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CLIENT ALERT

September 23, 2021

Proposed Tax Reform Could Drastically Impact Estate & Gift Exemptions and Limit Common Estate Planning Strategies

By J. Aaron Bennett

As you know, Congress has been considering tax reform over the last several months. Until recently, it was unclear whether any of the wide-ranging proposals would gain enough traction to become law. Last week, however, the House Ways and Means Committee released a much-publicized tax bill (the "Bill") that, if enacted, would drastically alter current Federal estate and gift tax laws and eliminate the use of certain common estate planning strategies.

Background. While the Bill is just a proposal, the Bill seems to have more support than other recent tax reform attempts. Many political insiders believe that some version of the Bill could be enacted in the coming weeks. Here are certain key estate planning related components that warrant your attention.

Specifically, the Bill:

1. Reduces the estate and gift tax exemption amount from $11.7 million to $6.02 million, effective January 1, 2022, with a 40% estate and gift tax rate;
2. Causes "grantor trusts" established after the date of enactment, or contributions to existing grantor trusts, to be includible in the grantor's taxable estate; and
3. Eliminates valuation discounts on the gifts of non-business related assets made after the date of enactment.

Reduces Estate and Gift Tax Exemption. As a result of these potential changes, individuals concerned about preserving family wealth from estate taxation may only have a limited window of time to take advantage of the current higher exemptions. To take full advantage of the temporary increased exemption, however, gifts need to be significant – at a minimum, gifts must exceed the projected exemption amount ($6,020,000, less the donor's already used exemption amount). Gifts less than this amount will shelter the future appreciation of the gifted assets, but will not be as effective from an estate tax minimization perspective.

Eliminates Grantor Trust Benefits. As mentioned above, the Bill effectively eliminates the "grantor trust" planning technique that allowed a grantor to give assets to a trust that was excluded from the grantor's taxable estate, but permitted the grantor to bear the trust's income tax liability (allowing the trust to grow income tax free, and the grantor's income tax payments reduce their estate and not be considered an additional gift). Many common estate planning trusts like Spousal Lifetime Access Trusts (SLATs), Grantor Retained Annuity Trusts (GRATs), Intentionally Defective Grantor Trusts (IDGTs), Qualified Personal Residence Trusts (QPRTs), and Irrevocable Life Insurance Trusts (ILITs) are all potentially eliminated from planning after the Bill is enacted.

Grantor Trusts that are *in existence and funded* before the date the Bill is enacted, however, are grandfathered into the current rules. So, there is a very small window (perhaps only a few days) of time while any planning involving "grantor trusts" remains viable.

Eliminates Valuation Discounts on Non-Active Business Interests. Finally, the well-recognized concept of valuation discounts in gift planning may be substantially limited by the Bill, and the change would be effective as of the date of enactment. The details of this change are beyond the scope of this article, but the changes are aimed at substantially limiting transfers of family business interests.

Recommended Actions. The Bill is still just a proposal, and there will be changes to its components as it is considered further by Congress. If the Bill garners enough votes in Congress, however, there is a good chance that at least some of the changes discussed above could become law in some form or another very soon.

Although it is difficult to identify who should consider taking action at this time, individuals who anticipate having an estate in excess of $6 Million, or married couples in excess of $12 Million may want to consider taking advantage of currently permissible planning techniques before any changes become law. Please contact Aaron Bennett or any member of our Business, Tax and Estate Planning Team if you have any questions or would like to discuss your particular situation.

J. Aaron Bennett *is a member of the Carruthers & Roth* ***business, tax and estate planning practice*** *and has a broad-based practice serving individuals and families, businesses and entrepreneurs. He especially focuses on estate and tax planning, closely held business planning and employee benefits. Aaron may be reached at 336-478-1105 or* ***jab@crlaw.com****.*