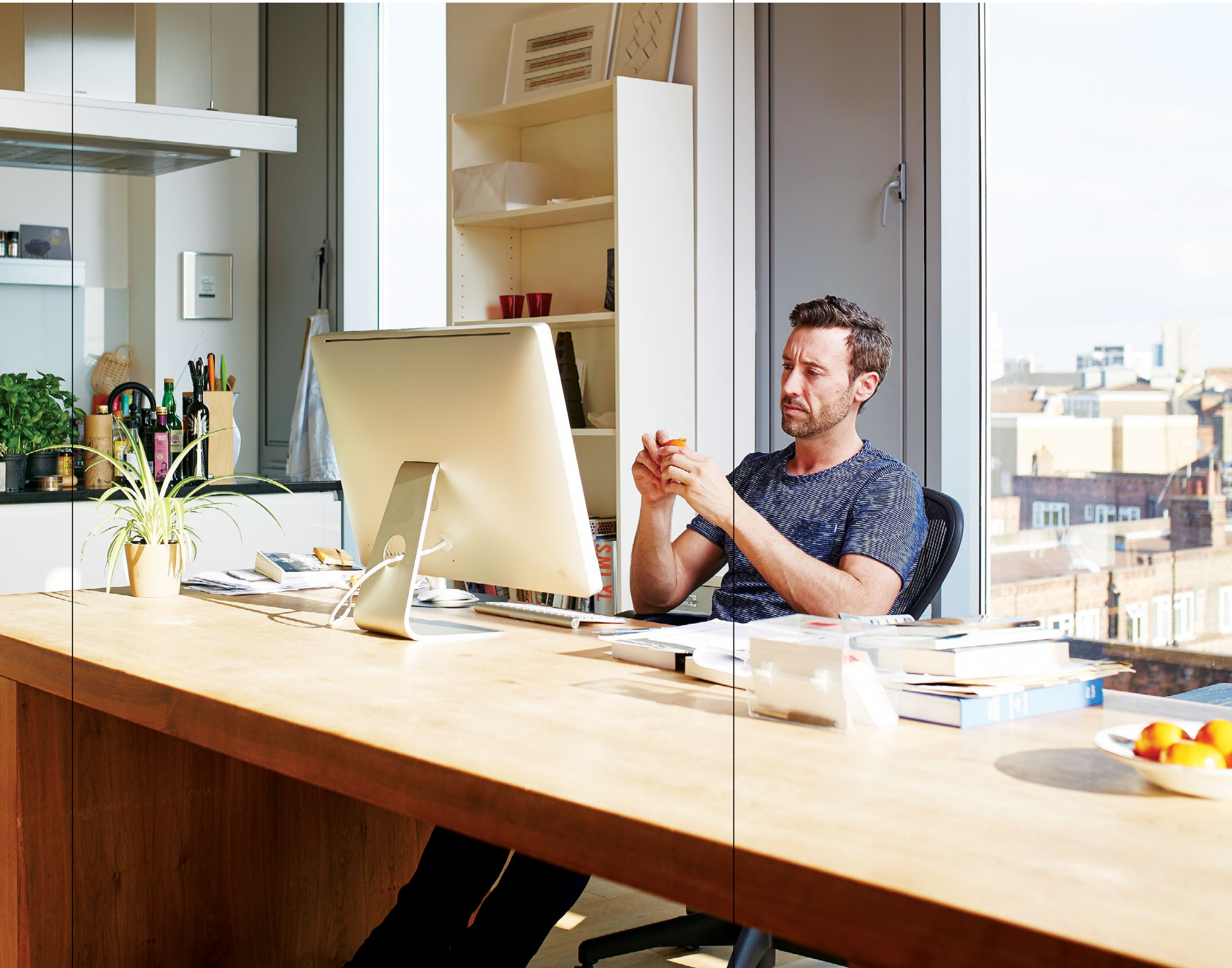
William Blair

Maximizing the impact of your capital

2022 Planning Strategies: Uncertain Times Call for Certain Measures



High-net-worth individuals and families, philanthropists, and business owners should evaluate their tax and estate plans so they are best positioned for the long-term outlook. You might consider reviewing the following strategies to help meet your financial, wealth-transfer, and philanthropic goals.

1. Reassess Near- and Long-Term Goals
2. Review Current Estate Plan
3. Plan Annual Gifting
4. Assess Roth Conversion
5. Evaluate Wealth Strategies in a Low Interest Rate Environment
6. Consider Using Historically High Lifetime Tax Exemption
7. Review Important Retirement Ages
8. Evaluate Asset Allocation and Location
9. Charitable Giving
10. Philanthropy Strategies

Build Back Better Act

In late 2021, the U.S. House of Representatives passed the Build Back Better Act, a sweeping social safety net and climate bill that is to be paid for through a number of tax increases.

We believe clients should be aware of provisions that could be most impactful to their individual circumstances, but focus more broadly on tried and true strategies and a general reevaluation of near- and long-term goals. The chart below is a helpful synopsis of the current Build Back Better Act as of the writing of this publication. It outlines provisions that were part of the original Biden administration tax plan that have subsequently been eliminated, as well as provisions that made it into the current bill.

Proposal	In/Out	Details
Individual income tax rates	Out	Increasing the top individual income tax rate from 37% to 39.6% for individuals with >$400,000 in income
Capital gains	Out	Increasing the LTCG and qualified dividend rate to 25% for individuals with >$400,000 in income
Estate tax	Out	No changes to the estate tax or ending the step-up in basis were included in the bill
Surtax on wealthy individuals	In	Imposing a 5% surtax to individuals with income >$10 million. An additional 3% surtax would apply to income >$25 million
State and Local Tax (SALT) deduction	In	Increasing the SALT exemption amount (currently a $10,000 cap) to $80,000 through 2030
"Backdoor" Roth IRA conversions	In	Individuals would be prohibited from converting after-tax contributions (to either a 401(k) or a traditional IRA) to a Roth account beginning in 2022
Roth conversion limits	In	Prohibit Roth conversions for those earning >$400,000, or couples earning >$450,000, beginning in 2032
Capping aggregate retirement account balances	In	Prohibit individuals with aggregate balances >$10 million in tax-advantaged retirement accounts and income >$400,000 from making further contributions to IRAs. Those affected required to take RMDs, regardless of age. More stringent distribution requirements for individuals with aggregate retirement savings of >$20 million. Would take effect beginning in 2029.
Corporate Minimum Tax	In	Imposing a 15% minimum tax on corporations to close loopholes and incentives in the tax code allowing them to pay a lower rate

Reassess Near- and Long-Term Goals

Living through a pandemic has made people take a step back and look at both near- and long-term goals.

- Saving for your children's college education
- Lowering debt
- Increasing retirement savings
- Funding trusts for heirs
- Expanding philanthropic donations

These are just a few of the goals we hear most often from clients. Which mean most to you?

Review Current Estate Plan

Given today's environment, it is particularly important that your estate documents are up to date.

- Review wills, trusts, and beneficiary designations to confirm they reflect your current wishes
- Double-check to make sure your medical directives and powers of attorney for health and property are up to date in case of extended illness or incapacity
- Review ownership titles on all property and assets

When assets are not titled correctly, property may not pass to the intended heirs or testamentary trusts (which go into effect at death) and may not be funded according to your estate plan.

Plan Annual Gifting

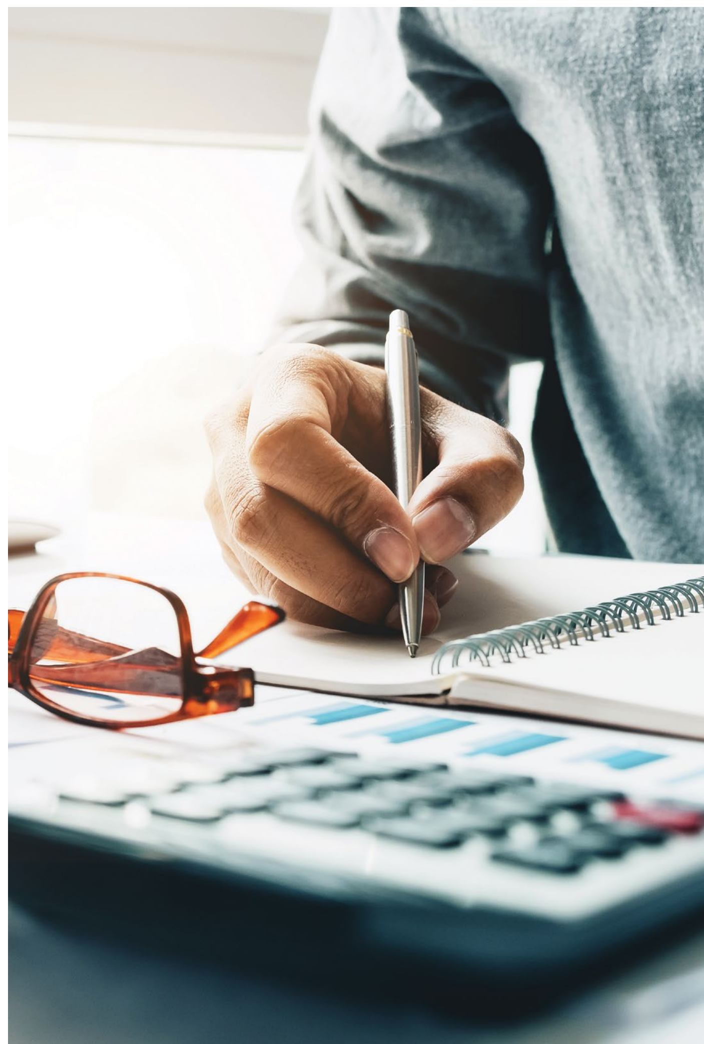
Annual gifting allows you to give loved ones tax-exempt gifts throughout your lifetime.

Currently, the IRS allows you to gift up to $16,000 gift-tax-free to an individual in one year. There is no limit to the number of recipients you can make an annual exclusion gift to and it does not tap into the $12.06 million lifetime exemption. Establishing gift trusts for one's children, funded with annual exclusion gifts, is also a strategy to consider.

Contributing to Roth IRA accounts for children is another gifting option for children who have earned income. You can match their earnings up to $6,000 for such Roths. These are great savings vehicles since they are funded with after-tax dollars and future distributions will be income tax-free.

Funding 529 education plans is another option to help children and grandchildren through tax-exempt gifting. And you can front-load five years' worth of exclusion gifts in one tax year for such plans, funding it up to $80,000, or $160,000 if you are married. However, if you take advantage of this strategy, you are not allowed to make annual exclusion gifts to the beneficiary over the next four years.

In addition to the annual exclusion gifts, you can also pay for tuition or medical bills for individuals directly to the institutions gift-tax-free. There is no cap to such payments and you can still make annual exclusion gifts of up to $16,000 gift-tax-free to the same beneficiary.



Assess Roth Conversions

Converting a traditional IRA (tax deferred growth) to a Roth IRA (tax-free growth) has been popular recently with the Secure Act of 2020.

One of the provisions of the Secure Act requires any non-spouse beneficiary to deplete an inherited account within 10 years of receipt, limiting the prior "stretch" IRA advantage over the beneficiary's lifetime. Doing a Roth conversion now could minimize the impact of the new rule since tax-free withdrawals from an inherited Roth IRA will also extend to your children.

In addition, some employer-sponsored 401(k) plans also allow for in-plan Roth conversions of both pretax and after-tax contributions, although after-tax conversions may be disallowed starting in 2022 should the Build Back Better Act pass.

Both types of conversions are ideal for individuals who expect higher taxes in the future and/or want to accelerate income in a year with lower tax rates. Keeping in mind that under current legislation income tax brackets revert to higher tax brackets in 2026, you may want to consider doing a full or partial conversion now.

You may also want to consider a Roth conversion if you have a long investment time frame for the tax-free earnings to grow and can pay the tax cost of the conversion with non-retirement funds.

Note: The current provisions of the Build Back Better Act as passed by the House would prohibit all taxpayers from converting their after-tax contributions to a Roth IRA in a so-called "backdoor" conversion method. The bill would also prohibit after-tax Roth conversions in a 401(k).

Roth IRA Conversion Analysis

	Yes	No
Can you afford to leave the IRA or 401(k) funds untouched throughout retirement, funding your expenses through other sources of income instead?	Your wealth-transfer plan will likely benefit from a Roth conversion	You may still benefit from a Roth IRA or 401(k) conversion, but it is advisable to run a personalized cost-benefit analysis
Will you be in the same or a higher tax bracket in the future?		
Can you pay the tax on the conversion by using funds from outside the IRA or 401(k) plan?		
Can you convert without negatively affecting your current income tax planning?		
Can you continue to fulfill your other financial planning objectives (e.g., charitable giving)?		

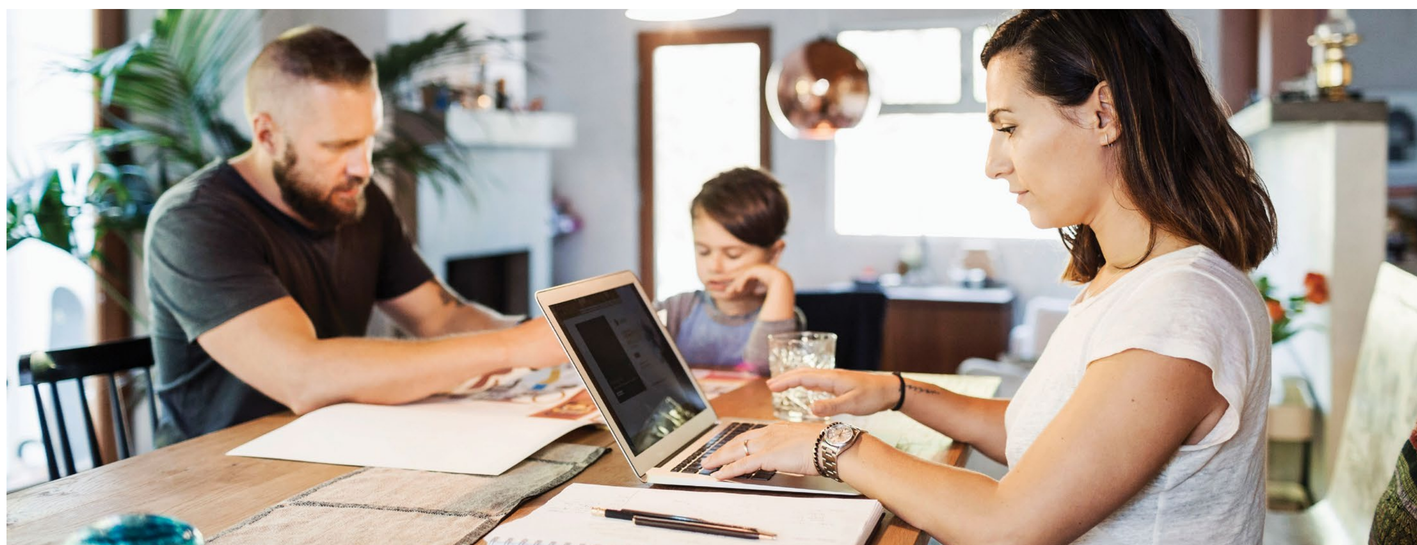
Evaluate Wealth Strategies in the Current Low Interest Rate Environment

If you are considering transferring some of your wealth, here are a few strategies to consider in the current low interest rate environment:

- A grantor retained annuity trust (GRAT) is often referred to as an estate freeze strategy as it allows you to gift future asset appreciation to heirs without paying gift tax. When establishing a GRAT, the grantor contributes assets in trust but retains a right to receive the initial value of the assets over the life of the GRAT. They can be structured as zeroed-out GRATs which would not use any of your gift tax exemption, making GRATs an effective wealth transfer tool for those who have already fully utilized their lifetime exemption. GRATs have also risen in popularity since the hurdle rate, or the IRS Section 7520 rate, is historically low.

- Intra-family lending is also common during the current low interest rate environment. Family members can offer more flexible lending terms than going through a commercial process and it provides a way for family members to keep wealth within the family. The loans can be part of your overall legacy plans, including transferring a family business or helping family members finance major purchases. The Internal Revenue Service requires a minimum loan rate be based on its applicable federal rate (AFR). If you have existing family loans, now is also a good time to consider refinancing.

- Selling assets to an intentionally defective grantor trust (IDGT) can be an effective estate planning strategy to remove appreciating assets from your estate while maintaining an income stream. As the grantor, you can seed the trust with a gift and then sell additional assets to the trust in exchange for an interest-bearing note—typically a rate equal to the applicable federal rates. You pay income taxes during the term of the IDGT, allowing the trust to grow income tax free. (Interest payments on the note are not considered income.) But all appreciation of the assets goes to your beneficiary when the trust is distributed.



Consider Using Historically High Lifetime Tax Exemption

The lifetime gift and estate tax exemption is at a record high of $12.06 million per individual for 2022. The historically high lifetime tax exemption is scheduled to expire at the end of 2025—reverting to the previous level of $5 million, adjusted for inflation.

Presently, you can gift up to $12.06 million during your lifetime or at death without ever having to pay gift or estate taxes on this amount. For married couples, both spouses each qualify for the $12.06 million exemption, creating an opportunity to pass up to $24.12 million free of transfer taxes. The value of your estate above your available exemption is taxed at 40% at death. Keep in mind the exemption applies to gifts and estate taxes combined—often referred to as a "unified" exemption. So any exemption used for lifetime gifting reduces the amount that can be used to offset the estate tax at death.

There are three "transfer" taxes included in the unified federal exemption system:

- Gift tax applies to the transfer of property made while a person is living
- Federal estate tax applies to the transfer of property at death
- Generation-skipping tax (GST) is a tax on the transfer of property that skips a generation and transfers during lifetime or at death

Gifting assets in trust. Allows you to specify provisions for beneficiaries, including: how much they can access; when distributions can occur; and what the funds can be used for.

A Dynasty Trust – any trust that lasts one generation below that of the grantor can maximize the legacy passed onto heirs using the generation gift tax exemption. A significant drawback of a dynasty trust is that you are making a sizeable irrevocable gift.

Spousal lifetime access trust. A SLAT—an irrevocable trust set up by one spouse for the other to be used during his or her lifetime—has become a popular estate planning strategy used by married couples to take advantage of the lifetime exemption.

The appeal of SLATs is that one spouse can create the trust using his or her exemption and make the other spouse the primary beneficiary. This way you reduce your taxable estate but retain indirect access to the assets as long as your spouse, the primary beneficiary of the SLAT, is alive. Both spouses can each create a SLAT for the other spouse and use their respective exemptions.

Review Important Retirement Ages

The Secure Act, enacted late in 2019, changed retirement rules to strengthen your retirement security. Among the key changes was required minimum distributions (RMD) beginning at age 72 versus 70 ½. Note: There are currently multiple Congressional proposals pending that are being referred to as "SECURE Act 2.0." These proposals include increases to the RMD age to as high as age 75 and higher catch-up contribution limits.

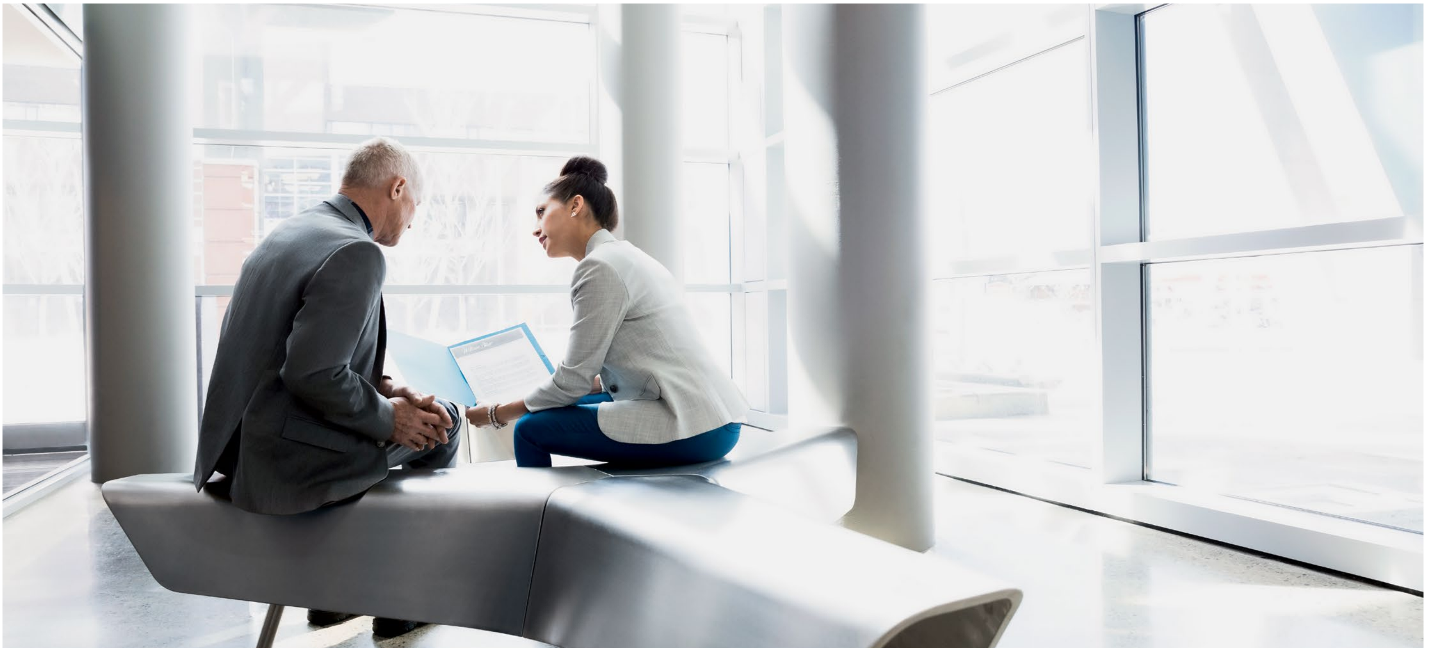
Important Retirement Ages

Age	Milestone
50	Begin making catch-up contributions, an extra amount that those 50 and over can add to 401(k) and other retirement accounts.
55	Early withdrawal penalty exception for distributions from certain employer-provided plans such as 401(k) for those who are age 55 and over and separate from service (does not apply to IRAs).
59½	No more tax penalties on early withdrawals from employer-provided retirement savings plans such as 401(k) plans and other individual retirement accounts.
62	Earliest age to collect Social Security retirement benefits; however claiming early reduces monthly benefits.
65	Sign up for Medicare and Medicare Part D.
66-67	Receive Social Security full benefits, depending on your birth year.
66-70	Earn Social Security delayed retirement credits.
70½	Eligible to make qualified charitable contributions from individual retirement accounts.
72	Start taking required minimum distributions from most retirement accounts.

Evaluate Asset Allocation and Location

It is a good practice to periodically re-evaluate your asset allocation and review how your assets are distributed across different vehicles—non-qualified accounts, retirement accounts, trusts, insurance, foundations, and other investments.

Is an asset used to fund your family's lifestyle, or should it be a future gift for your children or charity? If you have a trust with a charitable beneficiary, for example, it may make sense to fund it with assets that have a potentially higher tax liability given the possibility of increased income taxes in the future. If you have a gift trust for heirs with a long-term investment goal, funding it with growth-oriented investments could be your best option. Determining the purpose and future intention of your funds is critical in reassessing your finances.



Charitable Giving

Enhanced charitable deduction expired in 2021. The Cares Act, which expired at the end of 2021, included several tax incentives to encourage individuals and groups to support their charitable goals. One was the elimination of the adjusted gross income limitation (previously 60%) on cash charitable donations for those who itemize their taxes. Individuals may deduct cash contributions of up to 100% of their adjusted gross income in 2020 as well as 2021. These contributions must be paid directly to a qualified charity and not through donor-advised funds, private foundations, or other supporting organizations.

Giving appreciated securities to charities. By gifting long-term appreciated securities directly to a qualified public charity, you will effectively increase the amount of your gift—taking advantage of a double income tax benefit. You will get a charitable deduction on the fair market value of the gifted security and avoid paying capital gains tax on the security donated.

Qualified charitable distribution (QCD) continues. While the Secure Act raised the RMD age limit to 72, it did not change the age at which an individual can make a qualified charitable distribution (QCD) from their IRA, which remains at age 70 ½. With the new RMD age limit, the Secure Act creates a new one-and-a-half-year window when IRA distributions may qualify as charitable contributions and are not recognized as taxable income if the distribution is made directly from the IRA to a qualified public charity. At age 72, QCDs can satisfy RMDs and lower your taxable income by the amount of your donation up to $100,000 per year.

Using donor-advised funds (DAFs). Instead of giving directly to a charity or setting up a foundation, DAFs allow donors to pool donations into one fund, deduct the entire contribution in one year, and advise the fund manager over time on the charities to donate to. DAFs have been growing in popularity in recent years for their tax advantages, simplicity, and convenience. Donations can be done by the donor online, while the recordkeeping is handled by the fund manager.

Consider giving more or differently.

For taxpayers who contribute more than their annual limit, the excess is not lost but can be carried forward up to five years. Both options require the cash to go directly to a qualified public charity, i.e., not through a foundation or donor-advised fund.

Here are additional ways to help the charities you are close to: Consider converting project-based grants to unrestricted support; accelerating your payment schedules; providing loans to nonprofits; or offering multiyear grants. If you supported an event in the past but the nonprofit was forced to cancel it because of COVID-19, reallocate those funds to a general operating budget.

You may also want to collaborate on grantmaking. Increasingly, individual donors, family and corporate foundations, and large national foundations are coming together—working collaboratively to make a bigger impact around specific challenges. Environmental, social, governance (ESG) investing—also known as sustainable investing—is among the many ways grant making can make a long-term impact on society while earning positive returns.

Engage your next generation. Philanthropy can be a powerful way for families to pass on their shared beliefs and values. It can also provide special opportunities for families to spend time together, collaborate, and learn more about one another. Integrating philanthropic conversations and activities into family life is an excellent way to encourage a sense of financial responsibility among younger generations. And giving together can be a bonding experience for family members of all generations. If you are looking for family volunteer opportunities, reach out to William Blair. Learn what other donors are funding by participating in regional grantmaker associations. Connect with your wealth advisor or local community foundation to find opportunities to collaborate with other funders.

Contact Your William Blair Wealth Advisor

William Blair is dedicated to helping you meet your financial and philanthropic goals with a focus on your evolving needs. Our team of dedicated wealth planning professionals and our philanthropy strategies team are here to serve you. To discuss these wealth planning strategies, please contact your William Blair wealth advisor or email *PWM@williamblair.com*.

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