page 2
IRS makes change to crypto reporting

Working in retirement: financial considerations

page 3
Bill would give donor-advised funds charity deadline

Legal Matters®

Estate Planning
fall 2021

Planning for high-net-worth families with possible tax law changes

If certain proposed changes to federal tax law pass, they could have a big effect on high-net-worth individuals and families.

While it is unclear exactly what changes will go through, now is the time for people who might be affected to plan ahead.

Currently, individuals can give up to $11.7 million in assets during life or at death without paying gift or estate taxes. Couples can give up to $23.4 million without paying these taxes.

These exemption levels are the highest they have ever been. They are scheduled to sunset on Dec. 31, 2025, reverting to pre-2018 levels in 2026. The exemption will go back down to between $6 million and $7 million, adjusted for inflation (with twice that amount for a couple).

At that time, gifts larger than those amounts will incur gift or estate tax at approximately 40% of the amount transferred.

Under current law, a recipient of a gift or bequest is not required to pay income taxes on the amount received. Instead, a recipient of a lifetime gift takes a "carryover" in basis in the gift, retaining the basis of the person who made the gift. That means that the unrealized gain the giver accrued will be taxed when the recipient sells the asset.

Assets transferred at death are given a "step-up" in basis to fair market value, which removes any unrealized gains in the assets owned at the time of death.

Changes proposed

In May, the U.S. Treasury Department released *General Explanations of the Administration's Fiscal Year 2022 Revenue Proposals,* which lays out the Biden administration's revenue proposals.

©DmitryPoch

Here are the proposals that could affect high-net-worth taxpayers:

Income tax rates would increase. The top income tax rate for individuals (and likely trusts) would increase from 37% to 39.6%. That was the rate prior to 2018. In 2022, the new rate would apply to taxable income over $509,300 for joint filers and $452,700 for single filers. After 2022, the tax rates would be adjusted based on inflation.

continued on page 3

IRS makes change to crypto reporting

©artjazz

In the latest draft of IRS Form 1040, the agency has made a slight but essential change to the wording of the question related to virtual currency.

On the 2019 and 2020 tax returns, the following question appeared: "At any time during 2020, did you receive, sell, send, exchange, or otherwise acquire any financial interest in any virtual currency?"

The question led many people to wonder whether the IRS was trying to create a database of cryptocurrency investors, even if they had not sold their interests. It was also so broad that taxpayers and advisors found it tough to answer.

The new draft question seems to hint that the IRS is focused on taxable transactions. The new question is: "At any time during 2021, did you receive, sell, exchange, or otherwise dispose of any financial interest in VC?"

The two most notable changes are the removal of the word "send," which appeared in the 2020 version. Also, the agency has replaced "acquire any financial interest" with "dispose of any financial interest."

Crypto tax compliance

The IRS has been cracking down on noncompliance with tax reporting requirements related to cryptocurrency investments.

The agency has been receiving far fewer tax returns reporting crypto investments than there are taxpayers invested in bitcoin and other virtual currencies. The original question was added to Scheduled 1 of the 2019 return in an attempt to boost compliance.

The IRS soon realized that Schedule 1, which is used to report business income, rental property income, and other things such as moving expenses and self-employment taxes, isn't filed by many taxpayers. For example, a W-2 wage earner who invested in bitcoin wouldn't be required to file Schedule 1 and would be missed.

Then, for the 2020 return, the IRS moved the question to the top of Form 1040, which every taxpayer has to file. As a result, the IRS got a somewhat more complete answer to its question.

Tough to answer

Taxpayers and their advisors found the original question challenging to answer.

The IRS has been cracking down on noncompliance with tax reporting requirements related to cryptocurrency investments.

For one thing, the IRS hadn't provided guidance on what each element of the question covers. For example, what counts as a "financial Interest" in cryptocurrency? Taxpayers wondered if owning an interest in a company that mines cryptocurrency would qualify.

The major impact of the changed language is that it seems that taxpayers would no longer have to say "Yes" if they sent cryptocurrency between wallets or exchanges or simply bought some.

The 2021 draft Form 1040 is likely to be revised before being finalized and it remains to be seen whether clearer guidance on answering this question will be provided.

Working in retirement: financial considerations

For retirees who want to go back to work, there are some important financial considerations to keep in mind.

An advisor can help you think through the implications for you.

Consider these factors:

Social Security benefits: If you return to work, it's possible that your additional income could bring you over the annual earnings limit for Social Security. That means you could temporarily lose all or part of your benefits before you reach full retirement age. After you hit full retirement age, you can work without affecting your benefits. For someone who isn't receiving Social Security yet, returning to work is a way to delay benefits. Also, your benefit will increase each year until you turn age 70 if you wait to file.

Required minimum distributions (RMDs): If you go back to work, you must take distributions from your 401(k) and any pre-tax IRAs if you are over age 70 ½. That does not apply to Roth IRAs. However, if you are deferring funds into the new

continued on page 4

Bill would give donor-advised funds charity deadline

A bill introduced in the Senate would have the effect of moving more money out of donor-advised funds and private foundations and into working charities.

For donor-advised funds, the bill, called the Accelerating Charitable Efforts Act or ACE Act, would establish deadlines for distributing money to charities. It would also tighten certain regulations for private foundations.

Under current law, donor-advised funds do not have a minimum payout rate. These charitable accounts are created and funded by individuals to distribute to charities in the future.

Donor-advised fund account holders receive a tax deduction when they put money into the fund. Opponents of these accounts argue that it's not fair for the account holder to receive such a benefit before the money reaches a charity.

The proposed Act would place a time limit on when donor-advised funds are required to give money to charities. Under the bill, donor-advised funds would be required to give money to charities within 15 years to qualify for a tax break. These rules would apply to new contributions made to existing funds.

Under current law, private charitable foundations are required to give 5% of their assets each year for charitable activities. Under the ACE Act, these foundations would no longer be allowed to count salaries paid to family members as part of that 5% payout.

Planning for high-net-worth families with possible tax changes

continued from page 1

Taxes on long-term capital gains and qualified dividends would change. Long-term capital gains and qualified dividends would be taxed at ordinary income rates for taxpayers with adjusted gross incomes over $1 million ($500,000 for married filing separately). The result would be a federal tax rate as high as 43.4%, which is equal to a proposed tax rate of 39.6% plus 3.8% Net Investment Income Tax. The higher tax rate would apply only to the portion of a taxpayer's adjusted gross income that is greater than $1 million. The change would be retroactive to April 2021.

Gifts and transfers at death would be "income realization events." Under the proposals, any gifts and transfers at death would be treated as "income realization events." In essence, that means that gifts and bequests would be treated as though the donor (1) sold the property and realized any gain or loss; (2) repurchased the property; and (3) gifted identical replacement property.

As a result, the donor would recognize any previously unrealized gain and pay income taxes on the "phantom" gain. Most transfers of appreciated property to trusts and distributions from trusts would trigger realization of gain and income taxes.

Here are some of the exemptions that would apply:

- The first $1 million worth of "phantom gain" would be exempt from tax for single taxpayers ($2 million for married couples).
- For capital gains on the sale of a principal residence, single taxpayers could exclude an additional $250,000 in gains and married taxpayers could exclude an additional $500,000 in gains.
- Transfers of appreciated property to charity would not be considered a taxable capital gain.
- While transfers to a surviving spouse at death would not trigger immediate gain recognition, the surviving spouse would take a carryover basis in the transferred assets. That means that the assets would be taxed either at the death of the surviving spouse or sooner if they were gifted during life. This change would begin in 2022.

What to do

While these proposals are not set in stone, here are some planning options to consider:

- Ensure that your adjusted gross incomes in 2022 is less than $1 million to avoid higher rates on long-term capital gains and qualified dividends. Deferring charitable contributions into 2022 or later could be beneficial.
- Bring some income into 2021 before tax rates potentially rise, such as by converting a traditional IRA to a Roth IRA.
- Consider taking advantage of the current lower income tax rates on long-term capital gains by accelerating gains and recognizing them in 2021.
- Make larger gifts in 2021 to take advantage of the large gift tax exemption and potentially avoid income tax on gifts in future years.
- Consider moving assets with a higher basis into your taxable estate.

The future of these proposals is uncertain. Consult an estate planning attorney to decide what's best for your plan.

©DmitryPoch

This newsletter is designed to keep you up-to-date with changes in the law. For help with these or any other legal issues, please call our firm today. The information in this newsletter is intended solely for your information. It does not constitute legal advice, and it should not be relied on without a discussion of your specific situation with an attorney.

Working in retirement: financial considerations

continued from page 2

employer's 401(k), most plans will allow you to push off your RMD unless you are an owner of the business at a level of 5% or more. With a new job, it might also be possible to roll your outside retirement accounts into the new one to avoid having to take your RMD from your pre-existing accounts. Check the rules of your new employer's plan.

Qualified plans: A job that provides a tax-deferred savings plan could allow you to save more, especially if you are able to contribute up to the annual limit and make catch-up contributions. If you return to work part-time, you might also be able to take distributions from a qualified plan while working, depending on the rules of the plan.

Health insurance: Many people return to work for the health insurance. If you're on Medicare, find out whether the new company's insurance will work alongside it. Also, be aware that as your income rises, your Medicare Part B premiums might also increase over the standard amount, depending on your income level. While group insurance coverage is typically less expensive, it can be worth keeping your private insurance policy as well. You might not be able to get the policy again at the same rates in the future.

©photographee.eu

Income taxes: Making money means paying income taxes, of course. A new job could push you into a higher tax bracket. You might be able to avoid that by deferring funds in a tax advantaged plan. Social Security benefits are taxable as well, depending on the level.