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Impeding Major Retirement and Estate Tax Law Changes and Prognostication

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Retirement

Report on the Economic Well-Being of U.S. Households in 2020

- Report released in May 2021.
- 27% of adults in 2020 considered themselves to be retired, even though some were still working in some capacity.
- 13% of retirees had done some work for pay or profit in the prior month.
- 4% of all adults considered themselves retired and were still working.
- Retirees with more education were more likely to work in retirement.

Report on the Economic Well-Being of U.S. Households in 2020

Reasons for the timing of retirement among retirees.

Note: Respondents could select multiple answers.

Reason	Percent
Voluntary	
Wanted to do other things	48
Reached normal retirement age	45
Didn't like the work	14
Unanticipated or involuntary	
Health problem	29
Care for family members	15
Forced to retire or lack of work	11

Report on the Economic Well-Being of U.S. Households in 2020

- Social Security was the most common source of income in retirement in 2020.
- 81% of retirees had one or more sources of private income.

Sources of income in the prior 12 months among retirees (by age).

Note: Among retirees. Respondents could select multiple answers. Sources of income include the income of a spouse or partner.

Source	Retirees age 65 and older	All retirees
Social Security	93	79
Pension	68	59
Interest, dividends, or rental income	50	46
Wages, salaries, or self-employment	25	32
Cash transfers other than Social Security	7	12

Report on the Economic Well-Being of U.S. Households in 2020

- About 75% of non-retired adults have at least some retirement savings. The other 25% does not have any.
- 81% of retirees had one or more sources of private income.

Report on the Economic Well-Being of U.S. Households in 2020

Forms of retirement savings among non-retirees.

Note: Among non-retirees. Respondents could select multiple answers.

Savings type	Percent
Defined contribution pension	54
Savings not in retirement accounts	48
IRA	33
Defined benefit pension	21
Other retirement savings	12
Business or real estate	9
None	26

Report on the Economic Well-Being of U.S. Households in 2020

- Only 36% on non-retirees thought their retirement savings was on track, 45% said it was not on track and the rest were not sure.

Retirement saving and self-assessed preparedness (by age and race / ethnicity).

Note: Among non-retirees.

Characteristic	Any retirement savings	Retirement savings on track
Age		
18–29	62	28
30–44	71	34
45–59	83	40
60+	87	48
Race / ethnicity		
White	80	42
Black	63	23
Hispanic	58	22
Asian	85	47
Overall	73	36

Report on the Economic Well-Being of U.S. Households in 2020

- Self-directed retirement accounts frequently have complex rules on withdrawals and rely on individuals to have the skills and knowledge required to manage their own investments.

Comfortable investing in self-directed retirement savings (by gender and education).

Note: Among non-retirees with self-directed savings.

Education	Men	Women
High school degree or less	36	25
Some college/technical or associate degree	43	27
Bachelor's degree or more	60	31

How much do I need to retire?

- Experts say your retirement income should be about 80% of your final pre-retirement salary.
- Comfortable lifestyle?
- 401(k) Participants believe they need \$1.9 million on average and many are not on track to get there

How much do I need to retire?

- Retirement Savings: The 4% Rule
- To generate \$80k annually in retirement you would need a nest egg at retirement of about \$2 million ($\$80,000 / .04$).
- This strategy assumes a 5% return on investments (after taxes and inflation).

How much do I need to retire?

- Percentage of your salary.
- Should have an amount equal to your annual salary in accumulated savings by age 30.
- This requires 15% of your gross salary beginning at age 25 and investing at least 50% in stocks.
- Age 40 – 2x annual salary.
- Age 50 – 4x annual salary.
- Age 60 – 6x annual salary.
- Age 67 – 8x annual salary.

Social Security

- You can start receiving Social Security retirement benefits as early as age 62.
- If you delay taking your benefits up to age 70, your benefit amount will increase.
- Taking benefit before full retirement age:
 - Advantage – collect benefits for a longer period-of-time.
 - Disadvantage – benefit will be reduced.

- Example:

A Person born in 1960 or later would reach full (normal) retirement age at 67 and receive a \$1,000 monthly retirement benefit.

If they choose to start receiving benefits at 62 then they would receive an additional 60 months of payments, however the benefit would be reduced to \$700 monthly. This is a 30% reduction.

In addition, if the spouse was to receive the \$500 monthly retirement benefit at age 67 but received benefits early at 62, the benefit would be reduced to \$325 monthly. This is a 35% reduction.

Social Security

- Spousal Benefit.
- You can only collect spousal benefits and wait until 70 to claim your retirement benefit if both of the following are true:
 - You were born before January 2, 1954.
 - Your spouse is collecting his or her own Social Security retirement benefit.
- This makes you eligible to file a “restricted application,” which allows you to collect a spousal benefit while delaying benefits on your own earnings record.
- Under a [law Congress passed in 2015](#), people born after January 1, 1954, cannot file a restricted application, regardless of how old they are when they file for benefits. They are covered by what Social Security calls “deemed filing.” When they claim retirement benefits, they are also deemed to be claiming any spousal benefits they are entitled to, except under narrow circumstances.

How to reduce or avoid taxes on your Social Security benefit:

1. Stay below the taxable thresholds.
 - Up to 50% of Social Security income is taxable for individuals with a total gross income including Social Security of at least \$25,000, or couples filing jointly with a combined gross income of at least \$32,000.
 - Up to 85% of Social Security benefits are taxable for an individual with a combined gross income of at least \$34,000, or a couple filing jointly with a combined gross income of at least \$44,000.
 - Retirees who have little income other than Social Security won't be taxed on their benefits.
2. Manage your other retirement income sources.
3. Consider taking IRA withdrawals before signing up for Social Security.
4. Save in a Roth IRA.

Types of Retirement Plans

- Here are some of the types of retirement accounts you might be eligible to use:
 - 401(k).
 - 403(b).
 - 457(b).
 - IRA.
 - Roth IRA.
 - SIMPLE IRA.
 - SEP IRA.

401(k)

- Offered through employer
- For 2022, contributions by employees who participate in 401(k), 403(b), most 457 plans, and the Federal government's Thrift Savings Plan is \$20,500, up from \$19,500 (an additional \$6,500 catch-up contribution if you're age 50 or older).
- Solo 401(k) allows contributions up to \$61,000 in 2022 (plus catch-up contribution).
- Contributions deducted from taxable income
- Subject to Required minimum distributions, and taxed upon withdrawal.
- Penalties for early withdrawals before 59 ½
- Employer has option to match a portion of contributions

Profit Sharing

- Additional pre-tax contribution employers can make to employees' retirement accounts that are tax-deductible for the employer.
- It's a bonus with tax benefits to the employee
- Flexible to employer – contributions made by tax filing deadline (including extension)
- Make greater contributions to highly compensated employees without failing discrimination testing. Combine with 401(k) can be up to \$61,000 in 2022
- Employers can choose a vesting schedule.

Cash Balance Plan

- Many owners and partners are looking for larger tax deductions and accelerated retirement savings.
- Age-dependent. The older the participant, the higher the contribution
- The actual contribution is determined by a formula specified in the plan document. It can be either a percentage of pay or a flat dollar amount.
- A participant's account is credited each year with a "pay credit" (such as 5 percent of compensation from his or her employer) and an "interest credit" (either a fixed rate or a variable rate that is linked to an index such as the one-year treasury bill rate).
- When a participant becomes entitled to receive benefits under a cash balance plan, the benefits that are received are defined in terms of an account balance.

Cash Balance Plan

Who are Cash Balance Plans good for:

1. Partners or owners who desire to contribute more than \$61,000 a year to their retirement accounts.
Adding a Cash Balance Plan allows to rapidly accelerate savings with pre-tax contributions as high as \$100,000 to \$260,000, depending on their age.
2. Companies already contributing 3-4% to employees, or at least willing to do so. While often established for the benefit of key executives and other highly compensated employees, other employees benefit as well. The plan normally provides a minimum contribution between 5% and 7.5% of pay for staff in the Cash Balance Plan or a separate Profit Sharing 401(k) plan.
3. Companies that have demonstrated consistent profit patterns. This is a pension plan with required annual contributions, consistent cash flow and profit is very important.
4. Partners or owners who desire to “catch up” or accelerate their pension savings. Maximum amounts allowed in Cash Balance Plans are age-dependent. The older the participant, the faster they can accelerate their savings.

403(b)

- For nonprofit or tax-exempt organizations

457(b)

- Offered through state and local governments
- Funds can be withdrawn before age 59 ½ without incurring a penalty, if you have left the job.

- Available to those with earned income
- For 2022, the total contributions you make each year to all your traditional IRAs and Roth IRAs can't be more than \$6,000 (\$7,000 if you're age 50 or older).
- For 2020 and later, there is no age limit on making regular contributions to traditional or Roth IRAs.
- If you file a joint return, you may be able to contribute to an IRA even if you didn't have taxable compensation as long as your spouse did. Each spouse can make a contribution up to the current limit; however, the total of your combined contributions can't be more than the taxable compensation reported on your joint return.

IRA Contribution Limits

- For 2022, if you are covered by a retirement plan at work then you can take a deduction based upon your modified AGI:
- Full deduction for the amount of your contribution:
 - Single or HOH: \$68,000 or less.
 - Married filing joint: \$109,000 or less.
- Partial deduction for the amount of your contribution:
 - Single or HOH: \$68,000 to \$78,000.
 - Married filing joint: \$109,000 to \$129,000.
 - Married filing separate: less than \$10,000.
- No deduction for the amount of your contribution:
 - Single or HOH: \$78,000 or more.
 - Married filing joint: \$129,000 or more.
 - Married filing separate: \$10,000 or more.

IRA Contribution Limits

- For 2022, if you are NOT covered by a retirement plan at work then you can take a deduction based upon your modified AGI:
- Full deduction for the amount of your contribution:
 - Single or HOH: any amount.
 - Married filing joint: any amount.
- If spouse is covered by a plan at work, then a partial deduction for the amount of your contribution based upon modified AGI:
 - Married filing joint: \$204,000 to \$214,000.
 - Married filing separate: less than \$10,000.
- If spouse if covered by a plan at work, then no deduction for the amount of your contribution based upon modified AGI:
 - Married filing joint: \$214,000 or more.
 - Married filing separate: \$10,000 or more.

... Roth IRA or Roth 401(k)

- Contributions are made with after-tax dollars. You are not subject to taxation when funds are withdrawn (if taken after 59 ½).
- A blend of regular and Roth retirement account will give you greater flexibility to manage the withdrawals from each account.

Roth IRA Contribution Limits

- For 2022, your contributions to a Roth IRA are based upon your modified AGI:
- Full contribution allowed:
 - Single or HOH: \$129,000 or less.
 - Married filing joint: \$204,000 or less.
- Partial contribution allowed:
 - Single or HOH: \$129,000 to \$144,000.
 - Married filing joint: \$204,000 to \$214,000.
 - Married filing separate: less than \$10,000.
- No deduction for the amount of your contribution:
 - Single or HOH: \$144,000 or more.
 - Married filing joint: \$214,000 or more.
 - Married filing separate: \$10,000 or more.

.... SIMPLE IRA

- Plan for small business with 100 or fewer employees
- Employees need to have earned at least \$5,000 during previous two years and expected to earn at least \$5,000 in current year.
- Contributions to SIMPLE retirement accounts is \$14,000, up from \$13,500 (an additional \$3,000 catch-up contribution if you're age 50 or older).
- An employer can choose to either make a dollar-for-dollar match of up to 3% of a worker's pay or contribute a flat 2% of compensation, whether the employee contributes or not.
- Low administrative cost

SEP IRA

- Plan for small business with several employees and self-employed individuals.
- Individual must be at least 21 years old, have worked for the employer in at least three of the previous five years, and have received a minimum of \$600 in compensation from the employer during the current year to qualify
- Employers make contributions, Lesser of 25% of compensation or \$61,000 in 2022.
- Contributions are vested immediately
- Can start a SEP for their self-employed business even if they participate in an employer's retirement plan at a second job.
- Low administrative cost

SECURE Act

- The Setting Every Community Up for Retirement Enhancement (SECURE) Act was signed into law on December 20, 2019. The Act includes reforms that could make saving for retirement easier and more accessible for many Americans.
- The legislation reflects policy changes to defined contribution plans such as 401(k)s, defined benefit pension plans, individual retirement accounts (IRAs) and 529 college savings accounts.
- Most provisions in the law went into effect on January 1, 2020.

SECURE Act

- Repeals the maximum age for traditional IRA contributions past 70 ½, as long as you are still working.
- Increases the required minimum distribution (RMD) age for retirement accounts to 72 (up from 70½).
- Inherited IRA distributions generally must now be taken within 10 years. Exceptions for assets left to surviving spouse, a minor child, disabled beneficiary or beneficiaries who are less than 10 years younger than the original owner.

SECURE Act

- Allows parents to withdraw up to \$10,000 from 529 plans to repay student loans.
- Permits parents to withdraw up to \$5,000 from retirement accounts penalty-free within a year of birth or adoption for qualified expenses.

SECURE Act

- Small business owners can receive a tax credit for starting a retirement plan, up to \$5,000.
 - Credit for smaller employers of \$250 per non-highly compensated employees eligible to participate in a workplace retirement plan at work (minimum credit of \$500 and maximum credit of \$5,000).
 - Applies to small employers with up to 100 employees over a 3-year period and applies to SEP, SIMPLE, 401(k), and profit-sharing types of plans.
 - If the retirement plan includes automatic enrollment, an additional credit of up to \$500 is now available.

- Changes to workplace retirement savings plans:
 - Allows long-term, part-time workers to participate in 401(k) plans. (500 hours over 3 consecutive years).
 - Raises the cap for auto enrollment contributions in employer sponsored retirement plans from 10% of pay to 15%.
 - Allows “lifetime income investment” to be distributed from your workplace plan.
 - Fiduciary Safe Harbor for the Selection of Lifetime Income Provider.
 - Increases transparency into retirement income with “lifetime income disclosure statements.”
 - Department of Labor (DOL) to provide a template for a model lifetime income disclosure by December 20, 2020, (one year from the date of enactment). Once that template is finalized, plan sponsors who currently offer defined contribution plans will need to work with their third-party service providers to update the language in their plan disclosures to comply with the new rules.

Build Back Better Act (BBBA)

- Also known as the Budget Reconciliation Bill
- Retirement Provisions stripped from updated version of BBBA (released October 28, 2021). What could have happened? Will they return in SECURE 2.0?
 - Retirement Plan auto-enrollment and escalation mandates.
 - Refundable Saver's Credit – those without any income tax liability are eligible to receive the benefit in the form of a contribution to their retirement account. Increase from current benefit of \$1,000 to \$1,500.

Build Back Better Act (BBBA)

- The current 3-year statute of limitations for any substantial errors (willful or otherwise) relating to the reporting of the valuation of IRAs would be extended to 6 years. Similarly, the statute of limitations would be extended to 6 years for any taxes due to an IRA losing its tax-exempt status. This is effective for taxes with respect to which the 3-year statute of limitations ends after Dec. 31, 2021.
- Limits the ability of high-income individuals to defer or avoid excessive amounts of taxes through the use of retirement plans.

Build Back Better Act (BBBA)

- Mega IRAs – retirement accounts in excess of \$10 million.
 - Limits the amount an individual can contribute to IRAs and Defined Contribution Plans. Applies to single taxpayers over \$400,000 and joint filers and head of household with incomes over \$450,000. (Contributions to a SEP or SIMPLE IRA are still permitted. Also does not prohibit contributions to be made on his or her behalf to an employer-sponsored retirement plan, such as a 401(k) plan or a non-qualified deferred compensation plan).
 - Requires employer-sponsored defined contribution plans to report account balances in excess of \$2.5 million to the IRS.
 - No more “backdoor Roth” Eliminates Roth conversions for single filers over \$400k and joint/HOH over \$450k. Prohibits all employee after-tax contributions in qualified plans and using after-tax contributions for Roth conversions.

Build Back Better Act (BBBA)

- Mega IRAs – retirement accounts in excess of \$10 million
 - Increases the Required Minimum Distribution (RMD), 50% of the account balance over \$10mil must be distributed. If two or more IRAs and DC plans that exceed \$20 million, RMD is the lesser of the amount needed to bring the aggregate to \$20million across all accounts or the aggregate balance in just the Roth account. Once an individual takes the distribution needed to get the balances to \$20million, they need to satisfy the 50% rule

Build Back Better Act (BBBA)

- Restrictions on certain investments that have the potential of generating astonishing rates of return but are not available to most investors.
 - An IRA will be prohibited from holding a security if the issuer requires the IRA owner to have a minimum level of assets or income, have completed a specified level of education; or hold a specific license or credential.
 - Lowers the threshold from 50% to 10% of an IRA balance which can be invested by its owner in non-tradable investments offered on an established securities market and prevents investment in an entity of which the IRA owner is an officer.

Infrastructure Investment and Jobs Act

- Smoothing option for Defined Benefit Plans
 - Extends the provision of the 2012 Act – the pension requirement will continue to be lower, allowing companies to have lower mandatory contributions for their DB plans. (modifies the interest rate stabilization period and percentages used to determine the applicable interest rates for valuing single-employer plan liabilities that affect a plan's minimum funding requirements.)
 - Temporarily boosting tax revenues (more corporate tax) at the risk of future retirement plan funding shortfalls

SECURE 2.0

- What will be a part of SECURE 2.0? Approved by House Ways and Means Committee May 5, 2021
 - Allow long-term, part-time workers to participate in 401(k) plans. (500 hours over 2 consecutive years (currently 3 years).
 - Increase the required minimum distribution (RMD) age for retirement accounts to 75 by 2032. Reduce RMD penalty. Waive RMDs for savings < \$100k.
 - Individuals in their early 60s would be able to invest an extra \$10,000 annually into 401(k) and certain other plans. (Currently \$6,500 for 50 and up)

SECURE 2.0

- Employees could elect that some or all matching contributions be treated as Roth contributions.
- Employers could match a portion of a worker's student loan payments and deposit that in the person's retirement account, even for people who aren't saving on their own.
- Allow employers to offer gift cards or other modest-dollar incentives to encourage retirement-plan participation.
- National database to track down lost or missing retirement accounts.

- Allow plan sponsors more time to correct missed contributions to employees' retirement account without penalties.
- Allow collective investment trusts in 403(b) plans – often used by plans to lower fees
 - Certain conditions must be met. (1) the plan is subject to ERISA, (2) the plan sponsor accepts fiduciary responsibility for selecting the investment that participants can select under the plan, (3) the plan is a governmental plan, or (4) the plan has a separate exemption from the securities rules.

Estate Tax

Definitions

- Estate tax – is a tax levied on assets of a decedent over a specific amount (exemption) at the time of their passing.
- Gift tax – is a tax levied on gifts (taxable), given in a year which is over the annual exclusion and cumulatively are over the exemption amount.
- Exemption Amount – set by statute and increases every year by inflation. Currently as of 2021 is \$11,700,000 per person (set to expire in 2026 and goes down to \$6,500,000).
- Portability – the ability of a spouse to inherit the unused portion of a deceased spouse's exemption amount. Married couples therefore have a total of \$23,400,000 exemption.

Definitions

- Annual gift exclusion – a de minimis amount (\$15,000) which can be given every year to any individual (non-spouse) without using any exemption amounts.
- Estate tax rates – rates start at 18 percent, but quickly hit the top rate of 40 percent at \$1,000,000 above the exemption amount.
- Step-up basis – an asset passed on to a beneficiary has its income tax basis increased to the fair value at the time of death. This allows the estate or the beneficiary to sell the asset without an income tax being imposed, thereby avoiding the potential double tax of estate and income tax.

History – Estate Tax Exemption

Year	Exemption	Top Tax Rate
1997	\$600,000	55%
2002	\$1,000,000	50%
2004	\$1,500,000	48%
2006	\$2,000,000	46%
2009	\$3,500,000	45%
2010	\$5,000,000	35%
2017	\$5,490,000	40%
2021	\$11,700,000	40%

Current Rules

New York	
Exemption Amount	\$5,930,000
New York Cliff Amount	\$292,500
Portability	No
Top Tax Rate	16%
No Gift Tax Returns (3 Year Clawback)	-
Step-up Basis	Follows the Federal
Inheritance Tax	None

••• Estate Numbers for 2019 (The Most Recent Year Published)

- Currently, the percentage of deceased individuals who had an estate return filed on their behalf is less than .15 percent, and less than half of those paid tax.
- For 2019, there were over \$20 billion tax dollars generated by estate taxes, and approximately 44 percent of the returns were audited for correctness.
- The current state of estate taxation for 2021, is, as follows:

Exemption Amount	\$11,700,000
Portability	Yes
Tax Rate	40%
Step-up Basis	Yes

- Remember that all lifetime gifts, in excess of the annual exclusion, are added to assets held at death, to determine total estate assets. However, gifts in New York escape transfer taxation if the giver outlives the 3-year clawback period.
- Note that for Federal purposes, non-taxable gifts given before January 1, 2022 will continue to be non-taxable, even if the exemption amount is later lower.

Proposals for Estate/Gift Taxation

1. New, new, new framework for the Build Back Better Plan – released late Thursday, October 28, 2021.
 - Scaled back version has no modifications to estate/gift tax exclusions or the basis step-up rules.
 - This is great news – however, it is being done through “reconciliation” which allows changes to be made.
2. Ways and Means Committee Draft. This was the version we were assuming would be passed until late October.
 - Reduction of exemption to 6.0 million.
 - Dramatic restrictions on use of grantor trusts, including SLAT’s and ILIT’s.
 - Elimination of valuation discounts for non-operating assets.

Proposals for Estate/Gift Taxation

3. Additional changes proposed.
 - Elimination of step-up basis (IRC Section 1014).
 - Taxation as capital gains of appreciated assets.
 - Tax rate changes.
 - Elimination of portability.
- It would be wonderful if Congress passed the estate frame-work. But they will almost certainly change something.
- Additionally, there is a very good chance that final vote, and signature by the President will not come until very late in the year, or even early in 2022.
- This means that you need to make decisions and take action without having all the rules in place.

So, What Can We Do?

- First realize that you may be subject to estate/transfer tax.
 - You should inventory all your assets.
 - All assets!
 - Everywhere (worldwide).
 - You can project into foreseeable future.
 - Bequests.
 - Sales.
 - Valuation issues.

So, What Can We Do?

- Second, know that all decisions are yours and should be made with all available information.
 - Provide for loved ones/charities.
 - Control may be an issue.
 - Many options are irreversible.
 - Document your wishes.
 - Taxes are not the only major consideration.

So, What Can We Do?

- It is a process, with lots of options, that takes time.
 - As it is a long process, you need to start it immediately if you want to have it done in 2021.
 - The pressure may be reduced, assuming the bill is passed, as is; however, this is still something that must be addressed.
 - Consider including some/all stakeholders.
- There are many different options to assist in reducing your taxable estate.
 - Gifting to family members, to maximize the annual exclusion. This can add up quickly.

So, What Can We Do?

- Example: Married couple with 4 children and 11 grandchildren.

$$\begin{array}{r}
 4+4 \text{ (Spouses)} \\
 \hline
 8 \text{ Children} \\
 11 \text{ Grandchildren} \\
 \hline
 19 \\
 \times 15000 \\
 \hline
 \$ 285,000 \times 2 = \underline{\underline{\$ 570,000}}
 \end{array}$$

A year in transfers/every year.

So, What Can We Do?

- Gifts for tuition/medical above the annual exclusion.
- Gifts to charities – during life rather than at death (income tax deduction).
- Plus, if you donate appreciated stock, you avoid the capital gains tax (triple duty) and remove future appreciation as well.

So, What Can We Do?

- Traditional planning techniques, for 2021 and beyond.
 - Balancing estates.
 - Use of credit shelter trusts.
 - Family limited partnerships.
 - Use of other trusts.
 - There are dozens of trusts.

So, What Can We Do?

- Timing may be critical.
 - Gift limits for lifetime exemption:
 - 2021 – \$23,400,000.
 - 2022 – ??? (\$6,000,000/\$12,000,000)
 - Internal Revenue Service ruling IR.2019-189 allows NO clawback on gifts if exception amounts decrease.
 - If you currently have an 11.7 million exemption and know it will go to 6.0 million in 2022, it is only the amount from 6.0 to 11.7 million that we are trying to utilize.
 - Use it or lose it.

... Gifting/Transfers During Your Lifetime Becomes Important

- Use of family partnerships may allow for discounts due to:
 - Lack of marketability; and
 - Lack of control
- NOTE: This may be affected by new legislation (either updates to proposed law or new laws in the near future) curtailing use of valuation discounts
 - Transfers to next generation at lower value.
- Use of trust allows for some degree of control/restrictions.



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Questions



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