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PUTTING IT ON & TAKING IT OFF: MANAGING TAX BASIS TODAY (FOR TOMORROW)

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I. INTRODUCTION

A. Tax Reform

1. Generally

a. On December 22, 2017, the "To provide for reconciliation pursuant to titles II and V of the concurrent resolution on the budget for fiscal year 2018"[2] act, more commonly known as the "Tax Cuts and Jobs Act" ("TCJA") became law. TCJA makes significant changes to the U.S. income tax system including reducing the top income tax rate but eliminating most itemized deductions of individual taxpayers, limiting the deductibility of business interest expense, reducing the corporate tax rate to 21%, adding a special deduction for business income of "pass-thru" entities, and changing the taxation of foreign earnings.

b. A complete discussion of the TCJA is beyond the scope of this outline, but a number of significant changes were made to the income and transfer taxation of individuals and partnerships, disregarded entities, and other non-corporate entities. These are discussed in detail in these materials.

c. Unless otherwise indicated, all changes are effective for tax years beginning after December 31, 2017, and most of the provisions will expire after December 31, 2025, due to the "Byrd rule,"[3] as adopted by the U.S. Senate, which require the affirmative vote of three-fifths of the members (60 Senators if no seats are vacant), which did not occur with TCJA. Thus, most of the provisions of TCJA will "sunset," reverting back to the law that was in place when the provisions were enacted (as discussed later in these materials).

2. Pertinent Changes to the Income Taxation of Individuals and Trusts

a. TCJA adds subsection 1(j) to the Internal Revenue Code of 1986, as amended (the "Code"), that temporarily decreases the highest Federal ordinary income tax rate from 39.6% to 37% (for individual taxpayers with taxable income over $500,000, married

[1] These materials were initially prepared for the 52nd Annual Heckerling Institute on Estate Planning (2018), published by LexisNexis Matthew Bender, and are reprinted with the permission of the Heckerling Institute and the University of Miami. Portions of this material have been previously presented by Turney P. Berry & Paul S. Lee. *See also* Turney P. Berry and Paul S. Lee, *Retaining, Obtaining, and Sustaining Basis*, 7 Est. Plan. & Community Prop. L. J. 1 (Fall 2014).

[2] P.L. 115-97. The Senate parliamentarian removed the short title "Tax Cuts and Jobs Act" as extraneous. Hereinafter, P.L. 115-97 will nonetheless be referred to as the "Tax Cuts and Jobs Act" or "TCJA."

[3] Section 313 of the Congressional Budget Act of 1974, as amended (2 U.S.C. 644).

individuals filing joint returns with taxable income over $600,000, and trusts with taxable income over $12,500).[4]

b. TCJA adds temporarily increases the standard deduction to $12,000 for single filers and $24,000 for joint return filers,[5] but also temporarily limits the deduction for state and local sales, income, or property tax to $10,000.[6]

c. TCJA adds new subsection 67(g) of the Code that temporarily suspends all miscellaneous itemized deductions that are subject to the 2 percent of adjusted gross income floor (for example, unreimbursed employee expenses, tax preparation fees, and other expenses to produce or collect income or expenses to manage, conserve, or maintain property held to produce income).[7] Notably, it is unclear from the wording section 67(g) of the Code whether this suspension also includes trustee fees, which are exempted from the 2 percent floor under section 67(e)(1) of the Code.

d. Effective for 2018, TCJA permanently amends the measure of inflation used for indexing of both income and transfer tax purposes, relying on "chained CPI" (Chained Consumer Price Index for All Urban Consumers or C-CPU-I) rather than CPI (CPI-U) used prior to the enactment of TCJA. The IRS has issued Revenue Procedure 2018-18,[8] publishing the new values for certain items adjusted for 2018 using chained CPI.

3. Pertinent Changes to Transfer Taxation

a. Effective for estates of decedents dying and gifts made after December 31, 2017, TCJA adds new subparagraph section 2010(c)(3) to the Code that temporarily doubles the basic exclusion amount from $5 million to $10 million, which means, as adjusted for inflation, the Applicable Exclusion Amount for 2018 is $11.18 million per person.[9]

b. As a result, the GST exemption amount for 2018 will also be approximately $11.2 million per person.[10]

c. In order to address the issue of "clawback" (the risk that prior gifts covered by a gift tax exclusion that is greater than the estate tax exclusion available at the time of death, thereby giving rise to the risk of an estate tax liability), TCJA adds section 2001(g)(2) of the Code, which provides, "The Secretary shall prescribe such regulations as may be necessary or appropriate to carry out this section with respect to any difference between—(A) the basic exclusion amount under section 2010(c)(3) applicable at the time of the decedent's death, and (B)

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[4] § 1(j) of the Internal Revenue Code of 1986, as amended (the "Code"). Hereinafter, all section references denoted by the symbol § shall refer to the Code, unless otherwise noted. *See* Rev. Proc. 2018-18, 2018-10 I.R.B. 392.

[5] § 63(c)(7).

[6] § 164(b)(6).

[7] § 67(g).

[8] Rev. Proc. 2018-18, 2018-10 I.R.B. 392.

[9] *Id.*

[10] *See* § 2631(c).

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Also available as part of the eCourse
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