2021 Estate and Tax Client Planning Letter

Dear Client:

2021 is presenting unique challenges and opportunities for advisers to consider important tax and estate planning issues.

The covid-19 virus has introduced issues most of us never anticipated. Given the terrible news about deaths and illness, a planner needs to reflect on whether all of his or her clients have completed even the most basic estate planning – wills, trusts, durable powers of attorney and living wills. It is very unpleasant to consider how many of our friends and clients suddenly fall ill without having completed these essential documents.

Despite the terrible news we see daily, 2021 also presents a "perfect storm" for planning opportunity for many of our clients.

1. Political change suggests less favorable laws for gifting may be coming. Is this the time to make gifts, outright or in trust for younger generation family members?

2. The CARES Act of 2020 allowed retirement plan participants to avoid all required minimum distributions for 2020. In 2021, required minimum distributions are back. If political change results in higher income tax rates, might this be the best year to convert traditional IRAs to Roth IRAs? Consider a trust to hold the Roth IRA for children and grandchildren.

3. Interest rates are at record lows for our lifetime. Many planning opportunities are best utilized when interest rates are low (GRATs, IDGTs, CLATs, private annuities). Will political change take these opportunities away? Act before this occurs.

4. The SECURE Act of 2019 has eliminated lifetime stretch out of retirement plan benefits for many beneficiaries. The conduit trust is no longer the best planning alternative for inherited retirement plans – an accumulation trust for beneficiaries may be a better alternative.

These factors are our challenges as planners. We owe it to our clients to at least have a discussion with them about these issues in our uncertain and difficult time.

Transfer Taxes

The exclusion from liability for transfer taxes – gift, estate and generation-skipping taxes has been increased to the highest level ever –$11.70 million per person in 2021. Married couples can transfer $23.40 million without transfer tax liability. Portability is preserved.

The "problem" with this increased exclusion is that by law it sunsets at the end of 2025, and reverts to the 2017 exclusion amounts, indexed for future inflation. In addition, planners cannot discount the "political risk" of changes – and possible reductions in the exclusion – by the current administration.

Individual Income Taxes

There have also been significant changes in the income tax laws. The rule allowing fair market value at death to be the income tax basis to an heir has been preserved, for now. Income tax rate brackets have been reduced and the top individual rate capped at 37%. Married persons filing jointly reach this rate only above $628,300 of taxable income; $523,600 for single persons. The income tax rates on income left in trusts remains highly compressed, with the top rate of 37% applying to income in excess of $13,050. The income tax rates are likely to be increased on high income taxpayers.

There have been many changes in determining which deductions may be claimed. State and local tax deductions are capped at $10,000 on a tax return. Interest deductions on new home mortgages are only allowed on $750,000 of acquisition debt. Home equity loan interest may not be deducted unless the loan is used to acquire, repair or improve one's home. Personal exemptions are repealed, replaced with an enhanced standard deduction and child tax credit. The miscellaneous deductions of employees, investors, union members, hobbyists and others are now completely denied through 2025. This is causing more people to use the standard deduction rather than itemizing their deductions. Planning suggests advising clients to "bunch" their charitable donations in order to get the maximum tax benefit in years where contributions are made – and no loss of tax benefits in years when no donations are made. Donor Advised Funds have emerged as the ideal planning vehicle to accomplish this strategy.

Business Income Taxes

Dramatic changes in the taxation of businesses have occurred. The tax rate on C corporations has been reduced to 21%. Should there be a rush to become a C corporation? Political change suggests a higher rate (28%?) is coming. Many pass-through entities (proprietorships, S corporations, partnerships and LLCs) are allowed to reduce taxable income by 20% if they qualify under a series of complex Qualified Business Income rules under the new Code Section 199A. Despite the complex rules, many taxpayers will qualify for this deduction regardless of the business in which they are involved. The complexities of this law only affect persons with taxable income for 2021 over $329,800 (married filing jointly), and $164,900 (all others). Beyond these thresholds, the extensive complications of this law take hold.

Are There Tax-Savings Opportunities For You?

You may want to consider addressing the new opportunities and challenges of 2021. Among the issues to be discussed:

- Are basic and crucial documents in place (will, trust, durable power of attorney, health care directive)?