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Estate Tax Considerations for 2022: How Clients Can Plan in an Uncertain Time

6 Dec 2021

The Internal Revenue Service ("IRS") has released annual inflation adjustments for 2022. These include increased gift, estate, and generation-skipping transfer ("GST") tax exemptions (the "unified credit"), annual gift tax exclusions, and retirement account limits. The changes are as follows:

- The unified credit will increase to $12.06 million for an individual (from $11.7 million in 2021). This means that a married couple will have $24.12 million of available exemption (up from $23.4 million in 2021) assuming portability is properly elected on the predeceased spouse's federal estate tax return.
- The annual gift tax exclusion will increase to $16,000 (from $15,000 in 2021). As a result, individuals will be able to give $16,000 per year ($32,000 for a married couple) to any number of persons (or trusts) tax free.
- The annual gift tax exclusion for gifts to non-US citizen spouses will increase to $164,000 (from $159,000 in 2021). Note that gifts made to a US citizen spouse are not taxable in any amount whether made during the spouse's lifetime or at death.
- The contribution limit for employees who participate in 401(k), 403(b), most 457 plans, and the federal government's Thrift Savings Plan will increase to $20,500 (from $19,500 in 2021).

However, the IRS also cautioned that legislation pending in Congress might affect 2022 tax returns and taxpayers should consult future IRS guidance to determine if the adjusted figures remain applicable in 2022. Specifically, tax experts anticipated that two recent pieces of legislation - the Infrastructure Investment and Jobs Act (IIJA) and the Build Back Better (BBB) bill - could have resulted in significant changes to federal estate and gift tax law.

The IIJA, which invests in the nation's infrastructure, was signed into law by President Biden on November 15, 2021. However, it failed to include any of the initially proposed and anticipated changes to the current estate tax regime. Notably, the IIJA does ***not***:

- Reduce the unified credit, which was expected to drop to $5 million per person as of January 1, 2022;
- Increase the federal estate tax rate, which remains at 40% in 2022;
- Eliminate the step-up in basis at death in favor of carry-over basis;
- Recognize income tax realization at the time of a transfer event (i.e. by gift or death) rather than sale ("deemed realization");
- Disallow valuation discounts for closely-held entities holding nonbusiness assets; or
- Reduce the availability of intentionally defective grantor trusts as estate tax reduction vehicles.

The BBB bill, a social spending bill which addresses childcare and affordable housing, passed in the House of Representatives on November 19, 2021 and is now being debated in the Senate. Although the BBB bill contains some changes to the federal income tax, it also does not include any significant adjustments to estate and gift tax laws.

What does this mean for your estate planning? Although it appears any immediate changes are on hold, you should not be complacent. If your assets are significant enough to constitute a taxable estate, year-end planning has even more significance in 2021. First, the BBB bill has not yet passed. As the IRS warns, the bill - which has already undergone significant revisions - could be renegotiated and signed in a different form. Second, the unified credit (which was doubled by the 2017 Tax Cuts and Jobs Act) is scheduled to drop to $5 million per person on January 1, 2026, unless Congress acts sooner. When this happens, taxpayers who have not used the "extra" exemption will lose it forever. Therefore, clients should consider additional gifting, especially because the IRS has already confirmed that there will be no "clawback" for use of the increased exclusion amount if a taxpayer dies after the unified credit has been reduced. In addition, the current low interest rate environment makes certain estate tax planning strategies increasingly attractive. These strategies, which include sales to intentionally defective grantor trusts, intra?family loans, and grantor retained annuity trusts, may not be available in the future, as signaled by the Biden administration. Given what is expected on the horizon, it is important that all estate plans be reviewed for any potential impact.

At Jackson & Campbell, P.C., we remain available to develop comprehensive gift and estate tax strategies and help clients navigate the ever-changing tax landscape.

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