Preparing Clients for Legislative Updates

Palm Beach Estate Planning Council

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Sasha A. Klein, Esq. LLM

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Sasha Klein is a Partner with PwC Private, where she specializes in high net worth individual (HNWI) consulting services with a particular emphasis on business-owning families, cross border HNWIs, and family offices, as well as other HNWI clients in the Asset and Wealth Management practice. Prior to joining PwC, Sasha was a Partner and Chair of the estate and tax planning group at Ward Damon, where she was responsible for client development, execution of new business, and sustaining strong client's relationships. She has extensive experience counseling clients on innovative tax and estate planning, including advising clients on structuring wealth to achieve their goals, including protecting against risk and minimizing taxes over multiple generations.

Sasha is an author, lecturer, and community leader. She lectures nationally and is a frequent published author on a range of estate planning, wealth management and tax law topics. She is also very involved in national and state bar and bankers' associations, as well as volunteering and supporting several civic and charitable organizations with the goal of bettering the community in which we live, including being the chair of the Diversity, Equity and Inclusion Committee for her children's school and serving on their Board of Trustees.

Sasha earned a Juris Doctorate and a Law and Business degree from Vanderbilt University Law School and a post doctorate (LL.M.) in tax law from University of Florida College of Law – Graduate Tax Program. Legal Recognitions include Accredited Estate Planner Designation, The Best Lawyers in America, Florida Legal Elite, Jupiter Top Lawyers, and Palm Beach Top Lawyers. Additionally, she was named the Florida Bankers Association 2018 Trust Member of the Year and has received writing awards for published articles.

Always passionate and spirited, Sasha loves yoga, fitness, nutrition, traveling and spending time with her family.

Mark R. Parthemer, Esq. AEP

Managing Director,
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TIAA

Mr. Parthemer is a Managing Director for TIAA, responsible for working with ultra high net worth clients and their advisors to develop practical and efficient wealth transfer plans. He joined TIAA, a Fortune 100 financial services firm, in 2021, after serving as Senior Fiduciary Counsel at Bessemer Trust. Prior to that, he was in private law practice in Pennsylvania and Florida, most recently as a Trust and Estate partner with Duane Morris LLP. He also spent several years at PricewaterhouseCoopers and was involved in private businesses.

Mr. Parthemer is a nationally recognized speaker and frequently published author. He is an ACTEC Fellow, serving on the Program, Digital Assets and Estate and Trust committees, and is in leadership of the Real Property Trust and Estate Section of the American Bar Association, the Florida Bankers Association (Board Member; Past Chair Legislation Committee) and the Florida and Pennsylvania Bar Associations. He is an Associate Editor and Columnist for the Journal of Financial Service Professionals, member of Synergy Summit (Past President), the Palm Beach County Estate Planning Council (Board Member), and the Palm Beach Tax Institute. He was awarded the 2014 Article of the Year from the American Bar Association's Probate & Property magazine and named the Florida Bankers Association 2015-2016 Banker of the Year.

He frequently is faculty for the University of Miami's prestigious Heckerling Institute, was an Adjunct Professor, Widener University School of Law, and guest lectures at the Dickinson School of Law and the LLM programs at the University of Miami School of Law and the University of Florida Levin College of Law. He has been quoted in the Wall Street Journal, Barron's, NY Times and MONEY Magazine, and has been honored by Best Lawyers in America with their Lifetime Achievement Award.

He earned a J.D. from The Dickinson School of Law, B.A. and B.S. degrees in philosophy and government from Franklin and Marshall College, conferred status of an Accredited Estate Planner, and completed MBA Phase I curriculum.

Do you have a Living Will?

"Yes, absolutely, no question, pull the plug!

Then, immediately put it back in to see if I restart."

– Bill Murray

SECTION I

Strategic Planning for Another Year of Change

Focusing on Individuals, Estates and Trusts

Clients Respond to Uncertainty in a Variety of Ways

Lots Being Discussed!

	House Ways and Means Proposals Sept. 13, 2021	For the 99.5% Act	American Housing and Economic Mobility Act of 2021	The Ultra-Millionaire Tax Act of 2021	The STEP ACT	The American Families Plan	Biden Administration Greenbook
Reintroduction of prior proposal?	YES but with new ideas	YES	YES	NO	YES but with new ideas	YES	YES but with new ideas
Pure revenue raiser or attached to spending project	Pay for $3.5 trillion Build Back Better Plan	Only Revenue	Pay for housing legislation	Only Revenue	Only Revenue	Pay for education and childcare plan	Released at the same time as budget
All or part retroactive to January 1, 2021	NO	NO	Part	NO	YES	Unknown	NO
Lowers exemption	YES	YES	YES	NO	NO	NO	NO
Increases Estate/Gift/ GST Rates	NO	YES	YES	NO	NO	NO	NO
Limit Valuation Discounts	YES	YES	NO	Allowed limitation through future regulations	NO	YES	YES (for income tax purposes only)
Elimination of perpetual GST exempt trusts	NO	YES	YES	NO	NO	NO	NO (but income tax recognition every 90 years)
Changing rules related to GRATS	NO	YES	YES	NO	NO	NO	NO
Grantor trust includible for Gift and Estate Taxes	YES	YES	YES	NO	NO	NO	NO
Impact on basis step up	NO	NO	NO	NO	YES	YES	YES
Increased enforcement	YES	NO	NO	YES	NO	YES	YES

Transfer Taxes Wealth Tax Income Taxes

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House Bill 5376
Summary of Proposed Tax Changes

Income Tax Provisions

What are the changes?

Top tax rate increase

- Currently 37%
- Proposed 39.6%

Expand Net Investment Income Tax (3.8%)

3% Surcharge

Who will it impact?

High Income Taxpayers

- Single taxpayers >$400,000
- Married taxpayers >$450,000

Surcharge based on modified adjusted gross income

- Married taxpayers filing separate on excess over $2,500,000
- Married taxpayers -on excess over $5,000,000
- Trusts and estates on excess over $100,000

What can clients do?

Accelerate income

- Roth Conversions
- Deferred Compensation

Postpone Deductions

- Gifts to charity
- Real estate taxes
- Medical expenses

House Bill 5376
Summary of Proposed Tax Changes

Capital Gains Tax Rate Provisions

What is the change?

Top tax rate increase

- Currently 20%
- Proposed 25%

Effective for gains recognized after September 13

Who will it impact?

- Single taxpayers >$400,000
- Married taxpayers >$450,000

What can clients do?

Pending effective date

- Recognize capital gains
- Defer realization events
- Defer recognition
- Consider a more tax efficient portfolio going forward

House Bill 5376
Summary of Proposed Tax Changes

Estate Tax

What are the changes?

Accelerate sunset of estate, gift and GSTT exemption increases under 2017 Tax Act

- Reverts to $5M per taxpayer adjusted for inflation
- For 2022, $12,060,000, reduced to $6,030,000
- Annual exclusion untouched ($16,000 in 2022)

Increase special valuation reduction under Section 2032A from $750,000 to $11,700,000

Elimination of valuation discounts for non-trade or business assets

Who will it impact?

Taxpayers with taxable gross estates

- >$5M (adjusted for inflation) for single taxpayers
- >$10M (adjusted for inflation) for married taxpayers

Families with qualifying farms and farmland

Passive assets (including those in an active trade or business unless used in hedging transactions or as working capital)

- valued as if the transferor had transferred such assets directly
- Nonbusiness assets not taken into account in valuing the interest in the entity (three valuations?)

What can clients do?

Make large gifts

- Greater than future exemption amount
  - GST Exempt Grantor Trusts
  - SLATs
  - Modify non-exempt trusts and do late GST allocation
- Charitable split interest trust planning

Ensure ownership qualification of farm and farm equipment to meet 25% and 50% tests

Engage in transactions before enactment

House Bill 5376
Summary of Proposed Tax Changes

Roth Conversion Changes

What are the changes?

Eliminates Roth conversion of after-tax dollars (i.e., “back door” Roths)

- Beginning in 2022

Eliminates all conversions for high earners

- Beginning in 2032

Who will it impact?

All Roth conversions of after-tax contributions will be disallowed regardless of income

High income taxpayers will not be allowed to convert any dollars beginning in 2032

- Single taxpayers >$400,000
- Married taxpayers >$450,000

What can clients do?

Conversions of after-tax contributions should be completed by the end of 2021.

High income taxpayers should consider conversion within the next 10 years.

- Also consider top tax bracket increase beginning in 2022

House Bill 5376
Summary of Proposed Tax Changes

Large Retirement Account Balances

What are the changes?

Contributions to IRAs limited for taxpayers with large retirement plan balances (combined)

- $10M+ IRA and Defined Contribution balances

Increased RMD on large retirement plan balances (combined)

- RMD is 50% of amount > $10M
- And 100% if >$20M

Who will it impact?

High income taxpayers

- Single taxpayers >$400,000
- Married taxpayers >$450,000

Note: *No grandfathering*

What can clients do?

High income taxpayers should consider:

- Keep income below threshold
- Roth conversion
- Terminating contributions
- Annuitization/withdrawals to fund life insurance
- Consider future tax rates

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House Bill 5376
Summary of Proposed Tax Changes

Grantor Trust Provisions

What are the changes?

Grantor trusts will be included in the gross estate

Sale or exchange between trust and owner treated as between third parties

Distributions from a grantor trust will be taxable gifts

Termination of grantor status will be a taxable gift

Who will it impact?

Grantor trusts

- Created on or after date of enactment
- Contributions made to existing trusts on or after date of enactment
- Credit given for prior gift tax paid
- Does not apply to revocable trusts nor trust otherwise includible

What can clients do?

Implement before date of enactment

Waive grantor trust status

House Bill 5376
Summary of Proposed Tax Changes

Noticeably Absent

What is not changed?

Capital Gains at Death

Carbon Tax

Decanting/Modification Realization Event

Elimination of Basis Adjustment

Estate/Gift/GST Tax Rate Increase

FICA Cap Extension

GRAT Rules Changes

GST Exemption Duration Limit

Non-Qualified Deferred Comp Limits

Wealth Tax

What can clients do?

Wait for Senate's Bill

In-between: Carried Interest

- Generally speaking, this is a performance fee vehicle rewarding fund managers with profits in excess of ownership interest
  - ➢ Receives capital gains treatment, not ordinary income
  - ➢ Potential for substantial future growth makes carried interest rights ripe for transfer planning
  - ➢ Navigate Section 2701 concerns via "vertical slice" planning or a transfer to a trust for a non-family member
- 2017 Tax Act imposed a 3-year holding period to receive long-term capital gains treatment

Build Back Better Act would extend to a 5-year holding period

For GRAT Fans Skeptical about the Future: “Shelf” GRATs

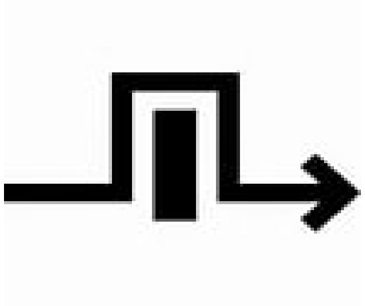
Four Risks to a Rolling GRAT Program

1. Donor dies
2. Assets decline in value
3. 7520 rises dramatically
4. Law change prohibits new short term GRATs

Substitution power to manage risk 2.

Shelf GRATS can mitigate risks 3 and 4.

SALT Cap Workaround if the Senate Balks



- Notice 2020-75, issued Nov. 10, 2020, alerts to forthcoming proposed regulations approving a workaround for pass through entities:
  - Entity pays state tax liability
  - Owners given benefit via reduction in net income
- Adopted in Connecticut, Louisiana, Maryland, New Jersey, Oklahoma, Rhode Island, and Wisconsin

SECTION II

Use It or Lose It: Gift and GSTT Exemptions

Using Exemption

How Much to Use

1. Only if more than future amount ($6,030,000?)
2. Ensure use of inflation adjustment

Spouses Who Can't Afford to Give It All Away

1. Pick one; don't do 50/50 and don't gift split
2. SLATs

Funding Gifting at Other Generations

<u>Funding Up a Generation</u>

1. Loans
2. GRATs
3. 678 trusts
4. Reverse preferred partnership

Funding Gifting at Other Generations

Funding a Next Generation

1. GRATs
2. Distributions from GST Non-Exempt Trusts
3. Next level planning for new Exempt Trusts

Clawback

- 2019 Treasury finalized regulations comforting taxpayers as to no claw back
- Also in 2019, Priority Guidance Plan referenced an anti-abuse rule that could invoke claw back
- ➢ *Aimed at inconsistent treatment of inter vivos transfers for estate tax purposes*
- Ambiguous language in September 9, 2021 Priority Guidance Plan has kindled anxiety among some whether that would be expanded beyond abusive situations and apply to all pre-sunset transfers
- ➢ *Perhaps expansion to cover NY State bar inquiry re GRITs and other intentionally 2701 failed transactions*

SECTION III

Capital Gains Planning

Simpler Deferral Techniques

- QOZ
- Charitable Remainder Trusts
- Section 1031 like-kind exchange
- Section 1035 for:
  - ✓ annuities
  - ✓ life insurance
  - ✓ endowment contracts
  - ✓ long-term care policies

Qualified Opportunity Zones

- Section 1400Z-2 added by 2017 Tax Act
- Deferral of gains invested in a QOF, QOZB or QOZBP within 180 days
- Elimination of up to 15% of capital gains via basis augmentation:
  - ➢ 10% if held 5 years
  - ➢ Additional 5% if held for 7 years
- Deferral until earlier of an inclusion event or December 31, 2026
- Potential for elimination tax on appreciation if held for more than 10 years and sold on or before December 31, 2047
- Inclusion events include sales and transfers by gift (except to a grantor trust), but not death (no basis adjustment)

Sample 20 Year Charitable Remainder Annuity Trust

- Annual payments to one or more persons for trust term*
- Remainder paid to one or more charities/family foundation
- October 2021 7520 rate is very low 1%, which hurts

20 Year Joint 5% CRAT Funded with $1,000,000 with 6% Growth Impact of Interest Rate			
	October 1%	August 1.2%	Hypothetical 5%
Returned to You**	Fails	$1,000,000	$1,000,000
Remainder to Charity	Fails	$1,367,856	$1,367,856
Income Tax Deduction	Fails	$0	$376,890

* Can be any term of years, or for one or more lifetimes.

** Must be at least 5%/year, but can be higher (subject to limitations).

Sample 20 Year Charitable Lead Annuity Trust

- Annual payments to private foundation or public charity for trust term*
- Remainder paid to, or for, heirs
- Can "zero-out" for gift/GST taxation
  - October 2021 7520 rate is very low 1%, which helps
  - Requires $55,415 annuity to zero-out

Joint Lifetime CLAT Funded with $1,000,000

5% Payout and 5% Growth and 4% Payout with 6% Growth

	No CLAT (20 Year)	October 5/5 20-Year CLAT	September 20-Year 4/6 CLAT
Current Taxable Gift	$0	$97,720	$278,176
Heirs**	$1,480,831	$1,000,000	$1,735,712
IRS (Estate Tax)	$1,211,589	$0	$0
Charity	$0	$1,000,000 ($50,000 annually for 20 years)	$800,000 ($40,000 annually for 20 years)
Optional Income Tax Deduction***	$0	$902,280	$721,824

* Can be any term of years, or for one or more lifetimes.

** Can be into trust, including a GST transfer tax-exempt trust, providing additional tax savings.

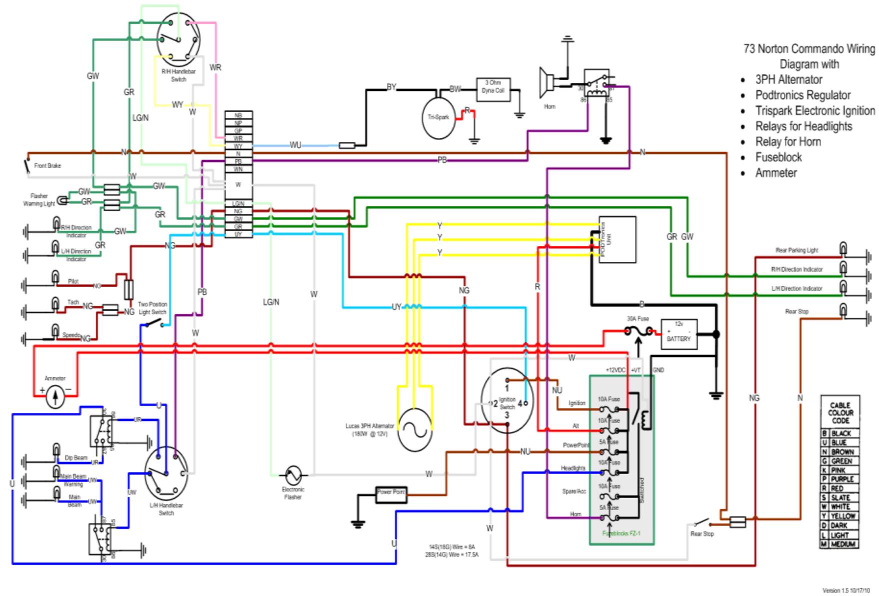
*** Deduction in first year if a grantor trust CLAT is established, but causes future earnings to be taxed to donor; otherwise, offset throughout term.

"From the sublime to the ridiculous there is but a single step."

– Napoléon Bonaparte, citing Thomas Paine

Sophisticated Deferral Techniques

- QSBS
- FLP/NIMCRUT
- PPLI



Section 1202 – Qualified Small Business Stock

If held at least 5 years:

- Exclude capital gains up to greater of $10,000,000 or 10 times basis
- Excluded gains not subject to 3.8% NIIT

Exclusion History

✓ 1993 50% exclusion for post Aug 11, 1993 stock (7% AMT addback)

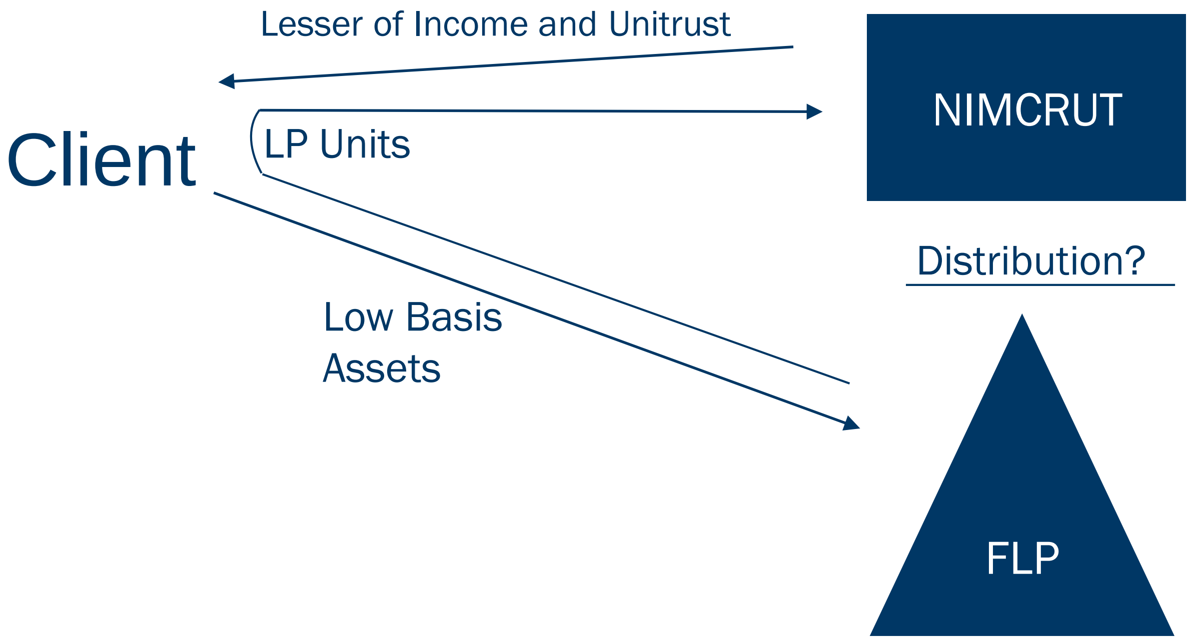
✓ 2009/2010 Transition rule; 75% exclusion (7% AMT addback)

✓ 2010 100% exclusion for post Sept 27, 2010 (no AMT)

Party like it's 1993

House Bill would repeal expansions

FLP/NIMCRUT



Lesser of Income and Unitrust
Client
LP Units
NIMCRUT
Distribution?
Low Basis
Assets
FLP

Cryptocurrency Loss Harvesting

Notice 2014-21: IRS declares cryptocurrencies are property

Cryptocurrencies are volatile

Some advisors selling every time there is a downswing (e.g., 5%) and then immediately repurchasing

IRC Section 1091 – wash sale rule prohibits a capital loss deduction if a taxpayer purchases a substantially similar <u>stock or security</u> within 30 days before or after such sale (emphasis added)

SEC has announced desire to characterize cryptocurrency as a security before 12/31/2021.

Private Placement Life Insurance (PPLI)

Consolidation Appropriations Act (12/27/20)

Interest rate reductions on tests determining qualification as life insurance (and non-MEC)

2% reduction for 2021; floats starting in 2022

Permanent life insurance benefited, especially accumulation structured product as is often used in PPLI

Example for a 50-year-old male:

Old test: $10MM premium required over $52MM death benefit (2020)

New test: Only $32MM death benefit.

Results in a Lower Hurdle

1, More can be funded

2. Net return increased via reduced mortality costs

More effective when taxes are less favorable

“ The trick now is to turn insight into foresight.

– Neale Donald Walsch

Thank you

“Before you become too entranced with gorgeous gadgets and mesmerizing video displays, let me remind you that information is not knowledge, knowledge is not wisdom, and wisdom is not foresight. Each grows out of the other, and we need them all.

– Arthur C. Clarke

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