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Current Conditions Present Historic Gifting Opportunities; Time to Review Retirement Plan Beneficiary Designations

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The dramatic decline in asset values caused by the emergence of COVID-19 as a significant health threat, combined with historically high gift tax exemptions and historically low interest rates make now an opportune time to focus on estate planning. In addition, the changes made by the SECURE Act to the tax treatment of IRAs and other retirement plans make reviewing beneficiary designations for such plans essential.

Unprecedented Gifting Opportunities

Transfer Tax Exemptions at Historic Highs; Asset Values at Historic Lows

The marked decline in value of many assets as a result of the global pandemic, while having many negative effects, may present an opportunity to transfer significant value through gifting. Assuming the depression in value is temporary, substantially more assets can be transferred using the available gift tax exemptions and exclusions now than even a few weeks ago. Moreover, any post-transfer rebound in value will have been removed from the donor's taxable estate at no tax cost.

The Tax Cuts and Jobs Act of 2017 (TCJA) raised the federal gift and generation-skipping transfer (GST) tax exemptions to historically high levels. In 2020, each US citizen or resident can give away up to $11.58 million free from federal gift and GST tax, subject to reduction for prior gifts. Typically, any exemption that is not used during lifetime will remain available at death. However, in the absence of further legislation, these exemptions are scheduled to be reduced at the end of 2025—and possibly even sooner depending upon the results of upcoming elections. This means that if you do not use these historically high exemptions now, you could lose them.

There are many potential strategies to take advantage of these historically high exemptions and low asset values, including so-called *dynasty trusts* for a donor's descendants that can continue free of gift, estate and GST tax in perpetuity and, for those concerned about parting with such significant sums during their lifetime, *spousal lifetime access trusts (SLATs)* that combine the benefits of dynasty trusts with the ability of the donor's spouse to receive trust distributions if necessary. Even simply making use of the $15,000 per person annual gift tax exclusion amount can be quite effective when combined with temporarily depressed asset values. Under current tax laws, the best assets to give typically include those that (i) have a high cost basis, (ii) are expected to appreciate significantly and/or (iii) are eligible for valuation discounts (for lack of marketability and/or control).

Interest Rates at Historic Lows

Already low interest rates have been further reduced to historical levels in an effort to support the economy in the face of the many ramifications of the COVID-19 pandemic. This reduction creates considerable opportunities to utilize so-called "estate freeze" planning techniques that take advantage of low interest rates such as *intrafamily loans*, *grantor retained annuity trusts (GRATs)* and *sales to intentionally defective grantor trusts (IDGTs)*. Because these techniques seek to "freeze" the value of existing assets in the donor's estate while giving away the appreciation above a "hurdle" rate of return (which is tied to prevailing interest rates), they require the utilization of little or no gift tax exemption and can typically be used in conjunction with the other strategies discussed in the preceding section. Although these techniques work best with assets expected to appreciate significantly, even traditionally low-growth assets may have substantial rebound appreciation potential and even moderate appreciation may be meaningful when the hurdle rate hovers near one percent.

Major Changes to the Tax Treatment of Retirement Plans

The Setting Every Community Up for Retirement Enhancement (SECURE) Act that became effective on January 1, 2020 changed the traditional tax treatment of qualified retirement plans such as IRAs, Roth IRAs, 401(k)s, 403(b)s in several important respects:

- The life expectancy payout method that historically allowed continued tax deferral after the participant's death for the lifetime of a designated beneficiary has been replaced with a 10-year payout method, with only the few exceptions noted below. Notably, there are no longer any required distributions during the 10-year payout period; instead, all of the assets of the plan must be distributed at some point within 10 years of the participant's death.
- The life expectancy payout method continues to apply if the designated beneficiary is: (1) the participant's surviving spouse, (2) the participant's minor child (for the duration of minority), (3) a person less than 10 years younger than the plan participant, (4) a disabled person or (5) a chronically ill person.
- The required beginning date for required minimum distributions has been increased to age 72 (from age 70½) for anyone born after June 30, 1949.
- Anyone who is over age 70½ and still receiving compensation may continue to contribute to a traditional retirement plan.

As a result of these changes, any plan that designates a trust as a beneficiary of a retirement plan should be reviewed. The trust may no longer function as intended, and technical changes to the trust provisions may be required to comply with the new rules. Even if a trust is not named as a beneficiary, it is prudent to review the impact of these changes on your plan.

Traditional retirement plans have always been popular charitable planning assets for the philanthropically inclined because, unlike an asset such as cash or stock, they typically carry a built-in ordinary income tax liability for any non-charitable recipient. One increasingly popular strategy in light of the new rules is to designate a charitable remainder trust (CRT) as the beneficiary. Notwithstanding the new rules, the CRT can provide a tax-advantaged lifetime annuity or unitrust interest for an individual beneficiary, with the remainder of the qualified plan assets passing to charity upon the individual beneficiary's death.

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