

Freeborn & Peters LLP Trusts and Estates Client Alert Bulletin - 3rd Quarter 2022

by Michael D. Whitty

A FREEBORN & PETERS LLP CLIENT ALERT



Topics Addressed in this Bulletin:

- Increased Estate and Gift Tax Exemptions Make January 2023 Gifts More Powerful
- Changes to Interest Rates Improve Some Estate Tax Planning Techniques, While Others Remain Powerful
- Estate Tax Portability Elections Simplified, Making It Easier for Surviving Spouses to Reduce or Eliminate Estate Tax
- Do a “Tax Planning Tune-Up” Before Selling a Business
- New Addition to Freeborn & Peters LLP’s Trusts & Estates Team

Increased Estate and Gift Tax Exemptions Make January 2023 Gifts More Powerful

Exemptions from the federal estate, gift, and generation-skipping transfer (“GST”) taxes have been indexed to inflation starting in 2010. For 2022, these exemptions (“EGT exemptions”) increased **\$360,000** (from \$11,700,000 to \$12,060,000) thanks to the inflation adjustment.

EGT exemption increases for 2023 have not yet been *officially* published (the official publication for 2022 increases was not published until November 2021). However, professionals have published reliable estimates made using the same techniques, formulas, and data as the US Treasury uses in calculating inflation adjustments. Those projections predict the EGT exemptions inflation adjustment for 2023 will be **\$860,000** (from \$12,060,000 to \$12,920,000).

The increase for 2023 alone will be enough to motivate donors to make tax-motivated wealth transfers of a meaningful size. Donors who have used all (or most) of their pre-2022 EGT exemptions, but have *not* used their 2022 exemption increases, could transfer **\$1,220,000** (or more) *without gift tax*. That amount is material enough to justify some serious planning, including transfers that would require an appraisal for gift tax purposes.

We encourage clients who would like to take advantage of this opportunity to work with us in the fourth quarter of 2022 so that plans are in place and documents will be ready for execution in January 2023.

Changes to Interest Rates Improve Some Estate Tax Planning Techniques, While Others Remain Powerful

Sections 1274 and 7520 of the Internal Revenue Code establish minimum “safe harbor” interest rates used in leveraged estate planning techniques, which the US Treasury updates every month for use in the following month, based on the Treasury bond interest rates for the preceding month. These are considered “safe harbor” rates because using interest rates at or above these minimums will allow the loan or other leveraged transaction to be respected for income tax purposes and estate and gift tax purposes.

These safe harbor interest rates have gradually increased from their all-time low in September 2020. **Rates are still low** when compared to the historical range since Sections 1274 and 7520 were enacted in 1984 and 1988, respectively. However, some estate tax savings techniques that were almost useless during the extremely low rates of the preceding two years are now viable.

There are still great **estate and gift tax savings opportunities** in making leveraged transactions when the property transferred into a grantor retained annuity trust (“GRAT”), transferred by an installment sale, or purchased using funds from a low-interest intra-family loan, will grow faster than the interest rate on the loan or annuity payable back to the transferor.

IRS Announces New Taxpayer-Friendly Procedure For Making Estate Tax Portability Election, Significantly Reducing Estate Taxes for Electing Surviving Spouses

Since 2011, the portion of a predeceasing spouse’s gift and estate tax exemption not used by that spouse has been transferable to the surviving spouse by making the so-called “**Portability Election**.” When the predeceasing spouse had enough wealth to require filing an estate tax return, but used less than their full exemption, the Portability Election would be made on that estate tax return. When the predeceasing spouse did not have enough wealth to require filing an estate tax return, the return could be filed solely for purposes of making the Portability Election (a “**Portability-Only return**”). A procedure announced in 2017 allowed the predeceasing spouse’s executor or personal representative to file that Portability-Only return within **two years** of the predeceasing spouse’s date of death (rather than the usual nine-month or extended fifteen-month deadline), or later if the filer submitted a request for a private letter ruling along with a user fee.

On July 8, 2022, the IRS released Revenue Procedure 2022-32, which provides a more taxpayer-friendly procedure for filing a Portability-Only return. Under the new procedure, (i) the **grace period** for filing a Portability-Only return without needing to request a private letter ruling is increased from two years to **five years** after the predeceased spouse’s date of death, and (ii) the filing of the return itself is **simplified** so that the taxpayer merely files the return with a special notice across the top of the first page. Rev. Proc. 2022-32 clarifies that eligibility for filing a Portability-Only return requires that (a) the predeceased spouse died after December 31, 2010, (b) the predeceased spouse was a citizen or resident of the United States on that date of death, and (c) the predeceased spouse was not otherwise required to file an estate tax return, and did not in fact file a timely estate tax return.

This new taxpayer-friendly procedure makes it almost a “no-brainer” for a surviving spouse to file a Portability-Only return. This is all the more true as existing law provides that the current high EGT exemption is scheduled to be cut in half at the end of 2025. For every \$1,000,000 of the deceased spouse’s unused estate tax exemption transferred to and usable by the surviving spouse, the surviving spouse’s estate would save 40% of that, or \$400,000. The maximum total tax savings where the predeceased spouse died in 2022 would be **\$4,824,000**. Where the surviving spouse declines to file the return (such as if he or she is too disabled or excessively frugal), the surviving spouse’s children would be wise to make the necessary arrangements and pay the expenses for preparing and filing the Portability-Only return.

Recent Cases and Rulings Emphasize Importance of Proper Tax Documentation and Appraisals

Recent cases and rulings in 2021 and 2022 have highlighted the importance of full and adequate documentation consistent with the requirements of Section 170(f) and its regulations in order to obtain an expected charitable deduction for income tax purposes. In another situation, a US Treasury Chief Counsel Advice memorandum (of similar legal weight to a revenue ruling) found that an out-of-date appraisal, used to value a gift of interests in a private company for reporting on a gift tax return, that did not reflect a pending sale of the company would *not* be respected, and in fact would cause the protections against gift tax audit adjustments built into the transfer transaction to be disregarded. The net result was a substantial amount of gift tax due.

Taxpayers should consult with estate planning counsel and tax advisors **before** implementing a gift transfer or transaction, so that the proper forms and procedures can be followed and an appraisal, if one is needed, properly reflects all relevant conditions as of the date of the gift.

Do a “Tax Planning Tune-Up” Before Selling a Business

When a business owner is first considering a sale of their business, before beginning the process of marketing the business, the owner should consult with tax counsel to identify and implement techniques that can provide significant income tax and estate and gift tax savings upon the sale. Implementing the techniques well in advance of the sale can allow transfers at a valuation that could be well below the eventual sales price of the company. In contrast, waiting too long before making gift transfers can invite the IRS to argue that the gift tax value of those transfers should be that eventual sales price for the company.

The **tax savings from early implementation of these techniques will often be more than enough to pay for all the legal fees on the sale**, and sometimes enough to also pay for the **commissions** for business brokers and investment bankers. Freeborn’s business owner clients should consult with the Trusts & Estates Practice Team or Corporate Practice Group as early as possible in the sales process.



New Addition to Freeborn & Peters LLP’s Trusts & Estates Team

Freeborn & Peters LLP is pleased to welcome [Abosede Odunsi](#) as a partner in its Chicago office. Odunsi joins Freeborn’s Corporate Practice Group and Trust and Estates Team, furthering the firm’s focus on strategic growth across all offices.

Odunsi focuses her practice on estate planning, tax planning, probate administration and guardianship matters for high-net-worth individuals, families, entrepreneurs and business owners. Prior to joining Freeborn, Abosede served as a partner at Hoogendoorn & Talbot LLP, where she designed and drafted estate plans using a variety of revocable and irrevocable trusts.

For more information, see our [press release](#).

ABOUT THE AUTHOR



Michael D. Whitty

Partner

Chicago Office
(312) 360-6192

mwhitty@freeborn.com

Michael Whitty is a Partner in the Corporate Practice Group. He concentrates his practice in estate planning, taxation, and estate and trust administration. Michael represents business owners, principals of venture capital and private equity funds, key executives, investors, and other high net worth individuals in planning for the preservation and transfer of their wealth.

140+ Attorneys. 5 Offices.

Freeborn & Peters LLP is a full-service law firm with international capabilities and offices in Chicago, Ill.; New York, Ny; Richmond, Va.; Springfield, Ill.; and Tampa, Fla. Freeborn is always looking ahead and seeking to find better ways to serve its clients. It takes a proactive approach to ensure its clients are more informed, prepared and able to achieve greater success – not just now, but also in the future. While the firm serves clients across a very broad range of sectors, it has also pioneered an interdisciplinary approach that serves the specific needs of targeted industries.

Freeborn's major achievements in litigation are reflective of the firm's significant growth over the last several years and its established reputation as a Litigation Powerhouse®. Freeborn has one of the largest litigation departments among full-service firms of its size – currently with more than 90 litigators, which represents about two-thirds of the firm's lawyers.

Freeborn is a firm that genuinely lives up to its core values of integrity, effectiveness, teamwork, caring and commitment, and embodies them through high standards of client service and responsive action. Its lawyers build close and lasting relationships with clients and are driven to help them achieve their legal and business objectives.

For more information visit: www.freeborn.com

CHICAGO

311 South Wacker Drive
Suite 3000
Chicago, IL 60606
(312) 360-6000
(312) 360-6520 fax

NEW YORK

1155 Avenue of the Americas
26th Floor
New York, NY 10036
(212) 218-8760
(212) 218-8761 fax

SPRINGFIELD

217 East Monroe Street
Suite 202
Springfield, IL 62701
(217) 535-1060
(217) 535-1069 fax

RICHMOND

901 East Byrd Street
Suite 950
Richmond, VA 23219
(804) 644-1300
(804) 644-1354 fax

TAMPA

1 Tampa City Center
201 North Franklin Street
Suite 3550
Tampa, FL 33602
(813) 488-2920

Disclaimer: This publication is made available for educational purposes only, as well as to provide general information about the law, not specific legal advice. It does not establish an attorney/client relationship between you and Freeborn & Peters LLP, and should not be used as a substitute for competent legal advice from a licensed professional in your state.