State of New Jersey on October 21, 2013 approved same sex marriages in New Jersey. Accordingly, same sex marriages began that day. Despite the recent development, many same sex couples are still in civil unions or domestic partnerships and have not legally married. Furthermore, many long term same sex couples are not in any form of legal union.

TAX ISSUES

1. FEDERAL ESTATE TAXES

To understand the estate planning considerations crucial to gay and lesbians, it is necessary to review how the estate tax system generally applies. An "estate" comes into being whenever any individual (or, "decedent") dies, owning any property. The term, "gross estate", includes all interests in property held by the decedent at the date of his or her death. See LR.C. Sections 2031, 2033. In addition, it can include various lifetime transfers, certain powers of appointment, annuity proceeds, life insurance proceeds and property interests with right of survivorship

The gross estate includes all assets owned by a decedent that are subject to probate, regardless of whether or not the decedent died with a valid will. See LR.C. § 2033. The probate

estate includes all assets that the decedent solely owned at the time of death, as well as any portion of an asset beneficially owned by the decedent at death, such as accrued interest, rent, or rights to declared but unpaid dividends. See Treas. Reg. § 20.2033-I(a)&(b). The term "gross estate" also includes non-probate assets. Frequently, individuals are led to believe that the federal estate tax can be avoided by titling assets so that they will pass outside of probate. However, the Internal Revenue Code establishes that the following assets are included in the gross estate:

(A) life insurance proceeds where the decedent owned the policy (I.R.C. § 2042);

(B) a survivor annuity which continues payments after the decedent*s death if the decedent paid for it (LR.C. § 2039);

(C) property owned as joint tenants with right of survivorship or tenants by the entirety (LR.C. § 2040);

(D) property that the decedent could have appointed for his or her own benefit, but did not appoint to his or her estate (LR.C. § 2041);

(E) property held in a revocable living trust (LR.C. § 2038);

(F) property transferred, but wherein the grantor retains the right to alter or revoke the beneficial ownership of the property (LR.C. § 2038); and

(G) the retention of a life estate in property (LR.C. § 2036).

In some instances, lifetime transfers may be recaptured in the calculation of the gross estate. The most notable situation arises when an insurance policy is transferred. If such policy is on the donor’s life and the transfer occurs within three years of death, the proceeds of that policy are included in the gross estate, even if the gift of the policy was exempt from gift tax due to the annual exclusion. See I.R.C. § 2035(a),(b)(2),(d)(2).

Federal law provides that every person is entitled to a credit shelter amount presently equivalent to $5,430,000. Any amounts over the credit shelter amount are subject to an estate

tax of Forty percent (40%). The government gives married individuals the benefit of an unlimited marital deduction. See I.R.C. § 2041. Therefore, any bequest made by one spouse to another is exempt from estate tax regardless of amount. However, this unlimited marital deduction is not available for a bequest made by a gay or lesbian person to a partner as a result of the Federal Defense of Marriage Act [28 U.S.C.A. § 1738C and I U.S.C .A. § 7]. Accordingly, if a person has assets in excess of the credit shelter amount then the federal estate tax will apply even if the assets are distributed directly to a registered domestic partner. However, in light of New Jersey now legalizing marriages among same sex couples, if a couple is legally married under New Jersey law then the unlimited marital deduction will apply for them in regard to their federal estate tax planning. In addition, a same sex couple that has legally married will be able to take advantage of the portability provision under federal law. Therefore, for the same sex couple who has married, they should be able to protect $10,860,000 without paying any estate tax.

2. **NEW JERSEY INHERITANCE AND ESTATE TAXES**

The State of New Jersey imposes two death taxes: (1) the New Jersey Transfer Inheritance Tax (hereinafter "inheritance tax") and (2) the New Jersey Estate Tax (hereinafter "NJ estate tax"). The former tax is assessed to the beneficiaries of an estate while the latter is assessed to the estate itself.

A) Inheritance Tax.

The inheritance tax is a transfer tax imposed on the transferee's right to receive a gift, devise, or bequest from a decedent. Unlike the estate tax, it is imposed directly upon the beneficiary, not the estate. However, for planning purposes, it should be noted that the personal representative of an estate, through a will, can be directed to pay this tax.

The tax is calculated after determining the value of property that may be received by a particular beneficiary against the relationship of the beneficiary to the decedent. As to this latter factor, the state establishes a different tax rate and amount of exemption, depending on the relationship of the beneficiary to the decedent.

(1) Classifications of Transferees.

The State of New Jersey created the following five categories of beneficiaries subject to the inheritance tax:

(a) Class A. Includes surviving spouses, domestic partners (as of date of registration), civil union partners, parents, grandparents, children, grandchildren, and any other lineal ancestor or descendant. This also includes registered domestic partners;

(b) Class B. Repealed;

(c) Class C. Siblings, as well as daughters-in-law and sons-in-law;

(d) Class D. More distant relatives and any other individuals not mentioned above; and

(e) Class E. Tax exempt charities and governmental bodies. Specifically, these transferees include the State of New Jersey and any political subdivision thereof; any educational institution, church, hospital, orphan asylum, public library or Bible and tract society or to, for the use of or in trust for any institution or organization organized and operated exclusively for religious, charitable, benevolent, scientific, literary or educational purposes, including any institution instructing the blind in the use of dogs as guides, no part of which inures to the benefit of any private stockholder or other individual or corporation; provided, that the exemption does not extend to transfers of property to such educational institutions and organizations of other states, the District of Columbia, territories and foreign countries which do not grant an equal, and like exemption of transfers of property for the benefit of such institutions and organizations of New Jersey. NJAC. 18:26-1.1.

(2) Inheritance Tax Rates

Pursuant to statutory law, the aforementioned beneficiaries are taxed at the following rates:

(a) Class A beneficiaries are completely exempt from the inheritance tax. N.J.S.A. § 54:34-2, et.seq.;

(b) Class C beneficiaries are each entitled to an exemption for the first $25,000.00. Thereafter, they are taxed at the following rates, pursuant to N.J.A.C. § 18:26-2.7:

Taxable Inheritance	Net Tax	% on Excess
$ 25,000.00	$ 0.00	11%
$ 1,100,000.00	$118,250.00	13%
$ 1,400,000.00	$ 57,250.00	14%
$ 1,700.000.00	$199,250.00	17%

(c) Class D beneficiaries are entitled to an exemption of $499.00 each. Thereafter, they are taxed at the following rates, pursuant to N.J.S.A. § 54:34-2(d):

15% on any amount up to $700,000.00, and

16% on any amount in excess of $700,000.00.

Interestingly, the tax on Class D transferees has a cruel twist in that a bequest in the amount of $500.00 or greater is taxed retroactive to the first dollar. Thus, an individual who receives $499.00 from an estate pays no tax, yet an individual who is to receive $500 must first pay a tax of $75.00 before receiving his or her net inheritance of $425.00.

(d) Class E beneficiaries are totally exempt from the inheritance tax. See N.J.S.A. 54:34-4.

New Jersey law exempts all transfers from a decedent to his or her spouse, registered domestic partner, civil union partner, children, parents or grandchildren N.J.S.A. 18:26-5.11. As I have also mentioned previously, this also applies to heterosexual couples 62 years of age or older who have registered as domestic partners. This represents a significant change in the New Jersey inheritance tax laws.

In situations where couples have not registered as domestic partners, entered into a civil union or legally married they will still be subject to New Jersey inheritance tax upon the death of one partner. It is important to remember that New Jersey takes the position that any jointly held

assets between non spouses is presumed to be owned 100 percent by the decedent. Accordingly, the surviving partner will have the burden to prove his or her contribution toward the asset. Otherwise, New Jersey Law provides that one hundred percent (100%) of the value of the asset will be included in the estate of the first person to die. [See N.J.S.A. § 18:265.11]

Note that it has been our experience that many gay and lesbian couples, who are elderly or keep themselves out of the gay and lesbian social and political circles, may not even be aware of the Domestic Partnership Act, the Civil Union Law or their legal right to marriage. Counsel should be sensitive to asking questions about relationships without offending, but questions should be asked to determine whether there are tax savings that could be realized by marriage, registration or entry into civil union.

Any inheritance tax that is outstanding must be paid within eight months from the date of the decedent's death. If the inheritance tax applies and the estate is not liquid (such as real estate, qualified retirement account, etc.], then the inheritance tax consequences can be devastating for couples.

(B) New Jersey Estate Tax

Prior to July 1, 2002 the New Jersey Estate Tax was intended to absorb the maximum credit allowed for estate death taxes under federal law. It provided for an estate tax in addition to the inheritance tax where the inheritance taxes paid to New Jersey were not sufficient to fully absorb the maximum allowable credit for such payments against the federal estate tax upon a New Jersey resident. [See N.J.S.A.§ 54:31-1 et.seq.] However, under the Economic Growth and Tax Relief Reconciliation Act of 2001 the credit was eliminated in 2006. To make up for this lost revenue stream, New Jersey has decoupled its estate tax from the federal estate tax and enacted their own laws.

Since the federal estate tax exemption is $5,430,000 and the New Jersey estate tax exemption only applies to the first $675,000 there could be a New Jersey tax and not a federal estate tax. The tax on a New Jersey estate of $5,430,000 is approximately $440,000. The New Jersey estate tax exempts all transfers to a spouse and a Class E beneficiary. However, estates passing to a domestic partner, whether registered or not will be subject to the New Jersey estate tax, but partners in civil union or a legal marriage will be exempt as “spousal-equivalents”.

(C) FEDERAL GIFT TAX RULES

After the Windsor case unlimited marital gifting is now available to same-sex married couples. The Internal Revenue Code provides that married couples can transfer an unlimited amount of assets back and forth between each other without triggering any gift tax consequences LR.C. § 2523. Accordingly, married couples can transfer money between spouses without the transfer being classified as a gift. This exemption does not apply to transfers between gay or lesbian partners who have not entered into a legal marriage. If living expenses are not split equally, one partner will likely be deemed to have made a gift to the other. This deemed" gift giving" can occur if one partner earns more than the other and the couple pools their income. Most likely, the Internal Revenue Service would deem the partner with the higher income as making a gift to the partner earning less. Suppose one partner owns a house, and the other lives there rent free. The owner will be deemed to have made a gift in the amount of half of the fair market value of the rent.

The tax consequences relating to gifts made between non-married partners can be significant. However, each person is entitled to give $14,000 per year to an unlimited amount of individuals. See I.R.C. § 2503. Therefore, the above mentioned issues will only come into play if the difference in income earned by partners is greater than $28,000. Therefore, partners must

keep a scrupulous paper trail to ensure that contributions to joint expenditures can be documented. Otherwise the Internal Revenue Service may consider contributions to joint expenditures as gifts.

The gifting issue also becomes a concern in home ownership. If a partner wants to pay his or her partner who owns the home for half of the property, then the owner is treated as having made a sale. Any gain from this sale must be reported and income tax might have to be paid on that amount. [See I.P.R.C. §121(b).] If on the other hand an owner decides to add his or her partner's name to the deed without requiring payment, this constitutes a gift equal to half of the value of the property. The amount of the gift will be subtracted from the owner's credit shelter amount. [See I.R.C. §2505.]

Consider contracts to permit the lower earning or lower asset partner the right to acquire equity in the joint residence for additional capital contributions or as consideration for contribution to the other's expenses. This can be done over time and can include an acquisition of the gift exempt amount each year until the interests are equalized.

3. ADDITIONAL TAX CONSIDERATIONS AFFECTING GAY AND LESBIAN COUPLES

There are other tax considerations which affect gay and lesbian couples. For instance, there are four different ways to own property:

(A) As a sole owner;
(B) As tenants in common with one or more people;
(C) As joint tenants with right of survivorship with one (usually) or more (rarely) other people;
(D) As tenants by the entirety with a spouse or civil union partner.

The first ownership method is self-explanatory. The fourth method is only available to married couples or civil union partners but note the different treatment of the two by federal law. Let's focus on the other two forms of property ownership: tenants in common and joint

tenants with right of survivorship. When a tenant in common dies, his interest in the property is distributed under his will or by the laws of intestacy. In contrast, in a joint tenancy with right of survivorship, when one owner dies, the surviving owner automatically owns the entire property by operation of law. No court involvement is necessary to transfer title. The fact that property is willed to another person is of no consequence since survivorship provision takes precedence over the bequest in a will.

Joint ownership with right of survivorship can be an effective way to keep assets out of probate. However, some state courts are reluctant to accept the assertion that two unrelated individuals intend to create survivorship rights in each other's property that they jointly own. Consequently, the language has to be specific. Also it is possible for joint tenants to convert their ownership to tenants in common by acting in a way that is inconsistent with joint tenancy (without ever changing title). Actions contesting joint ownership are rare, but a disgruntled family member could institute such a proceeding. Accordingly, if assets are owned jointly with right of survivorship, a will should specify that "all of my jointly owned assets go to my partner."

The passing of jointly owned assets to a partner can occasionally result in serious tax problems. The Internal Revenue Service treats the first person to die in an unmarried couple as owning one hundred percent (100%) of the assets in the estate. At the second person's death, the Internal Revenue Service also includes one hundred percent (100%) of the property in the decedent's estate. This results in a windfall for the government because the same property is taxed an extra time. It is possible to rebut this presumption, but the burden is on the decedent to show who contributed to the purchase and upkeep of the property and in what amounts. Potentially, decades of account statements and canceled checks could be required to satisfy this

burden. Without an adequate paper trail, it is difficult to prove contribution. If the same situation existed for a married couple, the assumption would be that half of the purchase of the property was by the husband and the other half was by the wife.

Another issue for gay and lesbian couples is whether or not to leave assets in their Will outright to their partner or into a trust. Presumably, at one partner's death a goal is to provide for the surviving partner. However, the surviving partner's Will might ultimately provide that upon his or her death the remaining assets pass to their respective family members or a new partner. The first person to die may not want his or her assets to eventually pass under the provisions of the surviving partner's will. Consequently, partners might want to specify that at the time of their death, their assets will be placed into a trust for the benefit of the surviving partner. The provisions of the trust can provide for income and principal to be available for the surviving partner. At the surviving partner's death the assets held in trust will revert to beneficiaries designated in the first partner's will. The establishment of a trust in the Will of the first partner to die preserves a control element.

Retirement Assets

Finally, for assets that pass outside the Will, such as an individual retirement account (IRA) or life insurance, beneficiaries should be designated. In Cozen O'Connor v Tobits, 2013 U.S. Dist. LEXIS 105507 (E.D. Pa. 2013), Sarah Farley married her female partner in 2006. Two weeks after the wedding, Farley was diagnosed with cancer, to which she succumbed in 2010. Shortly after her death, a legal battle ensued between Farley's parents and spouse over who should receive her assets.

Farley had married in Toronto, lived in Chicago and worked for a Philadelphia law firm. In Canada, same-sex marriage is legal. At the time Illinois, Pennsylvania and New Jersey did

not recognize same-sex marriages, but Illinois and New Jersey recognized civil unions. Farley had participated in her firms' profit sharing plan. The plan provided that a survivor annuity would be paid to a surviving spouse or, if no such person existed, then to the decedents parents. The plan stated it was governed by Pennsylvania law. However, the Eastern District of Pennsylvania ruled that ERISA preempted Pennsylvania law. The court held that after Windsor, with regard to ERISA benefits, the Federal Government must honor a state's recognition of a surviving spouse, and that Farley's spouse should receive the annuity.

Although this case came out in favor of the civil-union partnership, a different court could rule otherwise, and couples should save themselves the potential expense and stress of a lawsuit by clearly designating beneficiaries.

CONCLUSION

In preparing a life and estate plan, all individuals should obtain competent legal advice. Unfortunately, current federal law and some state law favors family members in areas involving control, such as selecting the personal representative of estate, health care representative and guardians. Current federal and some state laws also favors married couples for estate and gift tax planning purposes. Presumably, gay and lesbian individuals will not want to marry but will want to provide financial security to a surviving partner and to save unnecessary taxes. It is extremely important that a proper estate plan is established to achieve these results.