New Tax Law Affects Many Estate Plans

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On December 22, 2017, President Trump signed into law the Tax Cuts and Jobs Act of 2017 (referred to herein as TCJA or the Act). Although the most discussed provisions of the Act concern income tax changes, the new tax law also contains provisions that directly or indirectly affect estate planning.

The most important provision of the Act concerning estate planning essentially doubles the exemption available from gift and estate tax for lifetime gifts and transfers at death from $5 million to $10 million. After taking into account inflationary adjustments since 2011, the actual amount of the exemption is expected to be $11.2 million per person ($22.4 million per married couple), effective for transfers made and decedents dying after 2017. The generation-skipping transfer tax exemption also would be increased to $11.2 million per person ($22.4 million per married couple).

However, similar to the changes to the gift and estate tax exemption made in 2001, this change is not permanent. Rather, it will "sunset" at the end of 2025, and the exemption will revert to $5 million (plus inflationary adjustments since 2011, which made the actual exemption $5.49 million in 2017 and $5.6 million in 2018).

The new higher exemption level creates a number of opportunities and considerations:

- The higher exemption of $11.2 million per person ($22.4 million per married couple) will shield many clients from the estate tax entirely or substantially reduce their estate tax.
- The step-up in basis for income tax purposes for assets included in a client's estate remains available and will be the primary planning consideration for more clients.

- Clients concerned about the possibility that the new exemption will not be made permanent will want to consider substantial lifetime gifts in order to “lock in” the benefit of the higher exemption before it is scheduled to sunset. Note that TCJA directs the Treasury to issue regulations clarifying that gifts made prior to the end of 2025 will not be “clawed back” and rendered taxable in the event that the new higher exemption level is not extended.
- Clients who believe their estate will no longer be subject to tax may want to consider updates to and simplification of their plan structures. However, clients must remember the many non-tax benefits of trust and other structures that may be included in their plans (asset protection from lawsuits, second spouses, divorce, profligate beneficiaries, providing for minor or special needs beneficiaries, etc.).
- Clients need to consider the scheduled reduction in 2025 and also be aware that future administrations and Congresses could “turn back the clock” and reduce the exemption prior to that time. This suggests that, in addition to considering early gifts to lock in the exemption, clients should consider maintaining a structure that will be flexible enough to work if the exemption is reduced in the future.
- Clients with estates likely to exceed $11.2 million per person ($22.4 million per married couple) have the opportunity to make (additional) substantial gifts, perhaps on a leveraged basis depending on the asset given (interests in closely held businesses, family partnerships, etc.). The additional gifting capacity may also be useful in bolstering prior planning structures, forgiving loans, and the like.
- Clients will want to consider taking advantage of the increased GST exemption to create trusts that are GST exempt and effectively outside the transfer tax system on a perpetual basis. In addition, clients with existing trusts that may be subject to generation-skipping tax on distributions may want to consider early distributions to take advantage of the increased GST exemption.

Many of the other changes made in TCJA with respect to income taxes may affect planning, including:

- Changes to income tax rates and brackets applicable to individuals and corporations;
- Changes affecting deductibility of charitable contributions (fortunately, the ability to make direct contributions from IRAs by persons over 70 1/2 years of age was retained);
- Changes affecting deductibility of state and local taxes;
- Changes affecting deductibility of mortgage interest; and
- Special rates available to those conducting a business through a pass-through entity.

Please contact your Vorys estate planning attorney if you have any questions regarding the impact of the proposed tax law changes on your family and estate plan.