# COUNTDOWN TO END OF YEAR

SEPTEMBER, 2020

**What should you think about between now and the end of the year?**

December 31, 2020 represents one of the most important dates in the world of estate planning since the end of 2012 when the estate tax was set to be reinstated at pre-2001 levels. With a world turned upside-down by COVID and an election that promises drama up and down the ticket, the real-world tax and planning implications are significant.

Election Day is on November 3rd and the tax year for most individuals and families ends December 31st. There will be limited time and resources to conceive, construct and implement an estate plan that takes advantage of the current tax and market environment, while maintaining the flexibility to deal with future uncertainties. It is very possible that many of the tools used to take advantage of the current estate planning environment could be rendered ineffective with the flip of the calendar. With that in mind, many families and their advisors are already analyzing their plans. Where should you focus?

**Election impact on estate taxes at the Federal Level:**

On January 1, 2018, Congress increased the estate, gift, and generation-skipping transfer (GST) tax exemptions from $5 million (adjusted annually for inflation) to $10 million (also adjusted annually for inflation). The increased exemptions expire January 1, 2026. At that point, the estate, gift and GST tax exemptions will revert back to $5 million, adjusted for inflation. The inflation-adjusted exemption amount is $11.58 million per person in 2020.

However, tax laws can change at any point, Congress and the President may act to reduce the exemption amounts sooner than 2026. With the economic impact of COVID and other priorities, there are calls to increase revenue to the federal government. One way is to reduce the federal estate tax exemptions.

**Expiring tools**

Wealth advisors have been blessed with an increasingly generous estate planning environment over the last twenty years. Many tried and true techniques like the Grantor Retained Annuity Trust (GRAT) and the Intentionally Defective Grantor Trust (IDGT) provide an effective means for families to shift their wealth to the next generation and other constituencies. With an increased focus on revenue generation, the President and Congress could revisit these types of structures and eliminate or reduce their effectiveness to drive more tax dollars to the Federal coffers (e.g. by imposing a minimum GRAT period, further limiting valuation discounts, limiting basis step up, etc.).

**State Considerations**

Many states are also dealing with lost revenues due to the pandemic and increased costs for providing the goods and services their residents need. New York, California and Illinois are examples of states considering increased income taxes to cover their deficits. It is worth noting that many states have their own estate tax regimes that do not track to the Federal framework. For instance, in New York, when an estate exceeds the exempted amount (currently $5.74 million) by 5% or more, the entire estate is subject to the State's estate tax. This is important because not all states impose this type of tax. With the changing environment of 2020, wealthy families are analyzing state domiciles, residences and favorable trust situses like Tennessee for their planning needs going into 2021.

**Low interest rates**

History has taught us that no one has been able to accurately predict interest rates over a long period of time. What is known is that we are currently in a generationally low interest rate environment. The IRS issues Applicable Federal Rates (AFR), to provide guidance for all sorts of transactions. The Short Term AFR for September stands at 0.14%, the Mid-Term AFR stands at 0.35% and the Long-Term AFR stands at 1%. Low IRS-issued interest rates increase the effectiveness of many estate planning tools (like GRATS and IDGTS) and wealth transfer techniques like intra-family loans. At these levels, now is the time to take advantage of them.

**Volatile markets**

While the equity markets have seen a resurgence from their COVID lows, valuations remain volatile. For those maximizing their various estate planning exemptions, "temporarily" depressed valuations of assets can increase the effectiveness of many estate planning tools. With the election on the horizon and potential changes in many laws and regulatory regimes, the period of uncertainty provides an interesting window to use the generous transfer laws.

**Acting Now While Staying Flexible**

The importance of acting now cannot be overstated. The window of opportunity to take advantage of these conditions could close by the end of the year. If tax law changes occur in 2021, they will likely be retroactive to the beginning of the year. As a result, transactions should be finalized and documented before December 31, 2020.

Proper estate planning requires the coordination of many different experts. As the days count down toward the end of the year, each specialist (and institution) will be under severe strain to implement their clients' objectives. You do not want to be at the bottom of their "to-do" list.

One way to get a head start on implementation is to take this pre-election time to draft trusts with the idea of funding them through a promissory note. This provides flexibility if the election results are called into question and there is no immediate certainty as to which political party is the winner.

Excellent wealth planning combines structure with flexibility, allowing plans to remain durable over time but also account for changed circumstances within the law, the family or their assets. That said, the time between now and the end of the year represents one of the most generous estate planning environments ever. Be sure to take advantage of it to the extent that you can.