SAMALIN
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Estate Planning Strategies in a Low-Interest Environment

The federal government requires the use of certain interest rates (published by the IRS) to value various items used in estate planning, such as an income, annuity, or remainder interest in a trust. The government also has interest rates that a taxpayer may be deemed to use in connection with certain installment sales or intra-family loans. These rates are currently at or near historic lows, presenting several estate planning opportunities. Low interest rates generally favor certain estate planning strategies over others and may have a detrimental effect on others.

Grantor Retained Annuity Trust (GRAT)

In a GRAT, you transfer property to a trust, but retain a right to annuity payments for a term of years. After the trust term ends, the remaining trust property passes to your beneficiaries, such as family members. The value of the gift of a remainder interest is discounted for gift tax purposes to reflect that it will be received in the future. Also, if you survive the trust term, the trust property is not included in your gross estate for estate tax purposes. If the rate of appreciation is greater than the IRS interest rate, a higher value of trust assets escapes gift and estate taxation. Consequently, the lower the IRS interest rate, the more effective this technique generally is.

Charitable Lead Annuity Trust (CLAT)

In a CLAT, you transfer property to a trust, giving a charity the right to annuity payments for a term of years. After the trust term ends, the remaining trust property passes to your beneficiaries, such as family members. This trust is similar to a GRAT, except that you get a gift tax charitable deduction. Also, if the CLAT is structured so you are taxed on trust income, you receive an upfront income tax charitable deduction for the gift of the annuity interest. Generally, the lower the IRS interest rate, the more effective this technique is.

Installment Sale

You may also wish to consider an installment sale to family members. With an installment sale, you can generally defer the taxation of any gain on the property sold until the installment payments are received. However, if the family member resells the property within two years of your installment sale, any deferred gain will generally be accelerated. The two-year limit does not apply to stocks that are sold on an established securities market.

You are generally required to charge an adequate interest rate in return for the opportunity to pay in installments, or interest will be deemed to be charged for income tax and gift tax purposes. However, with the current low interest rates, your family members can pay for the property in installments, while paying only a minimal interest cost for the benefit of doing so. *(Continued on page 2)*

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Samalin Investment Counsel is a fee-only, nationally recognized SEC registered investment advisory firm. With offices in Chappaqua NY and NYC, we specialize in wealth management, pre and post divorce financial planning, retirement planning, and other related financial services.

Estate Planning Strategies in a Low-Interest Environment

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Low-Interest Loan

A low-interest loan to family members might also be useful. You are generally required to charge an adequate interest rate on the loan to avoid income tax and gift tax consequences. However, with the current low interest rates, you can provide loans — or refinance an existing loan — at a very low rate and family members can effectively keep any earnings in excess of the interest they are required to pay you.

Charitable Remainder Unitrust (CRUT)

You retain a stream of payments for a number of years (or for life), after which the remainder passes to charity. You receive a current charitable deduction for the gift of the remainder interest. Interest rates have no effect if payments are made annually at the beginning of each year. Otherwise, interest rates generally have only a minimal effect. However, in this case, a lower interest rate increases the value of the charitable remainder interest slightly less than a higher interest rate would.

The use of trusts involves a complex web of tax rules and regulations, and usually involves upfront costs and ongoing administrative fees. You should consider the counsel of an experienced estate professional before implementing a trust strategy.

FACTOR	GRAT	CLAT	CRUT
Lower interest rate	LV	LV	Minimal or no effect
Longer term of years	LV	LV	LV (shorten term to increase value
Higher annuity payment	LV	LV	N/A
Lower unitrust payout rate	N/A	N/A	HV

HV= higher value for remainder interest
LV= lower value for remainder interest

Key Retirement and Tax Numbers for 2021

Every year, the Internal Revenue Service announces cost-of-living adjustments that affect contribution limits for retirement plans and various tax deduction, exclusion, exemption, and threshold amounts. Here are a few of the key adjustments for 2021.

ESTATE, GIFT, AND GENERATION-SKIPPING TRANSFER TAX

- The annual gift tax exclusion (and annual generation-skipping transfer tax exclusion) for 2021 is $15,000, the same as in 2020.
- The gift and estate tax basic exclusion amount (and generation-skipping transfer tax exemption) for 2021 is $11,700,000, up from $11,580,000 in 2020.

STANDARD DEDUCTION

A taxpayer can generally choose to itemize certain deductions or claim a standard deduction on the federal income tax return. In 2021, the standard deduction is:

- $12,550 (up from $12,400 in 2020) for single filers or married individuals filing separate returns
- $25,100 (up from $24,800 in 2020) for married individuals filing joint returns
- $18,800 (up from $18,650 in 2020) for heads of households

The additional standard deduction amount for the blind or aged (age 65 or older) in 2021 is:

- $1,700 (up from $1,650 in 2020) for single filers and heads of households
- $1,350 (up from $1,300 in 2020) for all other filing statuses

Special rules apply if you can be claimed as a dependent by another taxpayer.

IRAS

The combined annual limit on contributions to traditional and Roth IRAs is $6,000 in 2021 (the same as in 2020), with individuals age 50 and older able to contribute an additional $1,000. The limit on contributions to a Roth IRA phases out for certain modified adjusted gross income (MAGI) ranges. For individuals who are covered by a workplace retirement plan, the deduction for contributions to a traditional IRA also phases out for certain MAGI ranges. (The limit on nondeductible contributions to a traditional IRA is not subject to phase-out based on MAGI.)

Employer Retirement Plans

- Employees who participate in 401(k), 403(b), and most 457 plans can defer up to $19,500 in compensation in 2021 (the same as in 2020); employees age 50 and older can defer up to an additional $6,500 in 2021 (the same as in 2020).
- Employees participating in a SIMPLE retirement plan can defer up to $13,500 in 2021 (the same as in 2020), and employees age 50 and older can defer up to an additional $3,000 in 2021 (the same as in 2020).

KIDDIE TAX: CHILD'S UNEARNED INCOME

Under the kiddie tax, a child's unearned income above $2,200 in 2021 (the same as in 2020) is taxed using the parents' tax rates.

Is It Time to Think About Tax-Free Income?

Federal and state governments have spent extraordinary sums in response to the economic toll inflicted by the COVID-19 pandemic. At some point it is likely that governments will look for ways to increase revenue to compensate for this spending and increase income taxes as a result. That's why it might be a good time to think about ways to help reduce your taxable income. Here are three potential sources of tax-free income to consider.

Roth IRA

Contributions to a Roth IRA are made with after-tax dollars — you don't receive a tax deduction for money you put into a Roth IRA. Not only does the Roth IRA offer tax-deferred growth, but qualified Roth distributions including earnings are not subject to income taxation. And the tax-free treatment of distributions applies to beneficiaries who may inherit your Roth IRA.

Municipal Bonds

Municipal, or tax-exempt, bonds are issued by state and local governments to supplement tax revenues and to finance projects. Interest from municipal bonds is usually exempt from federal income tax. Also, municipal bond interest from a given state generally isn't taxed by governmental bodies within that state, though state and local governments typically do tax interest on bonds issued by other states.

Health Savings Accounts

A health savings account (HSA) lets you set aside tax-deductible or pre-tax dollars to cover health-care and medical costs that your insurance doesn't pay. HSA funds accumulate tax-deferred, and qualified withdrawals are tax-free. While an HSA is intended to pay for current medical and related expenses, you don't necessarily have to seek reimbursement now. You can hold your HSA until retirement then reimburse yourself for all the medical expenses you paid over the years with tax-free HSA distributions — money you can use any way you'd like. Be sure to keep receipts for medical expenses you incurred.

Municipal bonds are subject to the uncertainties associated with any fixed income security, including interest rate risk, credit risk, and reinvestment risk. Bonds redeemed prior to maturity may be worth more or less than their original cost. Investments seeking to achieve higher yields also involve a higher degree of risk. Some municipal bond interest could be subject to the federal and state alternative minimum tax.

Tax-exempt interest is included in determining if a portion of any Social Security benefit you receive is taxable. Because municipal bonds tend to have lower yields than other bonds, the tax benefits tend to accrue to individuals with the highest tax burdens.

HSA funds can be withdrawn free of federal income tax and penalties provided the money is spent on qualified health-care expenses. Depending upon the state, HSA contributions and earnings may or may not be subject to state taxes. You cannot establish or contribute to an HSA unless you are enrolled in a high deductible health plan (HDHP).

To qualify for the tax-free and penalty-free withdrawal of earnings, a Roth IRA must meet the five-year holding requirement and the distribution must take place after age 59½ or due to the owner's death, disability, or a first-time home purchase (up to a $10,000 lifetime maximum). All investing involves risk, including the possible loss of principal, and there is no guarantee that any investment strategy will be successful.

The Congressional Budget Office estimates that the federal budget deficit will be roughly $3.7 trillion in fiscal year 2020 and $2.1 trillion the following fiscal year. By comparison, the federal budget deficit for fiscal year 2019 was $984.4 billion.

Sources: Congressional Budget Office, April 28, 2020; U.S. Department of the Treasury, May 2020

Is Now a Good Time to Consider a Roth Conversion?

This year has been challenging on many fronts, but one financial opportunity may have emerged from the economic turbulence. If you've been thinking about converting your traditional IRA to a Roth, now might be an appropriate time to do so.

CONVERSION BASICS

Roth IRAs offer tax-free income in retirement. Contributions to a Roth IRA are not tax-deductible, but qualified withdrawals, including any earnings, are free of federal income tax. Such withdrawals may also be free of any state income tax that would apply to retirement plan distributions.

Generally, a Roth distribution is considered "qualified" if it meets a five-year holding requirement and you are age 59½ or older, become permanently disabled, or die (other exceptions may apply).

Regardless of your filing status or how much you earn, you can convert assets in a traditional IRA to a Roth IRA. Though annual IRA contribution limits are relatively low ($6,000 to all IRAs combined in 2020, or $7,000 if you are age 50 or older), there is no limit to the amount you can convert or the number of conversions you can make during a calendar year. An inherited traditional IRA cannot be converted to a Roth, but a spouse beneficiary who treats an inherited IRA as his or her own can convert the assets.

Converted assets are subject to federal income tax in the year of conversion and may also be subject to state taxes. This could result in a substantial tax bill, depending on the value of your account, and could move you into a higher tax bracket. However, if all conditions are met, the Roth account will incur no further income tax liability and you won't be subject to required minimum distributions. (Designated beneficiaries are required to take withdrawals based on certain rules and time frames, depending on their age and relationship to the original account holder, but such withdrawals would be free of federal tax.)

WHY NOW?

Comparatively low income tax rates combined with the impact of the economic downturn might make this an appropriate time to consider a Roth conversion.

The lower income tax rates passed in 2017 are scheduled to expire at year-end 2025; however, some industry observers have noted that taxes may rise even sooner due to rising deficits exacerbated by the pandemic relief measures.

Moreover, if the value of your IRA remains below its pre-pandemic value, the tax obligation on your conversion will be lower than if you had converted prior to the downturn. If your income is lower in 2020 due to the economic challenges, your tax rate could be lower as well.

Any or all of these factors may make it worth considering a Roth conversion, provided you have the funds available to cover the tax obligation.

As long as your traditional and Roth IRAs are with the same provider, you can typically transfer shares from one account to the other. When share prices are lower, as they may be in the current market environment, you could theoretically convert more shares for each dollar and would have more shares in your Roth account to pursue tax-free growth. Of course, there is also a risk that the converted assets will go down in value.

USING CONVERSIONS TO MAKE "ANNUAL CONTRIBUTIONS"

Finally, if you are not eligible to contribute to a Roth IRA because your modified adjusted gross income (MAGI) is too high (see table), a Roth conversion may offer a workaround. You can make nondeductible contributions to a traditional IRA and then convert traditional IRA assets to a Roth. This is often called a "back-door" Roth IRA.

As this history-making year approaches its end, this is a good time to think about last-minute moves that might benefit your financial and tax situation. A Roth conversion could be an appropriate strategy.

All investing involves risk, including the possible loss of principal, and there is no guarantee that any investment strategy will be successful.

If your federal tax filing status is:	Your 2020 Roth contribution is reduced if your MAGI is:	You can't contribute to a Roth IRA for 2020 if your MAGI is:
Single or head of household	More than $124,000 but less than $139,000	$139,000 or more
Married jointly or qualifying widow(er)	More than $196,000 but less than $206,000	$206,000 or more
Married filing separately	More than $0 but less than $10,000	$10,000 or more

Note that your contributions generally cannot exceed earned income for the year. (Special rules apply to spousal IRAs.)

Seeking Sun or Savings? Explore a Retirement Move

Many people intend to retire in the place they call home, where they have established families and friendships. But for others, the end of a career brings the freedom to choose a new lifestyle in a different part of the country — or the opportunity to preserve more wealth and protect it from taxes.

This big life decision is not all about money or the weather. Quality -of-life issues matter, too, such as proximity to family members and/or a convenient airport, access to good health care, and abundant cultural and recreational activities. In fact, choosing a retirement destination typically involves a delicate negotiation of emotional and financial issues, especially for married couples who may not share all the same goals and priorities.

If you're nearing retirement, there's a good chance you have at least thought about living somewhere warmer, less expensive, or perhaps closer to children who have built lives elsewhere. Here are some important factors to consider.

Cost of Living

A high cost of living can become a bigger concern in retirement, when you may need to stretch a fixed income or depend solely on your savings for several decades. There's no question that your money will go further in some places than in others. The cost of living varies among states and even within a state, and it's typically higher in large cities than in rural areas. Housing is typically the largest factor — and often varies the most from place to place — but cost of living also includes transportation, food, utilities, health care, and, of course, taxes.

Selling a home in a high-cost area might enable you to buy a nice home in a lower-cost area with cash to spare. The additional funds could boost your savings and provide additional income. Moving to a more expensive locale may require some sacrifices when it comes to your living situation, future travel plans, and other types of personal spending.

Tax Differences

Seven states have no personal income tax — Alaska, Florida, Nevada, South Dakota, Texas, Washington, and Wyoming (Tennessee and New Hampshire tax only interest and dividend income) — and other states have different rules for taxing Social Security and pension income. Estate taxes are also more favorable in some states than in others. Property taxes and sales taxes also vary by state and even by county, so make sure to include them when calculating and comparing the total tax bite for prospective destinations.

The Tax Cuts and Jobs Act limited the annual deduction for state and local taxes to $10,000. This change resulted in federal tax increases for some wealthier households in high-tax states, and it may also factor into your relocation decision.

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TIPS FOR SNOWBIRDS

If you can afford the best of both worlds, you might prefer to keep your current home and head south for the winter. But if your choice of location is based largely on lower taxes, consider how much the costs of owning, maintaining, and traveling between two homes might cut into (or exceed) the potential tax savings.

To establish residency in the new state, you must generally live there for more than half of the year and possibly meet other conditions. You should also be aware that the tax agency in your old state may challenge your residency claim, especially if you still own property, earn income, or maintain other strong ties. If so, you may need to document your time and activities in each state and/or prove that your new home is your primary and permanent residence.

If you decide to live somewhere new on a full- or part-time basis, it may be worthwhile to rent for the first year, just in case the adjustment turns out to be more difficult than expected. You might also discuss the financial implications of a move with a tax professional.

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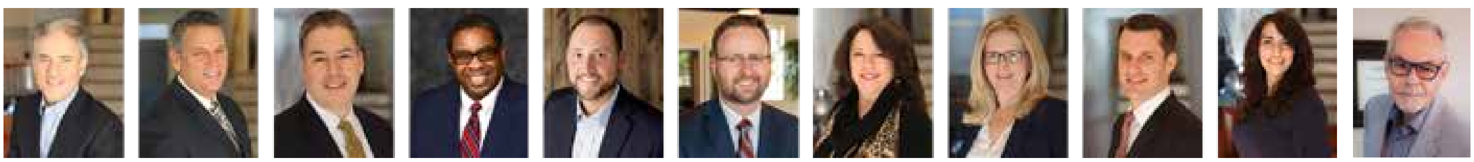

HALF OF U.S. ADULTS FEAR HEALTH-RELATED BANKRUPTCY

In July 2020, half of U.S. adults were concerned that a major health event in their household could lead to bankruptcy, compared with 45% in early 2019. Health-related bankruptcy fears increased significantly for younger people.

Percentage of U.S. adults extremely concerned/concerned about a health event leading to bankruptcy, by age group.