Proskauer

Personal Planning Strategies

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Estate, Gift and GST Tax Update

What This Means for Your Current Will, Revocable Trust and Estate Plan

The estate and gift tax regimes have been permanent and unified since the passage of The American Taxpayer Relief Act of 2012 (the "2012 Act"). In 2017, the Tax Cuts and Jobs Act (the "2017 Act") significantly increased the estate, gift and generation-skipping transfer ("GST") tax exemptions, which is scheduled to continue to be increased for inflation through December 31, 2025. And despite various proposals to lower the estate, gift and GST tax exemptions, none of them were enacted and thus the exemptions will increase for inflation in 2023 as set forth below.

Tax Exemption Inflation Increases for 2023

For 2023 the increases under the 2017 Act are as follows:

- In 2023, there is a $12,920,000 federal estate tax exemption and a 40% top federal estate tax rate. This is an $860,000 increase from the prior year.
- In 2023, there is a $12,920,000 GST tax exemption and a 40% top federal GST tax rate.
- In 2023, there is a $12,920,000 lifetime gift tax exemption and a 40% top federal gift tax rate.
- In 2023, the annual gift tax exclusion amount increases by $1,000 to $17,000.

Note that the increased exemption is scheduled to sunset on December 31, 2025. Under final regulations issued by the IRS and Treasury, it was clarified that the government will not claw back amounts given away between 2018 and 2025 with respect to someone who dies in 2026 or beyond when the gift and estate tax exemptions are set to return to a $5 million exemption, indexed for inflation, which applied under 2012 Act.

Under current law, these increased exemptions under the 2017 Act create opportunities to make larger lifetime gifts, to leverage more assets through a variety of estate planning techniques (such as a sale to a grantor trust) and to shift income producing assets to individuals such as children or grandchildren who may be in lower income tax brackets and/or reside in states with a low income tax rate or no state income tax.

In particular, those who previously used substantially all of their exemptions should consider making additional lifetime gifts to utilize the increased exemptions before they sunset at the end of 2025.

How do these changes affect your existing Proskauer estate planning documents?

Our estate planning documents are drafted to be flexible and, in general, their overall structure account for the increased exemption amounts. Still, there may be instances where you will want to update your documents.

It should be noted that while the estate tax exemption is portable among spouses at death, the GST tax exemption is not portable. Also, most states that have separate state estate tax regimes (such as Connecticut, Massachusetts and New York) do not permit portability of their state estate tax exemption amount. This creates an extra level of complication. Use of other estate planning options, such as bypass trusts at the first death of a married couple, may be most useful where these limits on portability are applicable.

Additionally, if you are a married couple and live in a state with a state estate tax (or own real property in a state with a state estate tax, such as Connecticut, Massachusetts or New York), there may be provisions that should be added to your documents which could save state estate taxes at the death of the first spouse.

Please do not hesitate to call us so that we can review your documents and make sure that they are up to date and reflect your current wishes.

Gift Tax Update

Exploit the Gift Tax Annual Exclusion Amount

In 2023, the gift tax annual exclusion amount per donee will increase to $17,000 for gifts made by an individual and $34,000 for gifts made by a married couple who agree to "split" their gifts.

There is plenty of time to take advantage of your remaining 2022 gift tax exclusion amount, being $16,000 for gifts made by an individual and $32,000 for gifts made by a married couple who agree to "split" their gifts, but in all cases, you should ensure that gifts are "completed" before December 31, 2022.

In lieu of cash gifts, consider gifting securities or interests in privately held companies or other family-owned entities. The assets that you give away now may be worth significantly less than they once were, and their value will likely increase in the future. So the $32,000 gift that your spouse and you make in 2022 (and the $34,000 gift that your spouse and you make in 2023) may have a built-in discount that the Internal Revenue Service cannot reasonably question. That discount will inure to the benefit of your beneficiaries if the value of those assets rises.

Your annual exclusion gifts may be made directly to your beneficiaries or to trusts that you establish for their benefit. It is important to note, however, that gifts to trusts will not qualify for the gift tax annual exclusion unless the beneficiaries have certain limited rights to the gifted assets (commonly known as "Crummey" withdrawal powers). If you have created a trust that contains beneficiary withdrawal powers, it is essential that your Trustees send Crummey letters to the beneficiaries whenever you (or anyone else) make a trust contribution. For a more detailed explanation of Crummey withdrawal powers, please see Crummey Withdrawal Notices – Recommended Practices at Personal Planning Strategies - Insights - Proskauer Rose LLP.

If you have created an insurance trust, remember that any amounts contributed to the trust to pay insurance premiums are considered additions to the trust. As a result, the Trustees should send Crummey letters to the beneficiaries to notify them of their withdrawal rights over these contributions. Without these letters, transfers to the trust will not qualify for the gift tax annual exclusion.

2022 Gift Tax Returns

Gift tax returns for gifts that you made in 2022 are due on April 18, 2023. You can extend the due date to October 16, 2023 on a timely filed request for an automatic extension of time to file your 2022 income tax return, which also extends the time to file your gift tax return. If you created a trust in 2022, you should direct your accountant to elect to have your GST tax exemption either allocated or not allocated, as the case may be, to contributions to that trust. It is critical that you not overlook that step, which must be taken even if your gifts do not exceed the annual gift tax exclusion and would, therefore, not otherwise require the filing of a gift tax return. You should call one of our attorneys if you have any questions about your GST tax exemption allocation.

New York Basic Exclusion Amount to Increase in 2023

As of January 1, 2023, the amount of property that will be able to pass free of New York State estate tax will increase to approximately $6,540,000 (New York has not yet released its adjusted estate tax exemption for 2023). Almost nine years ago, the New York State legislature passed, and the then New York Governor Andrew M. Cuomo signed, the Executive Budget for 2014-2015, which significantly altered New York's estate tax. The changes to the New York estate tax were made for the ostensible purpose of preventing the exodus of wealthy individuals from New York to more tax-favored jurisdictions, but the law will likely not have the desired effect.

The law increased the New York basic exclusion amount, which was previously $1 million per person. This increase was gradually made through January 1, 2019, after which the New York basic exclusion amount is equal to the federal exemption amount under The American Taxpayer Relief Act of 2012 (the "2012 Act"), but without regard to the Tax Cuts and Jobs Act of 2017. That essentially means that the New York State estate tax exemption is approximately equal to 50% of the federal estate tax exemption.

One of the most significant provisions in the law, however, is that no New York basic exclusion amount will be available for estates valued at more than 105% of the New York basic exclusion amount. In other words, New York estate tax will be imposed on the entire estate if the estate exceeds the exemption amount. Due to adjustments to the bracket structure in the new law, those estates that are valued at more than 105% of the New York basic exclusion amount will pay the same tax as they would have under the prior law.

For example, assume a person dies as a New York domiciliary on May 1, 2023, with an estate valued at $6.9 million and when the New York basic exclusion amount will be approximately $6,540,000. Because the value of the estate exceeds 105% of the then available New York basic exclusion amount ($6,540,000 x 105% = $6,867,000), the estate will be subject to New York estate tax on the entire $6.9 million. The New York State estate tax liability will be $625,200, which is the same as the amount that would have been due under the old law. In contrast, if an individual had died with an estate valued at $6.5 million, her estate would owe no New York estate tax under the new law because the New York basic exclusion amount will be applied to her estate. Under the old law, however, the decedent's estate would still have owed $574,000 in New York estate tax.

While New York has no gift tax, gifts made within three years of a decedent's death are added back, increasing the New York gross estate, where those gifts are subject to New York estate tax at a maximum rate of 16%. The add back does not include gifts made (a) three years prior to date of death, (b) gifts made on or after January 1, 2026, or (c) gifts made during a time when the decedent was not a resident of New York State. Moreover, since New York does not have a gift tax, it is usually more beneficial for New Yorkers to give away assets during their lifetimes in order to potentially avoid New York estate tax attributable to those assets at their deaths.

These changes in New York law present further estate planning opportunities using bypass trusts to set aside New York's basic exclusion amount (approximately $6,540,000 after January 1, 2023 and before January 1, 2024 for New York State estate tax purposes). The proper disposition of the basic exclusion amount is the cornerstone of estate planning for married couples. Significant tax savings can be achieved if the basic exclusion amount is set aside at the death of the first spouse, therefore "bypassing" estate taxation at the death to the surviving spouse. In addition, any growth that occurs in the trust also escapes estate taxation at the death of the surviving spouse. As New York's basic exclusion amount rises, the potential tax benefits from employing bypass trusts increase as well.

If you wish to discuss any aspect of the new law as it relates to your estate planning, please contact one of the lawyers in the Private Client Services Department at Proskauer.

Connecticut Estate Planning Update

Connecticut Raises Basic Exclusion Amount Passing Free From Estate and Gift Tax to $12,920,000 in 2023

As of January 1, 2023, the Connecticut basic exclusion amount will equal the federal estate and gift tax exemption amount (the “federal exemption”) of $12,920,000 per person (up from the Connecticut basic exclusion amount of $9,100,000 per person in 2022).

Time Period	Connecticut Basic Exclusion Amount From Estate and Gift Tax
Prior to January 1, 2018	$2,000,000
January 1, 2018 to December 31, 2018	$2,600,000
January 1, 2019 to December 31, 2019	$3,600,000
January 1, 2020 to December 31, 2020	$5,100,000
January 1, 2021 to December 31, 2021	$7,100,000
January 1, 2022 to December 31, 2022	$9,100,000
January 1, 2023 and beyond	Equal to the federal exemption – $12,920,000 in 2023

In the last decade, the Connecticut basic exclusion amount lagged far behind the federal exemption. The difference was amplified by the passing of the Tax Cut and Jobs Act in 2017 which significantly increased the federal exemption. Beginning January 1, 2023, the Connecticut basic exclusion amount will be tied to the federal exemption.

The increased Connecticut basic exclusion amount increases the potential tax benefits from employing bypass trusts in estate plans. The proper disposition of the basic exclusion amount is the cornerstone of estate planning for married couples. Significant tax savings can be achieved if the basic exclusion amount is set aside at the death of the first spouse, therefore “bypassing” estate taxation at death to the surviving spouse. In addition, any growth that occurs in the trust also escapes estate taxation at the death of the surviving spouse. And unlike under federal law, the Connecticut basic exclusion amount is not portable between spouses so it is a use it or lose it tax regime.

The increased Connecticut basic exclusion amount also provides additional opportunities for lifetime gifting, especially for those who were previously unable to utilize the full federal exemption due to the lower Connecticut basic exclusion amount. Note that the increased federal exemption under the Tax Cuts and Jobs Act is set to sunset on December 31, 2025, at which time the federal exemption (and thus, the Connecticut basic exclusion amount) will revert to $5,000,000, as adjusted for inflation. In light of this, there are benefits to using the increased Connecticut basic exclusion amount prior to death.

If you wish to discuss the increased Connecticut basic exclusion amount as it relates to your estate planning, please contact one of the lawyers in the Private Client Services Department at Proskauer.

New Jersey Estate Tax Was Eliminated on January 1, 2018

On January 1, 2018, the New Jersey State estate tax was eliminated altogether for the apparent purpose of preventing the exodus of wealthy individuals from the State.

It is important to note that New Jersey’s inheritance tax has not been repealed by this law. Inheritances to spouses, children and grandchildren are not subject to New Jersey’s inheritance tax. But the New Jersey inheritance tax is levied on inheritances passing to siblings, nieces, nephews and other unrelated individuals so bequests to certain beneficiaries may still be subject to inheritance tax despite the changes to New Jersey’s estate tax.

If you wish to discuss any aspect of the 2018 law as it relates to your estate planning, please contact one of the lawyers in the Private Client Services Department at Proskauer.

Make Sure That You Take Your IRA Required Minimum Distributions by December 31, 2022

If you are the owner of a traditional IRA, you must begin to receive required minimum distributions ("RMDs") from your IRA and, subject to narrow exceptions, other retirement plans, by April 1 of the year after the year in which you turn 72 (your required beginning date). Previously the starting age was 70 ½. You must receive those distributions by December 31 of each year. If you are the current beneficiary of an inherited IRA from someone who died before 2020, you must take RMDs by December 31 of each year regardless of your age. The RMDs must be separately calculated for each retirement account that you own, and you, not the financial institution at which your account is held, are ultimately responsible for making the correct calculations. The penalty for not withdrawing your RMD by December 31 of each year is an additional 50% tax on the amount that should have been withdrawn. Please consult us if you need assistance with your RMDs.

If you are the non-spouse current beneficiary of an inherited IRA from someone who died in 2020 or after, the SECURE Act changed the RMD distribution rules. If the decedent died before his or her required beginning date then you must receive distributions under the 10-year rule. The 10-year rule requires that the full distribution of your IRA must be made by December 31 of the year containing the 10^{th} anniversary of the decedent's death but you are not required to take RMDs each year. But if the decedent died after his or her required beginning date then you must take RMDs each year following the year of the date of death and the full balance of the IRA must be distributed by December 31 of the year containing the 10^{th} anniversary of the decedent's death. Additionally there are some narrow exceptions to these rules. If you wish to discuss any aspect of how the RMD rules changed as a result of the SECURE Act, please contact one of the lawyers in the Private Client Services Department at Proskauer.

Understanding the Inflation Adjustments to the Estate, Gift and Generation-Skipping Transfer Exemption Amounts

The gift and estate tax basic exclusion amount (the “BEA”) is the amount that a person can give or bequeath to other people without triggering gift tax during life or estate tax upon death. Since 2018, the BEA has been equal to $10,000,000 adjusted for inflation since 2010. This year, it is $12,060,000 per person. But due to the inflation adjustment built into the formula for determining the BEA in any given year, the size of the BEA will increase considerably on January 1 of each of the next three years. The Internal Revenue Service has already announced that the BEA will increase to $12,920,000 on January 1, 2023 — an $860,000 increase. It is too soon to estimate the 2024 and 2025 inflation adjustments with any precision, but the 2024 inflation adjustment will likely be between $620,000 and $870,000, and the 2025 inflation adjustment could easily reach into the mid-to-high six figures as well. By January 1, 2025, the exclusion amount will be around $14,000,000 per person.

High-net-worth individuals stand to benefit from these inflation adjustments. Those who have used up all or a substantial portion of their current gift tax exclusion amounts will be able to move additional assets out of their estates ahead of the scheduled reduction in the BEA on January 1, 2026, when it is scheduled to be reduced by 50%. Individuals with a large amount of unused exclusion soon will have even more. For individuals with estates that are close to, or just above, the current exclusion level, these inflation adjustments may mean the difference between a significant estate tax liability and none at all.

It is possible for high-net-worth individuals to take advantage of the looming inflation adjustments even before they take effect. For example, imagine that Susie has used up $11,700,000 of gift tax exclusion by making a large gift in 2021. Susie would like to take advantage of depressed stock market valuations by transferring stock to her children now, before the market fully recovers. Under normal circumstances, a grantor retained annuity trust (“GRAT”) (This article and our podcast address GRATs in greater detail) would be an attractive option for someone like Susie. But, given the coming inflation adjustments, Susie might consider simply loaning $2,000,000 of stock to an intentionally defective grantor trust for her children’s benefit, knowing that she will likely have sufficient exclusion to forgive the loan in the not-too-distant future.

The coming inflation adjustments will also affect the size of the gift tax's annual exclusion amount, which is the amount that an individual can gift to another individual without incurring any gift tax or consuming any lifetime gift tax exemption in a particular year. In 2022, the annual exclusion amount is $16,000 per donor (or $32,000 for a married couple), but it will increase to $17,000 per donor (or $34,000 for a married couple) in 2023, and will likely increase further to $18,000 per donor (or $36,000 for a married couple) in 2024.

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