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Five Tax Benefits that Might Go Away if President Trump Is Not Reelected

By Sean R. Weissbart[*]

As the calendar turns to another presidential election year, it's never too early to start thinking about tax preparation as the next occupant of the oval office will likely have a major impact on the nation's tax laws and policy. If a Democrat wins the White House, we can expect significant change to the tax laws.[1] Indeed, the Democratic presidential candidates have made varying tax proposals to eliminate or curtail certain tax benefits available under current law. Based on these proposals, here are five tax strategies to take advantage of in 2020 that might go away if President Donald Trump is not reelected:

1. Make Gifts to Take Advantage of Record High Exemption Amounts: Every U.S. person is given an "exemption amount" – currently $11.58 million[2] – of gifts they can make before additional gifts are subject to a gift tax. If the exemption amount is not used during one's lifetime, the remaining amount is available to offset gifts made at death. The current tax rate on gifts over the exemption amount is 40%. Although Democrats universally support decreasing the exemption amounts, Senator Bernie Sanders has proposed one of the most extreme changes to this law: he would reduce the exemption amount to $3.5 million and increase the tax rate to a maximum of 77%.[3]

However, taxpayers can take advantage of the current exemption amounts and lower tax rates by making gifts in 2020. This is especially important for taxpayers with wealth concentrated in a single asset such a residence, closely held business, or farm, because if these assets exceed the exemption amount they might need to be sold to pay the tax.

2. Use Short-Term GRATS to Make Tax-Free Gifts: Senator Elizabeth Warren has proposed raising money for affordable housing by eliminating one of the most common estate-planning techniques: the short-term Grantor Retained Annuity Trust (GRAT).[4] Like all trusts, GRATs are created when someone, known as the grantor, transfers property to a trust. This amount would ordinarily be considered a taxable gift by the grantor to the trust. But in the case of a GRAT, the amount considered a taxable gift is reduced (or even eliminated) because the grantor (the trust's funder) retains an interest in the trust: every year the trustee must distribute a fixed amount of money (referred to as an annuity) back to the grantor. To determine the value of the taxable gift, the grantor reduces the value of the annuity payments from the amount transferred to the trust.

GRATs have the potential to provide the biggest tax benefits when interest rates are low because the trustee must pay the annuity payment to the grantor with a rate of interest based on the federal §7520 rate in effect at the time of the creation of the trust. To the extent the trust's assets appreciate more than the interest rate, which is

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[1] All section references herein are to the Internal Revenue Code of 1986, as amended, and the regulations promulgated thereunder, unless otherwise specified.

[2] Rev. Proc. 2019-44 §3.41.

[3] For the 99.8 Percent Act, S. 309, 116th Cong. (introduced on January 31, 2019).

[4] American Housing and Economic Mobility Act of 2019, S. 787, 116th Cong. (introduced on March 13, 2019).

more likely when interest rates are low, the beneficiaries receive this excess appreciation free of gift tax.

Senator Warren has proposed mandating a minimum 10-year term for GRATs because there is less predictability for the growth of an asset over this longer period.[5] This makes 2020 the perfect time to create a short-term GRAT. Anyone with disposable wealth who believes a certain asset will appreciate more than the §7520 rate – at a near record low of two percent for GRATs created in January 2020 – should create a short-term GRAT and transfer the excess appreciation free of federal gift tax.

3. Realize Capital Gains at Lower Tax Rates: Former Vice President Joe Biden has proposed raising money to pay for universal healthcare by almost doubling the tax rate on capital gains.[6] Currently, long-term capital gains (generally gains on the sale of stock held for more than one year) are taxed at 0%, 15%, or 20% depending on a taxpayer's income,[7] but under Biden's plan, the top rate will nearly double to 39.6% for those earning more than $1 million. If you are considering selling stock, it may be wise to realize the gain in 2020, to avoid paying double the tax rate if Biden's proposal becomes law.

4. Invest in Non-Publicly Traded Assets to Avoid Being Taxed on Unrealized Gains: Mayor Pete Buttigieg has proposed taxing wealthy Americans on the yearly appreciation in their publicly traded stock – even though the stock has not been sold and might depreciate the following year.[8] This is known as a ''mark-to-market'' tax regime. Under current law, tax is only paid when the asset is sold.[9] Although Democratic candidates have also made proposals for added taxes on non-publicly traded assets, it may be possible to avoid this new tax by investing in real estate, farms, and retirement accounts that will not be subject to this mark-to-market tax regime.

5. Create Trusts to Avoid the Wealth Tax: Senator Sanders has been a fierce advocate of a wealth tax that would impose an additional annual tax on the wealth of Americans worth $16 million or more with tax rates ranging from 1% to 8%.[10] However, it may be possible to remove wealth from an individual's ''balance sheet'' by transferring it to a trust for the benefit of family members and distribute the trust income on an annual basis to family members who are in lower tax brackets. Although there are intricate tax rules that can tax the creator of a trust on its income or consolidate the holdings of multiple trusts, with careful planning, these punitive tax regimes may be avoided.

Even better, the trusts can be structured so that the assets of the trust can be returned to the creator, if he or she desires the money in the future. Many states have laws that allow completed gifts to a trust where the creator is named as a discretionary beneficiary of the trust provided someone other than the creator is named as the trustee.[11] This ''independent person'' can be the creator's best friend or attorney. Whether or not you live in a state that sanctions these trusts, individuals can create out-of-state trusts to benefit from preferential laws in other states.

CONCLUSION

On November 3, 2020, American voters will either hand President Trump a second term or elect a Democratic candidate. It remains to be seen how much of a political mandate he or she will carry into the White House–or whether the balance between Democrats and Republicans will change in the House and the Senate—but the next president will undoubtedly have a significant say in shaping tax policy and possible reforms to the Internal Revenue Code. Understanding the potential impact of the candidates' tax positions as they take shape is the best way to be prepared for what lies ahead in 2021 and beyond.

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[5] S. 787.

[6] Joseph Biden, *Presidential Candidate Platform on Health Care,* available at https://joebiden.com/healthcare/.

[7] §1(h), §1(j), §1221.

[8] *Buttigieg Seeks Capital Gains Tax Hike*, Daily Tax Rep. No. 217 (Nov. 12, 2019).

[9] §1001.

[10] Sen. Bernie Sanders, *Presidential Candidate Platform on Tax on Extreme Wealth,* available at https://berniesanders.com/issues/tax-extreme-wealth/.

[11] These trusts are commonly referred to as Domestic Asset Protection Trusts. *See, e.g.,* Alaska Stat. §13.36.310, §34.40.110 (Alaska); 12 Del. C. §3570-§3576 (Delaware); Nev. Rev. Stat. §166.010-§166.170 (Nevada). DAPTs are completed gifts because, under state law, creditors cannot reach the assets. *See* PLR 9837007, PLR 200944002.

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