

## Private Client Services Alert

February 13, 2018

### Key Points

- Each individual's exemptions from federal estate, gift and GST taxes have roughly doubled to approximately \$11,200,000
- The increased exemptions are available only temporarily, through 2025
- We recommend that you review the terms of your existing estate plan and consider additional tax-free gifts



---

## Dramatic Change to Federal Estate, Gift and Generation-Skipping Tax Exemptions

The Tax Cuts and Jobs Act (the "Act"), which took effect on January 1, 2018, is the most comprehensive update to the Internal Revenue Code in decades. In addition to making sweeping changes to the federal income tax laws, the Act makes significant, albeit temporary, changes to the federal estate, gift and generation-skipping transfer (GST) tax laws.

### Federal Estate, Gift and GST Tax Exemption Amounts Double

Under the Act, each individual's exemptions from federal estate, gift and GST taxes have roughly doubled, from \$5,490,000 (\$10,980,000 for a married couple) in 2017 to approximately \$11,200,000 (\$22,400,000 for a married couple) in 2018. The exemptions are scheduled to further increase with inflation for each year through 2025.

Absent further changes to the tax law, the increased exemptions are available only temporarily, through 2025. On January 1, 2026, the exemptions are scheduled to revert to 2017 levels, indexed for inflation. (Some practitioners have asked whether lifetime gifts in the amount of the increased exemptions made prior to 2026 will be subject to tax if the exemptions are subsequently reduced. While this seems unlikely, it remains an open question.)

Wealthy individuals can take advantage of the increased exemption currently by making lifetime gifts to their children and more remote descendants (or other family and friends), or to trusts for their benefit. Selecting the optimal property to transfer is critically important. Factors, such as whether valuation discounts can be taken, the prospects for appreciation in the property and the income tax basis in the property, should all be considered. Techniques, such as gifts and sales to intentionally defective grantor trusts, as well as grantor-retained annuity trusts, which preserve the use of the valuable gift and estate

tax exemptions, remain viable. Forgiving family indebtedness may also be attractive in light of the increased exemption amounts.

### **Impact on Individuals and Families**

The increased federal estate, gift and GST tax exemptions will have an important impact on many individuals and families:

- In light of the dramatic increase in the estate and GST tax exemptions, we strongly recommend that you review the terms of your existing estate plan to ensure that the provisions in your documents are still in line with your current wishes. For instance, your will, lifetime trusts or even beneficiary designations may provide for disposition of an amount based on the estate or GST tax exemption in effect at your death, and you may wish to consider whether such a provision would result in “overfunding” the disposition in the event of death prior to 2026. In some cases, it may be possible to simplify your plan as a result of the increased exemption. In all cases, flexibility should be built into your estate-planning documents to anticipate both the expiration and the extension of the federal tax law changes, as well as the possible enactment of related state tax law changes.
- As a result of the increased exemptions, fewer estates will be subject to federal estate tax, at least until 2025. Income tax planning—specifically, planning to ensure that appreciated assets will benefit from having income tax basis stepped up to fair market value at death—will likely become the highest priority for individuals with nontaxable estates. If this is your situation, you may wish to review, and possibly unwind, certain estate-planning transactions that you have undertaken in the past.
- As discussed above, given the temporary increase in the gift and GST tax exemptions, you now have a window of opportunity to make large, tax-free gifts to your children and more remote descendants (or other family and friends), or to trusts for their benefit.

### **Tax Rates Unchanged and Step-Up in Basis on Death Preserved**

The highest marginal federal estate and gift tax rates remain unchanged at 40 percent, and the GST tax rate remains unchanged at a flat 40 percent. The new law also preserves the step-up in income tax basis for assets owned at death.

### **Gift Tax Annual Exclusion Increases**

In addition to the higher lifetime exemptions, the amount that can be given tax-free pursuant to the so-called “annual exclusion” has increased from \$14,000 in 2017 to \$15,000 in 2018 as a result of inflation adjustments. In other words, individuals can now give \$15,000 per year, and married couples can give \$30,000 per year, to all of their children and grandchildren or anyone else without using any part of their valuable gift tax exemption.

### **State Tax Law**

In reviewing your existing estate plan and evaluating gifting options, you should bear in mind any applicable state estate and gift tax laws. As an example, for a New York resident, the state estate tax exemption is currently \$5,250,000 and is scheduled to increase in 2019, but only to the pre-Act federal

exemption amount. The benefit of the New York estate tax exemption phases out abruptly once the value of the taxable estate exceeds the amount of the exemption. As a result of this estate tax “cliff,” the entire taxable estate is subject to New York estate tax at graduated rates up to a maximum of 16 percent. Since the federal estate tax exemption is now much higher than the New York exemption, many New York estates that are not subject to federal estate tax will be subject to substantial New York estate tax. Steps that can be taken to minimize this result may include lifetime gifting (New York imposes no gift or GST tax) to reduce the taxable estate. Impending changes in state tax laws should certainly be monitored.

**Conclusion**

This is a high-level summary of the federal estate, gift and GST tax changes brought about by the new law. Individual circumstances will determine what kind of planning is warranted as a result of these changes. We encourage you to contact us to discuss how these changes impact your estate planning.

## Contact Information

If you have any questions regarding this alert, please contact:

**Seth D. Slotkin**

[sslotkin@akingump.com](mailto:sslotkin@akingump.com)

+1 212.872.7480

New York

**Timothy P. Tehan**

[ttehan@akingump.com](mailto:ttehan@akingump.com)

+1 214.969.2871

Dallas

**Elizabeth E. Harris**

[eharris@akingump.com](mailto:eharris@akingump.com)

+1 212.872.7407

New York