Estate Planning Tips and Updates

Attorneys from Chamberlain Hrdlicka look at how estate planning is working now.

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Recent legislation provides unprecedented opportunities to minimize or avoid estate, gift and generation-skipping transfer taxes (GSTT). However, Congress giveth and taketh away, both through the planned sunset of the Tax Cuts and Jobs Act (TCJA) increased exemptions and through the recent changes to retirement planning in the Secure Act.

(Related: A Big IRA Question: Do I Change the Beneficiary Post-Secure Act? (https://www.thinkadvisor.com/2020/03/10/the-million-dollar-question-do-i-change-ira-beneficiary-post-secure-act/))

Help your clients navigate this uncertainty with the following planning tips.

1. Increased Estate Tax Exemption Amounts: Use 'Em or Lose 'Em

The current applicable exemption amount of $11.58 million each — $23.56 million per married couple — allows many of our clients to avoid transfer taxes altogether.

However, the rules require use of these amounts from the bottom up, not from the top down, and the applicable exclusion amount reverts to its prior inflation adjusted amount, say $6 million, on Jan. 1, 2026. If your client with a gross estate of $11 million previously made, say, $7 million of gifts, the rules eliminate any claw back of those gifts if death occurs in 2026. But your client has no applicable exclusion amount remaining per Example (1) in Treasury Regulations Section 20.2010-1(c)(2)(i). That is, after the sunset this client has a gross estate of $4 million and no remaining exemption.

According to that example, clients with gross estates exceeding approximately $6 million should consider implementing one or more strategies, including gifts and sales to grantor trusts, before the end of 2025 to ensure the full use of the disappearing exemption. This timetable also assumes that nothing changes between now and Jan. 1, 2026, a period that includes two presidential elections and four congressional elections. Use it or lose it, and use it sooner rather than later, to make sure your clients take full advantage of this opportunity.

2. Use of the Increased Generation-Skipping Transfer Tax (GSTT) Exemption

The TCJA also increased the GSTT exemption to $11.58 million each. This increase allows many of our clients to exempt transfers for several generations if not in perpetuity under the laws of certain states, but clients must intentionally draft trusts to establish legal situs in states like Nevada to take advantage of longer perpetuities periods.

Longer perpetuities periods mean avoiding additional estate, gift and GSTT taxes for longer periods, normally a net positive. But the valued advisor will include provisions to cause inclusion for succeeding generations; this utilizes additional exemption amounts and further protects assets from both “creditors and predators” and unnecessary taxation.

Although the automatic allocation rules may help, your clients should probably file gift tax returns to allocate GSTT exemption to any such transfers to ensure proper allocation. Timely filed gift tax returns including adequate disclosures of non-gift transactions (i.e., sales to grantor trusts) also start the applicable statute of limitations with respect to such transactions.

3. Annual Exclusion Gifts

Even with the increased exemption amounts, continued annual exclusion gifts (currently $15,000) remain an essential part of most estate tax reduction planning, removing the amount of the gift and future appreciation thereon. And, the tax-exclusive nature of the gift tax makes gifts more tax-efficient. However, use high-basis assets for giving where possible, as gifting during life costs the basis step-up at death in most cases. Finally, consider affirmatively allocating GSTT exemption to annual exclusion gifts to trusts. This does not always occur as one might think, or worse assume.

4. Basis Harvesting

The increased exemption amounts often mean clients with previous trust planning no longer face estate tax issues.

Consider reforming, amending or decanting an existing trust to add older generations in a way to cause inclusion in their estates. This inclusion triggers the basis step-up rules in the code and may dramatically reduce taxes upon a liquidity event, such as the sale of a business interest previously gifted or sold over to the trust.

If the existing trust constitutes a grantor trust with a swap power, consider using the swap power to remove low-basis assets from the trust in exchange for high-basis assets from an individual, the former now includable in the individual's estate and thus eligible for the basis step-up.

5. Secure Act Age Changes

For individuals born after July 1, 1949, the Secure Act raises the beginning age for minimum distributions to 72.

6. Employer Inducements

The Secure Act increases the current $500 credit for setting up a retirement plan to $5,000 in some circumstances. The Act also provides a $500 credit for three years to encourage the use of auto-enrollment.

7. Changes for Inherited IRAs

The Secure Act significantly curtails the use of "stretch" IRAs. For deaths after Dec. 31, 2019, a recipient of an IRA from the deceased must generally take distributions from the IRA over no more than a 10-year period. However, the new rules except accounts inherited by a spouse, by a minor child, a disabled or chronically ill person, or anyone less than 10 years younger than the deceased account owner. Carefully review previous beneficiary designations relying on the old "stretch" provisions to ensure they still work.

8. Secure Act Changes for Annuities

The "stretch" IRA provisions general apply to annuities as well, with one important exception. Annuities making payments before Jan. 1, 2020 may still pay out over two lives.

The Secure Act encourages greater investment in annuities through 401(k) plans, and particularly those offered by smaller businesses, by decreasing the risk associated with offering annuities. That is, the employers offering annuities as investments no longer have fiduciary duties with respect to those potential annuity investments-assuming they choose an issuer in good standing with the applicable state insurance commission.

The Secure Act also offers portability for annuities upon employment changes, allowing direct transfers between retirement plans. This maintains the investments inherent in the annuities and avoids expensive surrender charges and fees.

These eight points represent just a handful of the many ideas to consider when advising your clients in an ever-changing tax and investment landscape. As always, consult an experienced tax professional for assistance in navigating these rocky shoals.

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