
Fall 2020 – Best Time in 100 Years to Make Gifts

This Client Alert explains why right now may be the best time in the past 100 years for clients to consider transferring wealth to successive generations.

The Current Transfer Tax Landscape

Current High Federal Exclusion Amounts

The Federal gift and estate tax exclusion amount is \$11.58 million per person. The Federal generation-skipping transfer (GST) tax exemption amount is also \$11.58 million per person. Historically, this is the largest amount for both the Federal gift and estate tax exclusion and GST tax exemption.

D.C., Maryland, Virginia & Florida

The D.C. estate tax exclusion amount is \$5,762,400. The Maryland estate tax exclusion amount is \$5 million. Neither D.C. nor Maryland have a gift tax. Neither Florida nor Virginia have a state gift or estate tax.

Gift, Estate and GST Tax Rates

Gifts in excess of the lifetime exclusion are subject to a Federal gift tax rate of 40%. With the exception of a short period of time (namely, from 2010 – 2012 when the rate was 35%), this is the lowest maximum rate in over 80 years. The Federal estate tax and GST tax rates are also historically low at 40%. The maximum D.C. estate rate is 16% on amounts in excess of \$10,000,000 and the maximum Maryland estate tax rate is 16% on amounts in excess of \$10,100,000.¹

This means that at the present time, a married couple may give approximately \$23 million during lifetime to family members without triggering any Federal gift taxes, with transfers in excess of the exclusion amount taxed at 40%. Further, amounts given during life by D.C. and Maryland residents may also avoid a separate estate tax of up to 16%.

The 2020 General Election – What Happens if the Democrats Sweep?

Federal Gift and Estate Taxes Potentially Increasing in 2021

If Vice President Biden wins the Presidency, the Democrats maintain control of the House and are also able to take control of the Senate, the prevailing belief is that the Federal gift and estate taxes will become more robust and wealth transfers to subsequent generations will become more difficult and expensive to achieve. Prior to March, this was the general expectation; however, in the aftermath of the COVID-19 pandemic, the pressure to raise revenues will be even greater, making this expectation more likely.

One likely change is a reduction of the Federal gift and estate tax exclusion amount (from \$11.58 million) to a range of \$3.5 to \$5 million.² These potential changes place a premium on using the current \$11.58 million gift exclusion **this year** before it can be reduced next year.

Other possible changes include: (i) imposing higher gift and estate tax rates (i.e., applicable to transfers after the exclusion amounts are used), (ii) eliminating the so-called “step-up in basis” rule that increases the income tax basis of assets upon the owner’s death, (iii) taxing unrealized capital gains upon the owner’s death, (iv)

¹ After considering the Federal estate tax deduction for state death taxes, the maximum effective rate of the D.C. and Maryland estate taxes is 9.6%, which means that the aggregate maximum estate tax rate is 49.6% (Federal and D.C./Maryland).

² Note that even if the Democrats do not win, the exemption is slated to be reduced to roughly \$6 million in 2026.

restricting the use of grantor retained annuity trusts (GRATs), (v) eliminating valuation discounts in inter-family transfers of property, and (vi) eliminating the use of so-called “grantor” trusts to achieve wealth transfers free of gift and estate taxes.³ Engaging in certain techniques now and having the benefit of the current rates, laws, strategies and techniques can help achieve wealth transfers at potentially a significantly lower cost.

Retroactive Legislation

Often, when a legislative tax bill is enacted as law, the effective date is retroactive to the date that the bill was introduced. Sometimes the retroactivity has been challenged as being unconstitutional. In most instances, the courts have opined that such legislation was constitutional. Acting now would allow transactions to potentially avoid legislation enacted during 2021 and made retroactive to January 1, 2021.

Other Factors

Reduced Asset Values

Due to the COVID-19 pandemic, the financial markets and overall economy have reduced assets values. While the markets have regained significant value over the past few months, many assets and private companies still suffer depressed values. Engaging now can help achieve wealth transfers at current lower values.

Historic Low Interest Rates

Interest rates are at historic lows. The August applicable Federal rates are: short-term 0.17%, mid-term 0.41%, long-term 1.12%; and the 7520 rate will be 0.4%.⁴ These interest rates are used in many of our recommended wealth transfer strategies. In most cases, the lower the rate, the lower the costs of inter-generational transfers.⁵ Thus, even if there is no change in the government and consequently no change in the Federal gift and estate taxes, it is an extraordinary time for wealth transfers.

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We are all anxious about the current events (virus, financial and political). These same events, however, have created a unique, and limited time opportunity to mitigate the tax costs of transferring wealth.

If you have any questions, please contact one of our lawyers.

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³ Furthermore, discussion of a wealth tax has surfaced with greater frequency, albeit such a tax is not likely a near term reality.

⁴ September 2020 rates are being projected to be even lower!

⁵ With respect to the Section 7520 rate, to put this current rate level into perspective – prior to 1990, the valuation rate for transfers was fixed at 10%, and then in 1990, Congress implemented Section 7520 with the idea that the valuation rate for transfers should be based on changing interest rates. When the valuation tables were released, separate tables were released for various valuation rates with 0.2% intervals. The lowest valuation rate in the then tables was 2.0%. We are now have a 7520 rate of 0.4%!