

NEW LEGISLATION PROPOSES SWEEPING ESTATE TAX CHANGES

Trusts & Estates Alert
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After years of calling for a comprehensive overhaul of the federal tax code, congressional Republicans unveiled their plans for sweeping tax change on November 2nd. The Tax Cuts and Jobs Act (H.R. 1) is being billed as “real relief from today’s complex, costly, and unfair tax code” by Rep. Kevin Brady (R-Tx.), Chairman of the House Ways and Means Committee. The proposed bill is likely to come under fire from special interests, congressional Democrats, and some congressional Republicans, with the result that taxpayers and their advisors must wait to see what is contained in any final legislation. As it stands now, the proposed legislation would substantially alter the taxation of wealth transfers in the United States:

- **Increased Personal Estate Tax Exemption.** Currently, an individual is entitled to a \$5 million estate and gift tax exemption, as indexed annually for inflation (\$5.49 million in 2017). The proposed legislation seeks to double that amount to \$10 million, which would also be indexed to increase annually for inflation. A married couple would be able to transfer \$20 million, plus the inflation adjustment, without paying any estate or gift tax.
- **Repeal of the Estate Tax.** The proposed bill seeks to completely repeal the estate tax for individuals dying after December 31, 2023.
- **Increased Exemption and Repeal of Generation-Skipping Transfer Tax (“GSTT”).** In parallel with the estate tax, the bill proposes the repeal of the GSTT for a transfer to an individual two or more generations below the transferor occurring after December 31, 2023. Prior to the repeal, the GSTT exemption would be increased to \$10 million per person, indexed for inflation, just like the estate and gift tax exemption.
- **Continued Step-Up in Basis at Death.** Under current law, an individual’s income tax basis in property that he or she inherits from a decedent is the fair market value of the property as of the decedent’s date of death. The current statute defines property “acquired from the decedent” as property which was includible in the decedent’s gross estate and subject to estate tax. The stepped-up income tax basis is essentially a trade-off – because estate tax was paid on the property (or would have been paid, if the decedent’s estate exceeded the \$5 million exemption amount plus the applicable inflationary adjustment), the inheritor has full basis in the property and can sell the property in short order

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without triggering a significant capital gains tax. The proposed legislation keeps the stepped-up basis provision even after the 2023 estate tax repeal. This gives taxpayers both benefits, eliminating estate tax and allowing their beneficiaries to receive stepped-up basis in inherited assets.

- **Adjusted Gift Tax Rates and Increased Exemption.** Also proposed are changes to the gift tax regime. Even after the estate tax and GSTT repeal, the gift tax would remain in place. However, for gifts made after December 31, 2023, the top gift tax rate would be 35%, down from 40%. The gift tax exemption would be \$10 million per person, indexed for inflation.
- **Changes to the Charitable Income Tax Deduction.** While there are no proposed changes to the charitable deduction for estate tax purposes, and it remains to be seen how the proposed estate tax repeal would impact charitable giving at death, lifetime charitable giving will continue to be a powerful income tax tool under the proposed legislation. The charitable income tax deduction is preserved, but with an increase on the deductibility limit for cash contributions to public charities. Under the bill, the deductibility limit would increase to 60% of the taxpayer's adjusted gross income, up from 50%. Further, the bill would deny any deduction for contributions to institutions of higher education in exchange for seating rights at athletic events.

Significant changes to the transfer tax regime may be on the horizon. Until the landscape becomes clearer, taxpayers should continue to monitor and maintain their current estate plans, keeping in mind that the estate tax, gift tax, and GSTT exemptions are scheduled to increase to \$5.6 million per person in 2018. In addition, the gift tax annual exclusion is scheduled to increase from \$14,000 per donee to \$15,000 per donee as of January 1, 2018.

For more information on the proposed Tax Cuts and Jobs Act, and its impact on estate planning, please contact one of the members of the Hodgson Russ Trusts & Estates Practice.