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TAX AND WEALTH ADVISOR ALERT: STRIKE WHILE THE GIVING IS GOOD—HISTORICALLY HIGH ESTATE AND GIFT TAX EXEMPTIONS MAY BE REDUCED OR ELIMINATED AS EARLY AS JANUARY 1, 2021

With the economy still struggling, one bright spot remains for those who are willing to make an investment of time and money in estate planning. The combination of lowered asset values, reduced interest rates, and historically high estate and gift tax exemptions present a unique opportunity to implement estate planning techniques that will yield significant tax savings. But those looking to take advantage of this unique opportunity should act now, because a rebound in asset values and the outcome of the November 2020 election may make this unique opportunity go away.

The Gift, Estate, and GST Tax Exemptions for 2020

The Tax Cuts and Jobs Act of 2017 created a significant opportunity to transfer wealth by effectively doubling the federal estate and gift tax exemption for transfers made after 2017. The current exemption for 2020 allows an individual to transfer up to $11,580,000 (or up to $23,160,000 for a married couple) over the course of his or her lifetime without incurring gift or generation-skipping transfer ("GST") tax. Any unused amount is available to eliminate estate and GST tax upon the individual's death. Moreover, a surviving spouse inherits the unused gift and estate tax exemption (but not the GST tax exemption) of the first spouse to die if an election is made on a timely filed estate tax return for the first spouse's estate.

Any amounts gifted during life or transferred upon death in excess of the federal estate and gift tax exemption (over $11,580,000 for an individual or $23,160,000 for a married couple) are subject to a 40% estate and gift tax rate at death, plus any taxes that may be imposed by the decedent's state of domicile (Wisconsin has neither an estate nor gift tax). In addition to the gift or estate tax, a separate GST tax of 40% is imposed on transfers in excess of the exemption amount that are made to grandchildren or more remote descendants.

The Scheduled Reduction of the Gift, Estate, and GST Tax Exemptions

Currently, the estate and gift tax exemptions are the **highest** they have ever been since the modern estate tax was implemented in 1916 (with the single exception of 2010, when the estate tax was briefly repealed). However, effective January 1, 2026, the exemption will be reduced to $5,000,000 (or effectively $10,000,000 for a married couple), adjusted for inflation back to 2010.

This means that while currently a married couple can transfer over $20,000,000 without estate or gift tax, if exemptions are cut in half as scheduled on January 1, 2026, then the same couple can only transfer approximately $10,000,000 without estate or gift tax. At a 40% tax rate, the couple creates an approximate $4,000,000 in savings by making a transfer today at current exemption levels. That is $4 million going to their beneficiaries rather than taxes!

And the good news is that gifts made now utilizing 2020’s record-high exemptions may not be “clawed back” as provided in regulations published by the IRS, even if exemptions are later reduced on January 1, 2026, or eliminated by Congress sooner as explained below. The importance of these “anti-clawback” regulations is that taxpayers can utilize today’s higher exemption amounts without fear of future penalty or “clawback” and should act before the scheduled reduction.

The Presidential Election

While a deadline of December 31, 2025, for the scheduled reduction may seem like plenty of time to take advantage of these high exemptions, the 2020 presidential and congressional elections and the impact of the pandemic may bring about some drastic changes to estate planning as soon as January 1, 2021.

First, there is a real possibility that taxes may be increased to support the massive amounts spent by Congress on COVID-19 relief. The gift, estate, and GST tax rates could be viewed as the easiest taxes to raise because they would impact only the wealthiest of taxpayers, and not those perceived to be struggling the hardest due to the novel pandemic. It is possible for the gift, estate, and GST tax rates to be increased from the current 40% to 55% or even higher.

Second, there is speculation that if the Democratic Party wins the presidency and gains control of Congress following the November 2020 election, the exemption amount might be reduced to an amount as low a $3,500,000 even before the expiration date of January 1, 2026. In fact, such a change could be effective as soon as January 1, 2021, if Congress passes legislation having retroactive effect.

Additionally, while the Democratic Party’s presidential nominee, Joe Biden, has not proposed any specific changes to the estate exemption amounts and tax rates, his recently released economic plan calls for the "wealthiest Americans [to] shoulder more of the tax burden," including raising federal estate taxes "back to the historical norm." This seems to indicate that if Biden and the Democratic Party are successful come November, exemptions going forward could be significantly lower than they are under current law, and thus most tax commentators believe that the current exemption amounts are the best we are going to see.

Maximize Higher Gift, Estate, and GST Tax Exemptions Before It is Too Late—Plan Now!

Gifting assets outright or in trust now, while the exemption levels are still at their historic high, allows taxpayers to "lock in" these high exemption amounts without fear of a clawback or an exemption reduction as soon as January 1, 2021. There are several effective estate planning structures that can be used to take advantage of depreciated asset values, record-low interest rates, and record-high exemption amounts, but waiting for official election results come November 3 will likely make it difficult to implement these structures.

Some of these structures require several months to implement. Other than planning to reduce gift and estate taxes, there are many other considerations for taxpayers when transitioning wealth to their family, e.g., how and when to benefit family members; choosing trustees; choosing the state of trust administration for asset protection and income tax planning objectives; considering multi-generational planning; and charitable giving and identifying which assets to gift. Additionally, since certain assets may require professional valuations, these transactions may require more time to implement, so now is the time to act in order to ensure that the transactions can be completed before year's end.

Conclusion

The current confluence of lowered asset values, reduced interest rates, and historically high estate and gift tax exemptions may make this one of the best times in history to transfer wealth efficiently with minimal estate tax implications, but the time to act is now. Many estate planning techniques take time to implement, so do not wait until November 2020 to consider making changes to your estate plan.

Regardless of which political party stays in power or takes control in November, our team at O'Neil Cannon realizes that there is no one-size-fits-all strategy to address your estate planning goals and objectives. We are prepared and ready to help you build a comprehensive plan tailored to your needs. If you are interested in taking advantage of these unparalleled opportunities for tax savings, please speak to your regular OCHDL contact, or the author of this article, attorney Britany E. Morrison, to discuss how you can strike while the giving is good.