2024 WICPA TAX CONFERENCE

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FEDERAL TAX UPDATE

Get insights on the hottest legislative, judicial and IRS developments impacting practitioners during the upcoming filing season, including a look at "Taxmageddon"

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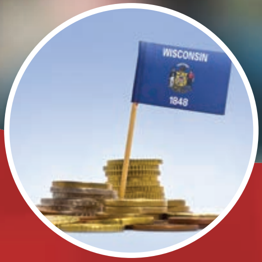
Hear about the new Wisconsin tax laws, changes to 2024 Wisconsin tax returns, updates on DOR administrative and procedural initiatives affecting tax practitioners, and more



WISCONSIN TAX UPDATE

Find out about the latest updates on Wisconsin case law and legislative and administrative developments that have occurred in the past year

MONDAY, NOV. 11 & TUESDAY, NOV. 12

BROOKFIELD CONFERENCE CENTER & WICPA CPE LIVESTREAM

MATERIALS AT A GLANCE

The following materials are from the Tuesday afternoon sessions of the 2024 WICPA Tax Conference held on Monday, Nov. 11 & Tuesday, Nov. 12, including:

- Tax Effects of Partnership Interest Transactions
- Estate Planning in a "Higher" Interest Rate Environment
- Year-end Tax Planning

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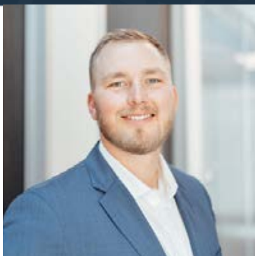

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1 – 2 p.m.

Tax Effects of Partnership Interest Transactions

John A. Sikora, J.D., *Shareholder, von Briesen & Roper, s.c.*

Tax Effects of Partnership Interest Transactions

John Sikora, von Briesen & Roper, s.c.

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John Sikora is a Shareholder in the Tax, Real Estate and M&A sections at von Briesen & Roper, s.c. He represents clients in tax planning and the buying and selling of businesses and real estate. John has taught the tax practice and procedure course and the corporate income tax course at Marquette University Law School and the taxation of partnerships and S corporations course at the University of Wisconsin-Milwaukee masters program. He has been a frequent presenter to the State Bar of Wisconsin and the WICPA, has presented to the ABA Tax Section, has authored articles for the Journal of Taxation, Journal of Real Estate Taxation, TAXES – The Tax Magazine and other tax publications. He is a former chair of the Board of Directors of the State Bar of Wisconsin Taxation Section, a former editor of the *Wisconsin State Bar Tax News,* has been included in *The Best Lawyers in America*®, Tax (2003-2023), and was named Best Lawyers® Tax "Lawyer of the Year", Milwaukee for 2013.

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Objectives

- Principles/rules – 5 general "tax categories" of transactions
- Subchapter K
- Apply principles/rules to commonly encountered deals, which often involve, for tax purposes, more than 1 of those transactions
- Discussion applies to all tax partnerships (will refer generally to LLCs for which no check the box election made)

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Partnership Transaction Categories for Discussion

- Formation/contribution
- Distribution
- Redemption
- Transfer of interest
- Liquidation/termination

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Formation/Contribution - General Principles/Rules

- Nonrecognition – IRC 721(a)
  - Exception – investment company – 721(b)
  - Exception – liability shifts – 731/752
  - Exception – disguised sale rules - 707
- With exceptions, generally carryover basis for contributor - 722
- With exceptions, generally carryover basis for partnership – 723
- With exceptions, generally holding periods tack – 1223(1) and (2)

Formation/Contribution - General Principles/Rules - continued

- Inclusion of share of partnership debt in outside basis – IRC 752
- Inside/outside basis differences created
- 704(c) disparities, which if existing will have effect on later transactions – 704(c)(1)(A)

Distributions – General Principles/Rules

- Partner
  - Nonrecognition of gain except to extent cash exceeds outside basis (marketable securities treated as cash; reduction of share of partnership liabilities treated as receipt of cash) – IRC 731(a)(1)
  - Nonrecognition of loss except upon liquidation of interest with only money, unrealized receivables and inventory received in the distribution – 731(a)(2)
  - Basis in property received
    - Distributions other than in liquidation of partner's interest - same basis as partnership, limited by partner's outside basis minus money received – 732(a)
    - Distributions in liquidation of partner's interest – partner's outside basis minus money received – 732(b)

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Distributions – General Principles/Rules - continued

- Partnership
  - Nonrecognition – IRC 731(b)
  - Generally, no adjustment to basis of undistributed property – 734(a)

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Distributions – General Principles/Rules - continued

- Partnership - continued
  - However, under 734(b):
    - If 754 election existing or there is a "substantial basis reduction"
    - Then:
      - the basis of undistributed property is increased by the amount of gain recognized by the partner on the distribution under 731(a)(1) or, if by reason of 732(a)(2) or 732(b) the partnership's basis in the distributed property exceeds the basis in the distributed property to the recipient partner, such excess
      - the basis of undistributed property is decreased by the amount of loss recognized by the partner on the distribution under 731(a)(2) or, if by reason of 732(b) the partner's basis in the distributed property exceeds the partnership's basis in the distributed property, such excess

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Distributions – General Principles/Rules - continued

- Other distribution principles/rules
  - Distribution of property contributed to a partnership to a partner other than the contributor within 7 years after the contribution can give rise to gain or loss to the contributing partner, determined based on FMV of the property at the time of the distribution – IRC 704(c)(1)(B)(i)
  - If a partner has "net precontribution gain" and the partner receives a distribution of property from the partnership within 7 years of contributions by that partner that create the net precontribution gain, that partner will recognize gain equal to the lesser of the precontribution gain and the excess of the FMV of the distributed property over the partner's outside basis – IRC 737

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Distributions – General Principles/Rules - continued

- Other distribution principles/rules - continued
  - If a partner receives in a distribution unrealized receivables or "substantially appreciated" inventory (sometimes referred to as "hot assets") in "exchange" for all of part of his interest in other partnership property, such transaction is generally treated as a sale between the partner and partnership – IRC 751(b)(1)(A)
  - If a partner receives in a distribution other partnership property in "exchange" for all or part of the partner's interest in "hot assets", is generally treated as a sale transaction between the partner and partnership – 751(b)(1)(B)
  - Exceptions – a distribution of property the partner contributed to the partnership; and payments described in 736(a) (discussed below)

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Redemptions – General Principles/Rules

- Distribution principles/rules generally apply if redemption is of less than all of partner's interest
- However, specific additional provision (IRC 736) relates to payments in liquidation of the interest of "a retiring partner or a deceased partner"
- First determination in applying 736 is to determine what portion of such payments is in exchange for partner's interest in partnership property (sometimes referred to as 736(b) payments)

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Redemptions – General Principles/Rules - continued

- In making such determination:
  - If capital is not a material income producing factor for the partnership and the retiring or deceased partner was a general partner

    then:
  - Payments for the partner's interest in partnership property do not include payments with respect to unrealized receivables nor goodwill except to the extent the partnership agreement provides for a payment with respect to goodwill

Redemptions – General Principles/Rules - continued

- After determining amount deemed received for the retired or deceased partner's interest in partnership property, distribution rules/principles are applied to that amount
- Payments not made in exchange for the retired or deceased partner's interest in partnership property ((sometimes referred to as 736(a) payments) are considered a distributive share of partnership income if determined with regard to the income of the partnership and as a guaranteed payment if determined without regard to the income of the partnership

Transfers of Interests – General Principles/Rules

- Generally considered the sale or exchange of a capital asset – IRC 741
- Exception – Amounts received in exchange for partner's interest attributable to partner's interest in unrealized receivables or inventory items are treated as other than for sale or exchange of capital asset – 751(a)
- In determining amounts realized in connection with transaction, reduction in share of partnership debt is included in amount realized

Transfers of Interests – General Principles/Rules - continued

- Transferee's initial basis in acquired partnership interest determined under general tax principles (e.g., cost if a purchase - IRC 1012)
- Cost basis will include transferee's share of partnership liabilities under 752
- Other partners generally unaffected by transfers of interests of a partner

Transfers of Interests – General Principles/Rules - continued

- Generally, partnership's basis in property does not change upon transfer of interest – IRC 754 and 743(a)
- Exceptions – If Section 754 election or "substantial built-in loss" existing:
  - Partnership basis in property is increased by the excess of the transferee partner's outside basis over such partner's share of inside basis – 743(b)(1)
  - Partnership basis in property is decreased by the excess of the transferee's partner's share of inside basis over such partner's outside basis – 743(b)(2)
  - Such increases or decreases are with respect to the transferee partner only – 743(b)(2) flush language

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Consolidations and Mergers – General Principles/Rules

- Generally, a partnership terminates only if no part of any business, financial operation or venture continues to be carried on by at least 2 partners - IRC 708(b)(1)
- If a partnership is divided into 2 or more partnerships, any resulting partnership in which members of the prior partnership hold greater than a 50% interest in capital and profits is deemed to be a continuation of the prior partnership - 708(b)(2)(B)
- If 2 or more partnerships merge or consolidate, the resulting partnership is deemed a continuation of any merging or consolidating partnership whose members own more than 50% of the resulting partnership (and the other partnerships to the merger terminate) – 708(b)(2)(A); if under this rule the resulting partnership could be considered a continuation of more than 1 of the merging or consolidating partnerships, it is considered a continuation of the partnership credited with the contribution of assets having the greatest FMV (net of liabilities) to the resulting partnership (and the other prior partnerships are deemed terminated) – Reg. Section 1.708-(c)(1)

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Consolidations and Mergers – General Principles/Rules - continued

- Typical merger (e.g., merger under state law) treated as an "assets over" transaction
  - First, each terminating partnership is treated as transferring all its assets and liabilities to the resulting partnership
  - Second, each terminating partnerships is deemed to distribute the interests in the resulting partnership to its partners in liquidation of their interests
- Thus, formation/contribution rules and liquidation/termination principles/rules generally apply
- Possible to structure also as "assets up" transaction (in which steps are reversed)

Liquidation/Termination – General Principles/Rules

- A partnership terminates only if no part of any business, financial operation or venture continues to be carried on by at least 2 partners - IRC 708(b)(1)
- Principles/rules under 731 discussed above applicable to partner recognition of gain or loss
- Principles/rules under 732(b) discussed above applicable to partner basis in property received

Effect on Taxable Years/Determining Allocations – General Principles/Rules

- Generally, taxable year of the partnership will not close as a result of the transactions – IRC 706(c)(1)
- And, generally, taxable year of the partnership will not close as to a partner as a result of sale or exchange of less than the partner's entire interest or reduction in the partner's interest in the partnership – 706(c)(2)(B)
- Taxable year of the partnership does close for a partner if the entire interest of the partner in the partnership terminates – 706(c)(2)(A)
- Method for determining partner's share of partnership items when interest changes – see Regulation Section 1.706-4

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Transaction I - Purchase of Interests in DRE

- Application of principles to situation – addition of member to single member disregarded entity – by cross purchase (e.g., purchase by B of 70% of interests in XYZ, LLC, a SMLLC, from A for $100)
- Common deals in which occurring:
  - Final step in sale of S corporation business re: which there has been (usually immediately preceding) F reorganization restructuring, if seller retaining an interest in business
  - Sale of part of business operated as LLC, for example real estate business if tax assessment concern present

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Transaction I - Purchase of Interests in DRE - continued

- Analysis of transaction - Rev. Rul. 99-5, situation 1
  - Transaction results in new tax partnership being formed (assuming no check the box election), as now 2 owners
  - A recognizes gain or loss on the sale of 70% of the assets of XYZ, LLC
  - A and B then deemed to contribute assets deemed held by each (70% by B, 30% by A); formation rules/principles apply

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Transaction I - Purchase of Interests in DRE - continued

- Practice suggestions/observations
  - Allocation of purchase price among assets important
    - Have noticed this is sometimes overlooked, particularly if interests in more than one SMLLC being acquired in the deal
    - Allocation may be important to A, as A will be deemed to be selling assets, gains from which may be subject to different tax rates
  - Agreement on IRC 704(c) method important to both
  - Some assert 754 election necessary for B; is it?
  - Other

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Transaction 2- Acquisition of Interests in DRE

- Application of principles to situation – addition of member to single member disregarded entity – by contribution (e.g., A owns all interests in XYZ, LLC, a SMLLC; B contributes $100 to XYZ for 70% of interest in XYZ)
- Common deals in which occurring:
  - Investment in business by employee
  - Investment in business operated as LLC, for example real estate business if tax assessment concern present

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Transaction 2 – Acquisition of Interests in DRE - continued

- Analysis of transaction - Rev. Rul. 99-5, situation 2
  - Transaction results in new tax partnership being formed (assuming no check the box election), as now 2 owners
  - Contributions are deemed made to the new partnership by A (of the assets held by the LLC) and B (of $100)
  - Formation rules/principles apply

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Transaction 2 – Acquisition of Interests in DRE - continued

- Practice suggestions/observations
  - Allocation of purchase price among assets important
    - Have noticed this is sometimes overlooked
    - Allocation is important regarding establishing 704(c) differences
  - Agreement on IRC 704(c) method important to both
  - Some assert 754 election should be considered; should it?
  - Other

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Transaction 3 - Purchase of All Interests in Tax Partnership by One Buyer

- Application of principles to situation – buyer, B, purchases all of membership interests in RST, LLC, a multi-member LLC taxed as a partnership, from its 3 members (R, S and T)
- Common deals in which occurring:
  - Purchase of a business
  - 1031 transactions in which the LLC holds real property, and another (exchanger in the 1031) wants to acquire the real property as replacement property (particularly in situations in which permit, transfer tax or other issues present)

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Transaction 3 – Purchase of All Interests in Tax Partnership by One Buyer - continued

- Analysis of transaction - Rev. Rul. 99-6, situation 2
  - Transaction results in termination of tax partnership, as now 1 owner
  - Tax treatment - R, S and T:
    - Transfer of interest rules/principles
    - I.e., application of 741 and 751(a)

Transaction 3 – Purchase of All Interests in Tax Partnership by One Buyer - continued

- Analysis of transaction - Rev. Rul. 99-6, situation 2 - continued
  - Tax treatment - B:
    - First, RST is deemed to make a liquidating distribution of its assets to R, S and T
    - Then, B deemed to purchase all of those assets by purchase
    - Thus, asset purchase rules/principles (purchase price basis in assets and holding period in assets beginning on day of purchase)

Transaction 3 – Purchase of All Interests in Tax Partnership by One Buyer - continued

- Practice suggestions/observations
  - Allocation of purchase price among assets important
    - Have noticed this is sometimes overlooked
    - Allocation is important regarding 751(a) application as to R, S and T
    - Allocation is important to B, as has purchased assets
  - EINs/IRC 1060/other reporting issues
  - Other

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Transaction 4 - Purchase of All Interests in Tax Partnership by One (related) Buyer

- Application of principles to situation – L, who is a 30% member of LM LLC, a two-member LLC taxed as a partnership, purchases all of the membership interests (70%) from the other member (M)
- Common deals in which occurring:
  - Purchase of the business by L
  - Implementation of buy-sell provisions in an operating or other agreement by reason of triggering events (such as death, disability, exercise of ROFR, relating to M's interest)

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Transaction 4 - Purchase of All Interests in Tax Partnership by One (related) Buyer - continued

- Analysis of transaction - Rev. Rul. 99-6, situation 1
  - Transaction results in termination of tax partnership, as now 1 owner
  - Tax treatment - M:
    - Transfer of interest principles/rules
    - I.e., 741 and 751(a) application

Transaction 4 – Purchase of All Interests in Tax Partnership by One (related) Buyer - continued

- Analysis of transaction - Rev. Rul. 99-6, situation 1 - continued
  - Tax treatment - L:
    - First, LM is deemed to make a liquidating distribution of its assets (in 30/70 proportion) to L and M
    - Then, L is deemed to purchase all of the assets of LM LLC that were deemed distributed by LM to M; L',s basis in those assets is purchase price paid by L to M for the 70% interest, and new holding period commences
    - As to the 30% of the assets distributed to L, distribution principles/rules apply

Transaction 4 – Purchase of All Interests in Tax Partnership by One (related) Buyer - continued

- Practice suggestions/observations
  - Allocation of purchase price among assets important
    - Allocation is important regarding 751(a) application as to M
    - Allocation is important to L, as has purchased assets
  - EIN/other reporting issues
  - Other

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Transaction 5 - Purchase of Some Interests in Tax Partnership by Buyer

- Application of principles to situation – buyer, D, purchases the entire 30% membership interests of E in DEF LLC, a three-member LLC taxed as a partnership in which D, E and F are the members
- Common deals in which occurring:
  - Purchase of interest in the business by another increasing his/her/its interest
  - Implementation of cross purchase buy-sell provisions in an operating or other agreement by reason of triggering events (such as death, disability, exercise of ROFR, relating to E’s interest)

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Transaction 5 - Purchase of Some Interests in Tax Partnership by Buyer - continued

- Analysis of transaction – transfer of interest principles/rules
  - Partnership continues
  - Tax treatment - E:
    - Transfer of interest principles/rules
    - I.e., 741 and 751(a) application

Transaction 5 - Purchase of Some Interests in Tax Partnership by Buyer - continued

- Analysis of transaction – transfer of interest principles/rules - continued
  - Partnership continues
  - Tax treatment - D:
    - Typical tax treatment purchase – cost basis in partnership interest and holding period commencing on purchase
    - Basis to include share of partnership liabilities

Transaction 5 - Purchase of Some Interests in Tax Partnership by Buyer

- Practice suggestions/observations
  - Allocation of purchase price among assets important
    - Allocation is important regarding 751(a) application as to E
    - Allocation is important regarding potential 754 election
  - Section 754 election or mandatory 743 adjustment issues
  - Allocation of income in year of sale/issues
  - Other

Transaction 6 - Purchase of Some Interests in Tax Partnership by Buyer

- Application of principles to situation – buyer, G, purchases half of E's 30% membership interest in DEF LLC, a three-member LLC taxed as a partnership in which D, E and F are the members
- Common deals in which occurring:
  - Purchase of interest in the business by employee
  - Acquisition of interest in the business by unrelated person relating to circumstances affecting E or the business, such as desire of E to sell some of interest to third party and waiver of ROFR (by D and F) under typical operating agreement

Transaction 6 - Purchase of Some Interests in Tax Partnership by Buyer - continued

- Analysis of transaction – transfer of interest principles/rules
  - Partnership continues
  - Tax treatment - E:
    - Transfer of interest principles/rules
    - I.e., 741 and 751(a) application

Transaction 6 - Purchase of Some Interests in Tax Partnership by Buyer - continued

- Analysis of transaction – transfer of interest principles/rules - continued
  - Partnership continues
  - Tax treatment - G:
    - Typical tax treatment purchase – cost basis in partnership interest and holding period commencing on purchase
    - Basis to include share of partnership liabilities

Transaction 6 - Purchase of Some Interests in Tax Partnership by Buyer

- Practice suggestions/observations
  - Allocation of purchase price among assets important
    - Allocation is important regarding 751(a) application as to E
    - Allocation is important regarding potential 754 election
  - Section 754 election or mandatory 743 adjustment issues
  - Allocation of income in year of sale/issues
  - Other

Transaction 7 – Merger of 2 Tax Partnerships

- Application of principles to situation – HIJ LLC, in which H, I and J each own a one-third interest and UVW LLC, in which H owns a 40% interest and I and J each own a 30% interest, merge, with the resulting entity being renamed HIJUVW LLC; assume net value of assets of HIJ exceeds net value of assets of UVW
- Common deals in which occurring:
  - Combination of businesses
  - Restructuring in advance of potential planning for sale of businesses

Transaction 7 – Merger of 2 Tax Partnerships - continued

- Analysis of transaction
  - Initially, HIJUVW could be deemed to be a continuation of both HIJ and UVW under merger/consolidation principles/rules
    - Determination of which it will be based on which LLC contributed the greatest asset value (net of liabilities) (here, assumed to be HIJ)
    - Other LLC (here, assumed to be UVW) is deemed to terminate for tax purposes

Transaction 7 – Merger of 2 Tax Partnerships - continued

- Analysis of transaction - continued
  - Unless structured as "assets up" transaction, is deemed "assets over" transaction – therefore, contribution of assets and liabilities by UVW to HIJ in exchange for interests in HIJ, followed by distribution of interests in HIJ by UVW to its partners
  - Thus, formation/contribution and liquidation/termination principles/rules apply

Transaction 7 – Merger of 2 Tax Partnerships - continued

- Practice suggestions/observations
  - 704(c)/reverse 704(c) disparities, issues, method
  - Reporting matters
  - EINs
  - Other

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Questions/Comments

Thank you for your attention

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1 – 2 p.m.

Estate Planning in a “Higher” Interest Rate Environment

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Estate Planning in a “Higher” Interest Rate Environment

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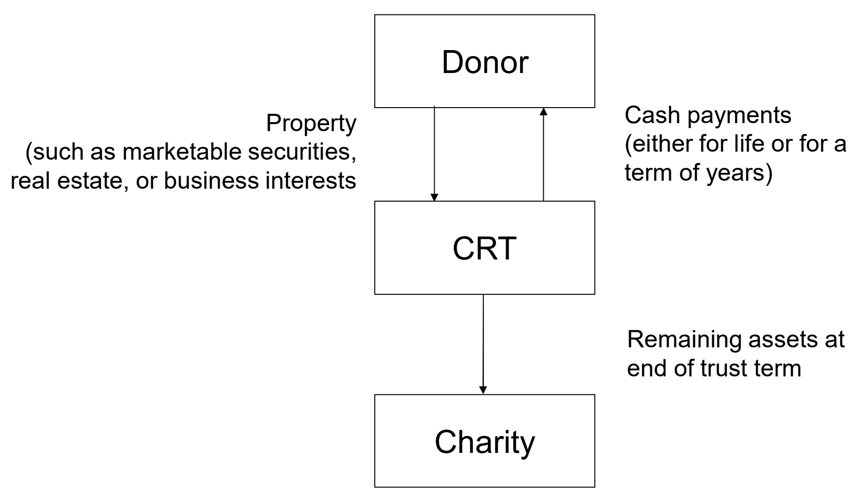
October 21, 2024

Historic §7520 Rates (%)

	JAN	FEB	MAR	APR	MAY	JUN	JUL	AUG	SEP	OCT	NOV	DEC
2024	5.20	4.80	5.00	5.20	5.40	5.60	5.40	5.20	4.80	4.40	4.40	
2023	4.60	4.60	4.40	5.00	4.40	4..20	4.60	5.00	5.00	5.40	5.60	5.80
2022	1.60	1.60	2.00	2.20	3.00	3.60	3.60	3.80	3.60	4.00	4.80	5.20
2021	0.60	0.60	0.80	1.00	1.20	1.20	1.20	1.20	1.00	1.00	1.40	1.60
2020	2.00	2.20	1.80	1.20	0.80	0.60	0.60	0.40	0.40	0.40	0.40	0.60
2019	3.40	3.20	3.20	3.00	2.80	2.80	2.60	2.20	2.20	1.80	2.00	2.00
2018	2.60	2.80	3.00	3.20	3.20	3.40	3.40	3.40	3.40	3.40	3.60	3.60
2017	2.40	2.60	2.40	2.60	2.40	2.40	2.20	2.40	2.40	2.20	2.40	2.60
2016	2.20	2.20	1.80	1.80	1.80	1.80	1.80	1.40	1.40	1.60	1.60	1.80
2015	2.20	2.00	1.80	2.00	1.80	2.00	2.20	2.20	2.20	2.00	2.00	2.00
2014	2.20	2.40	2.20	2.20	2.40	2.20	2.20	2.20	2.20	2.20	2.20	2.00
2013	1.00	1.20	1.40	1.40	1.20	1.20	1.40	2.00	2.00	2.40	2.00	2.00
2012	1.40	1.40	1.40	1.40	1.60	1.20	1.20	1.00	1.00	1.20	1.00	1.20
2011	2.40	2.80	3.00	3.00	3.00	2.80	2.40	2.20	2.00	1.40	1.40	1.60
2010	3.00	3.40	3.20	3.20	3.40	3.20	2.80	2.60	2.40	2.00	2.00	1.80
2009	2.40	2.00	2.40	2.60	2.40	2.80	3.40	3.40	3.40	3.20	3.20	3.20
2008	4.40	4.20	3.60	3.40	3.20	3.80	4.20	4.20	4.20	3.80	3.60	3.40
2007	5.60	5.60	5.80	5.60	5.60	5.60	6.00	6.20	5.80	5.20	5.20	5.00
2006	5.40	5.20	5.40	5.60	5.80	6.00	6.00	6.20	6.00	5.80	5.60	5.80
2005	4.60	4.60	4.60	5.00	5.20	4.80	4.60	4.80	5.00	5.00	5.00	5.40
2004	4.20	4.20	4.00	3.80	3.80	4.60	5.00	4.80	4.60	4.40	4.20	4.20
2003	4.20	4.00	3.80	3.60	3.80	3.60	3.00	3.20	4.20	4.40	4.00	4.20
2002	5.40	5.60	5.40	5.60	6.00	5.80	5.60	5.20	4.60	4.20	3.60	4.00
2001	6.80	6.20	6.20	6.00	5.80	6.00	6.20	6.00	5.80	5.60	5.00	4.80
2000	7.40	8.00	8.20	8.00	7.80	8.00	8.00	7.60	7.60	7.40	7.20	7.00

CHARITABLE REMAINDER TRUSTS

Charitable Remainder Trust “CRT”



What is a CRT?

- A tax-exempt trust designed to pay you or your beneficiaries a stream of income for life or for a term of years.
- The income stream can be a fixed dollar amount or a fixed percentage of the trust's value determined annually.
- At the end of the term, the assets that remain are paid to the charities of your choice, which can be changed by creator of trust.

What Objectives can a CRT Accomplish?

- Increase income during Donor's lifetime (i.e. supplemental retirement plan)
- Achieve asset diversification
- Obtain income tax deduction against high income
- Immediately reduce value of estate without regard to living out a term
- Leave charitable legacy

Types of CRTs

- Charitable Remainder Annuity Trust
  - Income stream is a fixed dollar amount
  - Income does not fluctuate
  - Steady predictable payout
  - No additional contributions allowed

Types of CRTs, cont.

- Charitable Remainder Unitrust
  - Income stream is a fixed percentage of the value of the trust assets
  - Trust re-valued each year (require “qualified appraisal” if Donor or related or subordinate party serve as Trustee)
  - Income fluctuates with asset value
  - Additional contributions allowed

Charitable Remainder Unitrust Distribution Options

- NI-CRUT
  - Can limit unitrust amount to lesser of trust accounting income or applicable percentage
- NIM-CRUT
  - Can provide that shortfalls in unitrust amount are made up in later years when trust income exceeds unitrust amount
- FLIPs
  - NI-CRUT on NIM-CRUT is converted to straight unitrust on trigger date or event

Who can be a donor?

- An Individual, Corporation, Partnership or Trust
- Donor characteristics that make CRT beneficial:
  - High Income Tax Bracket
  - Own Appreciated Asset
  - Desire to Avoid Capital Gains and Estate Taxes
  - Desire to Contribute to Charity

Who can receive trust income?

- Donor
- Spouse
- Children
- For lifetime(s) or term of years (maximum term of 20 years)

Who can be a charitable beneficiary?

- Public Charities
  - Hospitals
  - Churches
  - Schools/Universities
- Private Foundations

Who can be a trustee?

- Individual
  - The donor could be the trustee of their own CRT; however, if not administered correctly, tax advantages could be lost
  - Independent appraiser needed for hard to value assets in a CRUT
- Corporate Trustee
  - Bank or trust company
- Charity

What are the benefits for the donor?

- Current income tax charitable deduction
- Defer or avoid capital gains tax on the trust's sale of the low-basis property
- Convert asset to income (i.e. cash flow)
- Retain income stream for life or a term of years
- Reduce estate tax
- Benefit one or more charities of choice

What are the income tax implications?

- The donor is allowed a current income tax charitable deduction upon the transfer of assets to the CRT
  - The amount of the tax deduction is based upon several factors, including the donors' age and the present value of the future interest
- No capital gains tax is recognized when the CRT sells the assets since the CRT is a tax-exempt entity
- Income (annuity or unitrust payment) is taxable to the donor when received

Income Taxation of CRT

- Generally exempt from income tax
- Exemption lost if any UBTI
- Application of private foundation rules
- Informational tax returns required to be filed annually

Taxation of Income Recipient

- 4 Tier System
  - Ordinary income
  - Capital gain
  - Other income (for example, tax-exempt income)
  - Corpus/Return of principal

Gift Tax Implication

- No gift tax on value of charitable remainder or when Donor retains income interest

- Gift is made when income interest paid to someone other than Donor

- Retain testamentary right to revoke survivor's income interest to avoid gift

Estate Tax Implications

- No estate tax payable on charitable remainder
- When Settlor retains income interest, trust assets includible in gross estate, but deduct value of charitable remainder
- When trust provides for second beneficiary, if second beneficiary survives, value of survivor's interest is taxable

Additional Qualification Rules

- CRTs: The income stream retained by the donor cannot be less than 5% nor more than 50% of the fair market value of the trust assets
- CRTs: The charitable remainder interest must have a present value equal to or greater than 10% of the total amount initially transferred to the trust (and additional contributions in the case of a CRUT)
- CRATs, deduction will be denied if probability exceeds 5% that annuitant will survive beyond exhaustion of trust assets
- Subject to general income deduction limits

CRT Models

- Rev. Procs. 2003-53 to 2003-60 provide guidance for CRATs
- Rev. Procs. 2005-52 to 2005-59 provide guidance for CRUTs

What assets work best?

- Publicly Traded Marketable Securities
- Investment Real Estate
- Closely-Hold Business Stock
  - (NOT S Corporation Stock)
- Naming a CRT as beneficiary at death of an IRA may extend deferral past 10 years
  - The IRA account assets can empty into the CRT without causing income tax until the Trust makes distributions.
  - Trust can begin to earn capital gains and qualifying dividends that would be paid out after the ordinary income has been used to reduce overall taxation.

Michael Best

MARKETABLE SECURITIES EXAMPLE

Assumptions for Illustrations

Michael Best

- Charitable Remainder Annuity Trust ("CRAT")
- Entered into in November, 2024
- Highest/Best §7520 Rate is September, 2024: 4.8%
  - Both October and November §7520 Rate is are 4.4%

Assumptions for Illustrations, cont.

Term:	20 Years
Securities - FMV:	$1,000,000
Securities - Basis:	$200,000
Expected Growth:	6%
CRT Income Stream:	6% of beginning value, so is constant through term
Capital Gains Tax:	18% (combined federal & state)
Ordinary Income Tax:	40% (combined federal & state)
Estate Tax:	40%

Income Tax Results

	W/O CRAT	W/CRAT
Fair Market Value	$1,000,000	$1,000,000
Capital Gains Tax	- 144,000	- 0
Balance to Reinvest	$ 856,000	$1,000,000
6% Annual Income	$ 60,000	$ 60,000
Income over lifetime	$1,200,000	$1,200,000
Income tax deduction	$ 0	$ 239,422
Income tax benefit	$ 0	$ 95,769

Estate Tax Results

	W/O CRAT	W/CRAT
Gross Value of Estate	$ 856,000	$ 0
Estate Tax	-324,400	0
Net Estate for Heirs	$ 513,600	$ 0

Benefit Summary

Family Benefit (lifetime income + income tax benefit + net estate)	$1,713,600	$1,295,769
Amount to Charity	$ 0	$1,000,000
Total Benefit	$1,713,600	$2,295,769

CHARITABLE GIFT ANNUITIES

Charitable Gift Annuities (CGA) – General Characteristics

- Annuity contract between charity and donor
- Transaction is both a purchase of the contract and a charitable contribution
- Charity pays donor a regular, fixed sum each year for the rest of donor's life
- Amount of annuity depends on donor's age, size of the gift, immediate or deferred income payments, and whether a second person is to receive payments
  - Immediate annuity begins upon contribution
  - Flexible deferred annuity begins at a date no later than a set date
  - Testamentary annuity paid to someone other than decedent
- Issue of CGA's by charities is subject to state regulation

Charitable Gift Annuities – Tax Consequences

- Income Tax Treatment
  - Charitable contribution is equal to how much the value of the property contributed exceeds the FMV of the annuity
  - FMV of the annuity is measured using IRC § 7520 tables
  - Deduction is subject to donor's AGI limitations
  - If appreciated property is transferred, treated as a bargain sale and any capital gain realized is recognized by the donor as annuity payments are made (no gain if cash contributed)
  - Annuity payments contain both taxable income and return of capital

Charitable Gift Annuities – Tax Consequences (cont.)

- Gift Tax Treatment
  - Donor receives gift tax charitable deduction for amount going to charity which should be reported on gift tax return
  - If annuity is payable to a second person, portion of annuity is treated as gift (qualifies for $18,000 per year annual exclusion and marital deduction)
- Estate Tax Treatment
  - Single life annuity, no inclusion in donor's estate
  - Value of survivor's interest in two life annuity included in donor's estate
  - Estate tax charitable deduction allowed if established at death

Things You Can Do With a CGA You Can't Do With a CRT

- Payments from charitable annuities can be deferred. The rates for deferred annuities are higher than the rates for immediate annuities.
- Flexible deferred gift annuities can leave the start date open. The longer the annuity is deferred, the larger the annuity payment will be.
- Gift of marketable securities can be made in exchange for CGA in a case where 10% test might be satisfied but the 5% exhaustion text applicable to CRTs would not be met.

Things You Can Do With a CGA You Can't Do With a CRT, cont.

- Most of the private foundation rules apply to a CRT, but not to a CGA
  - Donor could give an office building and continue to maintain an office in the building in exchange for a charitable gift annuity
    - This would not be possible with a charitable remainder trust due to the self dealing rules, which do not apply to a public charity (which the annuity provider must be for this example to work).
  - Closely held stock can be given to a charity in exchange for a CGA
    - A family member could later purchase the shares at fair market value
    - Self dealing rules would prevent that in a CRT.

Differences between CRTs and CGAs

- Part of every annuity payment is likely to be tax free in a CGA.
- CGAs are simpler to set up and maintain than a CRT.
- If annuitant of CGA dies before life expectancy and has not recovered full investment in contract, the remaining unrecovered basis is allowed as a charitable deduction on final return.
- The 10% rule of the CGA is different than the CRT
  - The CGA test does not affect the donor but only the charity.
- The 5% exhaustion rule applies to CRTs, but not to CGAs.

Differences between CRTs and CGAs, cont.

- Remainder beneficiary cannot be changed with a CGA but can in a CRT.
- CGA is limited to one or two lives, but a CRT can have a term of years or be more than two lives.
- CGA can hold S corporation stock.
- Donor cannot control investments in CGA, but can in a CRT.

QUALIFIED PERSONAL RESIDENCE TRUST (QPRT)

What is a QPRT?

- Through a QPRT, it is possible to transfer a principal residence to a Trust.
- Settlor retains the right to live in the residence for a term of years (e.g., 3, 6 or 9 years) rent-free and pays all expenses related to the property.
- Property passes to remainder beneficiaries (usually children) at the end of the term.
- However, if the Settlor dies during the trust term, the full value of the property reverts to the Settlor's estate.
  - As a result, it is important to select an appropriate term.

What Objectives can a QPRT Accomplish?

- Passes residence to remainder beneficiaries at lower value
  - Retained right to live in the residence reduces the value of the gift measured at creation of the Trust.
- If the Settlor survives the term of the QPRT, the residence will be transferred to the Trust's beneficiaries.
  - In doing so, the value of the property escapes federal estate tax in the Settlor's estate.
  - In addition, any <u>appreciation</u> in the value of the property during the term of the QPRT also avoids the federal gift and estate tax.

Operations of QPRT

- Settlor can serve as the Trustee of the QPRT.
- Treated as a grantor trust for income tax purposes.
- The ability to deduct mortgage interest as well as property taxes during the trust term is not affected by the existence of a QPRT.
  - Need to get lender consent on transfer to Trust to not accelerate a loan
  - Each mortgage payment is treated as an additional gift, so best to have any mortgage paid off prior to transfer of a residence to a QPRT

Operations of QPRT, cont.

- To reduce mortality risk of death during term, consider setting up a QPRT for each spouse with the same residence with differing lengths on term of trust
  - Discounts for may be available if transferring 50% undivided interest in real estate.
- Like a GRAT, if the Settlor dies during the trust term, the assets in the QPRT are included in his or her estate, but any gift tax exemption used in establishing the QPRT is restored.
  - As result, the Settlor is in no worse position than if no QPRT was created.
- Real estate should be appraised for transfer.

Operations of QPRT, cont.

- Gift tax return(s) need to be filed to report transfer.
  - Basis of Settlor carries over to Trust/donees.
- Deed required to transfer property to and from QPRT.
  - Assign any insurance related to property to and from QPRT.
- If residence is sold during term of QPRT, the trust converts to a grantor retained annuity trust (GRAT).
  - Settlor cannot purchase the home from the QPRT during the term of the trust, but could purchase the home from the remainder beneficiaries

Operations of QPRT, cont.

- If Settlor wishes to continue to reside in the residence after the Trust term, this can be accomplished by paying a fair market value rent to the Trust's beneficiaries.
  - Create an Agreement to Lease when the QPRT is created.
    - Executed between donor as creator of trustee and as trustee.
    - Usually structured as triple net lease to keep rental income lower for remainder beneficiary owners of property.
    - Prudent to get fair market rental appraisal when lease begins after termination of QPRT.
    - Consider an entity, like an LLC, to hold the property in the hands of the remainder beneficiaries.

QPRT Gift and Estate Tax Savings Illustration

- To illustrate, the amount of the deemed taxable gift and potential tax savings, based on (i) a 3, 6 or 9-year QPRT term, (ii) the fair market value for the residence being $1,000,000, (iii) an assumed 4% annual appreciation in the residence, and (iv) a 40% estate tax rate, is as follows:

Term of Years	Taxable Gift	Value at End of Trust Term	Potential Death Tax Savings
- 3	$823,490	$1,124,864	$120,550
- 6	$664,210	$1,265,319	$240,444
- 9	$520,600	$1,423,312	$361,085

GRANTOR RETAINED INTEREST TRUST (GRIT)

What is a GRIT?

- A GRIT is an estate planning tool that has been around for many years, but, after the Revenue Reconciliation Act of 1990, GRITs were essentially eliminated as a wealth transfer technique among family members
  - GRITs are still a viable tool for unmarried couples or to leave property to a niece or nephew because IRC § 2702 does not apply to them due to the fact that the remainder beneficiary is not a lineal descendant of the Settlor.
- Settlor retains the right to receive all income from the Trust.
- Property passes to remainder beneficiaries at the end of the term.

What Objectives can a GRIT Accomplish?

- Passes property to remainder beneficiaries at lower value
  - Retained right to income reduces the value of the gift measured at creation of the Trust.
- If the Settlor survives the term of the GRIT, the gifted property will be transferred to the Trust's beneficiaries.
  - In doing so, the value of the property escapes federal estate tax in the Settlor's estate.
  - In addition, any <u>appreciation</u> in the value of the property during the term of the GRIT also avoids the federal gift and estate tax.

Operation of a GRIT

- Settlor can serve as the Trustee of the GRIT.
- Treated as a grantor trust for income tax purposes.
- At creation of the trust, the value of the remainder interest is treated as a gift to the remainder beneficiary.
  - Gift tax return must be filed to report remainder interest.
  - Basis of Settlor carries over to Trust/donee

Operation of a GRIT, cont.

- Unlike a GRAT, a GRIT cannot be “zero’d out” for gift tax purposes (the calculation is similar to that of a QPRT).
  - The gift can be reduced by having a longer trust term, but then mortality risks for the Settlor are higher.
- If the unmarried partners use a GRIT, if the relationship is terminated during the GRIT term, the trust should be drafted to replace the remainder beneficiary with new remainder beneficiaries (like nieces or nephews) that are not lineal descendants of the Settlor.

Operation of a GRIT, cont.

- Like a GRAT, if the Settlor dies during the trust term, the assets in the GRIT are included in his or her estate, but any gift tax exemption used in establishing the GRIT is restored.
  - As result, the Settlor is in no worse position than if no GRIT was created.
- If the assets transferred to the GRIT generate income at a rate lower than the IRS's discount rate for the month of the transaction (November rate is 4.4%), the difference passes to the remainder beneficiary gift tax free.
- Appreciating stock that does not historically pay dividends (but can) is an example of a good asset to contribute to a GRIT.

GRIT Gift and Estate Tax Savings Illustration

- Calculations for a GRIT gift and potential estate tax savings are exactly the same as a QPRT, so see slide 43 for example.

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Year-end Tax Planning

Robert Keebler, CPA/PFS, MST, AEP (Distinguished), *Partner, Keebler & Associates, LLP*

Year-end Tax Planning

2024

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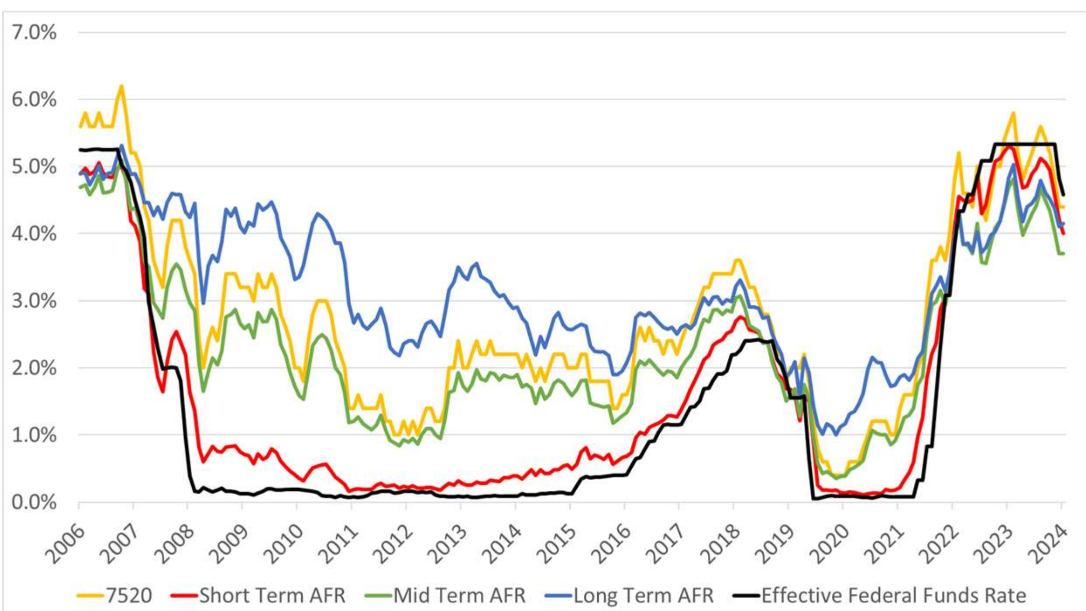

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Critical Themes

– Gain & loss harvesting

– Roth conversions

– Estate & trust

– Charitable planning

Year-end Planning: Annual General Checklist

- ❑ Bracket Management
  - ❑ Bonuses
  - ❑ Recognition events
  - ❑ Time business expenses –AMT awareness
- ❑ Itemized Deduction Timing
  - ❑ Medical expenses
  - ❑ Property tax
  - ❑ Charitable contributions
  - ❑ Disaster Area casualty losses
- ❑ Gain Harvesting
  - ❑ Current < Future rate ?
  - ❑ Consider forced recognition events (e.g. warrants)
- ❑ Loss Harvesting
  - ❑ Offset gains
  - ❑ $3,000 ordinary income offset

Year-end Planning: Annual General Checklist

- ❑ Retirement Planning
  - ❑ Fund IRAs
  - ❑ Fund 401ks
  - ❑ Fund pension plans
  - ❑ Optimize Traditional/Roth mix
  - ❑ Consider Roth conversions
  - ❑ Review RMDs
  - ❑ Review NUA
- ❑ Education Planning
  - ❑ Time tuition payments
  - ❑ Fund 529 plans
  - ❑ Fund Coverdell accounts
- ❑ Executive Planning
  - ❑ Review NQCD
  - ❑ Review NQSOs / ISOs
  - ❑ Review concentrated positions
- ❑ Charitable Planning
  - ❑ Consider QCDs
  - ❑ Consider appreciated assets
  - ❑ Consider DAFs
- ❑ Estate Tax Planning
  - ❑ Make annual exclusion gifts
  - ❑ Make medical gifts
  - ❑ Make tuition gifts

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Year-end Planning: Annual General Checklist

- ❑ Estimated Taxes
  - ❑ Review payments & estimated taxable income
  - ❑ Extra payment to reduce penalty
  - ❑ Additional W-2 withholding to eliminate penalty
  - ❑ AMT review
- ❑ Medical Expense Planning
  - ❑ Review Medicare premiums
  - ❑ Review HSA contributions
  - ❑ Review FSA balance
- ❑ Significant Financial Events Next Year
  - ❑ Recognition events
  - ❑ New investments
  - ❑ Re-allocation plans
  - ❑ Vesting
- ❑ Major Life Events Next Year
  - ❑ Family changes
  - ❑ Job changes
  - ❑ Moving

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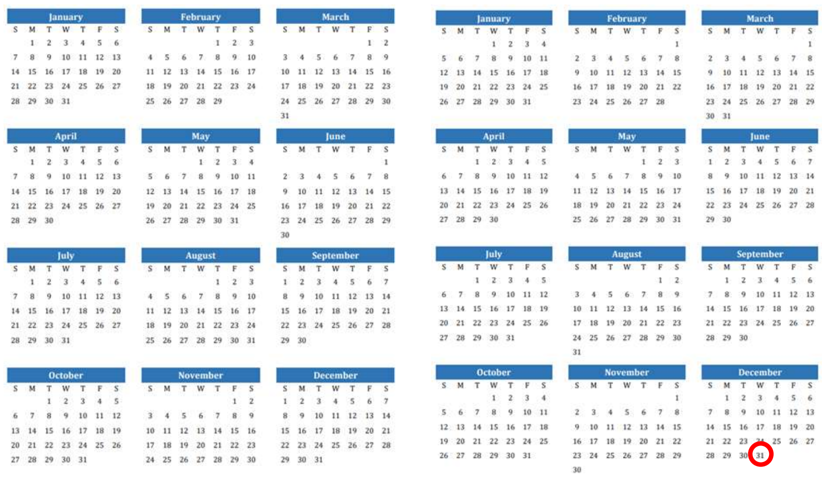
TCJA Sunset – Coming Soon!

2024 2025



General Democratic Party Tax Policy Themes

UNLIKELY GIVEN THE ELECTION RESULTS

- Additional payroll taxes on high-earners
- Increase the marginal rate imposed on high-income individuals
- Increase the capital gains rate imposed on high-income individuals
- Tax wealth generally; various ideas include an annual wealth tax & tighter rules related to estate & gift taxes
- Increase the corporate income tax rates

President Elect Trump Campaign Trail Promises

- Extend or make permanent the TCJA tax cuts
- Repeal Inflation Reduction Act tax credits
- New exemptions:
  - Tip income (payroll and income tax)
  - Social security benefits
  - Overtime pay
- Unspecified additional cuts for working families (Vague comments from the former president and an idea float by Senator Vance to increase the CTC to $5,000.)
- Further decrease the corporate tax rate from 21% to 15% for American manufactures
- Promote homeownership through tax incentives
- Make car loan interest payments deductible

Reconciliation

The Path Through the Senate to Tax Reform

- Reconciliation bills only require a simple majority (51 votes) in the Senate, as opposed to the usual 60 votes, so they cannot be filibustered.
- It is frequently used to end filibusters in the Senate when one party lacks a 60-vote majority but controls the Senate, the House, and the presidency.
- According to the Senate's interpretation of the Congressional Budget Act, reconciliation can only address taxes, spending, revenue, and the debt limit.

Expect a huge Republican drafted bill and a party-line vote.

Strategic Thinking
Preparing for Year-end 2025 Tax Reform

- Agility is critical
- Flexibility is critical
- Ongoing client communication is critical
- The monthly AICPA/PFS update should be helpful

2024 Rates

TOP OF EACH BRACKET

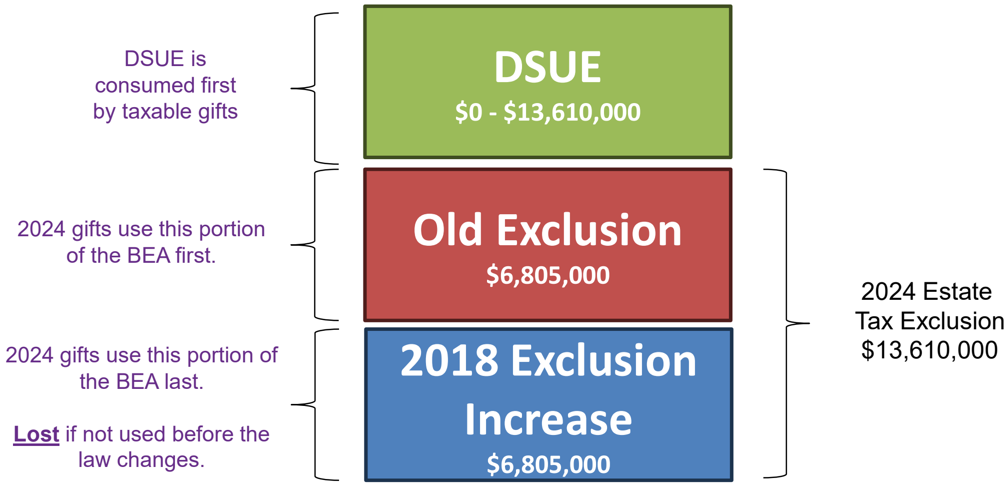
	S	MFJ/QW	MFS	HOH	T&E
10%	$ 11,600	$ 23,200	$ 11,600	$ 16,550	$ 3,100
12%	$ 47,150	$ 94,300	$ 47,150	$ 63,100	-
22%	$ 100,525	$ 201,050	$ 100,525	$ 100,500	-
24%	$ 191,950	$ 383,900	$ 191,950	$ 191,950	$ 11,150
32%	$ 243,725	$ 487,450	$ 243,725	$ 243,700	-
35%	$ 609,350	$ 731,200	$ 365,600	$ 609,350	$ 15,200
37%					

TOP OF EACH CAPITAL GAINS BRACKET

	S	MFJ/QW	MFS	HOH	T&E
0%	$ 47,025	$ 94,050	$ 47,025	$ 63,000	$ 3,150
15%	$ 518,900	$ 583,750	$ 291,850	$ 551,350	$ 15,450
20%					

Estate & Gift Taxes

Exclusion Reduction Math – "Use It or Lose It"



2024 Year-end Update

Tax Provisions of Interest

- Deduction for Business Meals
  - Coronavirus-related relief provided a 100% deduction, but this sunset on 12/31/22
  - 50% of meals are deductible currently

Tax Provisions of Interest

- Bonus Depreciation
  - The TCJA provided for 100% bonus depreciation through 2022
    (i.e. 100% deduction for property that would otherwise be capitalized & depreciated)
  - It is scheduled to phased out in 20% intervals from 2023-2026

2018-2022	**100%**
2023	**80%**
2024	**60%**
2025	**40%**
2026	**20%**
2027	**0%**

Select Expiring TJCA Changes: The 12/31/25 Cliff – Back to 2017 Law

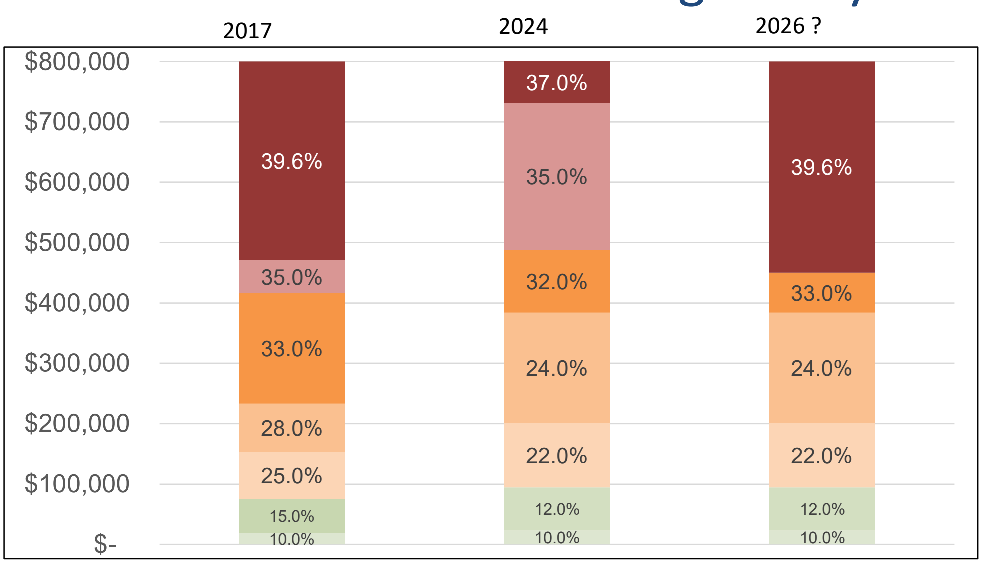
- Individual tax brackets
- Child tax credit
- AMT
- Standard deduction
- Personal exemptions
- Home mortgage interest – acquisition and equity loans
- Charity cash percent limitation
- Misc. itemized deductions, including casualty losses
- PEASE limitation
- Moving expenses
- Student loan & home mortgage discharge
- Certain ABLE account provisions
- 199A
- Estate & gift tax exemption

Select Expiring TJCA Changes
The 12/31/25 Cliff – Back to 2017 Law

- 461(l) excess business losses
- Bonus depreciation
- SALT deduction limit
- Opportunity zone rollovers

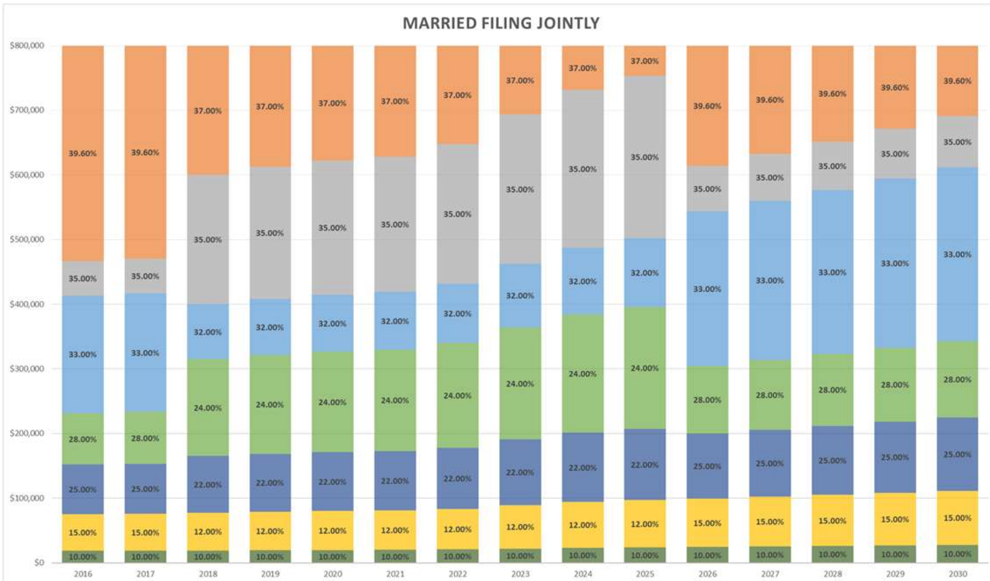
Core Year-End Planning

Tax Rates - Married Filing Jointly



The 2026 rate structure example is a combination of the following proposals and campaign promises from the Democratic Party: (1) No tax increases for anyone earning less than about $400,000; (2) 39.6% rate for income greater than $450,000 as proposed in the 2025 Green Book, & (3) Sunset of the TCJA otherwise.

Tax Rates - Rates if Sunset Occurs as Scheduled



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Tax Rates – Standard Deductions

2024

CURRENT STANDARD DEDUCTION

S	MFJ/QW	MFS	HOH
$ 14,600	$ 29,200	$ 14,600	$ 21,900

2026

PROJECTED SUNSET STANDARD DEDUCTION

S	MFJ/QW	MFS	HOH
$ 8,250	$ 16,550	$ 8,250	$ 12,200

Projected deduction amounts consider 2017 figures adjusted for approximate historic inflation & projected inflation.

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Tax Reform - Itemized Deductions

THE OLD RULE WAS TO

ACCELERATE DEDUCTIONS

THE NEW RULE IS TO

TIME DEDUCTIONS

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Gain & Loss Harvesting

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Capital Gain Harvesting

- Strategy:
  - Taxpayer expects to be in a higher tax bracket in the future
  - Sells assets in the current year, pays tax a lower tax rate and steps up basis
  - Repurchases the same or similar assets
- Effect: Shifts recognition of capital gain from a higher future rate to a current lower rate

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Capital Gain Harvesting
Tradeoffs

- On the surface, it appears that taxpayers should always harvest gains
- However, harvesting gains introduces a tradeoff between lower tax rates versus the loss of tax deferral
  - Tax is paid at a lower rate, but it is paid sooner
  - Need to determine a crossover point at which selling sooner makes more sense; A way to conceptualize this would be to use a return on investment (ROI) approach

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Capital Loss Harvesting

- Harvesting Capital Losses: Selling assets at a loss to offset capital gains
- Reduces or eliminate tax on current capital gain
- On the surface, loss harvesting produces an economic benefit equal to the tax saved, however it generally only provides a timing benefit.
  - Assets purchased with the proceeds have a lower basis than the assets sold
  - Therefore, more capital gains tax is owed in the future
  - However, deferral remains valuable

Capital Gain Harvesting
Efficiency

- Capital losses are more tax effective if they can be used to offset income taxed at higher rates

	Short-Term Gain	Long-Term Gain
Short-Term Loss	NEUTRAL	INEFFECTIVE
Long-Term Loss	EFFECTIVE	NEUTRAL

- *Remember:* Capture the up to $3,000 capital loss which can offset ordinary income!
- *Warning:* Remember the wash sale rule prevents taxpayers from repurchasing a substantially similar security within 30 days of selling at a loss

Capital Gain Harvesting

Efficiency

NO WASH SALE RULE FOR DIGITAL ASSETS

Capital Gain & Loss Harvesting

Trusts & Estates

- *For Recent Deaths:*
  - IRC § 1014(a) – basis of decedent's property increased to fair market value
  - Most estates will have losses
- Gain & loss recognition complicated
  - Forced recognition for pecuniary bequests
  - Trapped losses

Kenan v. Commissioner,

114 F.2d 217 (2d Cir. 1940)

Kenan v. Commissioner, 114 F.2d 217 (2d Cir. 1940).

- A testamentary trust satisfied a pecuniary (dollar amount) bequest with a mix of cash and securities.
- The issue was whether the distribution of securities required the trust to realize the unrecognized capital gains?
- The court agreed with the Service that the distribution required the trust to recognize capital gain.
- The appeals court affirmed, reasoning that there was never a chance that securities distributed would change in value between the date of death and the date of distribution.

Kenan v. Commissioner, 114 F.2d 217 (2d Cir. 1940).

- The basis "step-up" usually minimizes any difference between fair market value and basis, minimizing risk that the *Kenan Doctrine* will force an early recognition event for the family.
- However, in a volatile market, estates are much more likely to have unrecognized gains and losses.
- Therefore, estate planners and administrators must consider how best to avoid the issue.

Note, the *Kenan Doctrine,* generally applies to items of income in respect of a decedent (IRD). This may include IRAs.

Kenan v. Commissioner, 114 F.2d 217 (2d Cir. 1940).

- The basis "step-up" usually minimizes the any difference between fair market value and basis, minimizing risk that the *Kenan Doctrine* will force an early recognition event for the family.
- However, in a volatile market, estates are much more likely to have unrecognized gains and losses.
- Therefore, estate planners and administrators must consider how best to avoid the issue; ideas may include:
  - Using fractional and residuary bequests
  - Planning for liquidity
  - Careful allocation of assets amongst beneficiaries

Kenan Gains

- *Kenan* gains are undesirable for two reasons:
  1. Loss of deferral – the tax paid early reduces future compounded asset value growth
  2. Potential exposure to a higher marginal income tax rate at the fiduciary compared to the individual level

- *Kenan* gains are often frustrating because:
  1. They are difficult to understand and therefore lead to conflict amongst family members and with advisors.
  2. They are often entirely avoidable recognition events.

Kenan Losses

- If the assets used to satisfy a pecuniary bequest have basis greater than fair market value (Kenan Losses) special rules apply.
  - The rule that bars recognizing losses on sales or exchanges of property between related parties, specifically does not apply to an estate. That is, the estate will be able to claim the loss. IRC § 267(b)(13).
  - **There is no exemption to the related party rules if the distribution is from a trust.**
    - A loss cannot be claimed by a trust which uses built-in-loss property to satisfy a pecuniary bequest. The general rule of § 267 applies to block claiming a related party loss and unlike an estate there is no exception.
    - However, the loss does not simply disappear. Rather, the transferor can generally use the previously disallowed loss to offset gain at a future sale. IRC § 267(d).
    - A Section 645 Election is a useful tool which can solve this problem.

Roth Conversions

Types of Roth Conversions

1. Bracket management conversions
   - Maximizing retirement funds

2. Estate planning conversions
   A. Income tax motivated
   B. Estate tax motivated

Roth Conversions - 2017 Tax Reform Refresher

TAX REFORM REPEALED THE ABILITY TO RECHARACTERIZE A ROTH CONVERSION

However, it is still possible to recharacterize a Roth contribution.

Mathematics of Roth IRA Conversions

- In simplest terms, a traditional IRA will produce the same after-tax result as a Roth IRA provided that:
  - The annual growth rates are the same
  - The tax rate in the conversion year is the same as the tax rate during the withdrawal years

$$A \times B \times C = D$$

$$A \times C \times B = D$$

Mathematics of Roth IRA Conversions

	Traditional IRA	Roth IRA
Current Account Balance	$ 1,000,000	$ 1,000,000
Less: Income Taxes @ 40%	-	(400,000)
Net Balance	**$ 1,000,000**	**$ 600,000**
Growth Until Death	200.00%	200.00%
Account Balance @ Death	$ 3,000,000	$ 1,800,000
Less: Income Taxes @ 40%	(1,200,000)	-
Net Account Balance to Family	**$ 1,800,000**	**$ 1,800,000**

Mathematics of Roth IRA Conversions

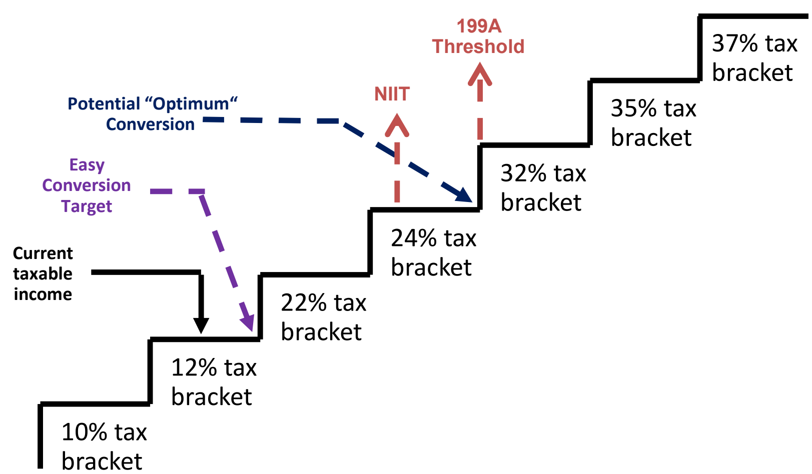
Reasons for converting to a Roth IRA

1. The taxpayer have special favorable tax attributes that need to be consumed such as charitable deduction carry-forwards, investment tax credits, NOLs, etc.…
2. The client expect the converted amount to grow significantly
3. Current marginal income tax rate is likely lower than at distribution
4. Cash outside the qualified account is available to pay the income tax due to the conversion
5. The funds converted are not required for living expenses, or otherwise, for a long period
6. The client expects their spouse to outlive them and will require the funds for living expenses
7. The client expects to owe estate tax

Mathematics of Roth IRA Conversions

- The key to successful Roth IRA conversions is often to keep as much of the conversion income as possible in the current marginal tax bracket
  - However, there are times when it may make sense to convert more and go into higher tax brackets
  - Need to take into consideration the 3.8% Medicare "surtax"
  - Need to take into consideration phase-outs of tax-benefits
  - Need to take into consideration the impact of AMT

Mathematics of Roth IRA Conversions



Non-Deductible Contributions: Basis

- When a traditional IRA has non-deductible contributions, a portion of the conversion to a Roth IRA will be non-taxable "basis" to the IRA owner
- In determining the non-taxable portion of a Roth IRA conversion, all traditional IRAs and IRA distributions during the year (including outstanding rollovers) must be combined for apportioning "basis"
  - See IRS Form 8606

Non-Deductible Contributions: Basis

Current year non-deductible IRA contributions	$	1,000
Prior year non-deductible IRA contributions		6,000
Total non-deductible IRA contributions	$	7,000
FMV of all IRAs	$	580,000
Outstanding rollovers		20,000
Distributions		-
Roth IRA conversions		100,000
Total value of IRAs, distributions and Roth IRA conversions	$	700,000
"Basis apportionment" factor		**0.0100**
Gross Roth IRA IRA conversion	$	100,000
Non-taxable portion		(1,000)
Taxable Roth IRA conversion	$	99,000

Roth Conversions

Frustrating Traps for the Unwary Professional & Client

- Consider the impact of Roth Conversion income on:
  - The taxation of Social Security benefits
  - Medicare part B premiums
  - ACA health insurance premium credit

Administrative Issues

- Estimated taxes
- State and local taxes
- Cash reserves
- Dollar cost averaged conversions
- Micro-conversions

Taxation of Roth IRA Distributions

Step 1:
(Non-taxable)

Contributions
> Regular contributions
> Rollovers from other Roth IRAs
> Rollovers from “designated Roth accounts”

↓

Step 2:
(Non-taxable)

Conversions (First-in, first-out basis)
> Taxable portion of prior conversion
> Non-taxable portion of prior conversion

↓

Step 3:
(Taxable)

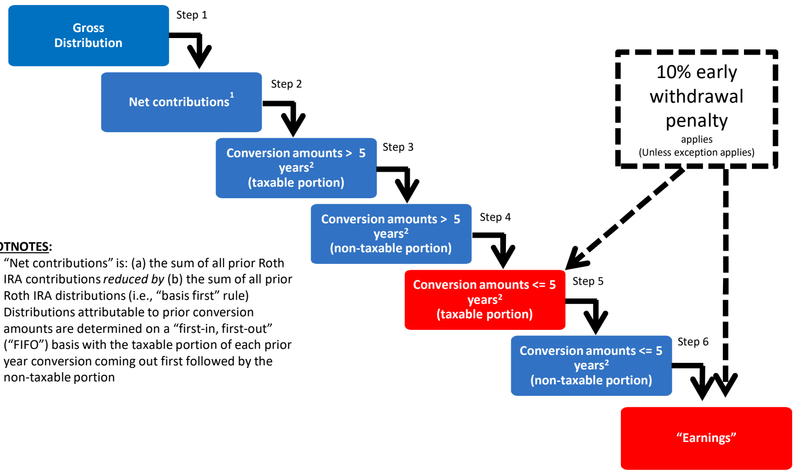
Earnings

Taxation of Roth IRA Distributions

	Distribution within 5 years	Distribution beyond 5 years
Age < 59½	Income Tax: Yes (earnings only) 10% Penalty : Yes (earnings & taxable portion of prior conversion amounts)	Income Tax: Yes (earnings only) 10% Penalty: Yes (earnings only)
Age ≥ 59½	Income Tax: Yes (earnings only) 10% Penalty: No	Income Tax: No 10% Penalty: No

Taxation of Roth IRA Distributions

"Ordering Rules"

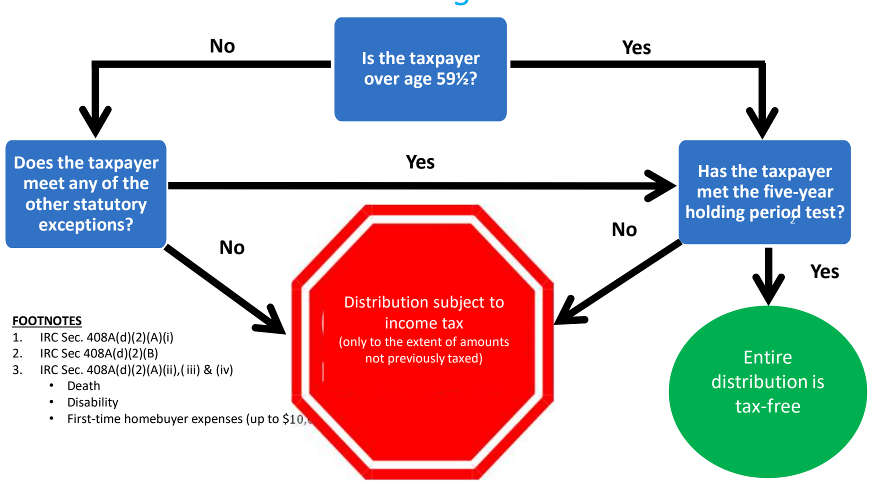


FOOTNOTES:

1. "Net contributions" is: (a) the sum of all prior Roth IRA contributions *reduced by* (b) the sum of all prior Roth IRA distributions (i.e., "basis first" rule)
2. Distributions attributable to prior conversion amounts are determined on a "first-in, first-out" ("FIFO") basis with the taxable portion of each prior year conversion coming out first followed by the non-taxable portion

Taxation of Roth IRA Distributions

"Seasoning Rule"

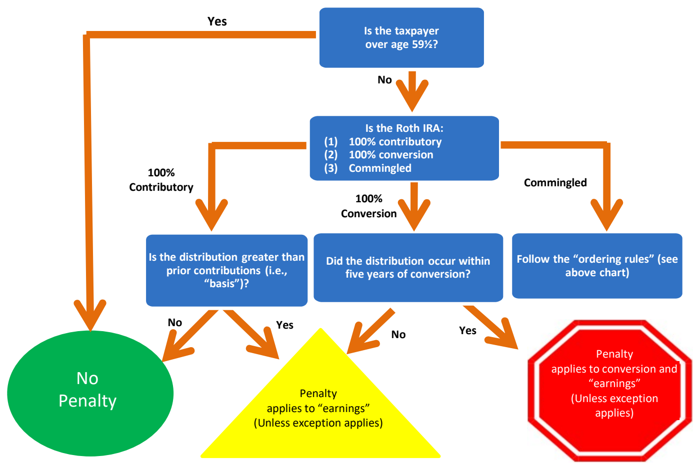


FOOTNOTES

1. IRC Sec. 408A(d)(2)(A)(i)
2. IRC Sec 408A(d)(2)(B)
3. IRC Sec. 408A(d)(2)(A)(ii),(iii) & (iv)
   - Death
   - Disability
   - First-time homebuyer expenses (up to $10,

Taxation of Roth IRA Distributions

"Penalty Box Rules"



Exceptions to 10% early withdrawal penalty :

1. Death
2. Disability
3. Series of substantially equal periodic payments
4. Medical expenses greater than 7.5% AGI
5. Health insurance premiums for unemployed individuals
6. Higher education expenses
7. First-time homebuyer expenses (up to $10K)

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More Income Tax Ideas

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Tax Aware Investing

Interest Income	Dividend Income	Capital Gain Income	Tax Exempt Interest	Pension and IRA Income	Real Estate, Solar, Oil & Gas	Roth IRA and Insurance
•Money market •Corporate bonds •US Treasury bonds <u>Attributes</u> •Annual income tax on interest •Taxed at highest marginal rates	•Equity Securities <u>Attributes</u> •Qualified dividends at LTCG rate •Return of capital dividend •Capital gain dividends	•Equity Securities <u>Attributes</u> •Deferral until sale •Reduced capital gains rate •Step-up basis at death	•Bonds issued by State and local Governmental entities <u>Attributes</u> •Federal tax exempt •State tax exempt	•Pension plans •Profit sharing plans •Annuities <u>Attributes</u> •Growth during lifetime •RMD for IRA and qualified plans •No step-up	<u>Real Estate</u> •Depreciation tax shield •1031 exchanges •Deferral on growth until sale •199A Deduction <u>Solar</u> • Large Credits • Enhanced Depreciatio n <u>Oil & Gas</u> •Large up front IDC deductions •Depletion allowances	<u>Roth IRA</u> •Tax-free growth during lifetime •No 70½ RMD •Tax-free distributions out to beneficiaries life expectancy <u>Life Insurance</u> •Tax-deferred growth •Tax-exempt payout at death

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Oil & Gas Investments

- *A client in the highest income tax bracket receives a $200,000 bonus.* With no planning much of it will be lost to taxation:

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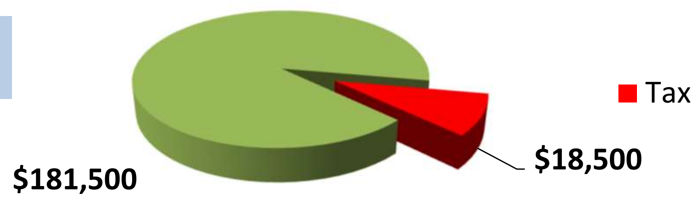
Oil & Gas Investments

- *However,* the taxpayer invests the $200,000 in an oil and gas drilling deal.
- 75% of the investment is spent on IDC by the operator and is immediately deductible by the client – this significantly reduces tax liability.

Remember, the AMT might limit this benefit.



Oil & Gas Investments

Caveat:

– Oil and gas investments can be risky.

– Tax savings should not be the only consideration.

Borrowing From Life Insurance Policies

- Life insurance can be used by a high-income taxpayer to shelter otherwise taxable income from high marginal rates
- A policy loan provides tax-free access to life insurance assets while allowing continued tax-deferred growth

Borrowing From Life Insurance Policies

Possible Purposes of a Strategic Policy Loan

- Pay expenses in a high-income, but cash-deficient period
- Re-invest at a higher return
- Delay selling an appreciated asset
- Pay the taxes on a Roth Conversion

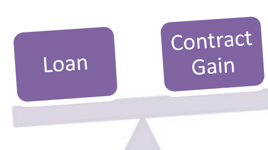
Borrowing From Life Insurance Policies

- Loans against a policy are generally NOT Taxable
- Exceptions
  - A loan against a policy classified as a modified endowment contract (MEC) (IRC§72(e)(5)) is taxable
  - Any outstanding balance on a loan when a policy is surrendered or lapses is taxable
- Tax is payable on excess of loan value over basis in the contract (Atwood v. Commissioner, TC Memo 1999-61)

Borrowing From Life Insurance Policies

- A MEC is a Life insurance contract that fails to meet the 7-pay test or is exchanged for such a policy
  - The 7-pay test limits premiums paid to a policy in the first seven years
  - The test was added in 1988 to eliminate a tax shelter
  - A loan from a MEC is taxed as follows:
    - Step 1: Determine the gain in the contract
    - Step 2: Determine taxable income, which equals the lessor of the loan or contract gain

Contract Gain = Cash Value (immediately before loan) - Investment in the Contract



Borrowing From Life Insurance Policies

CAUTION

- If the loan is not repaid before the policy holder dies, the death benefit is reduced by the outstanding balance
- Interest is charged on the loan and is added to the loan balance rather than required to be paid by the borrower
- The portion of the policy used as collateral or the entire policy will often move to safer, low growth assets
- Interest on the life insurance loan is not deductible

Defined Benefit Plans - Cash Balance Plans

Current Age	DC/401k Contribution	Cash Balance Allocation	Total
35	54,000	70,000	124,000
40	54,000	90,000	144,000
45	54,000	115,000	169,000
50	60,000	145,000	205,000
55	60,000	190,000	250,000
60	60,000	245,000	305,000

Please note these are prior-year figures to generally explain the potential significant tax benefit.

A Special Thanks to Shore-Tompkins for Providing this Slide.

Funding Tax Preference Accounts

DEFINED CONTRIBUTION PLAN LIMITS

IRA / ROTH IRA CONTRIBUTION LIMIT	$ 7,000
IRA / ROTH IRA "CATCH UP"	$ 1,000
401k ELECTIVE DEFERRAL	$ 23,000
401k ELECTIVE DEFERRAL "CATCH UP"	$ 7,500
SIMPLE IRA CONTRIBUTION LIMIT	$ 16,000
SIMPLE IRA "CATCH UP"	$ 3,500
SEP IRA EMPLOYEE PERCENTAGE MATCH LIMIT	25%
SEP IRA SELF-EMPLOYED PERCENTAGE MATCH LIMIT	20%
OVERALL LIMIT ON CONTRIBUTIONS TO DCPs	$ 69,000

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Funding Tax Preference Accounts
Encourage Clients to Fund Education Saving Plans

- Education Savings Accounts (ESAs) & Qualified Tuition Programs (QTPs/529s)
- Both provide annual tax-free growth & tax-free withdrawals for “qualified education expenses”
- QTPs offer a variety of annual savings incentives which vary by state: deductions, credits & grants
- ESAs can be used for primary & secondary in addition to higher education expenses
- The TCJA expanded QTP “qualified education expenses” to include primary & secondary higher education expenses
- “SECURE 2.0” also allowed 529 funds to be converted to Roth IRAs

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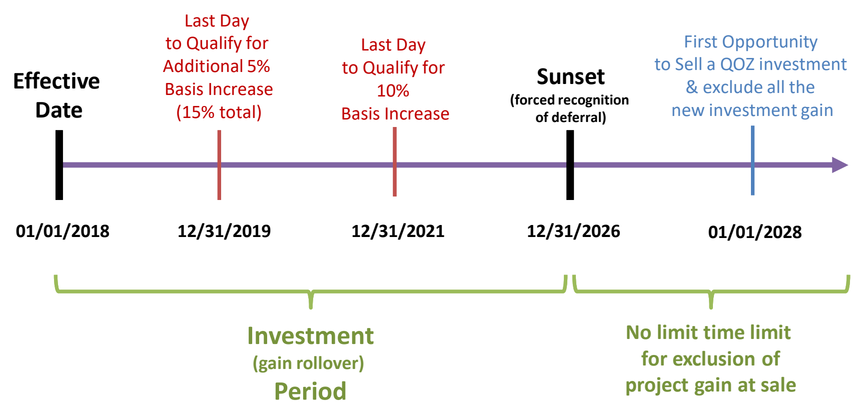
Opportunity Zone Timeline



Bonus Depreciation

- The TCJA provided for 100% bonus depreciation through 2022 (i.e. 100% deduction for property that would otherwise be capitalized & depreciated)
- It is scheduled to phased out in 20% intervals from 2023-2026

2022	**100%**
2023	**80%**
2024	**60%**
2025	**40%**
2026	**20%**
2027	**0%**

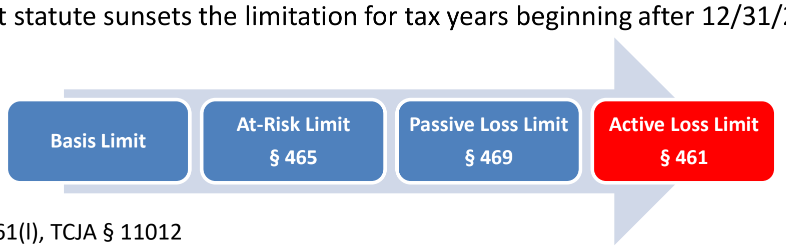
Section 179

- Before the TCJA, a taxpayer could expense up to $500,000 of property.
  - However, it was phased out if a business places over $2,000,000 of property in service during the tax year.
  - This phaseout of course makes it less useful for larger businesses, but those subject to the limitation could still use bonus depreciation.
- The TCJA increased the deduction limit to $1,000,000 and the start of the placed in-service limit to $2,500,000.
  - **This change was permanent; i.e. not subject to sunset.**
  - Section 179 will remain the useful for your client's small businesses following sunset (except rental real estate, generally).

IRC § 179, TCJA § 13101

Limitation on Excess Business Losses

- The TCJA amended Section 461 to add a new subsection (l)
- The new section disallows certain excess business losses
  - Must be carried-forward
  - Applies to taxpayers with income exceeding $500,000 (MFJ)
  - Applies at the partner or shareholder level
- The current statute sunsets the limitation for tax years beginning after 12/31/25



IRC § 461(l), TCJA § 11012

Qualified Business Income Deduction Math

Top Pass-through Rate	2013-2017	39.6%		78% of total corporate rate, including double taxation (39.6/50.5)
Top Pass-through Rate (199A limitations don't apply)	2018-2025	29.6%	37% x (1-20%) = 29.6%	74% of corporate rate, including double taxation (29.6/39.8)
Top Pass-through Rate (199A limitations apply)	2018-2025	37%		93% of corporate rate, including double taxation (37/39.8)
Top Pass-through Rate (if sunset occurs)	2026-?	39.6%		99% of corporate rate, including double taxation (39.6/39.8)
Corporate Tax Rate – single layer (basically)	1993-2017	35%		
Corporate Tax Rate – double tax (including taxes on dividends)	2013-2017	50.5%	35% + 23.8% x (1-.35)	
Corporate Tax Rate – single layer (does not sunset under TCJA)	2018-?	21%		
Corporate Tax Rate – double tax (including taxes on dividends)	2018-?	39.8%	21% + 23.8% x (1-.21)	

Trusts & Estates

Estate & GST Taxes

- The TCJA doubled the Basic Exclusion Amount and GST exemption in 2018-2024 ($10,000,000 in 2011 dollars)
- In 2026 the exemptions revert to pre-TCJA law ($5,000,000 in 2011 dollars)
- Tax reform proposals and negotiations are such that we should expect the exemption to substantially decrease

POTENTIAL
"USE-IT-OR-LOSE-IT"
OPPORTUNITY

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Estate & Gift Taxes

Exemption Reduction Math – "Use It or Lose It"

2024 gifts use this portion of the exclusion first.

Old Exclusion
$6,805,000

2024 gifts use this portion of the exclusion second.

Lost if not used before the law changes.

2018 Exclusion Increase
$6,805,000

2024 Estate Tax Exclusion $13,610,000

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Estate & GST Taxes

Exclusion Sunset Math

- Option 1
  - No planning
  - "Double" exemption sunsets 1/1/26 and is lost
- Option 2
  - Couple gifts $5,000,000 each to trust in 2024
  - Their previous gifts reduce their exemption by $5,000,000 to $0 (ignoring inflation adjustments) in 2026
  - Gifting during the "double period" accomplished nothing; i.e. same result as Option 1, ignoring growth outside of estate
- Option 3
  - Couple gifts $10,000,000 each to trust in 2024
  - Their previous gifts reduce their exemption $0 in 2026
  - $5,000,000 each (ignoring inflation adjustments) of additional exemption is captured

Estate & GST Taxes - IDEAS

- **Continue annual exclusion gifts**
  - $18,000 exclusion in 2024
- Continue medical & education gifts
- Tax-free gifts to use higher exemptions
- Portability elections to preserve exemptions
- Short-term GRATs (for ETIP to end before sunset)
- Short-term SCIN or private annuity
  - "Springing" SLATs (i.e. SLAT with contingent GPOA provision)
  - Split-dollar life insurance and GST
  - Premium financing

Estate & GST Taxes - *IDEAS*

- **Use Trusts to Create Additional Taxpayers**
  - $10,000 SALT deduction per trust
  - $191,950 Section 199A Threshold Amount per trust (2024)
  - $10,000,000 Section 1202 exclusion per trust
  - Creating an additional taxpayer now may provide a grandfathered opportunity to shift income & avoid tax increases

Estate & GST Taxes - *IDEAS*

- **Use trusts to avoid state income taxation**
  - Completed Gift Non-grantor Trusts
  - Incomplete Gift Non-grantor Trusts –
    - A trust settled in state with a trust code which facilitates the strategy
    - Transfer to the trust is not a completed gift and therefore does not incur gift tax because the settlor retains certain powers
    - Trust is a non-grantor trust
    - Useful to avoid income taxation in the settlor's resident state
    - Only possible in certain states including: Alaska, Delaware, Nevada, Wyoming

Estate & GST Taxes - *IDEAS*

Use trusts to avoid state income taxation

		Full SALT Deduction	No SALT Deduction	No State Tax
Income		$ 100	$ 100	$ 100
State Tax	**5%**	(5)	(5)	-
Federal Tax	**35%**	(33)	(35)	(35)
		$ 62	$ 60	$ 65

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High v. Low Interest Rates

- **Low Rates Favor**
  - GRATs
  - CLTs
  - IDGT Sales
  - Private Annuities
  - Freeze Partnerships
- **High Rates Favor**
  - QPRTs
  - CRTs
  - Reduced valuations

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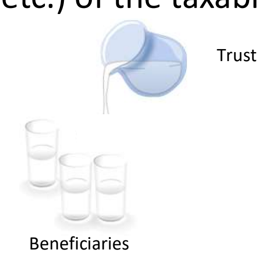
Fiduciary Tax & Accounting Issues

Foundational Concepts
Distributable Net Income (DNI)

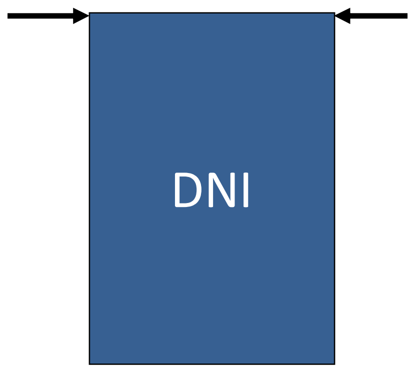
- Determines the amount of the trust's or estate's income distribution deduction.
- Determines how much the beneficiaries must report as income on their tax returns.
- Determines the character (e.g. interest, dividends, etc.) of the taxable income in beneficiaries' hands.



IRC § 661

Foundational Concepts
Distributable Net Income (DNI)

Trust/Estate
DNI acts as a ceiling for purposes of the allowable deduction



Beneficiary
DNI acts as a ceiling for the total amount of income the beneficiary must report on his/her tax return

Foundational Concepts - Types of "Income"

- Fiduciary accounting income
  - Governed by state law and the trust instrument
  - Determines the amount that may or must pass to the trust's or estate's beneficiaries
- Tax accounting income
  - Governed by state and federal income tax law
  - Determines who is taxed on the income

Foundational Concepts

Distributable Net Income (DNI) - Additional Issues

- Normally, capital gains and losses are trapped at the trust or estate level.
  - However, in the year of termination, the capital gain/loss passes out to the beneficiaries.
- Specific bequests do <u>not</u> carry out DNI to the beneficiaries.

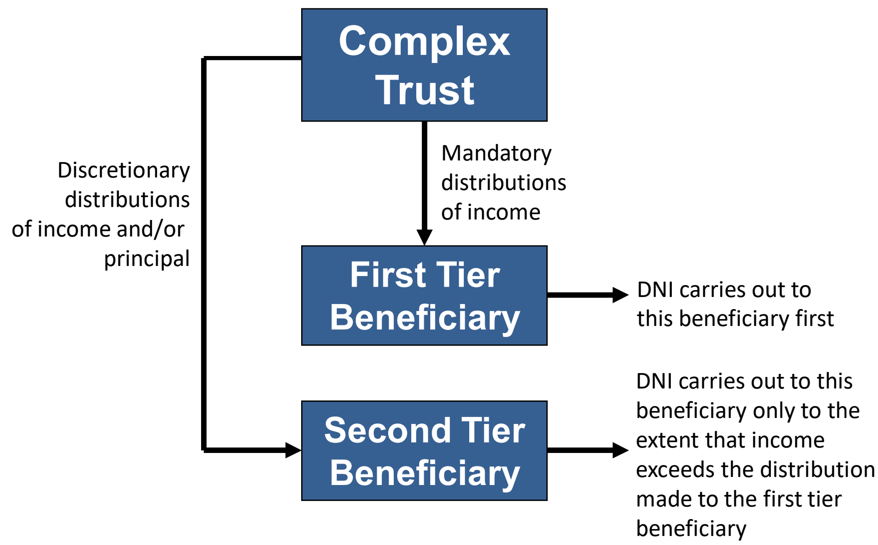
IRC § 661

Treas. Reg. § 1.643

Foundational Concepts – Tier Rules

- Apply to estates and complex trusts
- Two tiers
  - First tier beneficiary
    - Required distribution of income on a current basis
  - Second tier beneficiary
    - Receives any amount remaining (at the discretion of the trustee/executor)

Foundational Concepts – Tier Rules



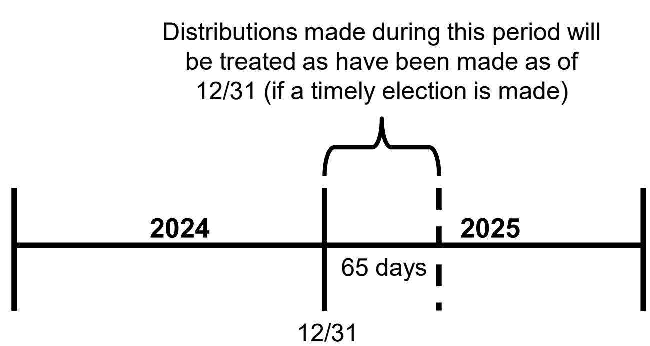
Foundational Concepts – Separate Share Rule

- Applies to both estates and complex trusts
- Treats multiple beneficiaries of an estate or single trust as if each were the sole beneficiary
- Determines how DNI carries out to each beneficiary
  - DNI is computed separately for each share

Foundational Concepts – “65-Day” Rule (IRC §663(b))

- Applies to estates and complex trusts
- Allows fiduciary to treat distributions made within 65 days after year-end to be treated as if they were made as of December 31st of the prior year
  - Limited to DNI (reduced by distributions made during the prior year)
- Election must be made by the due date of the tax return
  - Election is irrevocable
  - Annual election

Foundational Concepts – “65-Day” Rule



Foundational Concepts – Specific Bequests

- Do <u>not</u> carry out DNI
- Not taxable to trust/estate or beneficiaries
- Requirements
  - Paid at once OR
  - Paid in not more than three installments
- <u>Examples</u>
  - "I leave my brother Randy $250,000."
  - "I leave my sister Mary my boat"

Foundational Concepts
Charitable Deduction (IRC §642(c))

- Requirements
  - Paid from gross income
  - Paid pursuant to the governing document
- Must be actually be paid in the current year
  - Exception – pre-1969 trusts
- Unlimited in amount
- Taken as a deduction in computing adjusted gross income (AGI)

Foundational Concepts
Pecuniary Bequests to Charity
CCA 200644020

- Pecuniary bequest to charitable beneficiary
- Acceleration of income on IRD
- No IRC §642(c) deduction - terms of trust did not direct or require that the trustee pay the pecuniary legacies from the trust's gross income

Charity

Charity - Individual income tax deduction

- IRC §170 (a) Allowance of deduction

  (1) General rule

  There shall be allowed as a deduction any charitable contribution (as defined in subsection (c)) payment of which is made within the taxable year.

Charity - Percentage Limitations

Contributions to "Public Charities:"

Type of Property	Deductible Amount	AGI Limitation
Cash	Fair Market Value	60%
Property, if sold, would generate ordinary income or short-term capital gain.	Lesser of Basis or Fair Market Value	50%
Property, if sold, would generate long-term capital gain.	Fair Market Value*	30%*
Tangible personal property used by charity for its exempt purpose.	Fair Market Value*	30%*
Tangible personal property charity sells or doesn't use for its exempt purpose.	Lesser of Basis or Fair Market Value	50%

*Donor can elect to have 50% of AGI limit apply if amount of deduction is limited to basis.

CHARITY - Estates and trusts income tax deduction

IRC §642 (c) Deduction for amounts paid or permanently set aside for a charitable purpose

(1) General rule

(2) In the case of an estate or trust …, there shall be allowed as a deduction in computing its taxable income … any amount of the gross income, without limitation, which pursuant to the terms of the governing instrument is, during the taxable year, paid for a purpose specified in section 170(c) (determined without regard to section 170(c)(2)(A))….

Charity - The Statutes - Estate tax deduction

IRC §2055

(a) **In general** For purposes of the tax imposed by section 2001, the value of the taxable estate shall be determined by deducting from the value of the gross estate the amount of all bequests, legacies, devises, or transfers [to charity]

CHARITY - Types of Gifts

- Outright gifts
- Testamentary gifts
- Split-interest gifts
- "Endowment-type" gifts

Charity - Types of Gifts

- Qualified Charitable Distributions (QCDs) from an IRA
  - Taxpayer must be age 70½ or older
  - Distribution must be direct to charity.
  - Distribution cannot exceed $105,000 (in 2024).
  - Distribution can count towards RMD.
  - Distributions to donor advised funds & supporting organizations do not qualify.

IRC § 408(d)(8)

Charity - Types of Gifts

- Outright gifts
  - Qualified Charitable Distributions (QCDs) from an IRA
    - Income is never recognized by the taxpayer and no deduction is claimed on the return.
    - Generally more or equally as tax efficient as a distribution from the IRA and then a contribution to charity because QCDs are not subject to the other limits on deductions for charitable contributions.

IRC § 408(d)(8)

Charity - Types of Gifts

- Testamentary gifts
  - Very common; perhaps the most common way large gifts are made.
  - Can be a:
    - ➢ Specific amount of money (pecuniary bequest),
    - ➢ Specific asset (specific bequest or devise),
    - ➢ Percentage of the estate (fractional bequest), or
    - ➢ Residual amount.
  - Reduces the taxable portion of an estate.

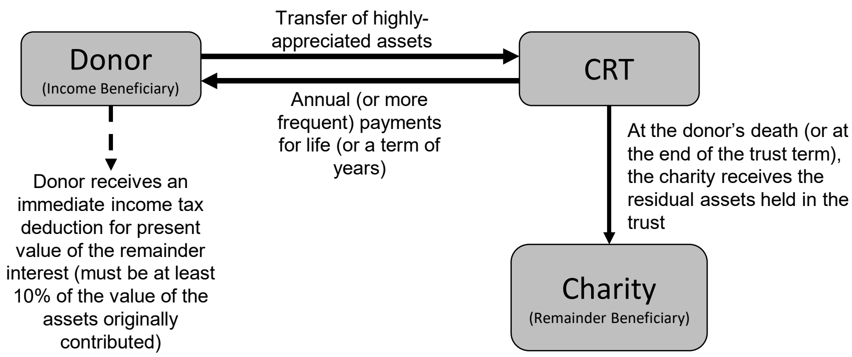
Charity - Types of Gifts

- Split Interest Gifts
  - Charitable Gift Annuities
  - Pooled Income Funds
  - Charitable Remainder Trusts
  - Charitable Lead Trusts

Charitable Remainder Trusts

Effective for those without charitable intent?

Charitable Remainder Trusts - *Overview*



Charitable Remainder Trusts - Types of CRTs

- Charitable Remainder Annuity Trust (CRAT)
  - The beneficiaries receive a fixed percentage of the initial trust value or a stated amount annually or more frequently.
  - The amount paid doesn't change from year-to-year.
  - The annual payment must be 5-50% of the fair market value of the assets at the time of contribution.
  - The term of the annuity can be:
    - For a term up to 20 years,
    - Over the life of the annuitant(s),
    - Over the shorter of the two, or
    - Over the longer of the two.

Charitable Remainder Trusts - Types of CRTs

- Charitable Remainder Unitrust (CRUT)
  - Income beneficiaries receive a stated percentage of the trust's assets revalued each year.
  - The distribution will vary from year to year depending on the investment performance of the trust assets and the amount withdrawn.

Charitable Remainder Trusts
Taxation of the Donor & Trust

- Donor generally does *not* realize gain or loss when property is transferred to the trust
- The donor generally will *not* realize gain or loss if and when the transferred assets are subsequently sold by the trustee of the CRT*
- Distributions in kind are treated as a sale of the property distributed, resulting in gain recognition by the CRT. [Reg. §1.664-1(d)(5)]

*Need to consider the binding commitment issue. See Rev. Rul. 78-197.

Charitable Remainder Trusts
Taxation of the Donor & Trust

- However, the grantor may be required to recognize gain if:
  - Property transferred is subject to indebtedness that exceeds grantor basis. 26 CFR 1.1001-2
  - Grantor receives property from the trust in exchange for the transfer to the trust

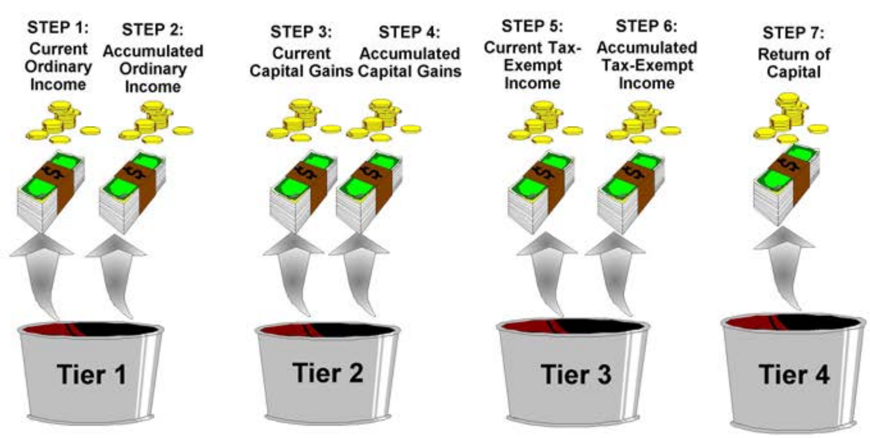
Charitable Remainder Trusts
Taxation of the Donor & Trust

- Avoiding a recognition event is a significant factor in maximizing the income tax advantages of a CRT; the most efficient transactions:
  - Involve a highly appreciated or tax-depreciated asset -> avoids significant taxation
  - Diversifies a concentrated position -> risk adjusted return increased without a recognition event
  - Transforms a growth asset to a needed income asset -> avoids recognition otherwise necessary

Charitable Remainder Trusts
Taxation of Distributions

- The character of income received by the recipient is subject to and controlled by the tier rules of IRC §664(b):
  - First, distributions are taxed as ordinary income
  - Second, distributions are taxed as capital gains
  - Third, distributions are taxed as tax-exempt income (e.g. municipal bond income)
  - Finally, distributions are assumed to be the non-taxable return of principal

Charitable Remainder Trusts
Taxation of Distributions



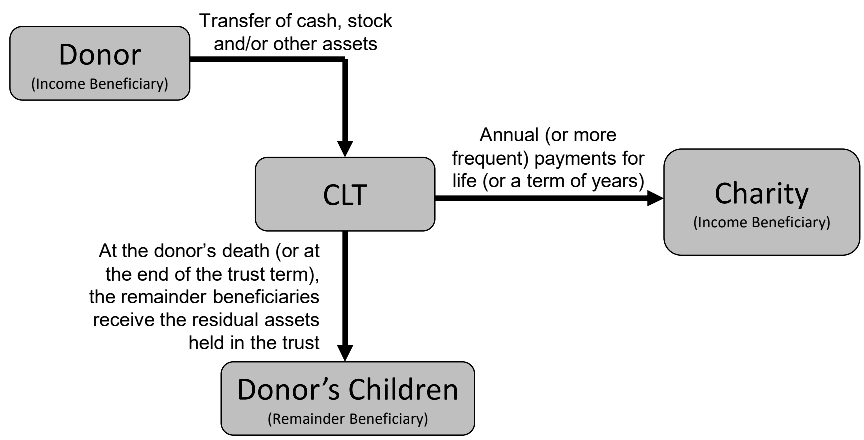
Charitable Lead Trusts

Effective for those without charitable intent?

Charitable Lead Trusts - Overview

- A Charitable Lead Trust (CLT) is a split interest trust consisting of an income interest and a remainder interest.
- During the term of the trust, the income interest is paid out to a named charity.
- At the end of the trust term, the remainder (whatever is left in the trust) is paid to non-charitable beneficiaries (e.g. children of the donor) that have been designated in the trust document.

Charitable Lead Trusts - Overview



Charitable Lead Trusts - Types

- Charitable Lead Annuity Trust (CLAT)
  - The charitable beneficiary receives a stated amount of the initial trust assets each year
  - The amount received is established at the beginning of the trust and will not change during the term of the trust regardless of investment performance (unless inadequate investment performance causes the trust to run out of assets)
- Charitable Lead Unitrust (CLUT)
  - The charitable beneficiary receives a stated percentage of the trust's assets each year.
  - The distribution will vary from year to year depending on the investment performance of the trust assets and the amount withdrawn

2024 Action Steps

2024 Action Steps - Checklist

- ❑ Bracket Management
  - ❑ Bonuses
  - ❑ Recognition events
  - ❑ Business expenses
  - ❑ AMT awareness
- ❑ Itemized Deduction Timing
  - ❑ Medical expenses
  - ❑ Property tax
  - ❑ **Charitable contributions**
  - ❑ Disaster Losses
- ❑ Significant Financial Events Next Year
  - ❑ Recognition events
  - ❑ New investments
  - ❑ Re-allocation plans
  - ❑ Vesting
- ❑ Major Life Events Next Year
  - ❑ Family changes
  - ❑ Job changes
  - ❑ Moving

2022 Action Steps - Checklist

- ❑ Retirement Planning
  - ❑ Fund IRAs
  - ❑ Fund 401ks
  - ❑ Fund pension plans
- ❑ Education Planning
  - ❑ Fund 529 plans
  - ❑ Fund Coverdell accounts
- ❑ Executive Planning
  - ❑ Review NQCD
  - ❑ Review NQSOs / ISOs
  - ❑ Review concentrated positions
- ❑ Estate Tax Planning
  - ❑ **Plan lifetime exemption gifts**
  - ❑ Plan annual exclusion gifts
  - ❑ Plan medical gifts
  - ❑ Plan tuition gifts

Year-end Planning
A Checklist of Ideas to Prepare for Tax Reform

- ❑ Bracket Management
  - ❑ Accelerate bonuses to avoid rate increases
  - ❑ Accelerate recognition events to avoid rate increases
  - ❑ Defer business expenses to capture a greater benefit if rates increase
  - ❑ Consider what reinstatement of the AMT would mean
- ❑ Itemized Deduction Timing
  - ❑ Carefully consider property tax payments
    - ➢ Defer to capture a greater benefit due to higher rates
    - ➢ Defer in-case the $10,000 SALT deduction cap is repealed
    - ➢ Accelerate to avoid additional itemized deduction limits
  - ❑ Carefully consider charitable contribution timing:
    - ➢ Defer to capture a greater benefit due to higher rates
    - ➢ Accelerate to avoid additional itemized deduction limits

Year-end Planning
A Checklist of Ideas to Prepare for Tax Reform

- ❑ Gain & Loss Harvesting
  - ❑ Harvest gains to avoid rate increases
  - ❑ Defer harvesting losses to offset rate increases
- ❑ Retirement Planning
  - ❑ Roth conversions before rates increase
  - ❑ NUA rollout before rates increase
  - ❑ Diversify concentrated positions before rates increase
- ❑ Executive Planning
  - ❑ Reconsider NQCD funding to avoid rate increases & increased payroll taxes
  - ❑ Consider ISO exercise in case the AMT returns in-force
  - ❑ Consider NQSO exercise to avoid rate increase & increased payroll tax
- ❑ Estate Tax Planning
  - ❑ Consider large lifetime gifts
    - ➢ Capture the large estate tax exemption
    - ➢ Avoid a forced recognition event

CONCLUSION