

CLIENT ALERT

April 14, 2021

Are you prepared if the “For the 99.5% Act” becomes law and estate and gift tax exemptions change?

By Robert A. Vigoda | Partner

Over the past twenty years, there has been a steady decline in the number of Americans subject to the federal estate and gift tax, and ample ways for even the wealthiest families to avoid or minimize the tax. This trend culminated in the increase in lifetime estate and gift exemptions, with the passage of the Tax Cuts and Jobs Act of 2017 (“TCJA”), with exemptions more than eleven times those that existed in 2002.

All of that may be about to change.

On March 25, a bill was formally proposed in the United States Senate, called the For the 99.5% Act, that would fundamentally change the current federal estate and gift tax system. The estate tax exemption would be reduced from \$11,700,000 to \$3,500,000, and the gift tax exemption would be reduced even more, down to \$1,000,000. As a result, lifetime gifts in excess of \$1 million would result in payment of gift tax. The proposed law increases the estate tax rate to 45% once a taxable estate exceeds \$3,500,000, and 50% and higher when the amount subject to tax exceeds \$10,000,000. These changes would be effective for gifts made and estates of decedents dying after December 31, 2021.

Perhaps more significant, particularly for a married couple with a net worth greater than \$7,000,000, is that some of the primary tools and strategies that have been used in the past to legally reduce or eliminate estate and gift tax will no longer be available. Planning to avoid estate and gift taxes by funding irrevocable grantor trusts, such as GRATs, SLATs and ILITs, will no longer be effective. Valuation discounts for intra-family transfers, which could reduce gift and estate taxes by 30-40%, would be significantly curtailed. Unlike the above changes to exemptions and rates, these changes would be effective when the new law is enacted.

Here are some planning techniques to consider implementing prior to enactment of this legislation.

- **Fund trusts with remaining TCJA gift tax exemptions.** Lock in the higher gift tax exemption and reduce estate tax exposure. Certain strategies allow the grantor of the trust to retain indirect access to income and principal if desirable (a so-called Spousal Lifetime Access Trust, or SLAT).
- **Make gifts of closely held business interests.** Under the proposed law, lack of control discounts of 9-16% will no longer be available for transfers to family members, making it more costly and difficult to transfer the family business to the next generation. Lack of marketability discounts would also be eliminated for passive assets under the proposed law.
- **Pre-fund Irrevocable Life Insurance Trusts (ILITs) to cover future premium payments.** Trusts owning life insurance are typically grantor trusts, whose assets may be subject to estate tax under the new law. Trusts funded before the effective date are grandfathered, but post-enactment gifts to cover premiums would result in estate tax on a pro-rata portion of proceeds.
- **Consider pre-enactment “zeroed out” GRATs.** This may be the last opportunity to plan with grantor retained annuity trusts (GRATs) to gift appreciating assets with no gift tax cost or audit risk. GRATs are particularly useful for gifts of assets eligible for discounts before new restrictions are enacted, and to fund ILITs.

The legislative process is rife with uncertainty, making planning for changes that might not occur or that change from proposal to enactment difficult. There are ways to hedge the risk that the effective dates for law changes end up being sooner than proposed and, therefore, impact planning that has already been implemented, resulting in gift tax being owed. Here are a few:

- Make a formula gift that would cap the amount of the gift to the exemption ultimately in effect in 2021.
- If gifting to a trust, include a provision that would allow the trustee or a beneficiary to reject (“disclaim”) the gifted interest within nine months of the gift, resulting in reversion to the grantor.
- Make a gift to a trust that qualifies for a marital deduction, allowing a married grantor to decide by the time an election must be made on a gift tax return (October 15, 2022) whether or not to claim the deduction depending on the outcome of legislation.
- Make a gift to a grantor trust of an amount no greater than the \$1,000,000 exemption amount in effect under the Act, and then sell assets up to the remaining TCJA exemption in return for a note, which can be forgiven as a gift in 2021 when there is certainty that the effective date for the exemption change will not be sooner than proposed.

If you wish to complete an estate tax plan that you have started with us or to further develop or act upon the estate tax plan you already have in place, please let us know soon. It will be important for you to provide us with updated asset and entity information as soon as possible so that we can avoid any delays in putting tax savings strategies into action before any new federal estate or gift tax laws may pass.

If you do not have an estate tax plan in place or in process, we recommend that you start immediately with us or another qualified firm before the demand for these services causes us to be unavailable to complete your plan before any new laws may be enacted.

For more information about this topic and how it might relate to your own estate plan, please contact your Rubin and Rudman attorney or any one of the attorneys in our [Trusts and Estates Department](#).

Rubin and Rudman LLP | 53 State St. Boston, MA 02109 | 617.330.7000 | www.rubinrudman.com

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