

Low Interest Rates and Asset Values Create Unique Opportunity for Gift Planning

April 2, 2020

The spread of the coronavirus has impacted the health and financial well-being of people worldwide. The safety and security of oneself and one's family are naturally of critical importance during these times. However, for individuals who have the means and ability to do so, the current economic environment presents a unique opportunity for gift-planning.

The federal gift and estate taxes apply, respectively, to transfers of wealth during life and at death. In each case, the measure of the transfer is the fair market value of the property given. In 2020 each individual has an exclusion against the federal gift and estate taxes of \$11.58 million, and gifts made during life have the effect of reducing the exclusion remaining at death. Strategies to minimize the federal gift and estate taxes frequently involve making lifetime gifts. Many of these gift strategies are particularly powerful when the value of the property given is low and when interest rates are low. Both such conditions exist at the present time. Accordingly, individuals who are concerned about tax-minimization and are otherwise secure are in the midst of a unique environment to make gifts for estate planning purposes.

Certain kinds of gifts that can work well when asset values and interest rates are low are as follows:

- Gifts of marketable securities, closely-held business interests and real estate: Much of this property has dropped suddenly in value. These assets can be transferred to family members now, or to trusts for their benefit, at a discount to their value from just a few months ago. A transfer of property at reduced values uses less of the donor's federal gift and estate tax exclusion. Any later appreciation in the property given or income generated by it does not use any of the donor's exclusion and is not included in the donor's estate.
- Sales to intentionally defective grantor trusts: This strategy involves selling assets to a trust in exchange for a promissory note. The trust is structured so that it is treated as being owned by the donor for income tax purposes (i.e., the donor pays the tax on the income). Because the trust is disregarded, such a sale should not trigger any built-in gain from the asset, nor are interest payments under the promissory note taxable to the donor. Income and appreciation from the property transferred are used to service the note. Because this is a sale, the donor is not treated as making a gift. Reduced asset values and interest rates make the sale cheaper and make it easier for the trust to pay off the note.
- Grantor retained annuity trusts ("GRATs"): A GRAT is a way for a donor to shift appreciation in the value of property to family members at little to know gift tax cost. The donor funds a trust with property and retains the right to receive annuity payments back for a short period

of time (perhaps 2-3 years). The annuity payments are structured so that the donor receives back the value of what he contributed, plus interest at a rate published by the IRS. That interest rate changes monthly and is 1.2% for GRATs funded in April 2020. To the extent the GRAT's property appreciates faster than that hurdle rate, the appreciation passes to family members.

- Charitable lead annuity trusts ("CLATs"): A CLAT works in a manner that is somewhat similar to a GRAT – annuity payments are made to charity for a term of years and any property remaining at the end of the term is payable to family members. Family can expect to benefit to the extent that the income and appreciation of the trust exceed the IRS's interest rate. A CLAT can be structured so that either the donor or the trust itself receives a charitable deduction for the value of the annuity payments.

Loans to family members are not treated as gifts if they meet certain requirements, including minimum rates of interest set by the IRS. The minimum interest rates for April 2020 are historically low. This may also present an opportunity to refinance existing intra-family loans to lock-in lower interest rates.

The federal estate and gift tax exclusion is indexed for inflation but is scheduled to drop by roughly half in 2026. Of course, it is possible that Congress may alter the exclusion amount sooner than 2026 as a way of raising revenue. Individuals who intend to use the exclusions should consider doing so sooner rather than later.

These are only some examples of planning opportunities that are currently available. Individuals who are contemplating making gifts to family members should contact their attorney at Goulston & Storrs to discuss their own particular circumstances.