Estate Planning in 2018 and Beyond

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Prominent Estate Tax Legislation

- Economic Growth & Tax Relief Reconciliation Act of 2001 & JGTRRA of 2003 ("the Bush tax cuts")
  - Sunset provisions scheduled for December 31, 2010
- Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010
  - Kicked the ball forward for 2 more years
- "Permanently" resolved with the American Taxpayer Relief Act of 2012
- Exemption doubled with Tax Cuts & Jobs Act of 2017

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Prominent Estate Tax Legislation

- ATRA made permanent key estate tax rules
  - Exemption stayed at (inflation-indexed) $5M
    - Would have been up to $5.6M for 2018
    - TCJA *doubled* it to $11.2M in 2018!
  - Gift and estate tax systems remained unified
  - State estate tax deduction remained
    - State estate tax credit permanently gone
  - Top estate (& gift & GST) rate rises to 40%...
    - …but made permanent!
  - Portability of estate tax exemption now *permanent*

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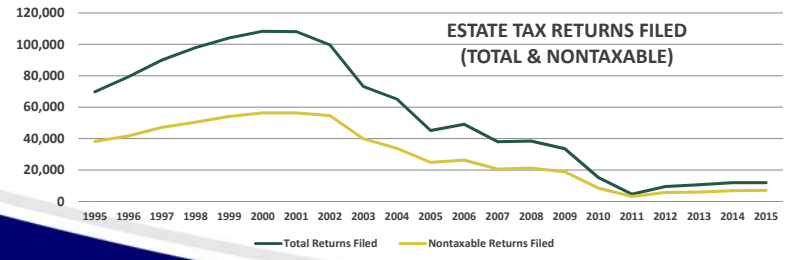
Estate Planning in 2018 & Beyond

- Scope of estate tax declining dramatically
  - May only be ~2,000 taxable estates annually now
    - And only ~half of those are taxable!?
  - Filings for portability rising, but tax exposure still declining



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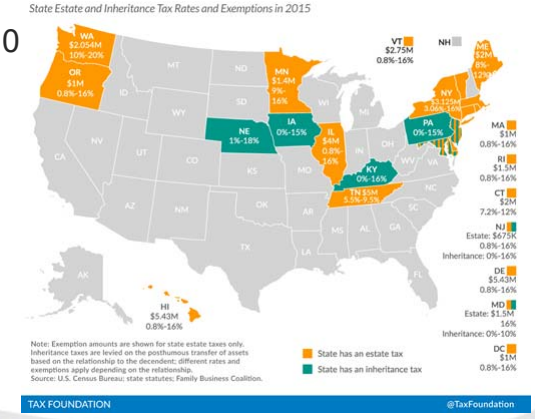
Estate Planning in 2018 & Beyond

- Estate Planning Under TCJA
  - Primary focus for most will shift to *state* estate taxes!
  - State decoupling 2.0
  - More pressure to repeal or recouple?
  - Will recoupled states move in line to $11.2M?



Source: Tax Foundation

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Rules/Requirements for Portability

- Portability allows a surviving spouse to carry over the "Deceased Spouse's Unused Exclusion Amount" (DSUEA)
  - Available to surviving spouse in addition to his/her own $11.2M basic exclusion amount (BEA)
    - BEA indexed over time
    - Carryover DSUEA amount is *not* indexed!

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Rules/Requirements for Portability

- *Requires* an estate tax return to be timely filed
  - Only available for deaths that had occurred after 2010
  - Simplified filing requirements for nontaxable estates
  - No proactive election to be made, beyond actually filing the return
    - Only opt *out* if not desired
- Applies for gift and estate tax exemptions
  - Does *not* apply for GST exemption, though
  - *No* state conformity at this point

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Examples of Portability

- Harold leaves $10M to wife Betty
  - Marital deduction reduces taxable estate to $0
  - Harold's unused exemption: $11.2M *portable to Betty*
  - Betty's (new) available exemption: $11.2M + $11.2M = $22.4M
- Harold leaves $7M to Betty and $3M to his children
  - Marital deduction only $7M
  - Remaining estate uses $3M of $11.2M exemption
  - Exemption ported to Betty: $8.2M
  - Betty's (new) available exemption: $8.2M + $11.2M = $19.4M

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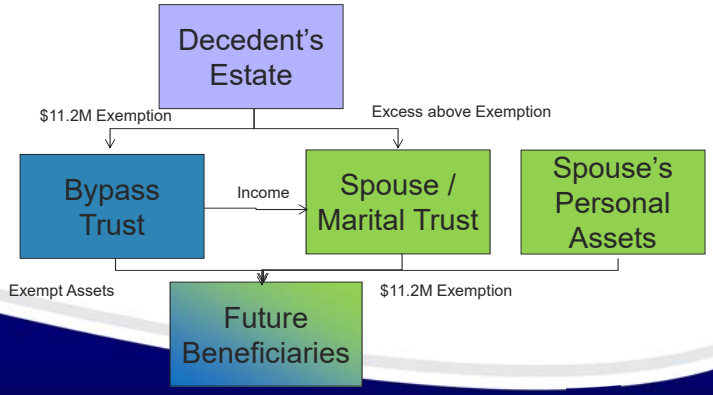
Planning for Portability

- The decline of the bypass trust
  - No longer necessary to preserve the estate tax exemption amount at the death of first spouse



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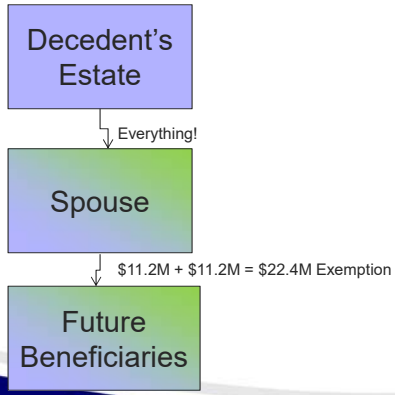
Planning for Portability

- The rise of the "I love you" Will
  - "Honey I leave you everything, including my assets and my estate tax exemption!"



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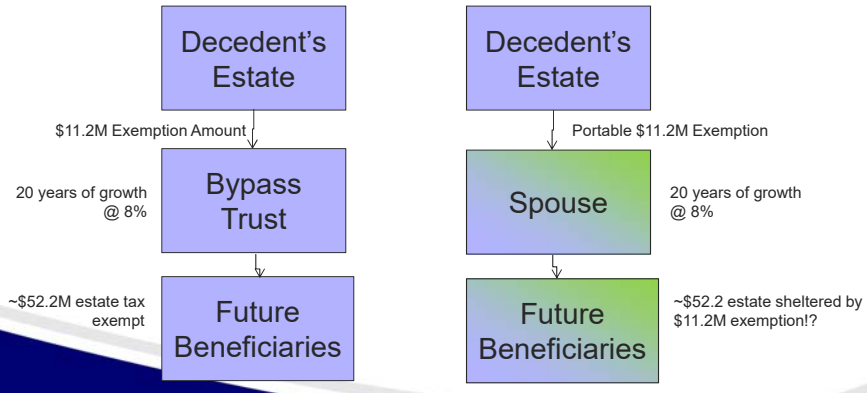
Planning for Portability

- When "bypass" trusts remain relevant
  - Sheltering *future growth* from exposure



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Planning for Portability

- When "bypass" trusts remain relevant
  - State estate tax planning
    - Relevant for (still) decoupled states
  - Using GST exemption for multi-generational trusts
    - GST exemption not portable at all!
  - Protecting exemption for/from remarriage
  - Asset protection and other *non-tax* reasons for trusts

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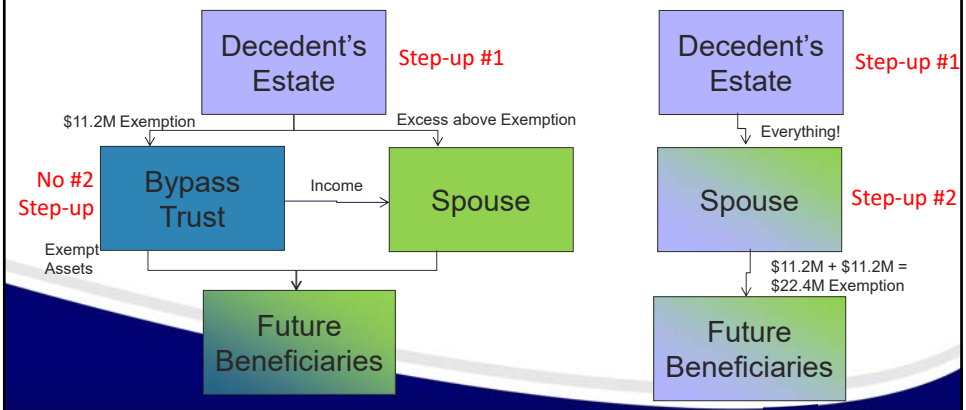
Planning for Portability

- Do you really want to create a bypass if you don't *have* to? Impact on step-up in basis:



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Planning for Portability

- Do you really want to create a bypass if you don't *have* to?
  - Unfavorable trust income taxation
    - Top tax rate 37% at only $12,500 of taxable trust income
    - 20% long-term capital gains, 20% qualified dividends, 3.8% Medicare surtax also apply
    - Doesn't apply if income passes through…
      - DNI deduction for trust
      - But does that defeat the purpose of the trust?

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Estate Planning in 2018 & Beyond

- 3 types of clients
  - High net worth (HNW) – exposed to estate tax
    - Net worth of $20M+
  - Potentially HNW – might be exposed some day
    - $2M to $20M?
    - Net worth that could grow (if client is young enough?)
    - Ongoing gifting to keep clients from crossing the line?
  - Everyone else

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Estate Planning in 2018 & Beyond

- *Most* clients will no longer have a Federal estate tax problem going forward!
  - Permanence finally pulled fence sitters out, but what now?
  - Will it be difficult to motivate estate planning?

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Estate Planning in 2018 & Beyond

- Any estate *tax* planning that remains will be primarily a *state* issue rather than Federal
  - Bypass trusts remain relevant at state level
    - But is it worth unfavorable income taxes & also losing step-up in basis?
  - It's not about what state the client *lives* in, but what state the client *dies* in!
    - Will clients be relocating (after 1st death?)
  - Challenges of mismatched state/Federal exemptions
    - Lifetime gifting & SLAT strategies?

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Estate Planning in 2018 & Beyond

- Introducing the Spousal Lifetime Access Trust (SLAT)
  - Structured similar to bypass trust
    - May distribute or retain income
    - May distribute or retain principal
    - Typically restricted to HEMS
  - Funded during life, *not* during death
    - Avoids state limitations when there's no gift tax
  - Can be done for both spouses…
    - But watch out for reciprocal trust doctrine

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Estate Planning in 2018 & Beyond

- Estate planning will shift away from estate *tax* planning
  - Renewed focus on *real* estate planning: the disposition of assets, including management, control, and protection
    - Providing for the needs and care of children/family
    - Still especially relevant for businesses!
    - Asset, divorce, & spendthrift protection
    - Revocable living trusts still useful for probate avoidance

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Estate Planning in 2018 & Beyond

- Estate planning will shift away from estate *tax* planning
  - *Income* tax ramifications of estate planning decisions
    - Preserving step-up in basis at death
    - Asset titling impact on step-up?
    - Avoiding trust tax rates where feasible?
    - Using portability to shelter IRAs?
  - Mandatory Form 8971 basis reporting to beneficiaries!
    - Began June 30 of 2016 (for estates since 7/31/2015)!

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Estate Planning in 2018 & Beyond

- Greater attention to "supporting" documents
  - Powers of Attorney
  - Health Care Powers of Attorney
  - Advanced Medical Directives
- Filing Form 706 returns will *rise*, though, to maintain portability carryover
  - How small is "too small" for an estate to file a return?
  - Simplified filing will help someday?

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Transitioning Estate Planning *in* 2018

- Unwinding estate planning strategies for income tax benefits?
  - Updating documents to remove bypass trusts?
    - Just an unnecessary complexity now?
  - Shifting distributions to existing bypass trusts?
  - Busting QPRTs? Re-evaluating FLPs? Unwinding ILITS?
    - But don't breach fiduciary duties of trustees!

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Estate Tax Legislation in the Future

- Further "crackdowns" on estate planning coming
  - *Generally targeted at ultra-high-net-worth*
    - Minimum time limit (10 yrs?) for GRATs
    - Restrictions on FLPs & valuation discount strategies
    - Elimination of IDGT strategies
    - Maximum duration for GST?
  - Limitations on stretch IRAs?
    - But relief on RMDs for small accounts?

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Estate Tax Legislation in the Future

- Future changes: Top rate: Maybe | Exemption: Unlikely

Year	Exemption	Top Rate
1916	$50,000	10%
1917	$50,000	25%
1918-1923	$50,000	25%
1924-1925	$50,000	40%
1926-1931	$100,000	20%
1932-1933	$50,000	45%
1934	$50,000	60%
1935-1939	$40,000	70%
1940	$40,000	70%
1941	$40,000	77%
1942-1976	$60,000	77%
1977	$120,000	70%
1978	$134,000	70%
1979	$147,000	70%
1980	$161,000	70%
1981	$175,000	70%
1982	$225,000	65%
1983	$275,000	60%
1984	$325,000	55%
1985	$400,000	55%
1986	$500,000	55%

Year	Exemption	Top Rate
1987-1997	$600,000	55%
1998	$625,000	55%
1999	$650,000	55%
2000-2001	$675,000	55%
2002	$1,000,000	50%
2003	$1,000,000	49%
2004	$1,500,000	48%
2005	$1,500,000	47%
2006	$2,000,000	46%
2007	$2,000,000	45%
2008	$2,000,000	45%
2009	$3,500,000	45%
2010	Repealed	N/A
2011	$5,000,000	35%
2012	$5,120,000	35%
2013	$5,250,000	40%
2014	$5,340,000	40%
2015	$5,430,000	40%
2016	$5,450,000	40%
2017	$5,490,000	40%
2018	$11,200,000	40%

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Summary

- Permanent increase of estate tax exemption removes most from scope of Federal estate tax
  - Focus on maximizing step-up in basis instead
  - Portability "simplifies" planning & reduces need for bypass trusts
- State estate tax dominant theme for many clients
  - Watch out for changes to state estate tax systems!
- From estate *tax* planning to *real* estate planning

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