RUSHFORTH FIRM LTD.
NEVADA TRUST ADVICE

2020 Year-End Estate-Planning Strategies

Election-Year Planning

Summary

The end of 2020 presents some unique estate-planning opportunities. With possible tax-law changes that could be triggered by a change of political control in 2021, it is important for those who have estates in excess of the estate tax applicable exclusion to consider some strategies that could trigger significant estate-tax savings. The strategies mentioned here are not all inclusive, and they are not mentioned in any order of priority. All persons must consider the techniques that best suit their goals and circumstances.

A. Gifts to Take Advantage of Estate-Tax Exclusion

A.1 Possible Political Change

Under current law, the estate tax exclusion is $11,580,000, and it will be cut approximately in half (with inflation adjustments) in 2026. If there is a change of political control, the estate tax exclusion could be reduced to $3,500,000 or less.[1] For those who can make sizeable gifts in 2020 without affecting their lifestyle, significant tax savings can result.

> SCENARIO 1 — $5-MILLION GIFT: For example, if an individual makes a gift of $5 million in 2020, and dies when the exclusion is $3.5 million, there will be a savings of the tax on $1.5 million (which is the difference between $5 million and 3.5 million). At 40%, the savings would be $600,000.

> SCENARIO 2 — $11.58-MILLION GIFT: If an individual makes a gift of $11.58 million in 2020, and dies when the exclusion is $3.5 million, there will be a savings of the tax on $8.08 million. At 40%, the savings would be $3,232,000.

For married couples who are not in a position to give away their full exclusion amounts, it may be prudent to use up one spouse's exclusion rather than using part of each spouse's exclusion.

> SCENARIO 3 — EQUAL GIFTS BY SPOUSES: If H and W each give away $5,790,000 (for a total of $11,580,000), the savings for each of them will be 40% of the difference between $5,790,000 and the $3,500,000 exclusion, which is $916,000 or $1,832,000 for both of them. That is a savings of $1,400,000 less than Scenario 2, above.

A.2 Other Factors

As part of gift-giving, consider using gifts of minority interests in business entities and fractional interests in real estate because gifts lacking marketability and ownership control are appraised under current law for less than their pro rata value. Proposed changes in the transfer-tax laws might require the reporting of such gifts at their pro rata value, rather than at their true fair-market value.

Some assets may have a lower value because of pandemic-created current market conditions, making it possible to give away potential post-pandemic appreciation tax free.

[1] For a more detailed discussion, see https://rushforthfirm.info/pdf/2021PossibleTaxChanges.pdf.

B. GRANTOR-RETAINED ANNUITY TRUST (GRAT)

A trust that provides for annuity payments for a term of years can produce a reduced taxable gift of the trust's assets after the term expires. Because of the current low-interest environment, the value of the remainder interest of a GRAT is at or near an all-time low. The GRAT does require income or cash to payout the required annuity.[2]

C. LOW-INTEREST LOANS; REFINANCING

The applicable federal rate ("AFR") is so low that intra-family loans can be an effective way to provide needed capital to your family members so that they can invest in growth assets that will mushroom in value outside of your taxable estate. If loans exist, perhaps they can be refinanced at a more optimal rate.[3]

D. GIFT AND/OR SALE TO GRANTOR TRUST

The current pandemic has reduced the current value for many assets. If those assets are expected to appreciate, it may be wise to give or sell those assets to a "grantor trust" for the benefit of family members. As to any amount contributed as a gift, the applicable exclusion would be used, and the estate tax will be eliminated on the contributed assets up to the exclusion amount. As to the portion that is sold, your estate would have a non-appreciating note, while the trust for your beneficiaries has appreciating assets. Under federal income-tax law, the settlor or grantor of a "grantor trust" is responsible to pay all tax on trust income. There are two basic advantages to a grantor trust in this scenario. First, as to any portion that is sold, there will be no capital gain tax. Second, the payment of the tax on trust income by the grantor allows the trust to grow without reduction for the payment of those taxes, while the payment of the tax is not treated as a gift.

E. SPOUSAL LIFETIME ACCESS TRUST

A Spousal Lifetime Access Trust (or "SLAT") is an irrevocable trust for the benefit of the settlor's spouse and other beneficiaries. Contributions to the trust are completed gifts and facilitate using the current applicable exclusion. During the lifetime of the settlor's spouse, there are no separate shares for the beneficiaries, and distributions to the beneficiaries are made in the trustee's discretion. Distributions made from the SLAT to the spouse will be included in the spouse's estate for estate-tax purposes, which means that such distributions will not generally be favored; however, the ability to make distributions provides a financial safety net for the spouse (and indirectly for the settlor). The spouse-beneficiary can have a power of appointment that allows the spouse to designate beneficiaries after death, which might include the settlor.

A SLAT must be funded with the settlor's separate property. Community property can be divided ("transmuted") into separate property if necessary.

If the SLAT is not done properly, the IRS may argue that the settlor made a gift with a retained interest, triggering estate taxation on trust assets. The IRS may argue that the spouses had an agreement or "understanding" that the settlor will receive benefits from the trust or that the spouse-beneficiary will designate the settlor as a beneficiary at any point in the future. To avoid that argument, one might instead use a gift to grantor trust (as discussed in D), with a

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[2] For more information about GRATs, see https://rushforthfirm.info/pdf/gratmemo.pdf.

[3] A loan payable to a trust can be negotiated to a lower rate only if there is a benefit to the trust's beneficiaries; otherwise, the trustee could be in breach of the trustee's fiduciary duties to the beneficiaries.

provision in the trust that allows an adviser to compel the trustee to make unsecured loans (and not distributions) to the settlor, providing the desired financial safety net.

F. IRAs to Charities

Making one or more charities – perhaps a private foundation or a donor-advised fund – the beneficiaries of IRAs and other retirement benefits will eliminate both the income tax and the estate tax from the tax equation, giving the charities 100% of the funds.

G. Charitable Lead Trust

Providing for one or more charities to receive an annual annuity for a term of years can produce a near-zero taxable value for the amount that passes to your beneficiaries after the term of years. While the beneficiaries will have to wait patiently, they will not have to share much with Uncle Sam.

If the charitable lead trust is done while you are living, the remainder interest is a taxable gift, which should be reported on a gift-tax return. If the charitable lead trust take effect at death, it can be modified at any time up to that point, and it does not require any lifetime transfers.[4]

H. Lifetime Charitable Remainder Trusts

A trust that provide for a unitrust or annuity payment for your lifetime with a distribution to one or more charities after your death, can provide an income stream, and income-tax deduction, and a deferral of the capital gain tax if highly appreciated assets are involved.

I. Post-Mortem Charitable Remainder Trusts

You might update your will or trust to allocate funds to a charitable remainder trust for one or more beneficiaries that provides those beneficiaries with distributions for their lifetime or for a term of years[5]. For estate-tax purposes, your estate will get a deduction for the actuarial value of the remainder interest that goes to charity. It will not reduce the tax to zero, but it will reduce the tax.

J. Conclusion

If there is going to be year-end planning done in 2020, now is the time to consider your options and take action. If you wait until after the 2020 election, you may find it impossible to get done what needs to be done.

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4 For more information about CLTs, see https://rushforthfirm.info/pdf/clt.pdf.

5 A charitable remainder trust for a younger beneficiary may be limited to a term of years because the law requires that the remainder interest going to charity must have an actuarial value of at least 10% of the value of the trust's assts.