



Potential Tax Alert September 2021: **Other than that, how did you enjoy the play, Mrs. Lincoln?**

By now, you're certainly aware that the House Ways & Means Committee released a mere 881 pages of legislative text last week containing several proposed changes to the current federal tax regime that would significantly impact wealthy Americans in a number of ways. Those changes have been summarized by the committee [here](#). The exact nature of potential changes (including the timing of when they become effective) remain far from certain. At the date of this writing, the Senate has yet to release its own proposals, and even within the House Democratic Caucus, many items remain up for debate.

While much of the Ways & Means proposal (with the ever catchy title of "Responsibly Funding Our Priorities") will likely change as it proceeds through the legislative process and be folded into a larger reconciliation package, the purpose of this Alert is to address what information we have in the moment and offer some considerations for action at this time. Of course, this Alert intends neither to be exhaustive nor tailored to any one taxpayer's unique circumstances, and we would expect that consultation with your attorney and tax advisor would necessarily be part of the consideration of any possible action steps.

A Summary of Key Personal Tax Elements of the Ways & Means Proposed Legislation:

- Beginning on Jan 1, 2022, the highest marginal ordinary income tax rate will increase from 37% to 39.6%. As well, the top bracket will begin at \$400,000 for individuals and \$450,000 for married couples. Currently the top bracket does not begin until \$523,600 and \$628,300 respectively.
- Beginning on Jan 1, 2022, an additional 3% surtax would be levied against income in excess of \$5 million.
- Beginning on Jan 1, 2022, the QSBS deduction would be cut by 50% for single owners earning over \$400,000 (and \$450,000 for married owners).
- Beginning on Sept 13, 2021, capital gains taxes will increase from 20% to 25% (plus the "Medicare surtax" of 3.8%, so effectively from 20% to 28.8%) for individuals with more than \$400,000 (\$450,000 for married filers) of total income, "marrying" the higher capital gains rate to the new proposed top bracket.
- Beginning on Jan 1, 2022, contributions to IRAs with a balance in excess of \$10 million will be disallowed. Roth IRA contributions and back door conversions will be disallowed for high income earners. And larger required minimum distributions from

large IRAs will be imposed, specifically 50% of the excess amount above the \$10 million threshold.

- Beginning Jan 1, 2022, the federal combined estate and lifetime gift tax exemption will be reduced from \$10 million (indexed for inflation, currently \$11.7 million) to \$5 million (indexed for inflation, and speculated to be \$5.9mm on Jan 1, 2022).
- Beginning on the date the bill is enacted (???), assets funded into an irrevocable grantor trust after the date will be included in the grantor's estate and sales between a grantor and his grantor trust will trigger recognition of gain. Further, valuation discounts will be unavailable for the transfer of minority interests in closely held passive assets.
- There are numerous other proposed changes in the draft as well of course.

With so much uncertainty and speculation about where these proposals will land and when they will be made effective, it's difficult to pick a path through and identify what actions you might consider taking. For example, if the capital gains increase effective date is already in our rear view mirror, then we just have to live with the change. But Senator Manchin continues to suggest a pause until 2022, making it at least possible that this change is one that may still be future dated. With all of that in mind, the list of items for your consideration below are just intended to be that – prompts for your consideration. Most if not all are ideas that we've been discussing for a while, and which ideas have now become more urgent with the introduction of proposed legislation.

Income & capital gains tax considerations:

- If you have traditional IRAs/401ks and a retirement asset base under \$10 million, consider a Roth conversion before the end of the year.
- If you have unexercised vested options that will be taxed as ordinary income / short-term capital gains, consider exercising them this year before the rates increase and the brackets compress.
- Because the proposal has left the \$10,000 SALT deduction alone for now, consider waiting to make state estimated payments in January 2022 instead of December 2021 to increase the value of that deduction.
- Consider taking capital gains before the end of the year in hopes that the effective date gets postponed into 2022. Acknowledging that "hope is not a strategy," acting quickly to take some gains now may wind up having the successful outcome of recognizing gains under a less punitive tax regime.

Estate & gift tax considerations:

- To the extent you anticipate having an estate tax exposure, consider making gifts to more fully use the current \$11.7mm estate and gift tax exemption before it gets cut in half. These gifts would need to be made this year, and if a grantor trust transaction is contemplated as part of the gift, action may need to be taken even more quickly.
- Once you have capped out your estate and gift tax exemption, consider making annual exclusion gifts to as many beneficiaries (e.g., children, grandchildren, spouses of children or grandchildren) as desirable on an annual basis. The annual exclusion



allowance is currently \$15,000 per year. As an example, for a married couple with 3 children and 4 grandchildren, that becomes a powerful tool (2 donors x \$15,000 x 7 donees = \$210,000 per year.

- To the extent you currently have a grantor trust and you anticipate wanting to “toggle off” grantor trust status at some point in the future, consider doing this before the date of enactment.
- Whether intended or unintended, irrevocable life insurance trusts (ILITs) are captured in the House proposal’s attack on grantor trusts. So for taxpayers who currently have or are considering trust owned life insurance with currently unfunded premiums, you may want to consider funding (with income producing property, cash, or possibly a promissory note) before the date of enactment.

Again, these ideas are not intended to be exhaustive, and many of them may not be suitable, appropriate, or applicable to your unique circumstances. There will be a lot of back and forth before Congress sorts out the final version of any tax bill. In the meantime, our firm continues to closely monitor changes on the legislative landscape, and we would be delighted to talk with you and your tax and legal advisors at your earliest convenience.

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