ALERT

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# Estate Planning Tips to Prepare for 2020

## There have been a number of significant recent estate planning developments which clients should consider taking advantage of in 2020.

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## TAKEAWAYS

- The historically high lifetime exemption amount for gift, estate and generation-skipping transfer taxes increased from $11.4 million to $11.58 million on January 1, 2020.
- The annual gift tax exclusion amount will remain at $15,000 per donee per year, or $30,000 per year for a married couple who "splits" gifts.
- The generation-skipping transfer tax (GSTT) exemption continues to (i) be at a historically high amount of $11.58 million as of January 1, 2020, and (ii) has the potential to exempt assets from GSTT for an unlimited number of generations with careful planning.

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The Tax Cuts and Jobs Act (the "Act"), which was signed into law on December 22, 2017, continues to provide extraordinary opportunities for our estate planning clients. However, some of the opportunities are temporary. Clients should consider implementing strategies to capitalize on the following opportunities in 2020.

**1. Take Advantage of the Temporary Increases in Exemptions from Gift and Estate Taxes.**

Currently, gratuitous transfers of property, whether by lifetime gift or upon death, in excess of the unified gift and estate tax exemption (the "lifetime exemption") and which are not otherwise exempt from transfer tax are taxed at a federal rate of up to 40%. The Act doubled the lifetime exclusion amount to $10 million, as adjusted for inflation. Beginning January 1, 2020, the already significant lifetime exemption increased to $11.58 million due to the inflation adjustment. With proper planning, married couples will be able to

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transfer up to $23,160,000 of property without incurring a transfer tax.

Although the lifetime exclusion is scheduled to increase for inflation through 2025 under the Act, the increase is temporary. Prior to the Act, the lifetime exemption was $5 million, indexed for inflation. Unless new laws are passed, the doubled exemption amount will terminate, and the lifetime exemption will revert to the prior $5 million level (adjusted for inflation) on January 1, 2026.

In November 2018, the IRS announced that individuals who use their exemption from 2018 through 2025 will not be adversely affected when the exemption is reduced to the pre-2018 level after December 31, 2025. Earlier this year, the Treasury Department and the IRS finalized regulations which clarify that there will be no “claw back” of gifts made by taxpayers on or before December 31, 2025, regardless of whether the lifetime exemption amount is subsequently decreased.

Clients should consult their advisors regarding which assets to transfer in order to optimize the benefits of any lifetime gifts. For example, it is generally advisable to make gifts of assets with a high tax basis and retain assets that have significantly appreciated. Retaining appreciated assets until death will result in those assets being included in the taxable estate and receiving a step-up in income tax basis. That, in turn, may reduce the income tax that will be due if the assets are sold. On the other hand, as discussed below, certain techniques such as a sale of assets to a grantor trust in exchange for a note can be effective to transfer appreciated assets while substantially leveraging the gift and GSTT exemptions.

**2. Take Advantage of the Temporary Increase in Exemptions from Generation-Skipping Transfer Taxes (GSTT).**

Like the lifetime exemption, the generation-skipping transfer tax exemption amount affecting transfers to grandchildren and more remote generations will increase to $11.58 million per individual or $23.16 million per married couple. However, this opportunity is also scheduled to sunset to pre-2018 levels in 2026.

The Act does not impose any limitation on the duration of a generation-skipping transfer to a trust beyond that imposed by state law. Thus, it is still possible under the Act to create a generation-skipping transfer trust under the laws of certain states that will continue in perpetuity and avoid the GSTT on the transferred amount plus appreciation after the date of the transfer.

Clients who have implemented planning techniques to take advantage of the GSTT exemption should ensure that their GSTT exemption is properly allocated by timely filing Form 709 with respect to the transfers.

All clients should consider taking advantage of the valuable current GSTT exemption, possibly leveraging its value using a sale to a grantor trust, and providing some protection of assets through the use of trusts

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for their beneficiaries. The sale technique is especially attractive given the current low interest rate environment, permitting appreciation on the transferred assets in excess of the required interest rate on an expanded asset base to pass to a long-term trust free of transfer tax for many generations. Moreover, sales and/or gifts of fractional interests in entities holding such assets can further enhance the tax savings, due to discounts for lack of control and lack of marketability.

**3. Be Sure to Make Your Annual Gifts.**

In 2020, individuals may make gifts of up to $15,000 per recipient without triggering the gift tax. Married couples eligible to split gifts may make gifts of up to $30,000 per recipient. Gifts to a spouse who is a U.S. citizen are not taxed, regardless of the value of the gift. The annual amount which may be given to noncitizen spouses without subjecting the transfers to gift tax has increased to $157,000 for 2020.

**4. Changes to Rules Affecting Inherited IRAs**

The Setting Every Community Up for Retirement Enhancement Act ( SECURE Act), which was signed into law on Friday, December 20, 2019, will drastically change the tax consequences of inherited IRAs. Under the pre-SECURE Act rules, a person who inherited a retirement account could "stretch" the payments from the inherited account based on his or her life expectancy, instead of the life of the original owner of the account. This technique allowed the recipient to "stretch" the payments over a longer period of time, thereby keeping the funds in the retirement account longer, where the funds could grow tax deferred. The SECURE Act requires a person who inherits an IRA from someone who dies after December 31, 2019, to receive the payments over a period of no more than 10 years, subjecting the funds to ordinary income tax once the 10-year period expires. (The effective date for inherited government retirement accounts is January 1, 2022.) The new rules do not apply to retirement accounts inherited by a spouse of the deceased owner, a minor child of the deceased owner (until he or she is no longer a minor), a disabled or chronically ill person or anyone who is not more than 10 years younger than the deceased account owner at the time of death. Clients with IRA plans should consult their advisors to discuss any necessary changes to their estate planning documents.

**5. Take Advantage of Income Tax Basis Planning.**

If a grantor trust owns assets with a low tax basis relative to their current fair market value, clients should consider exchanging those assets for cash or assets with a high tax basis during the life of the grantor. This type of exchange between an individual and grantor trust is not treated as a sale for income tax purposes, and, consequently, will not trigger an income tax. When the individual dies, under current law, the low basis assets that he or she owns will receive a "step-up" in basis equal to the fair market value of those assets at the time of death. If the assets are then sold, no tax will be owed on the sales proceeds up to the amount of the new "stepped-up" basis.

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**6. Be Aware of State-Level Developments.**

A significant number of states impose a form of estate or inheritance tax on their decedents. California and Florida continue not to impose an estate tax on their residents. In 2020, the New York State estate tax exclusion increased to $5.85 million for deaths on or after January 1, 2020, and before January 1, 2021. Decedents are required, with certain limited exceptions, to include the amount of gifts made within three years of their death in the calculation of their New York gross estate. Connecticut increased its estate and gift tax exemptions from $3.6 million in 2019 to $5.1 million as of January 2020.

Please contact our team to discuss ways in which you and your family may benefit from the opportunities afforded by the current law in 2020. If you have not had your estate plan reviewed since the changes in the law, we encourage you to contact us at your earliest convenience to ensure the changes in the law have not impacted your estate plan.

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