

Impact of Tax Cuts & Job Act on Estate Planning

Private Wealth & Taxation Group

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This is the first of a series of Bulletins discussing the significant tax law changes and planning opportunities presented by the Tax Cuts and Jobs Act (the "Act"). This Bulletin focuses on the gift and estate planning opportunities presented by the Act. Future Bulletins to follow in the coming weeks will address:

- Taxation of Passthroughs (the 20% deduction) and C corporations
- Planning to minimize state taxes using out of state trusts, etc.
- Planning to minimize state taxes including through the use of out of state trusts, etc.
- Changes to depreciation including bonus depreciation, section 179 and immediate expensing
- 1031 exchanges
- Planning for education
- Compensation planning
- International taxation
- And more.

Unlike other tax law developments which tend to restrict our planning, the Act opens the door for many new tax planning opportunities. As we develop our thinking we will continue to provide you with updates and insights.

The Impact of Tax Cuts and Job Act on Estate Planning

The focus of this Bulletin is the doubling of the estate, gift and generation skipping lifetime exemption:

1. Much to the surprise of many, the GOP tax legislation did not repeal the estate tax. Instead, the exemption amount (the amount each US citizen or domiciliary can pass free of gift, estate and generation skipping transfer tax) was increased beginning in 2018 from \$5.6 million to \$11.2 million (\$22,400,000 for married couples) and will continue to be subject to future inflation adjustments.
2. The increase in the exemption is not permanent and reverts back to the \$5.6 million exemption (with an inflation adjustment) in 2026, absent any further changes.
3. Assets held at death will continue to receive a step-up in basis to their appreciated value at date of death.

As a result of these new provisions, we note a few key areas of impact for our clients:

1. We have observed that many of our ultra high net worth clients were on the sidelines waiting to see if the estate tax would be repealed. Since that did not happen, we expect these clients to resume the planning process in the coming months.
2. Clients with assets that are, or are expected to grow, to be in excess of \$11,200,000 (\$22,400,000 for a married couples) should continue to do lifetime planning to minimize their estate tax liability. Bear in mind that many of

the estate planning techniques we employ provide benefits aside from tax savings. To name a few, there are succession planning and asset protection benefits regardless of tax savings. Nevertheless, as discussed below, careful consideration of each client's circumstances is suggested to determine whether it is prudent to take advantage of the increased exemption presently.

3. A major factor in deciding whether to use the increased exemption is that New York State's exemption will not be increased to match the new Federal exemption. The New York estate tax exemption is currently \$5,250,000 and will increase to match the *current* Federal exemption in 2019 (\$5 million adjusted for inflation, which is projected to be approximately \$5.73 million). However, it will not increase to match the new higher federal exemption of \$11.2 million (further adjusted for inflation). Thus, when taking full advantage of the increased Federal exemption, a New York State estate tax may be payable. This tax may be as much as \$1,258,800 prior to 2026, when the Federal exemption is scheduled to revert back to the current exemption amount. Further, if an estate is valued at an amount that is 5% greater than the applicable New York State exemption, the estate faces a cliff, where the full value of the estate is taxed (not just the amount in excess of the exemption). As a result, planning for the increased Federal exemption without accounting for the New York State estate tax may result in the unintended consequences of exposing an entire estate to the New York Estate Tax. One method of eliminating this New York State estate tax exposure is to limit the credit shelter trust to the New York exemption amount and make a partial QTIP election for the remaining estate. The estate will avoid New York State and Federal estate taxes, and the unused Federal exemption will be preserved for the surviving spouse. Estates may have to choose whether to fully utilize the Federal exemption and pay the state estate tax or avoid the state tax but not claim the full Federal Exemption. [1] Similar concepts may be applicable where an individual is either a resident of, or owns property located within, other states like New York which have a state estate tax. [2]
4. In addition to state estate tax considerations, state income tax planning will be more important in the light of the Act's limits to itemized deductions for state and local taxes. These limits will be explained in an upcoming Bulletin. Establishing personal residency in states that have no state income taxes, as well as setting up businesses in those states and sourcing state income taxes there, will also be more helpful than in prior years. In 2014 New York State enacted rules limiting the use of out of state trusts to avoid New York income taxes. Nevertheless, there may still be some limited planning that can be done. The relevant rules are complex so please contact us to discuss further.
5. Another consideration is that under the Act there appears to be an open question as to whether lifetime transfers that take advantage of the additional exemption will have any adverse consequences (such as claw-back) should the exemption revert to the prior levels in 2026. Although we do not anticipate there will be a claw-back for gifting done using the additional exemption, the statute directs Treasury to issue regulations to deal with a mismatch if a taxpayer gifts the increased exemption and then passes away after 2026 when the exemption is lowered. As a result, before going forward with additional gifting of the increased exemption, we recommend meeting to discuss the best way to take advantage of the additional exemption for each client's specific situation. In certain circumstances (such as when there may be a surviving spouse) we may recommend waiting to make additional gifts in excess of the \$5.6 million (indexed for inflation) reversion cap until the regulations or other guidance is issued.
6. Many wills and revocable trusts automatically maximize the use of the exemption to fund a credit shelter trust. The change in law thus will automatically increase the amount funding the credit shelter trust and decrease the amount passing to or in trust for the surviving spouse. While the surviving spouse may be a beneficiary of a credit shelter trust, that is not always the case. For example, an additional \$5.6 million (indexed for inflation) may be diverted from the surviving spouse - which may not have been intended. Each situation should be reviewed and documents may have to be modified to reflect the changes in the Act. We recommend that you call us to have your particular will or revocable trust reviewed to see if any changes should be made to this formula in light of the higher exemption amounts.
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As we continue to digest the 1100 pages of the final bill we encourage our clients and friends to reach out to us with your questions and concerns. A lively dialogue about practical concerns will be a help to us all. Also, please follow us on LinkedIn and Twitter at @Meltzerlippetax. We will be posting these Bulletins and other items of interest.

Meltzer Lippe, a full service law firm, has 25 attorneys in its Private Wealth and Taxation Practice Group which includes the Tax, Trust and Surrogates Court practice groups, making it one of the largest Tax and Trust and Estates groups in the New York metropolitan area. We look forward to discussing with you the numerous tax saving alternatives presented by the Act with respect to your estate planning, business and personal taxes.

[\[1\]](#) If the full Federal exemption is not used the unused portion may be carried forward to the surviving spouse's estate (portability) but that will not work for state estate taxes and inheritance taxes and the generation skipping tax.

[\[2\]](#) For our clients in nearby jurisdictions such as New Jersey, Connecticut and Pennsylvania please contact us if you would like an update on the estate and inheritance taxes imposed by these jurisdictions.



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