

Planning Considerations for the Rest of 2026 and Into 2027

2026 Year-End Estate Planning Advisory

November 19, 2026

Click here for the 2026 Year-End Estate Planning Table of Contents

---

2026 is the first full year under the permanent transfer tax rules of the One Big Beautiful Bill Act (OBBBA). The federal estate, gift and generation-skipping transfer (GST) exemption is now $15,000,000 per individual and is indexed for inflation, increasing to $15.48 million in 2027. Unlike the increased exemption enacted by the 2017 Tax Cuts and Jobs Act (TCJA), this exemption has no scheduled sunset. Given the historically high level of the exemption, the focus for most families has shifted from federal transfer tax to income tax efficiency, basis step-up, trust flexibility and coordination with state estate taxes. Clients whose wealth approaches or exceeds the exemption still have an important opportunity to remove future appreciation from the taxable estate. All clients should confirm that existing dispositive provisions, tax elections and fiduciary structures continue to work as intended.

Year-end checklist for 2026

Reasons to give before the end of 2026	Reasons to wait until 2027
Uses the 2026 annual exclusion before it expires	The 2027 exemption and annual exclusion are higher after inflation indexing
Anticipated growth leaves the estate sooner	Uses separate tax years for intra-spousal transfers and spousal lifetime access trust (SLAT) funding
Protects against a future law that lowers the exemption	Leaves time to get qualified appraisals for assets that are hard to value

Reasons to give before the end of 2026	Reasons to wait until 2027
Clears the 0.5% charitable floor if 2026 is the “bunching” year	Better choice if 2027 adjusted gross income (AGI) is expected to be higher, because the charitable deduction is worth more in a higher-income year

Review Formula Bequests

Many wills and revocable trusts use a formula clause that funds a credit shelter (bypass) trust with an amount equal to the available federal exemption, with the balance passing to a marital trust. With the exemption at $15 million in 2026 and $15.48 million in 2027, formulas drafted when exemptions were much lower can now produce unexpected results. The credit shelter trust may now receive far more than intended, and the marital share may shrink sharply or disappear entirely. That outcome may be inconsistent with the grantor's objectives or may not provide adequate support for the surviving spouse. This risk is heightened in blended families, where the two trusts often benefit different people, and in states that have decoupled their estate tax from the federal system, many of which set exemptions well below the federal level.

Families with multigenerational goals should also keep a key limitation in mind when reviewing formula plans: GST exemption is not portable. While a surviving spouse may use the deceased spouse's unused estate and gift tax exemption, any GST exemption the deceased spouse fails to allocate is lost at death. As a result, relying solely on portability risks wasting the first spouse's GST exemption.

A targeted review should consider building in post-mortem flexibility through tools such as disclaimer-based plans, qualified terminable interest property (QTIP)-eligible trusts that preserve the executor's election and carefully drafted powers of appointment, so that the plan can be adjusted to the circumstances that exist at death. Because these choices also affect basis at each spouse's death, formula reviews should be coordinated with the income tax planning discussed below.

Income Tax Basis Planning

With federal transfer tax exposure reduced for many clients, the tradeoff between lifetime gifts and income tax basis has become central. Low-basis assets held until death generally receive a step-up in basis, eliminating the built-in gain for heirs, whereas assets gifted during life retain the donor's carryover basis.

Revenue Ruling 2023-2 takes the position that assets held in a completed-gift grantor trust receive no section 1014 basis adjustment at the grantor's death unless they are included in the grantor's gross estate. Some commentators have long argued that grantor trust assets should receive a step-up because the grantor is treated as their owner for income tax purposes until death. That position is now being tested in *Belmont Investments, LLC v. Commissioner*, T.C. Docket No. 14039-25 (petition filed Oct. 3, 2025), in which a partnership made section 754 basis adjustments after the deaths of each spouse-grantor for interests held in irrevocable grantor trusts that were not included in their estates, disclosing the position on Form 8275; the IRS asserts underpayments of about $21 million.

Strategies to secure a basis step-up, where appropriate, include:

- Retaining low-basis assets in the taxable estate while gifting higher-basis assets.
- Using substitution powers, or buying assets back from grantor trusts, to “swap in” high-basis assets and “swap out” low-basis assets before death. Obtain appraisals for hard-to-value assets so that the swap does not create an inadvertent gift.
- Where a trust beneficiary has unused estate tax exemption, deliberately causing low-basis trust assets to be included in that beneficiary's estate. A general power of appointment, a properly structured distribution or the exercise of a limited power of appointment that triggers the Delaware tax trap can accomplish this, subject to careful asset-by-asset analysis and creditor considerations. The higher exemption makes this technique available to more beneficiaries.
- Using portability, especially together with QTIP planning, to preserve a second basis step-up at the surviving spouse's death.

These techniques require individualized modeling of basis profiles, expected appreciation, available exemption and liquidity. The table below summarizes the core tradeoff.

Factor	Lifetime Gift	Asset Kept Until Death
Recipient's basis	Same as the donor's (carryover)	Stepped up to value at death
Built-in gain	Passes to the recipient	Eliminated
Future growth	Removed from the estate	Stays in the estate
Assets in a completed-gift grantor trust	No step-up unless included in the grantor's estate (Rev. Rul. 2023-2)	N/A

Factor	Lifetime Gift	Asset Kept Until Death
Target client	Clients exposed to estate tax; high-basis or fast-growing assets	Clients not expected to owe estate tax; low-basis assets

Planning to Utilize Increased Federal Exemptions

Although OBBBA made the higher exemptions permanent, “permanent” in the tax code means only that there is no scheduled sunset; future legislation could still reduce the exemptions. For that reason, clients with significant transfer tax exposure may wish to accelerate strategic transfers. The higher exemption creates an opportunity to remove appreciating assets from the taxable estate permanently and to implement flexible, protective trust structures that support long-term succession goals.

For clients who now fall below the increased thresholds, the focus has shifted from minimizing estate tax to income tax efficiency and flexibility, including the basis planning discussed above. Asset-specific planning, such as for retirement accounts, has become an essential part of the overall plan for many families; for example, Roth conversions in lower-income years can leave heirs with assets that are free of income tax.

Gifting Techniques

Lifetime gifts are tax-exclusive and remove future appreciation from the estate. They can also be combined with valuation discounts and trust structures. However, as discussed under income tax basis planning, gifted assets do not receive a basis step-up at death, so the transfer tax savings should be weighed against capital gains deferral across the asset mix. For clients not expected to owe estate tax, retaining low-basis assets until death is often preferable, subject to cash flow needs and risk tolerance.

Trust-based approaches include:

SLATs. A SLAT provides access for a spouse while excluding the trust assets from both spouses' estates.

- To mitigate the risk that the reciprocal trust doctrine (under which interrelated trusts that spouses create for each other may be “uncrossed” and included in each grantor's estate) applies to paired SLATs, consider differing beneficiary classes, divergent powers of appointment, distinct termination dates and non-identical distribution standards.

- If one spouse must first transfer assets to the other to equalize estates, allow adequate time and substance between steps. For example, making intra-spousal transfers in late 2026 and funding the trust in 2027 keeps the steps in separate tax years, which is a conservative approach.
- Address what happens if the beneficiary spouse dies first or the couple divorces, since either event can cut off the grantor's indirect access to the trust. One possible solution is to authorize a trust protector to add the surviving spouse as a beneficiary of the trust created by the deceased spouse (if the surviving spouse is not already a member of the beneficiary class).

Dynasty trusts with GST exemption allocated. These trusts insulate assets from transfer tax over multiple generations and often provide robust long-term asset protection and governance benefits.

Other techniques that leverage the higher exemption include:

- Sales to grantor trusts and combined gift/sale structures to “freeze” values. Adequate disclosure on the gift tax return should be used to commence the statute of limitations, and qualified appraisals are essential for nonmarketable assets.
- Allocating more GST exemption to existing trusts that are not GST-exempt. In particular, confirm prior GST allocations and the inclusion ratios of existing trusts. For trusts that are only partially GST-exempt, consider allocating additional exemption or modifying the trust. The higher indexed exemption makes this easier to accomplish in 2027.
- Balancing spouses' estates to maximize use of both exemptions. Take care with transfers to a spouse who is not a US citizen: the unlimited marital deduction is unavailable, and the annual exclusion for those transfers is $194,000 for 2026 and $201,000 for 2027.
- Grantor retained annuity trusts (GRATs) and sales to intentionally defective grantor trusts (IDGTs). Model these against current section 7520 rates and applicable federal rates (AFRs), as discussed under freeze planning below.

Technique	Main benefit	Main risk or planning point
SLAT	Spouse keeps access while assets stay out of both estates	Reciprocal trust doctrine; the beneficiary spouse dying first; divorce
Dynasty trust (with GST exemption allocated)	Shields assets from transfer tax across generations; asset protection	GST exemption must be allocated correctly

Technique	Main benefit	Main risk or planning point
GRAT	“Zeroed-out” design avoids current gift tax; growth above the hurdle rate passes tax-free	Higher section 7520 rates reduce the benefit
Sale to an IDGT	No gain recognized on the sale; growth above the AFR builds up outside the estate	Rule of thumb: seed the trust with about 10% equity
Gift/sale combination	“Freezes” values	Needs adequate disclosure and qualified appraisals
Irrevocable life insurance trust (ILIT)	Keeps the death benefit out of the estate and provides liquidity	Premiums must be funded, for example through intrafamily loans

Techniques Leveraging the Higher Exemption

Building on the gifting techniques above, the current environment of higher exemptions and higher interest rates favors a review and strategic rebalancing of the overall estate plan. Additional opportunities include using the increased exemption to forgive intrafamily notes, particularly where refinancing at a lower rate is no longer available; making late allocations of GST exemption to existing non-exempt trusts to improve their multigenerational efficiency; using sales and gifts to “freeze” asset values (see freeze planning below); reassessing life insurance needs and ownership; and balancing spouses' estates so that both spouses' exemptions can be fully used. Planners should also be mindful of obstacles that can undermine a plan, such as a rule against perpetuities in jurisdictions that still impose one, state estate and inheritance taxes, and transfers to non-US citizen spouses, for whom the unlimited marital deduction is unavailable and the annual exclusion is limited.

Trust Income Tax Planning and the Medicare Surtax

Non-grantor trusts reach the top 37% bracket at just $16,000 of taxable income in 2026. The 2027 threshold is $16,500. These trusts are also subject to the 3.8% net investment income tax (NIIT) once undistributed net investment income exceeds the trust threshold.

Before December 31, trustees should model whether to shift distributable net income (DNI) to beneficiaries in lower brackets. Targeted distributions can also reduce trust-level NIIT where beneficiaries are below their own NIIT thresholds. Trustees should also evaluate distribution standards, beneficiaries' tax profiles and whether capital gains can be included in DNI where state law and the trust instrument allow.

Under the 65-day rule, the trustee of a complex trust may elect on a timely filed Form 1041 to treat distributions made by March 6, 2027 as made in 2026, providing a post-year-end window to fine-tune 2026 trust income tax results.

Starting in 2026, OBBBA replaces the former Pease limitation with a reduction of itemized deductions equal to 2/37ths (approximately 5.4%) of the lesser of the itemized deductions or the amount by which income exceeds the start of the 37% bracket. Former section 68(e), which exempted trusts and estates from the limitation, was repealed for taxable years beginning after December 31, 2025. Because trusts and estates reach the 37% bracket at just $16,500 (for 2027) (compared with $768,700 for joint filers), the reduction is far more significant at the fiduciary level, and it may apply even if all of the trust's income is capital gain or qualified dividends taxed at 20%. The issue will first arise when trusts and estates file their 2026 income tax returns in 2027.

Distribution deductions and trust-specific expenses. Read literally, the statute treats expenses unique to trusts and estates and distribution deductions under sections 651 and 661 as “itemized deductions” subject to the reduction. Applied to distribution deductions, this would tax about 5.4% of distributed income twice: once to the beneficiary and again to the trust. For example, a trust that distributes all $2 million of its income would deduct only about $1,892,000, so roughly $108,000 would be taxed to both the trust and the beneficiary, producing about $40,000 of additional tax. Treasury Regulation section 1.67-4 states that these deductions are not itemized deductions, and the IRS is bound by its regulations, but the regulation is issued under section 67 and its reach for section 68 purposes is uncertain. The IRS is unlikely to impose double tax on distributed income and may address the issue in the 2026 Form 1041 instructions, but it is more likely to apply the reduction to trust-specific administration expenses, where no double tax results.

Charitable deduction. The section 642(c) charitable deduction for trusts and estates is listed as an itemized deduction in section 67(b), so the reduction appears to apply. For example, a non-grantor trust that pays $600,000 of gross income to charity would lose about $30,000 of its deduction. For an estate passing entirely to charity, any income tax paid from the charitable share could reduce the set-aside deduction and create a circular computation; Hartwick College v. United States, 801 F.2d 608 (2d Cir. 1986), rejected a similar circular computation, but whether it applies here is unclear.

Planning note: Absent guidance, return preparers will need to choose a reporting position for 2026 returns. Many advisors expect to wait and see whether the 2026 Form 1041 instructions resolve the distribution deduction issue. Where the trust instrument permits (or can be amended to permit), a trustee may grant a current beneficiary an annual withdrawal right over an amount equal to the trust's anticipated income, so that income is taxed directly to the beneficiary under section 678 and no double tax arises. Because the 2/37ths reduction also applies to the section 691(c) deduction, accelerating income in respect of a decedent before death may be more attractive. Trustees should evaluate the reduction's effect on charitable distributions before planning for 2027.

Freeze planning in the current environment

Higher exemptions have not made the traditional estate freeze techniques summarized above obsolete. They still serve goals that go beyond transfer tax savings: preserving wealth, protecting against creditors, shifting income and structuring family governance. The current interest rate environment does, however, affect the efficiency of these techniques. GRATs, sales to IDGTs and intrafamily loans move wealth only to the extent the transferred assets outperform a statutory benchmark. For GRATs, that benchmark is the section 7520 rate. For sales and loans, it is the AFR. Both rates remain well above their 2020–2021 lows and show no sign of retreating, so the hurdle is higher. Assets with strong growth prospects, such as business interests ahead of a liquidity event or concentrated equity positions, can still clear it by a wide margin. If rates later fall, transactions completed now will still have moved all appreciation above the benchmark out of the estate.

GRATs remain effective because the grantor can “zero them out” so that the transfer uses little or no gift tax exemption, and any growth above the hurdle rate passes to the remainder beneficiaries free of transfer tax. This makes them especially useful for clients who have already used their exemption or prefer to preserve it.

Sales to IDGTs remain a cornerstone of freeze planning. Because the trust is a grantor trust, the grantor recognizes no gain on the sale and no income on the note payments, and appreciation above the AFR builds up outside the estate. With higher AFRs, success depends more on the assets' expected performance and on valuation discounts that can be supported. Larger exemptions make a larger gift component in the transaction more practical, which reduces reliance on interest-bearing notes.

Pairing these techniques with others, such as valuation discounts or the buyback and asset swap strategies described under income tax basis planning, can create additional opportunities.

Higher rates also make some techniques more attractive than they were when rates were low. These

strategies value a retained or charitable interest using the section 7520 rate, so a higher rate shifts value toward that interest and reduces the taxable gift or increases the charitable deduction.

Qualified personal residence trusts (QPRTs). A QPRT allows a grantor to transfer a primary or vacation residence to a trust while retaining the right to live there for a term of years. The taxable gift is the value of the remainder, and as the section 7520 rate rises, the grantor's retained term interest is worth more and the remainder (and therefore the gift) is worth less. Appreciation in the residence after the transfer passes to the remainder beneficiaries free of transfer tax. As with a GRAT, the grantor must survive the term, or the residence is included in the estate. A grantor who wishes to continue living in the residence after the term must pay fair market rent, which can further reduce the estate.

Charitable remainder trusts. A charitable remainder trust (CRAT) pays the grantor (or other noncharitable beneficiaries) a fixed annuity for life or a term of up to 20 years, with the remainder passing to charity. A higher section 7520 rate reduces the value of the annuity, increasing the grantor's charitable income tax deduction and making it easier to satisfy the requirements that the charitable remainder equal at least 10% of the initial value and that the probability of exhausting the trust not exceed 5%. A CRAT can also be used to sell a low-basis asset, such as a business interest before a liquidity event, without immediate recognition of gain at the trust level, spreading the income tax over the payment term.

Charitable Planning

In addition to the 2/37th (approximately 5.40%) reduction to itemized deductions of individuals with income above the 37% tax bracket threshold, 2026 is the first year of the 0.5% AGI floor on individual itemized charitable deductions. Consider bunching contributions into alternating years, for example through a donor-advised fund, to clear the floor efficiently, and compare front-loading gifts in 2026 with deferring them to 2027 based on each client's expected AGI.

Qualified Charitable Distributions (QCDs) remain a compelling tool for clients age 70½ and older to satisfy charitable intent and reduce taxable income outside the itemized deduction limitations. For clients age 73 and older, QCDs also count toward annual required minimum distributions (RMDs). The maximum QCD is $111,000 for 2026 and is estimated to be $114,000 for 2027.
Starting in 2026, non-itemizers can also take a new above-the-line charitable deduction of up to $1,000 for single filers or $2,000 for joint filers. This deduction is in addition to QCDs. Clients who take the standard deduction should make qualifying cash gifts before year-end.

For charitable gifts made through non-grantor trusts, account for the 2/37ths reduction described under trust income tax planning above.

Summary: review and reevaluate

OBBBA set the federal estate, gift and GST exemption at $15 million per person for 2026, indexed for inflation. As a result, most estate plans warrant review. For many families, the principal concern is no longer federal transfer tax but income tax efficiency, basis step-up, trust flexibility and state estate tax.

Formula bequests drafted when exemptions were lower may now put far more into the credit shelter trust than intended. That can shrink the marital share, which matters most in blended families and in states with their own estate tax. Because GST exemption is not portable, relying on portability alone can waste the first spouse's GST exemption.

Clients with significant estate tax exposure should still consider removing appreciating assets from the estate soon, through techniques such as SLATs, dynasty trusts, GRATs and sales to IDGTs, since future legislation could lower the exemption. Although higher section 7520 rates and AFRs raise the hurdle, freeze techniques remain effective for assets with strong growth prospects. Clients below the threshold may benefit more from retaining low-basis assets until death so that their heirs receive a basis step-up.

2026 Year-End Estate Planning Advisory Table of Contents:

- 2026–2027 Planning Priorities
- Select Updates Impacting Family Business Owners
- The Great Wealth Transfer: Planning Priorities for Families
- Planning Considerations for the Rest of 2026 and Into 2027
- Select Federal Caselaw Updates
- State of the States
- Relevant International Updates

To download a PDF of the entire advisory, click here.

CONTACTS

For more information, contact your Katten attorney or any of the following attorneys.



Joshua S. Rubenstein
+1.212.940.7150
joshua.rubenstein@katten.com



Diane B. Burks
+1.704.344.3153
diane.burks@katten.com



Charles Harris
+1.312.902.5213
charles.harris@katten.com



Tye J. Klooster
+1.312.902.5449
tye.klooster@katten.com



David M. Allen
+1.312.902.5260
david.allen@katten.com



Charlotte A. Castillo
+1.312.902.5434
charlotte.castillo@katten.com



Adam M. Damerow
+1.312.902.5250
adam.damerow@katten.com



Brianna Garland
+1.312.902.5242
brianna.garland@katten.com



Stuart E. Grass
+1.312.902.5276
stuart.grass@katten.com



Michael O. Hartz
+1.312.902.5279
michael.hartz@katten.com



Nicholas J. Heuer
+1.312.902.5549
nicholas.heuer@katten.com



Chris S. Hopkins
+1.312.902.5230
chris.hopkins@katten.com

Robert J. Hovey
+1.312.902.5426
robert.hovey@katten.com



Caitlyn E. Jensen
+1.312.902.5293
caitlyn.jensen@katten.com

Katie Keating
+1.312.902.5407
katie.keating@katten.com



Caitlin A. Kelly
+1.312.902.5419
caitlin.kelly@katten.com



Jonathan Kohl
+1.312.902.5619
jon.kohl@katten.com



Benjamin Lavin
+1.312.902.5670
ben.lavin@katten.com

Jay A. Mansker
+1.312.902.5268
jay.mansker@katten.com

Laura E. Marion
+1.312.902.5264
laura.marion@katten.com



Andrew L. McKay
+1.312.902.5315
andrew.mckay@katten.com



Kelli Chase Plotz
+1.312.902.5347
kelli.plotz@katten.com



Michael L. Sherlock
+1.312.902.5643
msherlock@katten.com



Abby Feinman
+1.310.788.4722
abby.feinman@katten.com



Carol A. Johnston
+1.310.788.4505
carol.johnston@katten.com



Avi Pariser
+1.310.788.4514
avi.pariser@katten.com

Megan E. Ricker
+1.310.788.4521
megan.ricker@katten.com



Ronni G. Davidowitz
+1.212.940.7197
ronni.davidowitz@katten.com



Cynthia Reed Altchek
+1.212.940.6710
cynthia.altchek@katten.com



Mal L. Barasch
+1.212.940.8801
mal.barasch@katten.com



Lawrence B. Buttenwieser
+1.212.940.8560
lawrence.buttenwieser@katten.com



Jonathan C. Byer
+1.212.940.6532
jonathan.byer@katten.com



Bonnie Lynn Chmil
+1.212.940.6415
bonnie.chmil@katten.com



Alexandra Copell
+1.212.940.8588
alexandra.copell@katten.com



Marla G. Franzese
+1.212.940.8865
marla.franzese@katten.com



Robert E. Friedman
+1.212.940.8744
robert.friedman@katten.com



Gale R. Helfgott
+1.212.940.6487
gale.helfgott@katten.com



Milton J. Kain
+1.212.940.8750
milton.kain@katten.com



Rebecca H. Lomazow
+1.212.940.6497
rebecca.lomazow@katten.com



Christina N. Romero
+1.212.940.6380
christina.romero@katten.com



Parker F. Taylor
+1.212.940.8668
parker.taylor@katten.com



Andrew B. Toporoff
+1.212.940.6356
andrew.toporoff@katten.com



Emily Tuten
+1.212.940.8617
emily.tuten@katten.com



Kathryn von Matthiessen
+1.212.940.8517
kathryn.vonmatthiessen@katten.com

Attorney advertising. Published as a source of information only. The material contained herein is not to be construed as legal advice or opinion.

©2026 Katten Muchin Rosenman LLP.

All rights reserved. Katten refers to Katten Muchin Rosenman LLP and the affiliated partnership as explained at katten.com/disclaimer.