Estate planning update - Important tax changes ahead

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The information below was recently sent out to many of McDonald Hopkins' estate planning clients. We encourage you to take a moment to read the information and stay tuned for further updates on estate planning ideas based on any developments to pending tax proposals. You can also click here for additional McDonald Hopkins insight on estate planning.

Even before last year, the historically high estate and gift tax exemption amounts were set to be reduced at the end of 2025. Then came the COVID-19 pandemic, the economic fallout of the pandemic, and the 2020 elections, which brought changes to both the White House and Congress. It now appears that significant changes in tax law, including reduced estate and gift tax exemptions, could happen sooner than expected. The information below covers some of the changes that have already occurred and some proposed changes that could significantly affect your estate plan.

Recently proposed tax changes

The 2017 Tax Act included a provision that doubled the estate and gift tax exemption to a level above $10 million (with inflation adjustments, it is at $11.7 million for 2021). The same law reduced income tax rates. Many of these tax reductions are set to expire in 2026, which would result in the lowering of the exemption to $5 million (with inflation adjustments, likely $6 million or more). While many thought it made sense to take a “wait and see” approach until closer to 2026, it may be more appropriate to review plans now. It appears that a reduction of the exemption could occur before 2026 - perhaps as soon as this year, based on stated policy positions. It is even possible that changes could be made retroactive to January 1, 2021.

Among tax changes in bills that have been recently introduced:

- **Effective January 1, 2022, as introduced:**
  - Federal estate tax exemption reduced to $3.5 million
  - Gift tax exemption reduced to $1 million
  - Estate and gift tax rate increases

- **Effective as of date of enactment:**
  - Limits on annual exclusions for gifts to trust and gifts of certain non-cash, restricted assets
  - Limits on valuation discounts for closely-held business interests, farms and real estate
  - Inclusion of grantor trusts in the estate of the grantor of assets transferred after the date of enactment to existing grantor trusts and to new grantor trusts
  - Grantor retained annuity trusts (GRATs) would be restricted
  - Capital gains tax on unrealized appreciation would be imposed on transfers during life and at death, with an exemption for transfers to a spouse (possibly effective for tax year 2021)

There could be other changes, including higher tax rates on ordinary income and capital gains, likely at income levels above $400,000. It may be necessary to act before new legislation is enacted to take advantage of planning opportunities that would be limited or eliminated by these proposals. It is very difficult to predict whether any of these changes will happen this year or, if they are enacted this year, whether they will be given retroactive effect. Despite this uncertainty, you should review your estate plan soon and consider whether, for example, you want to try to take advantage of the higher exemption before it is reduced. McDonald Hopkins can also review with you strategies that can protect against the risk of a retroactive reduction of the federal estate tax exemption.

SECURE Act

The SECURE Act, which became law in 2019, affects planning for inherited retirement benefits. Many recipients will be required to fully withdraw and pay tax on an inherited retirement account by the end of the tenth year following the death of the participant. (There are important exceptions for surviving spouses, minor children and certain other beneficiaries.) Prior to this change, many clients had planned for distributions over the life expectancy of the recipient in order to stretch out the distributions. Many clients have also named their trusts as the beneficiaries of their retirement accounts in order to have the trustee manage the payout for a beneficiary who is not competent, responsible, or experienced enough to directly inherit a large retirement benefit. Many of those trusts have a provision that should be reviewed and possibly changed to prevent the benefits from being paid out too soon to trust beneficiaries. For more details on how the SECURE Act may affect your estate plan, click here.

Other reasons to review your estate plan

There may be other reasons that require a review of your estate plan - changes in family circumstances or health, receipt of inheritances, relocation due to job changes or retirement. The mere lapse of time does not legally affect your documents, but some institutions are refusing to accept authority granted under powers of attorney and health care documents that are older than five years. And sometimes, it may be time to change the persons you have authorized to act on your behalf.

McDonald Hopkins strongly encourages individuals with large retirement accounts or an estate exceeding $3.5 million and couples with a combined estate exceeding $7 million to review their estate plans. Contact information for our Estate Planning and Probate attorneys is listed below.

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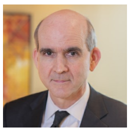

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